UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 40-F

o **REGISTRATION STATEMENT PURSUANT TO SECTION 12 OF THE SECURITIES EXCHANGE ACT OF 1934**

OR

þ **ANNUAL REPORT PURSUANT TO SECTION 13(a) OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended: December 31, 2012 **Commission File Number: 001-35297**

FORTUNA SILVER MINES INC.

(Exact name of Registrant as specified in its charter)

N/A
(Translation of Registrant's name into English (if applicable))

British Columbia, Canada
(Province or other jurisdiction of incorporation or organization)

1040	**N/A**
(Primary Standard Industrial Classification Code Number (if applicable))	(I.R.S. Employer Identification Number (if applicable))

200 Burrard Street, Suite 650
Vancouver, British Columbia, Canada V6C 3L6
604-484-4085
(Address and telephone number of Registrant's principal executive offices)

National Corporate Research, Ltd.
10 East 40th Street, 10th Floor
New York, New York 10016
(212) 947-7200
(Name, address (including zip code) and telephone number (including area code) of agent for service in the United States)

Securities registered or to be registered pursuant to Section 12(b) of the Act.

Title of each class	**Name of each exchange on which registered**
Common Shares	New York Stock Exchange

Securities registered or to be registered pursuant to Section 12(g) of the Act.

None
(Title of Class)

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act.

None
(Title of Class)

For annual reports indicate by check mark the information filed with this Form:

þ Annual information form þ Audited annual financial statements

Indicate the number of outstanding shares of each of the issuer 's classes of capital or common stock as of the close of the period covered by the annual report:

There were 125,268,751 common shares with no par value outstanding as of December 31, 2012.

Indicate by check mark whether the Registrant (1) has filed all reports to be filed by Section 13 or 15(d) of the Exchange Act during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports) and (2) has been subject to filing requirements for the past 90 days.

Yes þ No o

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data

File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files).

Yes o No o

EXPLANATORY NOTE

Fortuna Silver Mines Inc. (the "Company" or the "Registrant") is a Canadian issuer eligible to file its annual report pursuant to Section 13(a) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), on Form 40-F. The Company is a "foreign private issuer" as defined in Rule 3b-4 under the Exchange Act and Rule 405 under the Securities Act of 1933, as amended (the "Securities Act"). Equity securities of the Company are therefore exempt from Sections 14(a), 14(b), 14(c), 14(f) and 16 of the Exchange Act pursuant to Exchange Act Rule 3a12-3.

The Company prepares its consolidated financial statements in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board ("IFRS"). The Company began reporting in accordance with IFRS on January 1, 2011 and formerly reported in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"). All information is stated in U.S. dollars unless otherwise noted.

FORWARD-LOOKING STATEMENTS

This annual report on Form 40-F and the documents attached hereto contain "forward-looking statements" within the meaning of applicable securities laws. These statements appear in a number of different places and include statements regarding the intent, belief or current expectations of management and our directors or officers, primarily with respect to our future market size, our business, and our future operating performance. When the words such as "expects", "is expected", "anticipates", "believes", "plans", "projects", "estimates", "assumes", "intends", "strategies", "targets", "goals", "forecasts", "objectives", "budgets", "schedules", "potential" or variations thereof or stating that certain actions, events or results "may", "could", "would", "might" or "will" be taken, occur or be achieved, or the negative of any of these terms and similar expressions) are used, they are not statements of historical fact and are intended to identify forward-looking statements. Forward-looking statements relate to, among other things:

- mineral "reserves" and "resources" as they involve the implied assessment, based on estimates and assumptions that the reserves and resources described exist in the quantities predicted or estimated and can be profitably produced in the future;
- production rates at the Company's properties;
- cash cost estimates;
- timing to achieve full production capacity at the Company's properties;
- timing for completion of infrastructure upgrades related to the Company's properties and their completion on budget;
- timing for delivery of materials and equipment for the Company's properties; and
- the sufficiency of the Company's cash position, its reliance on revenue from its currently operating properties, and its ability to raise equity capital or access debt facilities.

You are cautioned that any such forward-looking statements are not guarantees that any of our projects or business operating units, divisions, subsidiaries, or affiliates will achieve any particular financial results. Our actual results may differ from those contained in the forward-looking statements due to risks or uncertainties facing us or due to facts differing from the assumptions underlying our predictions. Some of those risks and assumptions are set out under "Preliminary Notes – Cautionary Statement-Forward Looking Statements" outlined in the Company's Annual Information Form for the year ended December 31, 2012, a copy of which is attached as Exhibit 99.1 hereto, and include, but are not limited to:

- that all required third party contractual, regulatory and governmental approvals will be obtained for the development, construction and production of its properties,
- there being no significant disruptions affecting operations, whether due to labor disruptions, supply disruptions, power disruptions, damage to equipment or otherwise;
- permitting, development, expansion and power supply proceeding on a basis consistent with the Company's current expectations;
- currency exchange rates being approximately consistent with current levels;
- certain price assumptions for silver, gold, lead, zinc and copper;
- prices for and availability of natural gas, fuel oil, electricity, parts and equipment and other key supplies remaining consistent with current levels;
- production forecasts meeting expectations;
- the accuracy of the Company's current mineral resource and reserve estimates;
- labor and materials costs increasing on a basis consistent with the Company's current expectations; and
- assumptions made and judgments used in engineering and geological interpretation.

The Company advises you that the cautionary remarks included under the heading "Preliminary Notes – Cautionary Statement-Forward Looking Statements" in the Annual Information Form for the year ended December 31, 2012 expressly qualify, in their entirety, all forward-looking statements attributable to the Company or persons acting on its behalf. Unless required by law, the Company does not assume any obligation to update forward-looking statements, whether based on unanticipated events, changes in expectations, or otherwise. You should not place undue reliance on any forward-looking statements, which apply only as of the date of this annual report.

NOTES TO UNITED STATES READERS

Differences in United States and Canadian Reporting Practices

The Company is permitted, under a multijurisdictional disclosure system adopted by the United States, to prepare this annual report on Form 40-F in accordance with Canadian disclosure requirements, which are different from those of the United States. The Company prepares its financial

statements, which are filed with this annual report on Form 40-F, in accordance with IFRS, and they are subject to Canadian generally accepted auditing standards and the standards of the Public Company Accounting Oversight Board (United States). They may not be comparable to financial statements of United States companies.

Resource and Reserve Estimates

The terms "mineral reserve," "proven mineral reserve" and "probable mineral reserve" used in the Company's disclosure are Canadian mining terms that are defined in accordance with National Instrument 43-101 – Standards of Disclosure for Mineral Projects ("NI 43-101") under the guidelines set out in the Canadian Institute of Mining, Metallurgy and Petroleum (the "CIM") Best Practice Guidelines for the Estimation of Mineral Resource and Mineral Reserves (the "CIM Standards"), adopted by the CIM Council on November 23, 2003. These definitions differ from the definitions in the United States Securities and Exchange Commission (the "SEC") Industry Guide 7 under the Securities Act. Under Industry Guide 7 standards, mineralization may not be classified as a "reserve" unless the determination has been made that the mineralization could be economically and legally produced or extracted at the time the reserve determination is made. Under Industry Guide 7 standards, a "final" or "bankable" feasibility study is required to report reserves, the three-year historical average price is used in any reserve or cash flow analysis to designate reserves and the primary environmental analysis or report must be filed with the appropriate governmental authority.

The terms "mineral resource," "measured mineral resource," "indicated mineral resource" and "inferred mineral resource" used in the Company's disclosure are Canadian mining terms that are defined in accordance with NI 43-101 under the guidelines set out in the CIM Standards; however, these terms are not defined terms under Industry Guide 7 and are normally not permitted to be used in reports and registration statements filed with the SEC. Investors are cautioned not to assume that any part or all of mineral deposits in these categories will ever be converted into reserves. "Inferred mineral resources" have a great amount of uncertainty as to their existence, and great 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 pre-feasibility studies, except in rare cases. Investors are cautioned not to assume that all or any part of an inferred mineral resource exists or is economically or legally mineable. Disclosure of "contained ounces" in a resource is permitted disclosure under Canadian regulations; however, the SEC normally only permits issuers to report mineralization that does not constitute "reserves" by Industry Guide 7 standards as in place tonnage and grade without reference to unit measures.

Accordingly, information contained in this annual report on Form 40-F and the documents incorporated by reference herein containing descriptions of the Company's mineral deposits may not be comparable to similar information made public by U.S. companies subject to the reporting and disclosure requirements under the United States federal securities laws and the rules and regulations thereunder.

PRINCIPAL DOCUMENTS

The following documents have been filed as part of this annual report on Form 40-F as Exhibits hereto:

A. Annual Information Form

The Annual Information Form of Fortuna Silver Mines Inc. for the year ended December 31, 2012, is included as Exhibit 99.1 of this annual report on Form 40-F.

B. Audited Annual Financial Statements

The Company's audited consolidated financial statements for the years ended December 31, 2012 and December 31, 2011, including the auditor's report with respect thereto, are included as Exhibit 99.2 of this annual report on Form 40-F.

C. Management's Discussion and Analysis

The Company's Management's Discussion and Analysis for the year ended December 31, 2012 is included as Exhibit 99.3 of this annual report on Form 40-F.

TAX MATTERS

Purchasing, holding, or disposing of securities of the Company may have tax consequences under the laws of the United States and Canada that are not described in this annual report on Form 40-F.

DISCLOSURE REGARDING CONTROLS AND PROCEDURES

Disclosure Controls and Procedures.

Disclosure controls and procedures are designed to ensure that information required to be disclosed in the Company's annual filings and interim filings and other reports filed or submitted under the Exchange Act is duly recorded, processed, summarized and reported, within the time periods specified in SEC rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in the Company's reports is accumulated and communicated to management, including the Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") as appropriate, to allow timely decisions regarding required disclosure.

As required by Rule 13a-15(e) under the Exchange Act, the Company evaluated, with the participation of its CEO and CFO, the effectiveness of its disclosure controls and procedures as of December 31, 2012. Based on that evaluation, the CEO and the CFO have concluded that, as of the end of the period covered by this annual report on Form 40-F, the disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed in the Company's annual filings and interim filings and other reports filed or submitted under the Exchange Act, is recorded, processed, summarized and reported within time periods specified in SEC rules and forms and is accumulated and communicated to management, including the CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

Notwithstanding the foregoing, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that the Company's disclosure controls and procedures will detect or uncover every situation involving the failure of persons within the Company and its subsidiaries to disclose material information otherwise required to be set forth in the Company's periodic reports. The Company's disclosure controls and procedures are designed to provide reasonable assurance of achieving their objective of ensuring that information required to be disclosed in the reports that the Company files or submits under the Exchange Act is communicated to management to allow timely decisions regarding required disclosure.

Management's Annual Report on Internal Controls Over Financial Reporting.

Management is responsible for establishing and maintaining adequate internal controls over financial reporting and has designed such internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and preparation of financial statements for external purposes in accordance with IFRS.

In designing and evaluating the Company's internal controls over financial reporting, the Company's management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its reasonable judgment in evaluating the cost-benefit relationship of possible controls and procedures. Because of its inherent limitations, internal controls over financial reporting may not prevent or detect misstatements.

Management assessed the effectiveness of the Company's internal controls over financial reporting as of December 31, 2012. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in *Internal Control - Integrated Framework*. Based on this assessment, management believes that, as of December 31, 2012, the Company's internal controls over financial reporting were effective based on those criteria.

Attestation Report of the Registered Public Accounting Firm. This annual report on Form 40-F does not include an attestation report of the Company's registered public accounting firm because the Company is exempt from such requirement due its status as an "emerging growth company" under the Jumpstart Our Business Startups Act.

Changes in Internal Controls Over Financial Reporting. During the fiscal year ended December 31, 2012, there were no changes in the Registrant's internal controls over financial reporting that have materially affected, or are reasonably likely to materially affect, the Registrant's internal controls over financial reporting.

NOTICES PURSUANT TO REGULATION BTR

None.

IDENTIFICATION OF THE AUDIT COMMITTEE

The Registrant has a separately-designated standing audit committee established in accordance with Section 3(a)(58)(A) of the Exchange Act. The members of the audit committee are: Messrs. Robert Gilmore, Tomas Guerrero and Thomas Kelly.

AUDIT COMMITTEE FINANCIAL EXPERT

The board of directors of the Registrant has determined that Robert Gilmore, a member of the Registrant's audit committee, qualifies as an audit committee financial expert for purposes of paragraph (8) of General Instruction B to Form 40-F. The board of directors has further determined that each of Messrs. Robert Gilmore, Tomas Guerrero and Thomas Kelly is independent, as that term is defined in the Listed Company Manual of the New York Stock Exchange. The SEC has indicated that the designation of Robert Gilmore as an audit committee financial expert does not make him an "expert" for any purpose, impose any duties, obligations or liabilities on him that are greater than those imposed on members of the audit committee and the board of directors who do not carry this designation or affect the duties, obligations or liabilities of any other member of the audit committee or the board of directors.

CODE OF ETHICS

The Registrant has adopted a "code of ethics" (as that term is defined in Form 40-F), entitled the "Code of Business Conduct and Ethics and Whistle-Blower Policy", that applies to all of its directors, officers, employees, and consultants including its principal executive officer, principal financial officer, principal accounting officer or controller, and persons performing similar functions.

The Code of Business Conduct and Ethics and Whistle-Blower Policy is available for viewing on the Registrant's website at www.fortunasilver.com under "About Fortuna / Corporate Governance".

PRINCIPAL ACCOUNTANT FEES AND SERVICES

Deloitte LLP served as the Company's auditing firm for the fiscal years ended December 31, 2012 and 2011. Aggregate fees (in Canadian dollars) billed to the Company for professional services rendered by Deloitte LLP during the fiscal years ended December 31, 2012 and 2011 are as follows:

	2012	2011
Audit Fees	$374,848	$310,450
Audit-Related Fees	Nil	$ 64,200
Tax Fees	$147,721	$ 98,665
All Other Fees	$ 5,051	$ 15,000
	$527,620	$488,315

"Audit Fees" are the aggregate fees billed for the audit of the Company's consolidated annual financial statements, and for independent

accountant review of the interim financial statements and management discussion and analysis.

“Audit-Related Fees” are fees charged for assurance and related services that are reasonably related to the performance of the audit or review of the Company’s financial statements and are not reported under “Audit Fees”. This category comprises fees billed for reviews associated with the Company’s U.S. filings and its public financing by way of short-form prospectus.

“Tax Fees” are fees for professional services rendered for tax compliance and tax advice on actual or contemplated transactions.

“All Other Fees” are for amounts billed in 2011 for providing IFRS transition assistance, and amounts billed in 2012 for preliminary review of internal controls over financing reporting.

PRE-APPROVAL POLICIES AND PROCEDURES

The auditors of the Company obtain, as necessary, the pre-approval of the Audit Committee for any anticipated additional services required of the auditors for the coming fiscal year. If other service requirements arise during the year, the Audit Committee will pre-approve such services at that time, prior to the commencement of such services. Of the total aggregate fees paid by the Company to its auditors during the fiscal year ended December 31, 2012, $nil or 0% of the fees were approved by the Audit Committee pursuant to the de minimus exception provided by Section (c)(7)(i)(C) of Rule 2-01 of Regulation S-X.

OFF-BALANCE SHEET ARRANGEMENTS

The required disclosure is included in Notes 18(d) and 24 of the Registrant’s audited consolidated financial statements for the fiscal years ended December 31, 2012 and 2011, filed as part of this annual report on Form 40-F in Exhibit 99.2.

TABULAR DISCLOSURE OF CONTRACTUAL OBLIGATIONS

The required disclosure is included under the heading “Contractual Obligations” of the Registrant’s Management’s Discussion and Analysis for the fiscal year ended December 31, 2012, filed as part of this annual report on Form 40-F in Exhibit 99.3.

MINE SAFETY DISCLOSURE

Pursuant to Section 1503(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, issuers that are operators, or that have a subsidiary that is an operator, of a coal or other mine are required to disclose in their periodic reports filed with the SEC information regarding specified health and safety violations, orders and citations, related assessments and legal actions, and mining-related fatalities. For information regarding the Company’s mine safety disclosures, see “Mine Safety Disclosure” filed as Exhibit 99.5 to this annual report on Form 40-F.

NYSE CORPORATE GOVERNANCE

The Company’s common shares are listed on the NYSE. Sections 103.00 and 303A.11 of the NYSE Listed Company Manual permit foreign private issuers to follow home country practices in lieu of certain provisions of the NYSE Listed Company Manual. A foreign private issuer that follows home country practices in lieu of certain provision of the NYSE Listed Company Manual must disclose any significant ways in which its corporate governance practices differ from those followed by domestic companies either on its website or in the annual report that it distributes to shareholders in the United States. A description of the significant ways in which the Company’s governance practices differ from those followed by domestic companies pursuant to NYSE standards is as follows:

Shareholder Meeting Quorum Requirement: The NYSE is of the opinion that the quorum required for any meeting of shareholders should be sufficiently high to insure a representative vote. A quorum for a meeting of members of the Company is two persons who are, or who represent by proxy, shareholders who, in the aggregate, hold at least 5% of the shares entitled to be voted at the meeting.

Proxy Delivery Requirement: The NYSE requires the solicitation of proxies and delivery of proxy statements for all shareholder meetings, and requires that these proxies shall be solicited pursuant to a proxy statement that conforms to SEC proxy rules. The Company is a “foreign private issuer” as defined in Rule 3b-4 under the Exchange Act, and the equity securities of the Company are accordingly exempt from the proxy rules set forth in Sections 14(a), 14(b), 14(c) and 14(f) of the Exchange Act. The Company solicits proxies in accordance with applicable rules and regulations in Canada.

Shareholder Approval Requirement: The Company will follow Toronto Stock Exchange rules for shareholder approval of new issuances of its common shares. Following Toronto Stock Exchange rules, shareholder approval is required for certain issuances of shares that: (i) materially affect control of the Company; or (ii) provide consideration to insiders in aggregate of 10% or greater of the market capitalization of the listed issuer and have not been negotiated at arm's length. Shareholder approval is also required, pursuant to Toronto Stock Exchange rules, in the case of private placements: (a) for an aggregate number of listed securities issuable greater than 25% of the number of securities of the listed issuer which are outstanding, on a non-diluted basis, prior to the date of closing of the transaction if the price per security is less than the market price; or (b) that during any six month period are to insiders for listed securities or options, rights or other entitlements to listed securities greater than 10% of the number of securities of the listed issuer which are outstanding, on a non-diluted basis, prior to the date of the closing of the first private placement to an insider during the six month period.

The foregoing are consistent with the laws, customs and practices in Canada.

UNDERTAKING

Registrant undertakes to make available, in person or by telephone, representatives to respond to inquiries made by the SEC staff, and to furnish promptly, when requested to do so by the SEC staff, information relating to: the securities registered pursuant to Form 40-F; the securities in relation to which the obligation to file an annual report on Form 40-F arises; or transactions in said securities.

CONSENT TO SERVICE OF PROCESS

Form F-X signed by the Registrant and its agent for service of process has been filed with the SEC together with Registrant's Registration Statement on Form 40-F (001-35297) in connection with its securities registered on such form.

Any changes to the name or address of the agent for service of process of the Registrant shall be communicated promptly to the SEC by an amendment to the Form F-X referencing the file number of the Registrant.

SIGNATURE

Pursuant to the requirements of the Exchange Act, the Registrant certifies that it meets all of the requirements for filing on Form 40-F and has duly caused this annual report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: April 1, 2013

FORTUNA SILVER MINES INC.

By: *"Jorge Ganoza Durant"*

Name: Jorge Ganoza Durant
Title: President, Chief Executive Officer & Director

EXHIBIT INDEX

Exhibit	Description
99.1	Annual Information Form for the year ended December 31, 2012.
99.2	Audited consolidated financial statements for the years ended December 31, 2012 and December 31, 2011, including the auditor's report with respect thereto
99.3	Management's Discussion and Analysis for the year ended December 31, 2012
99.4	Consent of Deloitte LLP
99.5	Mine Safety Report
99.6	Consent of Eric N. Chapman
99.7	Consent of Thomas Kelly
99.8	Consent of Thomas Vehrs
99.9	Certification of Chief Executive Officer pursuant to Section 302 of the *Sarbanes-Oxley Act of 2002*
99.10	Certification of Chief Financial Officer pursuant to Section 302 of the *Sarbanes-Oxley Act of 2002*
99.11	Certification of Chief Executive Officer pursuant to Section 906 of the *Sarbanes-Oxley Act of 2002*
99.12	Certification of Chief Financial Officer pursuant to Section 906 of the *Sarbanes-Oxley Act of 2002*



FORTUNA
SILVER MINES INC.

ANNUAL INFORMATION FORM

For the Fiscal Year Ended December 31, 2012

DATED: March 27, 2013

CORPORATE OFFICE:

Suite 650, 200 Burrard Street
Vancouver, BC V6C 3L6, Canada
Tel: 604.484.4085
Fax: 604.484.4029

MANAGEMENT HEAD OFFICE:

Piso 5, Av. Jorge Chávez #154
Miraflores, Lima, Peru
Tel: 511.616.6060, ext. 2

TABLE OF CONTENTS

PRELIMINARY NOTES 1
- Cautionary Statement – Forward Looking Statements 1
- Cautionary Note to U.S. Investors Concerning Resource and Reserve Estimates 2
- Documents Incorporated by Reference 2
- Date of Information 3
- Currency 3

CORPORATE STRUCTURE 3
- Name, Address and Incorporation 3
- Intercorporate Relationships 4

GENERAL DEVELOPMENT OF THE BUSINESS 4
- Three-Year History and Recent Developments 4

DESCRIPTION OF THE BUSINESS 7
- General 7
- Risk Factors 8
- Material Mineral Properties 13

Caylloma Mine, Peru 13
San Jose Mine, Mexico 16

DIVIDENDS 19

DESCRIPTION OF CAPITAL STRUCTURE 19

MARKET FOR SECURITIES 19
Trading Price and Volume 20

DIRECTORS AND EXECUTIVE OFFICERS 20
Name, Occupation and Shareholding 20
Cease Trade Orders or Bankruptcies 22
Penalties or Sanctions 22
Conflicts of Interest 23

AUDIT COMMITTEE 23

LEGAL PROCEEDINGS 24

TRANSFER AGENT AND REGISTRAR 24

MATERIAL CONTRACTS 24

INTERESTS OF EXPERTS 24
Names of Experts 24
Interests of Experts 25

ADDITIONAL INFORMATION 25

Audit Committee Charter **Schedule "A"**

PRELIMINARY NOTES

Cautionary Statement – Forward Looking Statements

Certain statements and information in this Annual Information Form are not based on historical facts and constitute forward-looking statements or forward looking information within the meaning of applicable securities laws ("forward-looking statements"), including but not limited to, the Company's plans at its San Jose mine, Mexico and Caylloma mine, Peru, estimated production, capital and operating cash flow estimates and other matters.

Forward-looking statements express or involve discussions with respect to predictions, expectations, beliefs, plans, projections, objectives, assumptions or future events or performance (often, but not always, identified using words or phrases such as "expects", "is expected", "anticipates", "believes", "plans", "projects", "estimates", "assumes", "intends", "strategies", "targets", "goals", "forecasts", "objectives", "budgets", "schedules", "potential" or variations thereof or stating that certain actions, events or results "may", "could", "would", "might" or "will" be taken, occur or be achieved, or the negative of any of these terms and similar expressions) and are not statements of historical fact. Forward-looking statements relate to, among other things:

- mineral "reserves" and "resources" as they involve the implied assessment, based on estimates and assumptions that the reserves and resources described exist in the quantities predicted or estimated and can be profitably produced in the future;
- production rates at the Company's properties;
- cash cost estimates;
- timing to achieve full production capacity at the Company's properties;
- timing for completion of infrastructure upgrades related to the Company's properties and their completion on budget;
- timing for delivery of materials and equipment for the Company's properties; and
- the sufficiency of the Company's cash position, its reliance on revenue from its currently operating properties, and its ability to raise equity capital or access debt facilities.

Forward-looking statements are necessarily based upon a number of estimates and assumptions that, while considered reasonable by the Company as at the date of such statements, are inherently subject to significant business, economic, social, political and competitive uncertainties and contingencies and other factors that could cause actual results or events to differ materially from those projected in the forward-looking statements. The estimates and assumptions of the Company contained or incorporated by reference in this Annual Information Form ("AIF") which may prove to be incorrect, include, but are not limited to:

- that all required third party contractual, regulatory and governmental approvals will be obtained for the development, construction and production of its properties,
- there being no significant disruptions affecting operations, whether due to labor disruptions, supply disruptions, power disruptions, damage to equipment or otherwise;
- permitting, development, expansion and power supply proceeding on a basis consistent with the Company's current expectations;

- currency exchange rates being approximately consistent with current levels;
- certain price assumptions for silver, gold, lead, zinc and copper;
- prices for and availability of natural gas, fuel oil, electricity, parts and equipment and other key supplies remaining consistent with current levels;
- production forecasts meeting expectations;
- the accuracy of the Company's current mineral resource and reserve estimates;
- labor and materials costs increasing on a basis consistent with the Company's current expectations; and
- assumptions made and judgments used in engineering and geological interpretation.

In addition, there are known and unknown risk factors which could cause the Company's actual results, performance or achievements to differ materially from any future results, performance or achievements expressed or implied by the forward-looking statements. Known risk factors include, risks associated with project development; the need for additional financing; operational risks associated with mining and mineral processing; changes in national and local government legislation, taxation, controls, regulations and political or economic developments in Canada, Mexico, the United States, Peru or other countries in which the Company does or may carry on business; the possibility of cost overruns or unanticipated expenses; fluctuations in silver, lead, zinc and copper prices; title matters; uncertainties and risks related to carrying on business in foreign countries; environmental liability claims and insurance; reliance on key personnel; currency exchange rate fluctuations; competition; and other risks and uncertainties, including those described in the "Risks and Uncertainties" section in the "Risk Factors" section of this AIF and the Company's Management's Discussion and Analysis for the year ended December 31, 2012, available at www.sedar.com and www.edgar.gov.

Although the Company has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in forward-looking statements, there may be other factors that cause actions, events or results not to be as anticipated, estimated or intended. These forward-looking statements are made as of the date of this IAIF. There can be no assurance that forward looking statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, readers are cautioned not to place undue reliance on forward-looking statements. Except as required by law, the Company does not assume the obligation to revise or update these forward looking statements after the date of this document or to revise them to reflect the occurrence of future unanticipated events.

Cautionary Note to U.S. Investors Concerning Resource and Reserve Estimates

The terms "mineral reserve," "proven mineral reserve" and "probable mineral reserve" used in the Company's disclosure are Canadian mining terms that are defined in accordance with National Instrument 43-101 – Standards of Disclosure for Mineral Projects ("NI 43-101") under the guidelines set out in the Canadian Institute of Mining, Metallurgy and Petroleum (the "CIM") Best Practice Guidelines for the Estimation of Mineral Resource and Mineral Reserves (the "CIM Standards"), adopted by the CIM Council on November 23, 2003. These definitions differ from the definitions in the United States Securities and Exchange Commission (the "SEC") Industry Guide 7 under the Securities Act. Under Industry Guide 7 standards, mineralization may not be classified as a "reserve" unless the determination has been made that the mineralization could be economically and legally produced or extracted at the time the reserve determination is made. Under Industry Guide 7 standards, a "final" or "bankable" feasibility study is required to report reserves, the three-year historical average price is used in any reserve or cash flow analysis to designate reserves and the primary environmental analysis or report must be filed with the appropriate governmental authority.

The terms "mineral resource," "measured mineral resource," "indicated mineral resource" and "inferred mineral resource" used in the Company's disclosure are Canadian mining terms that are defined in accordance with NI 43-101 under the guidelines set out in the CIM Standards; however, these terms are not defined terms under Industry Guide 7 and are normally not permitted to be used in reports and registration statements filed with the SEC. Investors are cautioned not to assume that any part or all of mineral deposits in these categories will ever be converted into reserves. "Inferred mineral resources" have a great amount of uncertainty as to their existence, and great 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 pre-feasibility studies, except in rare cases. Investors are cautioned not to assume that all or any part of an inferred mineral resource exists or is economically or legally mineable. Disclosure of "contained ounces" in a resource is permitted disclosure under Canadian regulations; however, the SEC normally only permits issuers to report mineralization that does not constitute "reserves" by Industry Guide 7 standards as in place tonnage and grade without reference to unit measures.

Documents Incorporated by Reference

The information provided in this AIF is supplemented by disclosure contained in the documents listed below which are incorporated by reference into this AIF. These documents must be read together with the AIF in order to provide full, true and plain disclosure of all material facts relating to Fortuna Silver Mines Inc. (referred to herein as the "Company" or "Fortuna"). The documents listed below are not contained within or attached to this document. The documents may be accessed on SEDAR at www.sedar.com under the Company's profile, Fortuna Silver Mines Inc.:

Document	Effective Date / Period Ended	Date Filed on SEDAR website	Document Category on the SEDAR website
Management Information Circular	April 23, 2012	May 9, 2012	Management Proxy / Information Circular - English
Technical Report, Caylloma Property, Peru	March 22, 2013	March 26, 2013	Technical Report(s)
Technical Report, San Jose Property, Mexico	March 22, 2013	March 26, 2013	Technical Report(s)

Date of Information

This AIF is dated March 27, 2013. Except as otherwise indicated, the information contained herein is as at December 31, 2012, being the date of the Company's most recently completed financial year end.

Currency

Unless otherwise noted, all references to "$" in this AIF refer to United States dollars.

CORPORATE STRUCTURE

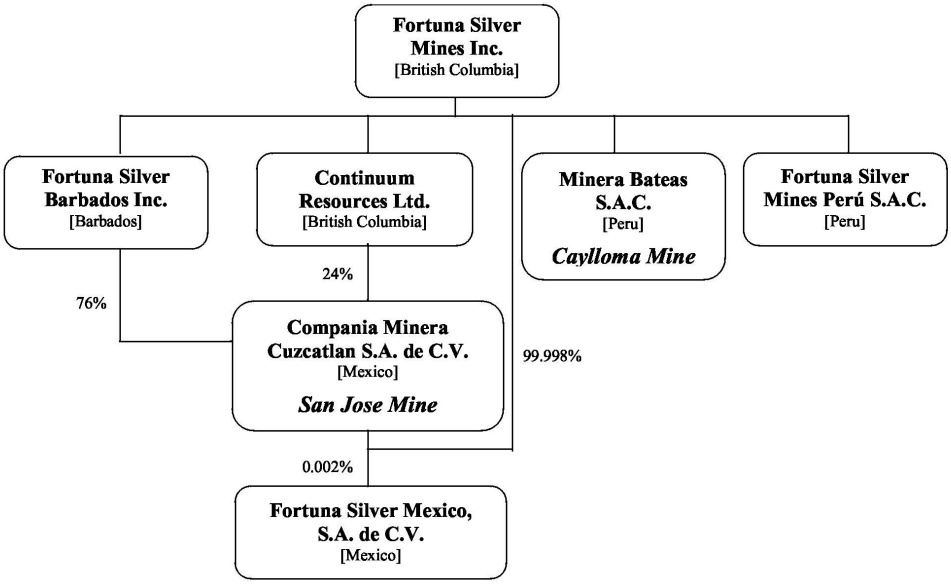
Name, Address and Incorporation

The Company was incorporated on September 4, 1990 under the laws of the Province of British Columbia under the name Jopec Resources Ltd. On February 3, 1999, the Company changed its name to Fortuna Ventures Inc. and on June 28, 2005 to Fortuna Silver Mines Inc.

The management head office of the Company is located at Piso 5, Av. Jorge Chávez #154, Miraflores, Lima, Peru. The corporate and registered office of the Company is located at 200 Burrard Street, Suite 650, Vancouver, BC V6C 3L6.

Intercorporate Relationships

The Company carries on a significant portion of its business through a number of 100%-owned subsidiaries, held either directly or indirectly, as follows:



GENERAL DEVELOPMENT OF THE BUSINESS

Three-Year History and Recent Developments

Caylloma Mine, Peru

The Company purchased in 2005 a 100% interest in the Caylloma mine and related mining concessions located in southern Peru. Following a significant upgrading and modernization of the ore processing plant, the Company returned the mine to production in October 2006. In 2009, the Company commissioned an expansion project that increased in plant capacity to 1,200 tonnes per day ("tpd") and added a copper circuit which started commercial production in December 2009. In 2010, the mine and plant operated at an average rate of 1,231 tpd, with production sourced primarily from the Animas Vein, and produced 1,906,423 ounces of silver at a cash cost of negative $5.99 per ounce, net of by-product credits.

In February 2010, the Company announced the discovery of high-grade silver mineralization in the upper portion of the Animas Vein. This traditionally polymetallic vein was then the source of 85% of the mine's ore production. The main focus of development of the Animas Vein in 2010 was to extend mineralization along strike towards the northeast on levels 10 and 12 and to prepare the resource blocks between levels 10 and 12 for mining, which was planned to extend below level 10 in 2011. In the upper part of Animas, development and preparation was focused on incorporating level 6 into the production plan.

In December 2010, the Company confirmed the discovery of two new high-grade silver ore shoots in the Bateas Vein, located in the central portion of the Caylloma property. Historically, the Bateas Vein was a significant producer of high-grade silver ore, with the past production coming from portions of the Bateas Vein located to the southwest of the newly discovered ore shoots. From these ore shoots along strike to the northeast, the Bateas Vein is open and essentially unexplored over a horizontal distance of approximately 1,150 meters where the Vein is projected to intersect with the San Cristobal Vein.

Production from the new ore shoots began in late June 2011. Exploration drifting towards the northeast area of the Bateas Vein was stopped in September in order to improve ventilation and infrastructure for auxiliary services in levels 10 and 12.

In 2011, the processing plant operated at an average rate of 1,264 tpd and silver production increased 5% year-over-year to 2,008,488 ounces. In January 2011, production of copper-silver concentrate was discontinued at Caylloma due to a material increase in treatment and refining smelter charges. Cash cost per ounce of silver, net of by-product credits, increased to negative $0.78 in 2011, with costs rising from negative $5.93 in Q1 to positive $6.48 in Q4. The increase was driven by cost increases and lower by-product credits in the second half of 2011, particularly in the fourth quarter. The decrease in by-product credits was primarily due to lower base metal prices (down 24% for lead and 21% for zinc) and a 13% decline in lead production. The unit cash cost per tonne increase reflects higher cost of skilled labor and industry related services, a trend common in the Peruvian underground mining industry since late 2010.

In 2012, despite higher ore production (up 3%) and silver head grades (up 4%), silver production at Caylloma increased just 1% year over year primarily because of a 5% decrease in metallurgical recoveries. Metallurgical recoveries were affected by the oxide content of ore mined in level 6 of the Animas Vein, which contributed 30% of ore production during the year. In fourth quarter of 2012, after extensive testing, the Company implemented recommendations to improve metallurgical recoveries. Positive results were achieved in November and December, with silver recoveries improving to 80%, and expected to reach 82% in 2013. Lower lead and zinc head grades and recoveries resulted in a year-over-year reduction in lead and zinc production of 9% and 4%, respectively.

Cash cost per tonne of processed ore at Caylloma for 2012 was $87.28, an increase of 26% from 2011, but only 1% higher than forecast. The increase resulted mainly from higher contractor tariffs and labor costs. Cash cost per payable ounce of silver for 2012 was $8.07, net of by-product credits, compared to negative $0.78 in the prior year.

Several cost containment initiatives were or are being implemented to help offset cost pressures. These relate mainly to changes in mining methods of narrow high-grade veins that will result in less mine preparation, the concentration of operations under a single contractor, ceasing production at peripheral veins, and the ongoing energy project to increase access to energy from the power grid.

Capital expenditures at Caylloma were $16.8 million in 2012, compared to $25.0 million budgeted for the year. The lower expenditures were due mainly to reducing the scope of and postponing refurbishment of the processing plant, postponing until 2013 the energy project, and delaying moderately the mine camp project. The new tailings facility was commissioned in January 2013.

The Company plans to direct an estimated $50.7 million in capital expenditures in 2013 to mine development, camp infrastructure, tailings dam expansion, and power grid upgrades.

The 2013 exploration program at Caylloma includes 31,000 meters of drilling primarily focused on resource delineation and exploration of silver- and gold-rich veins in the northern portion of the Caylloma property.

San Jose Mine, Mexico

Located in the state of Oaxaca in southern Mexico, the San Jose property covers a high-grade silver-gold bearing epithermal vein system. In late 2006, the Company acquired a 76% interest in the property, with Continuum Resources Ltd. owning the remaining 24%. In March 2009, the Company acquired all of the issued and outstanding shares of Continuum in exchange for 6,786,706 common shares of the company, and in so doing increased its ownership of San Jose to a 100% interest.

In December 2009, the Mexican Environmental Agency approved the Company's application for a change of land use from agricultural to industrial for the property. This was the final permit required to commence construction of a mine at San Jose and complemented the environmental impact study that was approved by the Mexican Environmental Agency in October 2009. By April 2010, the Company had completed a pre-feasibility study for the project and started construction activities.

Commercial production of the San Jose mine commenced on September 1, 2011 at an initial rate of 1,000 tpd, and the Company announced plans to increase production capacity from 1,000 tpd to 1,500 tpd. In 2011, the mine produced 490,555 ounces of silver and 4,622 ounces of gold at a cash cost of $4.69 per silver equivalent ounce, net of by-product credits. .

In 2012, San Jose completed its first full year of operation, producing 1,949,178 ounces of silver and 17,918 ounces of gold. This was 15% and 19%, respectively, above annual production guidance. The increased production resulted from mining higher grade ore ahead of schedule on level 1350, which contributed approximately 47% of mined ore, which was 160% above plan. By accelerating completion of the main access ramp and preparing levels 1350 and 1300 ahead of plan, the Company added operational flexibility to the mine that will help to sustain production in the face of potential ore variability and to secure the ramp-up of production to 1,500 tpd by the third quarter of 2013. Mine preparation peaked in Q4 2012 at 1,127 meters of underground development, compared to 614 meters, on average, during the first three quarters of the year. In Q4 2012, silver and gold head grades decreased compared to the first nine months of 2012 because of higher production of lower grade development ore from level 1300.

The San Jose processing plant performed within design parameters during 2012, with silver and gold recoveries of 88% and 87%, respectively, and average ore throughput of 1,055 tpd. Cash cost per tonne of processed ore for 2012 was $74.10, or 6% above forecast as a result of accelerated mine preparation in the fourth quarter and certain non-recurring items. Cash cost per payable ounce of silver for 2012 was $3.76, net of by-product credits.

In October 2012, the Company, working in collaboration with state and community authorities, completed construction of a thirteen kilometer water pipeline, connecting the Ocotlan water treatment plant with the San Jose mine site. The pipeline is delivering approximately 20% of the make-up water currently required for the San Jose mill.

Capital expenditures at San Jose in 2012 were $14.3 million, which is lower than the $30.8 million budgeted mainly due to the postponement of the dore plant project. The Company plans major capital expenditures during 2013 totalling $52.7 million for mine development, plant expansion, and tailings dam expansion.

The Company is conducting exploration drilling at San Jose to follow up on mineralized intercepts encountered in 2012. The 2013 exploration program includes 20,000 meters of drilling, with the principal targets located in the northern and southern extension of the Trinidad vein system. Additional drilling is planned on other targets identified on the 64,400 hectare property.

Updated Reserve and Resource Estimates

In March 2013, the Company released updated Mineral Reserve and Mineral Resource estimates for Caylloma and San Jose, as set forth in the Caylloma Report and the San Jose Report described below under "Description of the Business - Material Mineral Properties".

Financing

In 2010, the Company entered into a credit agreement with the Bank of Nova Scotia for a $20 million senior secured revolving credit facility. The proceeds of the facility may be used for general corporate purposes, including the development of the San Jose Project. The facility was intended to complement the Company's cash position and provide additional financing flexibility during the construction stage at San Jose. An increase of the credit facility to $40 million is expected to be completed in the first week of April 2013. No funds have been drawn under this facility.

On March 3, 2010, the Company completed a bought-deal public financing with a syndicate of underwriters co-led by CIBC and Canaccord Financial Ltd. pursuant to which the Company issued 15,007,500 common shares at a price of CAD$2.30 per share, for gross proceeds of CAD$34.5 million. Net proceeds were CAD$32.8 million after underwriting fees of CAD$1.7 million. The net proceeds from the financing were used to partially fund the mine construction at San Jose.

On December 23, 2010, the Company completed a second bought-deal financing with a syndicate of underwriters led by Canaccord Genuity Corp. pursuant to which the Company issued 11,500,000 common shares at a price of CAD$4.00 per share, for gross proceeds of CAD$46.0 million. Net proceeds were CAD$43.7 million after underwriting fees of CAD$2.3 million. The net proceeds from the financing were used to partially fund the mine construction as San Jose, to conduct exploration programs in Mexico and Peru and for general working capital.

TSX Listing

The Company graduated from the TSX Venture Exchange to the TSX and its common shares began trading on the TSX on January 18, 2010 under the symbol FVI.

NYSE Listing

The Company completed a listing application on the New York Stock Exchange and its common shares began trading on the NYSE on September 19, 2011 under the symbol FSM.

DESCRIPTION OF THE BUSINESS

General

Summary. The Company is engaged in silver and gold mining and related activities, including exploration, extraction, and processing. The Company operates the Caylloma mine in Peru and the San Jose mine in Mexico.

The lead-silver, zinc, and gold-silver concentrates produced by the Company at its Caylloma mine in Peru and its San Jose mine in Mexico are sold to international metals traders who in turn deliver the products to different clients around the world. The material sources of revenue for 2012 and 2011 are as follows:

By type of concentrate	2012	2011
· Lead-silver concentrate	42%	75%
· Zinc concentrate	9%	14%
· Gold-silver concentrate	49%	11%
By metal contained in concentrate:		
· Silver	67%	65%
· Lead	7%	15%
· Zinc	9%	14%
· Gold	17%	6%

The method of production both at Caylloma and San Jose consists of underground mining principally through cut and fill mechanized operations. Extracted ore is trucked to a conventional crushing, milling and flotation processing plant which consists of zinc, and lead-silver flotation circuits for Caylloma, and a gold-silver circuit for San Jose.

Specialized Skill and Knowledge. All aspects of the Company's business require specialized skills and knowledge. Such skills and knowledge include the areas of geology, mining, metallurgy, engineering, environment issues, permitting, social issues, and accounting. While increased activity in the resource mining industry has made it more difficult to locate and retain competent employees in such fields, the Company has been successful in finding and retaining personnel for the majority of its key processes.

Competitive Conditions. The Company competes with other mining companies, some of which have greater financial resources and technical facilities, for the acquisition of mineral property interests, as well as for the recruitment and retention of qualified employees.

Environmental Protection. The Company is currently in compliance with all material environmental regulations applicable to its exploration, development, construction and operating activities. The financial and operational effects of environmental protection requirements on capital expenditures, earnings and expenditures during the fiscal year ended December 31, 2012 were not material. The Company has recorded in its financial statements for the year 2012 an asset retirement obligation which reflects its environmental obligations associated with the Caylloma mine closure plan as approved by the Peruvian government and an updated closure plan for the San Jose mine.

Employees. The Company and its subsidiaries have 812 direct employees and 1,215 indirect employees through contractors.

Foreign Operations. The Company's material mineral resource properties are located in Peru and Mexico, each of which has a stable government, a mature mining industry and regulatory environment, and a non-volatile currency.

Health and Safety, Social and Environmental Policies . The Company is committed to maintaining the health and safety of its personnel by

minimizing hazards and providing training and safe equipment. A strong safety culture is encouraged so that all employees are empowered to report and address safety issues.

The Company has built strong relationships with the communities in which it operates, and is dedicated to innovative, sustainable projects and partnerships that build company engagement in local communities while respecting their values, customs and traditions.

The Company is committed to complying in all material respects with all environmental laws and regulations applicable to its activities. It interacts proactively with authorities and communicates openly about its activities. The Company works directly and collaboratively with local communities to protect and preserve the environment.

Risk Factors

The Company's ability to generate revenues and profits from its natural resource properties is subject to a number of risks and uncertainties including, without limitation, the following:

Risks Related to the Caylloma and San Jose Mines

Operating hazards and risks. Mining operations generally involve a high degree of risk, which even a combination of experience, knowledge and careful evaluation may not be able to overcome. Hazards such as unusual or unexpected formations and other conditions can occur. Operations in which the Company has a direct or indirect interest will be subject to all the hazards and risks normally incidental to exploration, development and production of precious and base metals, any of which could result in work stoppages, damage to or destruction of mines and other producing facilities, damage to life and property, environmental damage and possible legal liability for any or all damages. The Company may become subject to liability for pollution, cave-ins or hazards against which it cannot insure or against which it may elect not to insure. Any compensation for such liabilities may have a material, adverse effect on the Company's financial position.

Concentrate treatment charges and transportation costs. The Company has entered into agreements to sell its concentrate production from the Caylloma and San Jose Mines for 2013. Smelting and refining rates correspond to contract rates established mainly at 2012 year end. There is no assurance that the Company will be able to enter into smelting and refining contracts at similar competitive terms beyond 2013. The cost of transporting concentrate from the Mines to the smelters is dependent on, among other things, the concentrate destination. Transportation related costs have been volatile over the last several years and could continue to be volatile due to a number of factors, including changes in the price of oil, or a shortage in the number of vessels available to ship concentrate to smelters. Increases in these rates would have an adverse impact on the Company's results of operations and financial condition.

Risks Relating to the Company

Capital and operating costs, production schedules, and economic returns. The Company's expected operating costs and expenditures, production schedules, economic returns and other projections from a mining project which are contained in this document and in any technical reports, scoping studies, pre-feasibility studies and feasibility studies prepared for or by the Company are based on assumed or estimated future metals prices, cut-off grades, operating costs, capital costs, and expenditures and other factors any of which may prove to be inaccurate. Therefore, feasibility studies and other studies and reports may prove to be unreliable.

The Company's operating costs are affected by the cost of commodities and goods such as steel, fuel, electrical power and supplies, including reagents. Management prepares its cost and production guidance and other forecasts based on its review of current and estimated future costs, and assumes that the materials and supplies required for operations will be available for purchase. As the Company relies on certain third-party suppliers and contractors, these factors can be outside our control and an increase in the costs of, or a lack of availability of, commodities and goods may have an adverse impact on the Company's financial condition.

General economic conditions. Turmoil in global financial markets in recent years has had a profound impact on the global economy. Many industries, including the precious and base metals mining industry, have been impacted by these market conditions. Some of the key impacts have included contraction in credit markets resulting in a widening of credit risk, devaluations and high volatility in global equity, commodity, foreign exchange and precious metal markets, and a lack of market liquidity. The sovereign debt crisis in Europe has been the most visible risk to world financial stability. A continued or worsened slowdown in economic conditions, including but not limited to, consumer spending, employment rates, business conditions, inflation, fuel and energy costs, consumer debt levels, lack of available credit, the state of the financial markets, interest rates, and tax rates may adversely affect the Company's growth and profitability. Specifically:

- Under a worst case scenario a new global credit/liquidity crisis could impact the cost and availability of financing and the Company's overall market liquidity;
- the volatility of metal prices could impact the Company's revenues, profits, losses and cash flow;
- volatile energy prices, commodity and consumables prices and currency exchange rates could impact the Company's production costs; and
- the devaluation and volatility of global stock markets, which are not related to the Company's operations or assets, could impact the valuation of the Company's equity and other securities.

These factors could have a material adverse effect on the Company's financial condition and results of operations.

Competition. The mining industry is intensely competitive in all of its phases, and such competition could adversely affect the Company's ability to acquire suitable resource properties in the future.

Substantial reliance on the Caylloma and San Jose Mines . All of the Company's revenues in the current and prior years were generated by the Caylloma mine until September 2011 when commercial production commenced at the San Jose mine. For 2013, the Company anticipates a significant percentage of its future revenue will come from the Caylloma and San Jose mines. Unless the Company develops or acquires additional properties or projects, the Company will remain largely dependent upon the operation of the Caylloma and San Jose mines for its revenue and profits, if any. If for any reason production at either mine was reduced or stopped, the Company's revenues and profits would decrease significantly.

Additional businesses and assets may not be successfully integrated. The Company undertakes evaluations of opportunities to acquire additional mining assets and businesses. Any acquisitions may be significant in size, may change the scale of the Company's business, and may expose the Company to new geographic, political, operating, financial and geological risks. The Company's success in its acquisition activities depends on its ability to identify suitable acquisition candidates, acquire them on acceptable terms, and integrate their operations successfully. Any acquisitions would be accompanied by risks such as a significant decline in the relevant metal price after the Company commits to complete an acquisition on certain terms; the quality of the mineral deposit acquired proving to be lower than expected; the difficulty of assimilating the operations and personnel of any acquired companies; the potential disruption of the Company's ongoing business; the inability of management to realize anticipated synergies and maximize the financial and strategic position of the Company; the failure to maintain uniform standards, controls, procedures and policies; the impairment of relationships with employees, customers and contractors as a result of any integration of new management personnel, and the potential unknown liabilities associated with acquired assets and businesses. There can be no assurance that any assets or business acquired will prove to be profitable or that the Company will be able to integrate the required businesses successfully, which could slow the Company's rate of expansion and the Company's business, results of operations and financial condition could suffer.

Fortuna may need additional capital to finance other acquisitions. If the Company obtains further debt financing, it will be exposed to the risk of leverage and its operations could become subject to restrictive loan and lease covenants and undertakings. If the Company obtains equity financing, existing shareholders may suffer dilution. There can be no assurance that the Company would be successful in overcoming these risks or any other problems encountered in connection with such financings.

Political and country risk. The Company conducts, or will conduct, exploration, development and production activity in a number of countries, namely Peru and Mexico and potentially others. The State of Oaxaca in Mexico has a history of social conflicts and political agitation which can lead to public demonstrations and blockades that can from time to time affect the Company's operations. The Company is not able to determine the impact of potential political, social, economic or other risks on its future financial position, which include:

- Cancellation or renegotiation of contracts;
- Changes in foreign laws or regulations;
- Changes in tax laws;
- Royalty and tax increases or claims by governmental entities;
- Retroactive tax or royalty claims;
- Expropriation or nationalization of property;
- Inflation of costs that is not compensated by a currency devaluation;
- Restrictions on the remittance of dividend and interest payments offshore;
- Environmental controls and permitting;
- Opposition from local community members or non-governmental organizations;
- Civil strife, acts of war, guerrilla activities, insurrection and terrorism, and
- Other risks arising out of foreign sovereignty over the areas in which the Company's operations are conducted.

Such risks could potentially arise in any country in which the Company operates. Furthermore, in the event of a dispute arising from such activities, the Company may be subject to the exclusive jurisdiction of courts outside North America or may not be successful in subjecting persons to the jurisdiction of the courts in North America, which could adversely affect the outcome of a dispute.

Metal prices and marketability. The marketability of any metals acquired or discovered may be affected by numerous factors which are beyond the Company's control and which cannot be accurately foreseen or predicted, such as market fluctuations, the global marketing conditions for precious and base metals, the proximity and capacity of milling facilities, metal markets and processing equipment, and such other factors as government regulations, including regulations relating to royalties, allowable production, importing and exporting metals and environmental protection.

The price of the common shares of the Company, the Company's financial results and exploration, development and mining activities may in the future be significantly adversely affected by declines in the price of Ag, Au or other metals. The price of Ag, Au or other metals fluctuates widely and is affected by numerous factors beyond the Company's control such as the sale or purchase of metals by various central banks and financial institutions, interest rates, exchange rates, inflation or deflation, fluctuation in the value of the United States dollar and foreign currencies, global and regional supply and demand, the political and economic conditions of major metal-producing countries throughout the world, and the cost of substitutes, inventory levels and carrying charges. Future serious price declines in the market value of Ag, Au or other metals could cause continued development of and commercial production from the Company's properties to be impracticable. Depending on the price of Ag, Au and other metals, cash flow from mining operations may not be sufficient and the Company could be forced to discontinue production and may lose its interest in, or may be forced to sell, some of its properties. Future production from the Company's mining properties is dependent upon the prices of Ag, Au and other metals being adequate to make these properties economic.

In addition to adversely affecting the Company's reserve estimates and its financial condition, declining metal prices can impact operations by requiring a reassessment of the feasibility of a particular project. Such a reassessment may be the result of a management decision or may be required under financing arrangements related to a particular project. Even if the project is ultimately determined to be economically viable, the need to conduct such a reassessment may cause substantial delays or may interrupt operations until the reassessment can be completed.

Commodity forward and option contracts for base metals production. From time to time the Company may enter into agreements to receive fixed prices on any metal production to offset the risk of revenue losses if commodity prices decline; however, if commodity prices increase beyond the levels set in such agreements, the Company will not benefit from such increases.

Government regulation. Operations, development and exploration on the Company's properties are affected to varying degrees by political stability and government regulations relating to such matters as environmental protection, health, safety and labour, mining law reform, restrictions on production, price controls, tax increases, maintenance of claims, tenure, and expropriation of property. There is no assurance that future changes in such regulations, if any, will not adversely affect the Company's operations.

The activities of the Company require licenses and permits from various governmental authorities. While the Company currently has been granted the requisite licenses and permits to enable it to carry on its existing business and operations, there can be no assurance that the Company will be able to obtain all the necessary licenses and permits which may be required to carry out exploration, development and mining operations for its projects.

Environmental matters. All phases of the Company's operations are subject to environmental regulation in the various jurisdictions in which it operates. Environmental legislation is evolving in a manner which will require stricter standards and enforcement, increased fines and penalties for non-compliance, more stringent environmental assessments of proposed projects and a heightened degree of responsibility for companies and their officers, directors and employees. There is no assurance that future changes in environmental regulation, if any, will not adversely affect the Company's operations. Environmental hazards may exist on the Company's properties which are unknown to the Company at present which have been caused by previous or existing owners or operators of the properties.

Dependence on key personnel. The Company is dependent on a number of key management and employee personnel. The Company's ability to manage its exploration, development, construction and operating activities, and hence its success, will depend in large part on the ability to retain current personnel and attract and retain new personnel, including management, technical and unskilled employees. The loss of the services of one or more key management personnel, as well as a prolonged labor disruption, could have a material adverse effect on the Company's ability to successfully manage and expand its affairs.

The Company's ability to recruit and assimilate new personnel will be critical to its performance. The Company will be required to recruit additional personnel and to train, motivate and manage its employees. The international mining industry is very active and the Company is facing increased competition for personnel in all disciplines and areas of operation, including geology and project management, and there can be no assurance that it will be able to retain current personnel and attract and retain new personnel.

Director and officer conflicts of interest. Certain of the directors and officers of the Company also serve as directors and/or officers of other companies involved in natural resource exploration and development and consequently there exists the possibility for such directors and officers to be in a position of conflict. In such case, the Company's directors and officers comply with conflict of interest provisions in Canadian corporate law, including relevant securities regulatory instruments, in order to ensure that they exercise independent judgment in considering transactions and agreements in respect of which a director or officer has a material interest.

Title to properties. Although the Company has or will receive title opinions for any properties in which it has a material interest, there is no guarantee that title to such properties will not be challenged or impugned. The Company has not conducted surveys of the claims in which it holds direct or indirect interests and, therefore the precise area and location of the properties may be in doubt. The Company's properties may be subject to prior unregistered agreements or transfers or native land claims and title may be affected by unidentified or unknown defects. The Company has conducted as thorough investigation as possible on the title of properties that it has acquired or will be acquiring to be certain that there are no other claims or agreements that could affect its title to the properties.

Dilution from further equity financing. If the Company raises additional funding by issuing equity securities, such financing may substantially dilute the interests of existing shareholders of the Company and reduce the value of their investment.

Foreign currency. The Company's activities and operations in Mexico and Peru make it subject to foreign currency fluctuations. The Company's operating expenses are primarily incurred in Mexican pesos and Peruvian Sol, and the fluctuation of the US dollar in relation to these currencies will consequently have an impact upon the profitability of the Company and may also affect the value of the Company's assets and the amount of shareholders' equity. The Company has not entered into any agreements or purchased any instruments to hedge possible currency risks.

Exploration and development, and infrastructure. Development of the Company's non-producing properties will only follow upon obtaining satisfactory exploration results that confirm economically recoverable and saleable volumes of minerals and metal. The business of mineral exploration and development is speculative in nature and involve a high degree of risk, as few properties which are explored are ultimately developed into producing mines. There is no assurance that the Company's mineral exploration and development activities will result in any discoveries of reserves of commercial ore. The long-term profitability of the Company's operations will be in part directly related to the cost and success of its exploration programs, which may be affected by a number of factors.

Substantial expenditures are required to establish resources and reserves through drilling and development and for mining and processing facilities and infrastructure. Although substantial benefits may be derived from the discovery of a major mineralized deposit, no assurance can be given that minerals will be discovered in sufficient quantities to justify commercial operations or that the funds required for development can be obtained on a timely basis. Economic feasibility of a project is based on several other factors including anticipated metallurgical recoveries, environmental considerations and permitting, future metal prices, and timely completion of the development plan.

Completion of the development of the Company's advanced projects is subject to various requirements, including the availability and timing of acceptable arrangements for power, water, transportation, access and facilities. The lack of, or delay in, availability of any one or more of these items could prevent or delay development of the Company's advanced projects. There can be no assurance that adequate infrastructure, including road access, will be built, that it will be built in a timely manner or that the cost of such infrastructure will be reasonable or that it will sufficiently satisfy the requirements of the advanced projects. As well, accidents or sabotage could affect the provision or maintenance of adequate infrastructure.

The Company's operations require water, and its San Jose mine is located in a region where water is scarce. While the Company believes it holds sufficient water rights to support its current operations, future developments could limit the amount of water available to the Company. New water development projects, or climatic conditions such as extended drought, could adversely affect the Company. There can be no guarantee that the Company will be successful in maintaining adequate supplies of water for its operations.

Insurance. Where practical, a reasonable amount of insurance is maintained against risks in the Company's operations, but coverage has exclusions and limitations. There is no assurance that the Company's insurance will be adequate to cover all liabilities or that it will continue to be available and at terms that are economically acceptable. Losses from un-insured or under-insured events may cause the Company to incur

significant costs that could have a material adverse effect on its financial performance.

Estimation of mineral resources and reserves and precious metal recoveries. There is a degree of uncertainty attributable to the estimation of resources and reserves and to expected mineral grades. Mineral resources and mineral reserves may require revision based on actual production experience. Market fluctuations in the price of metals, as well as increased production costs and reduced recovery rates, may render certain mineral reserves uneconomic and may ultimately result in a restatement of mineral resources and/or reserves. Short term operating factors relating to the mineral resources and reserves, such as the need for sequential development of ore bodies may adversely affect the Company's profitability in any accounting period.

Reclamation. There is a risk that monies allotted for land reclamation may not be sufficient to cover all risks, due to changes in the nature of the waste rock or tailings and/or revisions to government regulations. Therefore, additional funds, or reclamation bonds or other forms of financial assurance may be required over the tenure of the project to cover potential risks. These additional costs may have material adverse impact on the financial condition and results of the Company.

Uncertainty of funding. The Company's operating cash flow from the Caylloma and San Jose Mines may not be sufficient to cover the current costs of exploration and development of the Company's other, non-producing properties. Exploration and development activities may be dependent upon the Company's ability to obtain financing through joint venturing, equity or debt financing or other means, and although the Company has been successful in the past in obtaining financing through the sale of equity securities, there can be no assurance that the Company will be able to obtain additional financing or that the terms of such financing will be favorable. Failure to obtain such additional financing could result in delay or indefinite postponement of further exploration and development of some of its projects.

Uncertainly of dividends on its common shares. The Company has paid no dividends on its common shares since incorporation and does not anticipate paying dividends in the foreseeable future. Payment of any future dividends will be at the discretion of the Company's board of directors after taking into account many factors, including the Company's operating results, financial condition and current and anticipated cash needs.

Legal Proceedings. Due to the nature of its business, the Company may be subject to numerous regulatory investigations, claims, lawsuits and other proceedings in the ordinary course of its business. The results of these legal proceedings cannot be predicted with certainty due to the uncertainty inherent in litigation, including the effects of discovery of new evidence or advancement of new legal theories, the difficulty of predicting decisions of judges and juries and the possibility that decisions may be reversed on appeal. There can be no assurances that these matters will not have a material adverse effect on the Company's business.

The Company is incorporated under the laws of British Columbia, Canada and the majority of the Company's directors and officers are not residents of the U.S. Consequently, it may be difficult for U.S. investors to effect service of process within the United States upon the Company or upon such persons who are not residents of the United States, or to realize in the United States upon judgments of U.S. courts predicated upon civil liabilities under U.S. securities laws. A judgment of a U.S. court predicated solely upon such civil liabilities may be enforceable in Canada by a Canadian court if the U.S. court in which the judgment was obtained had jurisdiction, as determined by the Canadian court, in the matter. There is substantial doubt whether an original action could be brought successfully in Canada against any of such persons or the Company predicated solely upon such civil liabilities.

Material Mineral Properties

The Company has two material mineral projects, described below.

Caylloma Mine, Peru

The Company owns a 100% interest in the Caylloma mine, Peru.

The following is the Summary from the technical report (the "Caylloma Report") entitled "Fortuna Silver Mines Inc.: Caylloma Property, Caylloma District, Peru" dated as of March* 22, 2013 *prepared by Eric N. Chapman and Thomas Kelly. The full text of the Caylloma Report is available for viewing on SEDAR at www.sedar.com and is incorporated by reference in this AIF. Defined terms and abbreviations used herein and not otherwise defined shall have the meanings ascribed to such terms in the Caylloma Report.

Summary

This Technical Report refers to the Caylloma property, an operating underground mine located in the Caylloma Province, Peru. Since June 2005, the Caylloma property has been 100 % owned by Minera Bateas S.A.C. (Minera Bateas), a Peruvian subsidiary of Fortuna Silver Mines Inc. (Fortuna).

The Caylloma property is located in the Caylloma Mining District, 225 kilometers north-northwest of Arequipa, Peru. The property is within the historical mining district of Caylloma, northwest of the Caylloma caldera complex and southwest of the Chonta caldera complex. Host rocks at the Caylloma property are volcanic in nature, belonging to the Tacaza Group. Mineralization is in the form of low to intermediate sulfidation epithermal vein systems.

Epithermal veins at the Caylloma property are characterized by minerals such as pyrite, sphalerite, galena, chalcopyrite, marcasite, native gold, stibnite, argentopyrite, and silver-bearing sulfosalts (tetrahedrite, polybasite, pyrargyrite, stephanite, stromeyerite, jalpite, miargyrite and bournonite). These are accompanied by gangue minerals, such as quartz, rhodonite, rhodochrosite, johannsenite (manganese-pyroxene) and calcite.

There are two different types of mineralization at Caylloma; the first is comprised of silver-rich veins with low concentrations of base metals and includes the Bateas, Bateas Techo, La Plata, Cimoide La Plata, San Cristóbal, San Pedro, San Carlos, Paralela, and Ramal Paralela veins. The second type of vein is polymetallic in nature with elevated lead, zinc, copper, silver and gold grades and includes the Animas, Animas NE, Santa Catalina, Soledad, Silvia, Pilar, Patricia, and Nancy veins.

Underground operations are presently focused on mining the Animas and Bateas veins. Exploration in 2012 focused on the expansion and

delineation of the Animas and Animas NE veins as well as the exploration of the recently discovered Nancy vein.

The 2012 Mineral Resource update has relied on channel and drill hole sample information obtained by Minera Bateas since 2005. Mineralized domains identifying potentially economically extractable material were modeled for each vein and used to code drill holes and channel samples for geostatistical analysis, block modeling and grade interpolation by ordinary kriging or inverse distance weighting.

Mineral Resource and Mineral Reserve estimates for the Caylloma property are reported as of December 31, 2012 and detailed in Table 1.1 and Table 1.2.

Economic values (NSR) for each mining block take into account the commercial terms of 2012, the average metallurgical recovery, the average grade in concentrate and long term projected metal prices. Mineral Reserves have been reported above a break-even cut-off value calculated for each vein, based on NSR values and operating costs. Mineral Resources have been reported above a US$30/t cut-off value based on NSR values.

Mineral Resources are categorized as Measured, Indicated and Inferred. The criteria used for classification includes, the number of samples, spatial distribution, distance to block centroid, kriging efficiency (KE) and slope of regression (ZZ).

Mineral Reserve estimates have considered only Measured and Indicated Mineral Resources as only these categories have sufficient geological confidence to be considered Mineral Reserves (CIM, 2010). Subject to the application of certain economic and mining-related qualifying factors, Measured Resources may become Proven Reserves and Indicated Resources may become Probable Reserves.

Table 1.1 Mineral Reserves as of December 31, 2012

Vein type	Category	Tonnes (000)	Ag (g/t)	Au (g/t)	Pb (%)	Zn (%)	Contained Metal	
							Ag (Moz)	Au (koz)
Silver Veins	Proven	11	872	0.06	0.43	0.64	0.3	0.0
	Probable	246	386	0.96	0.31	0.51	3.1	7.6
	Proven +Probable	257	407	0.93	0.31	0.51	3.4	7.7
Polymetallic Veins	Proven	1,242	92	0.33	1.48	2.20	3.7	13.2
	Probable	2,809	121	0.33	1.66	2.27	10.9	30.2
	Proven +Probable	4,052	112	0.33	1.60	2.25	14.6	43.4
Combined-All Veins	Proven	1,253	99	0.33	1.47	2.19	4.0	13.2
	Probable	3,055	142	0.38	1.55	2.13	14.0	37.8
	Proven +Probable	4,308	130	0.37	1.52	2.15	17.9	51.1

Table 1.2 Mineral Resources as of December 31, 2012

Category	Tonnes (000)	Ag (g/t)	Au (g/t)	Pb (%)	Zn (%)	Contained Metal	
						Ag (Moz)	Ag (Moz)
Measured	431	72	0.30	0.88	1.53	1.0	4.2
Indicated	1,170	82	0.34	0.75	1.40	3.1	12.8
Measured + Indicated	1,601	79	0.33	0.79	1.43	4.1	17.0
Inferred	6,633	101	0.27	1.84	2.58	21.5	58.5

Notes

- Mineral Reserves and Mineral Resources are as defined by CIM Definition Standards on Mineral Resources and Mineral Reserves
- Mineral Resources are exclusive of Mineral Reserves
- Mineral Resources which are not Mineral Reserves do not have demonstrated economic viability
- There are no known legal, political, environmental, or other risks that could materially affect the potential development of the Mineral Resources or Mineral Reserves at Caylloma or San Jose.
- Mineral Resources and Mineral Reserves are estimated as of June 30, 2012 and reported as of December 31, 2012 taking into account production-related depletion for the period of July 1, 2012 through December 31, 2012 with the exception of the Animas and Animas NE veins which were re-estimated using all exploration drilling information as of December 31, 2012
- Mineral Reserves are reported above a NSR breakeven cut-off of US$74.69/t for Animas, Animas NE, and San Cristóbal; US$226.77/t for Bateas, Cimoide La Plata, and La Plata; US$138.34/t for Soledad, Silvia, and Santa Catalina
- Mineral Resources are reported above a NSR cut-off of US$30/t
- Metal prices used in the NSR evaluation for Mineral Reserves are US$29.36/oz for silver, US$1,544/oz for gold, US$2,245/t for lead and US$2,139/t for zinc
- Metal prices used in the NSR evaluation for Mineral Resources are US$25.14/oz for silver, US$1,391.63/oz for gold, US$2,116/t for lead and US$2,006/t for zinc
- Metallurgical recovery values used in the NSR evaluation of sulfides are 82 % for silver, 45 % for gold, 93 % for lead, and 88 % for zinc; and of oxides are 64 % for silver, 45 % for gold, 46 % for lead, and 30 % for zinc
- Operating costs were estimated based on 2012 actual costs
- Tonnes are rounded to the nearest thousand
- The quantity and grade of the Inferred Resources reported in this estimation are conceptual in nature, and it is uncertain if further exploration will result in upgrading of Inferred Resources to Indicated or Measured Resource categories
- Totals may not add due to rounding

Minera Bateas continues to successfully manage the operation, mining 462,000 t of ore from underground to produce 2.0 Moz of silver, 2.8 koz of gold, 17.9 Mlbs of lead, and 22.4 Mlbs of zinc in 2012 while continuing to improve the mine infrastructure.

Fortuna believes there is good potential for a significant increase of the Mineral Resources at the Caylloma property particularly from the continuity of the current veins in operation as well as from the discovery of new veins. During 2012 important exploration projects were developed and new exploration targets were identified. Fortuna is committed in continuing its intensive exploration program, budgeting US$ 6.7 million to continue developing ongoing exploration projects over identified structures as well as the discovery of new targets. In addition to this US$ 4 million has been budgeted for work designed to upgrade Inferred Resources.

The construction of the first stage of the new tailings facility (N° 3) with 15 years life at a 1,300 tpd design capacity, as well as the granting of the operation permit by the Ministry of Energy and Mines in December 2012, has been a major milestone for Minera Bateas in order to assure available tailings disposal capacity for the coming years.

The mining operation has been developed under strict compliance of norms and permits required by public institutions associated with the mining sector. Furthermore, all work follows quality and safety international norms as set out in ISO 14001 and OHSAS 18000.

Minera Bateas continues developing sustainable programs to benefit the local communities including educational, nutritional and economical programs. The socio−environmental responsibilities of these programs contribute toward establishing a good relationship between the company and local communities.

This Technical Report represents the most accurate interpretation of the Mineral Reserve and Mineral Resource available at the effective date of this report. The conversion of Mineral Resources to Mineral Reserve was made using industry-recognized methods, actual operational costs, capital costs, and plant performance data. Thus, it is considered to be representative of actual and future operational conditions.

San Jose Mine, Mexico

The Company owns a 100% interest in the San Jose mine, Mexico.

The following is the Summary from the technical report (the "San Jose Report") entitled "Fortuna Silver Mines Inc.: San Jose Property, Oaxaca, México" dated as of March* 22, 2013 *prepared by Eric N. Chapman and Thomas Kelly. The full text of the San Jose Report is available for viewing on SEDAR at www.sedar.com and is incorporated by reference in this AIF. Defined terms and abbreviations used herein and not otherwise defined shall have the meanings ascribed to such terms in the San Jose Report.

Summary

This Technical Report has been prepared by Fortuna Silver Mines Inc. (Fortuna) in accordance with the disclosure requirements of Canadian National Instrument 43-101 (NI 43-101) to disclose recent information about the San Jose operation.

The San Jose mine is located in the central portion of the state of Oaxaca, Mexico. The project site is 47 km by road south of the city of Oaxaca and 0.8 km east of federal highway 175, the major highway between Oaxaca and Puerto Angel on the Pacific coast. The village of San Jose del Progreso is located 2 km to the southeast of the project site.

The San Jose mine is operated by Compania Minera Cuzcatlan S.A. de C.V., a Mexican subsidiary 100 % owned by Fortuna.

The San Jose Mine area is underlain by a thick sequence of sub-horizontal andesitic to dacitic volcanic and volcaniclastic rocks of Paleogene age. These units have been significantly displaced along major north- and northwest-trending extensional fault systems with the precious metal mineralization being hosted in hydrothermal breccias, crackle breccias, and sheeted and stockwork-like zones of quartz/carbonate veins emplaced within zones of high paleopermeability associated with the extensional structures.

The mineralized structural corridor extends for greater than 3 km in a north-south direction and has been subdivided into the Trinidad deposit area and the San Ignacio area. The Mineral Resource and Mineral Reserve estimates discussed in this Technical Report are located in the Trinidad deposit area.

The major mineralized structures or vein systems recognized in the Trinidad deposit area are the Trinidad, Fortuna and Bonanza vein systems. In addition to the major vein systems, secondary veins and zones of sheeted and stockworked quartz-carbonate veins are present between the Trinidad and Bonanza systems and locally in the hanging wall to the Bonanza vein system. To-date, drilling has defined the Trinidad and Bonanza vein systems over a strike length of approximately 700 meters and to depths exceeding 500 meters from the surface.

Minera Cuzcatlan commenced production at the San Jose mine in August 2011 and as of December 31, 2012 had produced 2.4 Moz of silver and 22 koz of gold. The mining method applied in the exploitation of the veins is overhand cut and fill using a mechanized extraction methodology. Production capacity at the mine is presently 1,000 tonnes per day but Minera Cuzcatlan plans to increase production levels to 1,500 tonnes per day during 2013.

In 2012 Minera Cuzcatlán successfully managed the operation of the San José mine, processing close to 350,000 tonnes of ore from its underground mining operation and producing approximately 1.97 Moz of silver and 17 koz of gold. During the year considerable investment was made to improve and expand the mine's infrastructure.

Mineral Reserves and Mineral Resources as of December 31, 2012 are reported in Table 1.1 and Table 1.2 respectively.

Mineral Reserve estimates have considered only Measured and Indicated Mineral Resources as only these categories have sufficient geological confidence to be considered Mineral Reserves (CIM, 2010). Subject to the application of certain economic and mining-related qualifying factors, Measured Resources may become Proven Reserves and Indicated Resources may become Probable Reserves.

Table 1.1 Mineral Reserves as of December 31, 2012

Classification	Tonnes (000)	Ag Eq. (g/t)	Ag (g/t)	Au (g/t)	Contained Metal	
					Ag (Moz)	Au (koz)

Proven	51	377	246	2.31	0.4	3.8
Probable	3,283	278	189	1.57	20.0	165.7
Proven + Probable	3,335	280	190	1.58	20.4	169.5

Table 1.2 Mineral Resources as of December 31, 2012

Classification	Tonnes (000)	Ag Eq. (g/t)	Ag (g/t)	Au (g/t)	Contained Metal	
					Ag (Moz)	Au (koz)
Measured	3	108	71	0.66	0.0	0.1
Indicated	53	108	74	0.60	0.1	1.0
Measured + Indicated	56	109	74	0.61	0.1	1.1
Inferred	4,257	273	185	1.57	25.3	214.9

Notes

- Mineral Reserves and Mineral Resources are as defined by CIM Definition Standards on Mineral Resources and Mineral Reserves.
- Mineral Resources are exclusive of Mineral Reserves.
- Mineral Resources which are not Mineral Reserves do not have demonstrated economic viability.
- Mineral Resources and Mineral Reserves are estimated as of June 30, 2012 and reported as of December 31, 2012 taking into account production-related depletion for the period of July 1, 2012 through December 31, 2012.
- Mineral Reserves are reported above an Ag Eq breakeven cut-off grade of 93 g/t. Mineral Resources are reported above an Ag Eq cut-off grade of 70 g/t.
- Metal prices used in the Ag Eq evaluation of Mineral Resources are US$25.14/oz for silver and US$1,391.63/oz for gold.
- Metal prices used in the Ag Eq evaluation of Mineral Reserves are US$29.36/oz for silver and US$1,544/oz for gold.
- Metallurgical recovery values used in the Ag Eq evaluation are 88% for silver and 89% for gold.
- Mining, processing and administrative costs were estimated based on first half of 2012 actual costs.
- Tonnes are rounded to the nearest thousand.
- The estimate of Mineral Resources may be materially affected by environmental, permitting, legal, title, taxation, socio-political, marketing, or other relevant issues.
- The quantity and grade of the Inferred Resources reported in this estimation are conceptual in nature, and it is uncertain if further exploration will result in upgrading of Inferred Resources to Indicated or Measured Resource categories.
- Totals may not add due to rounding.

Operating costs are reasonable for the production rates in a mine of this size and are comparable to other mines of the region of similar characteristics. Proposed capital expenditure for the coming year is considered reasonable in order to improve the facilities, equipment and infrastructure and guarantee the continuity and sustainability of the mining operation.

Recommended projects that have been planned for 2013 include:

1) **Expansion of the Concentrator Plant.** This project requires an investment of US$ 8.4 million, which includes construction of new facilities in different areas of the plant in order to increase production from 1,000 tpd to 1,500 tpd.

2) **Delineation drilling.** Minera Cuzcatlan is planning to conduct delineation drilling from underground in 2013. The goal of the program is to convert a total of 525,000 t of Inferred Resource to the category of Indicated Resource representing an estimated 5 Moz Ag Eq. To achieve this 32 drill holes totaling 9,060 m have been planned for 2013 at a budgeted cost of US$1,585,000.

3) **Brownfields exploration.** An extensive drilling campaign is planned for 2013 to build on the excellent results encountered in the north of the deposit in late 2012 (Fortuna, 2013). The purpose of the program is to increase the known extents of the mineralization to the north and south of the presently defined vein systems in order to expand the Mineral Resources. A total of 20,250 m of drilling has been planned for 2013 at a budget cost of US$2.9 million.

4) **Underground development.** The most important mining project for 2013 will be the underground development of the principal ramp by 980 m, which will allow mining to reach the 1,150 masl elevation. At this depth additional infrastructure will be installed to develop an operational level that will help ensure the continuity of the operation and allow greater production if the need should arise (such as due to a change in the mining methodology). The execution of Raise Boring to improve ventilation and access to underground services as the mine deepens is an important component of this project.

5) **Mine plan optimization and risk analysis.** The conditional simulation methodology used in the estimation of the primary veins results in the generation of 50 equi-probable realizations. By assessing these multiple potential scenarios the mine plan can be optimized with the identification of low and high risk regions of the deposit.

6) **Cuzcatlan laboratory.** The Cuzcatlan laboratory must continue to improve its accuracy and precision levels of assay results obtained from channel samples taken from the underground workings. This will ensure a higher level of confidence in the assay results and potentially allow the upgrading of material from Indicated to Measured Resources adjacent to these samples.

This Technical Report represents the most accurate interpretation of the Mineral Reserve and Mineral Resource available at the effective date of this report. The conversion of Mineral Resources to Mineral Reserve was made using industry-recognized methods, actual operational costs, capital costs, and plant performance data. Thus, it is considered to be representative of actual and future operational conditions. This report has been prepared with the latest information regarding environmental and closure cost requirements.

Fortuna believes there is excellent potential to increase the Mineral Resource at the San José property in 2013 with recent drilling demonstrating the continuation of robust ore grade mineralization in the Trinidad ore shoot to depth and to the north with the mineralization remaining open in

both directions.

DIVIDENDS

The Company has not paid any dividends on its common shares nor does it intend to pay any dividends on its shares in the immediate future as management anticipates that all available funds will be invested to finance further acquisition, exploration and development of its mineral properties.

DESCRIPTION OF CAPITAL STRUCTURE

The Company's authorized share capital is an unlimited number of common shares without par value. All common shares of the Company rank equally as to dividends, voting powers and participation in assets and in all other respects.

Voting. The holders of common shares are entitled to receive notice of, attend and vote at any meeting of the shareholders of the Company. Each common share carries one vote per share.

Dividends. The holders of common shares are entitled to receive on a pro-rate basis such dividends as the Board of Directors from time to time may declare, out of funds legally available therefor.

Rights on Dissolution. In the event of a liquidation, winding-up or dissolution of the Company, whether voluntary or involuntary or for the purpose of a reorganization or otherwise or upon any distribution of capital, the holders of the common shares have the right to receive on a pro-rata basis all of the assets of the Company remaining after payment of all of the Company's liabilities.

Pre-emptive, Conversion and Other Rights. No pre-emptive, redemption, sinking fund or conversion rights are attached to the common shares, and the common shares, when fully paid, will not be liable to further call or assessment. No other class of shares may be created without the approval of the holders of the common shares.

MARKET FOR SECURITIES

The Company's common shares were listed and posted for trading on the TSX Venture Exchange ("TSXV") until January 18, 2010 when the Company graduated to the Toronto Stock Exchange ("TSX"). On September 19, 2011, the Company's common shares were listed and posted for trading on the New York Stock Exchange ("NYSE"). The Company's shares currently trade on the NYSE under the symbol "FSM", on the TSX under the symbol "FVI", on the Lima Stock Exchange in Peru under the symbol "FVI", and on the Frankfurt Open Market, the unofficial market organized by Deutsche Börse in Germany, under the symbol "F4S".

Trading Prices and Volume

The following table provides the high and low prices (in Canadian dollars) and volume for the Company's shares as traded on the TSX during the fiscal year ended December 31, 2012:

Period	High ($)	Low ($)	Volume
December 2012	4.69	3.80	6,184,100
November 2012	5.51	4.49	6,185,500
October 2012	5.28	4.49	7,745,600
September 2012	4.83	4.70	7,349,600
August 2012	3.80	3.40	4,642,200
July 2012	3.66	3.28	3,980,500
June 2012	4.15	3.37	6,263,200
May 2012	4.15	3.03	7,091,800
April 2012	4.50	3.50	8,010,100
March 2012	7.01	4.27	14,514,500
February 2012	6.74	6.10	8,770,700
January 2012	5.72	5.52	6,920,300

DIRECTORS AND EXECUTIVE OFFICERS

Name, Occupation and Shareholding

The Board of Directors presently consists of seven directors. Each director will hold office until the next annual general meeting of the Company or until his successor is elected or appointed, unless his office is earlier vacated in accordance with the Articles of the Company, or with the provisions of the British Columbia *Business Corporations Act*.

The following are the full name, place of residence, position with the Company, and principal occupation within the preceding five years of each of the directors and executive officers of the Company:

Name, Position and Residency [1]	Principal Occupation or Employment [1]	Period as a Director of the Company
JORGE GANOZA DURANT President, Chief Executive Officer & Director Lima, Peru	President & CEO of the Company.	December 2, 2004 to present
SIMON RIDGWAY Chairman and Director British Columbia, Canada	Chairman of the Company, March 2006 to present; President & CEO of Radius Gold Inc. (mineral exploration), over five years.	January 25, 2005 to present
MICHAEL IVERSON [3] [4] Director British Columbia, Canada	Chairman & CEO of Niogold Mining Corporation (mineral exploration); President of Triple K Ventures Inc. (private management).	March 30, 1998 to present
TOMAS GUERRERO [2] [3] Director Lima, Peru	President of BO Consulting SA (geological engineering).	July 15, 2005 to present
MARIO SZOTLENDER [3] [4] Director Caracas, Venezuela	Independent Consultant and Director of several public mineral exploration companies; President of Rusoro Mining Ltd. (mineral exploration), November 2006 to August 2007.	June 16, 2008 to present
ROBERT GILMORE [2] [4] Director Colorado, USA	Independent Certified Public Accountant; Independent Financial Consultant, over five years; Director of Eldorado Gold Corporation (mining), over five years; Chief Financial Officer of NextAction Corporation (technology-based market), May 2006 to February 2008; Director of Layne Christensen Company (drilling, water treatment & construction services and products, and natural gas producer), January 2009 to present.	June 23, 2010 to present
THOMAS KELLY [2] Director Lima, Peru	Mining Engineer; CEO of Apurimac Ferrum (mineral exploration), 2011 to present; COO of Inca Pacific Resources, Inc. (mineral exploration), 2008 to 2010; Managing Director of AITCO BOL SRL (mineral exploration), 2005 to 2007.	April 11, 2011 to present
LUIS GANOZA DURANT Chief Financial Officer Lima, Peru	Chief Financial Officer of the Company.	N/A
MANUEL RUIZ-CONEJO Vice-President, Operations Lima, Peru	Vice-President, Operations of the Company, August 2011 to present; formerly Vice-President, Project Development, July 2009 to August 2011, and Vice-President, Business Development of the Company, February 2008 to July 2009.	N/A
THOMAS VEHRS Vice-President, Exploration Colorado, USA	Vice-President, Exploration of the Company.	N/A
ROBERT BROWN Vice-President, Corporate Development British Columbia, Canada	Vice-President, Corporate Development of the Company, August 2012 to present; President of Septemus Consulting Ltd. (corporate development consulting), June 2011to August 2012; President & CEO of Calibre Mining Corp. (mineral exploration), March 2007 to June 2011.	N/A
CESAR PERA Vice-President, Human & Organizational Development Lima, Peru	Vice-President, Human & Organizational Development of the Company, August 2010 to present; Partner, Hrlatam (human resources), January 2009 to July 2010; Vice-President, Administration and Human Resources, Pacifico Grupo Asegurador (insurance), September 2006 to December 2008.	N/A

Notes:

(1) The information as to country of residence, principal occupation, and shares held is not within the knowledge of the management of the Company and has been furnished by the respective nominees.
(2) Member of the Audit Committee of the Company.
(3) Member of the Compensation Committee of the Company.
(4) Member of the Corporate Governance and Nominating Committee of the Company.

As at the date hereof, the directors and executive officers of the Company beneficially own, directly or indirectly, or have control or direction over,

an aggregate of 754,860 common shares of the Company, representing approximately 0.6% of the issued shares of the Company.

Cease Trade Orders or Bankruptcies

As at the date of the AIF and during the 10 years prior to the date of the AIF, none of the directors or executive officers of the Company or a shareholder holding a sufficient number of securities of the Company to affect materially the control of the Company:

(a) is or has been a director or executive officer of any company (including the Company), that while that person was acting in that capacity:

(i) was the subject of a cease trade order or similar order or an order that denied the relevant company access to any exemption under securities legislation, for a period of more than 30 consecutive days, other than Simon Ridgway and Mario Szotlender who are directors of a company that was the subject of a cease trade order for a period of more than 30 consecutive days from each of the BC Securities Commission and the Alberta Securities Commission. The cease trade orders were issued as a result of that company's failure to file its annual financial statements within the prescribed deadline, and upon the company's filing of the outstanding documents, such orders were revoked. In addition, the SEC revoked this company's registration under Section 12(g) of the Securities Exchange Act of 1934 for failure to keep its filings with the SEC up-to-date. Upon receipt of the SEC's notice of proposed revocation, the company filed a settlement agreement with the SEC consenting to the revocation as the company was dormant;

(ii) was subject to an event that resulted, after the director or executive officer ceased to be a director or executive officer, in the company being the subject of a cease trade or similar order or an order that denied the relevant company access to any exemption under securities legislation, for a period of more than 30 consecutive days; or

(iii) within a year of that person ceasing to act in that capacity, became bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency or was subject to or instituted any proceedings, arrangement or compromise with creditors or had a receiver, receiver manager or trustee appointed to hold its assets; or

(b) has become bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency, or become subject to or instituted any proceedings, arrangement or compromise with creditors, or had a receiver, receiver manager or trustee appointed to hold the assets of the director, officer and shareholder.

Penalties or Sanctions

As at the date of the AIF and during the 10 years prior to the date of the AIF, none of the directors or officers of the Company or a shareholder holding a sufficient number of securities of the Company to affect materially the control of the Company has been subject to:

(a) any penalties or sanctions imposed by a court relating to securities legislation or by a securities regulatory authority or has entered into a settlement agreement with a securities regulatory authority other than the settlement agreement described in paragraph (a)(i) under "Cease Trade Orders or Bankruptcies" above; or

(b) any other penalties or sanctions imposed by a court or regulatory body that would likely be considered important to a reasonable investor making an investment decision.

Conflicts of Interest

There are no existing or potential material conflicts of interest between the Company or any of its subsidiaries and a director or officer of the Company or any subsidiary.

AUDIT COMMITTEE

Pursuant to the provisions of Multilateral Instrument 52-110 (the "Instrument"), the Company's Audit Committee has adopted a written charter (the "Charter") that sets out its mandate and responsibilities. The Charter is attached hereto as Schedule "A".

The Audit Committee is presently comprised of Robert Gilmore, Tomas Guerrero and Thomas Kelly. All members of the Committee are "independent" and "financially literate", within the meanings given to those terms in the Instrument.

The education and experience of each audit committee member that is relevant to the performance of his responsibilities as an audit committee member is as follows:

Audit Committee Member	Education and Experience
Robert Gilmore	Mr. Gilmore is a Certified Public Accountant and independent financial consultant with more than 30 years' experience working with resource companies. He is a graduate of the University of Denver with a Bachelor of Science degree in Business Administration, Accounting. He is Chairman of the Board and of the Audit Committee of Eldorado Gold Corporation, and is a director and Audit Committee Chairman of Layne Christensen Company. Mr. Gilmore has also served as Chairman of the Audit Committees of Global Med Technologies, MK Resources, Inc., Frontera Copper Corporation and Ram Power Corporation.

Tomas Guerrero	Mr. Guerrero is a geological engineer with over 30 years of mine geology and mineral exploration experience in Peru, Mexico, Bolivia, Venezuela, Chile, Argentina and Ecuador. Until 2001, Mr. Guerrero held a ten-year tenure as Director of Explorations for the Hochschild Group, a leading private Peruvian mining company with multiple mine operations. Under his leadership Hochschild discovered and put in production three mid size gold-silver mines. He is currently the principle of BO Consulting, an engineering consulting firm specializing in servicing the mining sector.
Thomas Kelly	Mr. Kelly has Bachelor and Masters Degrees in Mining Engineering from the Colorado School of Mines and is a Fellow of Aus.IMM and a Registered Member of SME. He has over 35 years of world-wide mineral industry experience including underground and open pit mining, project development, project management, corporate management and consulting services. Mr. Kelly has held senior positions with Freeport-McMoRan Copper & Gold Inc., AMEC Americas, Inca Pacific Resources Inc. and other recognized industry-leading companies. He is a recognized expert in project management/development and is fluent in Spanish.

The auditors of the Company, Deloitte LLP, obtain, as necessary, the pre-approval of the Audit Committee for any anticipated additional services required of the auditors for the coming fiscal year. If other service requirements arise during the year, the Audit Committee will pre-approve such services at that time, prior to the commencement of such services. No services were performed by the auditors pursuant to the *De-Minimus Non-audit Services* exemption contained in the Instrument.

During the Company's most recently completed fiscal year, the Company's auditors performed certain non-audit services. Fees charged (in Canadian dollars) by the auditors during the last two fiscal years are as follows:

	2012	2011
Audit Fees	$374,848	$310,450
Audit-Related Fees	Nil	$ 64,200
Tax Fees	$147,721	$ 98,665
All Other Fees	$ 5,051	$ 15,000
	$527,620	$488,315

"Audit Fees" are the aggregate fees billed for the audit of the Company's consolidated annual financial statements, and for independent accountant review of the interim financial statements and management discussion and analysis.

"Audit-Related Fees" are fees charged for assurance and related services that are reasonably related to the performance of the audit or review of the Company's financial statements and are not reported under "Audit Fees". This category comprises fees billed for reviews associated with the Company's U.S. filings and its public financing by way of short-form prospectus.

"Tax Fees" are fees for professional services rendered for tax compliance and tax advice on actual or contemplated transactions.

"All Other Fees" are for amounts billed in 2011 for providing IFRS transition assistance, and amounts billed in 2012 for preliminary review of internal controls over financing reporting.

LEGAL PROCEEDINGS

There are no known legal proceedings involving an amount exceeding 10% of the current assets of the Company to which the Company is a party or which any of its properties is the subject during the most recently completed financial year, or any such proceedings known to the Company to be contemplated.

TRANSFER AGENT AND REGISTRAR

The Company's transfer agent and registrar is Olympia Trust Company, at its offices in Vancouver, BC and Toronto, ON.

MATERIAL CONTRACTS

There are no contracts, other than those herein disclosed in this AIF and other than those entered into in the ordinary course of the Company's business, that are material to the Company and that were entered into during the most recently completed fiscal year ended December 31, 2012 or before the most recently completed financial year, but are still in effect as of the date of this AIF.

INTERESTS OF EXPERTS

Names of Experts

Eric N. Chapman and Thomas Kelly, each a Qualified Person as defined by NI 43-101, are the authors of the Caylloma Report and the San Jose Report. The Mineral Resource estimates were prepared under the supervision of Mr. Chapman. The Mineral Reserve estimate and the Mineral Resource estimate exclusive of Mineral Reserves were prepared under the supervision of Mr. Kelly.

Thomas Vehrs, a Qualified Person, is responsible for ensuring that the technical information contained in this AIF is an accurate summary of the original reports and data provided to or developed by the Company.

Interests of Experts

To the knowledge of the Company, the experts named above did not have any registered or beneficial interest, direct or indirect, in any securities or other property of the Company when the experts prepared their reports, other than Eric N. Chapman who currently holds 61,542 options in the Company, Thomas Kelly who currently holds 200,000 options in the Company, and Thomas Vehrs who currently holds 425,000 shares and 422,189 options in the Company.

Deloitte LLP are the auditors of the Company and are independent within the meaning of the Rules of Professional Conduct of British Columbia.

ADDITIONAL INFORMATION

Additional information relating to the Company is available for viewing at www.sedar.com. Information regarding directors' and officers' remuneration and indebtedness, principal holders of the Company's securities and securities authorized for issuance under equity compensation plans, if applicable, is contained in the Company's Information Circular pertaining to its Annual General Meeting held on June 6, 2012. Additional financial information is provided in the Company's audited financial statements for the fiscal year ended December 31, 2012 and the management's discussion and analysis thereon.

SCHEDULE "A"

FORTUNA SILVER MINES INC.
(the "Company")

AUDIT COMMITTEE CHARTER

PURPOSE

The primary function of the Audit Committee is to assist the Board of Directors of the Company (the 'Board") in fulfilling its oversight responsibilities by reviewing the financial information to be provided to the shareholders and others, the systems of internal controls and management information systems established by the senior officers of the Company ("Management") and the Company's internal and external audit process and monitoring compliance with the Company's legal and regulatory requirements with respect to its financial statements.

The Audit Committee is accountable to the Board. In the course of fulfilling its specific responsibilities hereunder, the Audit Committee is expected to maintain an open communication between the Company's external auditors and the Board.

The Audit Committee does not plan or perform audits or warrant the accuracy or completeness of the Company's financial statements or financial disclosure or compliance with generally accepted accounting procedures as these are the responsibility of Management.

RESPONSIBILITIES

Subject to the powers and duties of the Board, the Board hereby delegates to the Audit Committee the following powers and duties to be performed by the Audit Committee on behalf of and for the Board. Nothing in this Charter is intended to or does confer on any member a higher standard of care or diligence than that which applies to the directors as a whole.

External Auditors

The Audit Committee has primary responsibility for the selection, appointment, dismissal, compensation and oversight of the external auditors, subject to the overall approval of the Board. For this purpose, the Audit Committee may consult with Management.

The external auditors shall report directly to the Audit Committee.

Also, the Audit Committee:

a. recommends to the Board:

   i. whether the current external auditors should be nominated for reappointment for the ensuing year and if applicable, select and recommend a suitable alternative for nomination; and

   ii. the amount of compensation payable to the external auditors;

b. resolves disagreements, if any, between Management and the external auditors regarding financial reporting;

c. provides the Board with such recommendations and reports with respect to the financial statements of the Company as it deems advisable;

d. takes reasonable steps to confirm the independence of the external auditors, including but not limited to pre-approving any non-audit related services provided by the external auditors to the Company or the Company's subsidiaries, if any;

e. confirms that the external auditors are a 'participating audit' firm for the purpose of National Instrument 52-108 *Auditor Oversight* and are in compliance with governing regulations;

f. reviews the plan and scope of the audit to be conducted by the external auditors of the Company;

g. reviews and evaluates the performance of the external auditors; and

h. reviews and approves the Company's hiring policy regarding partners, employees and former partners and employees of the Company's present and former external auditors.

Audit and Review Process and Results

The Audit Committee has a duty to receive, review and make any inquiry regarding the completeness, accuracy and presentation of the Company's financial statements to ensure that the financial statements fairly present the financial position and risks of the organization and that they are prepared in accordance with generally accepted accounting principles. To accomplish this, the Audit Committee:

a. considers the scope and general extent of the external auditors' review, including their engagement letter and major changes to the Company's auditing and accounting principles and practices;

b. consults with management regarding the sufficiency of the Company's internal system of audit and financial controls, internal audit procedures and results of such audits;

c. ensures the external auditors have full, unrestricted access to required information and have the cooperation of management;

d. reviews with the external auditors the audit process and standards, as well as regulatory or Company-initiated changes in accounting practices and policies and the financial impact thereof, and selection or application of appropriate accounting principles;

e. reviews with the external auditors and, if necessary, legal counsel, any litigation, claim or contingency, including tax assessments, that could have a material effect upon the financial position of the Company and the manner in which these matters are being disclosed in the financial statements;

f. reviews the appropriateness and disclosure of any off-balance sheet matters;

g. reviews disclosure of related-party transactions;

h. receives and reviews with the external auditors, the external auditors' audit report and the audited financial statements;

i. makes recommendations to the Board respecting approval of the audited financial statements;

j. meets with the external auditors separately from management to review the integrity of the Company's financial reporting, including the clarity of financial disclosure and the degree of conservatism or aggressiveness of the accounting policies and estimates, any significant disagreements or difficulties in obtaining information, adequacy of internal controls over financial reporting, adequacy of disclosure controls and procedures, and the degree of compliance by the Company with prior recommendations of the external auditors;

k. directs management to implement such changes as the Audit Committee considers appropriate, subject to any required approvals of the Board arising out of the review; and

l. meets at least annually with the external auditors, independent of management, and reports to the Board on such meetings.

Interim Financial Statements

The Audit Committee:

a. reviews and determines the Company's practice with respect to review of interim financial statements by the external auditors;

b. conducts all such reviews and discussions with the external auditors and Management as it deems appropriate; and

c. makes recommendations to the Board respecting approval of the interim financial statements.

Involvement with Management

The Audit Committee has primary responsibility for overseeing the actions of management in all aspects of financial management and reporting. The Audit Committee:

a. reviews the Company's annual and interim financial statements, Management's Discussion and Analysis and earnings press releases, if any, before the Company publicly discloses this information;

b. reviews all of the Company's public disclosure of financial information extracted from the Company's financial statements, if such financial statements have not previously been reviewed by the Committee, prior to such information being made public by the Company and for such purpose, the CFO assumes responsibility for providing the information to the Audit Committee for its review;

c. reviews material financial risks with Management, the plan that Management has implemented to monitor and deal with such risks and the success of Management in following the plan;

d. consults annually and otherwise as required with the Company's CEO and CFO respecting the adequacy of the internal controls over financial reporting and disclosure controls and procedures and reviews any breaches or deficiencies;

e. obtains such certifications of annual and interim filings by the CEO and CFO attesting to internal controls over financial reporting and disclosure controls and procedures as deemed advisable;

f. reviews Management's response to significant written reports and recommendations issued by the external auditors and the extent to which such recommendations have been implemented by Management;

g. reviews with Management the Company's compliance with applicable laws and regulations respecting financial reporting matters, and any proposed regulatory changes and their impact on the Company; and

h. reviews as required with Management and approves disclosure of the Audit Committee Charter, and Audit Committee disclosure required in the Company's Annual Information Form, Information Circular and on the Company's website.

PROCEDURAL MATTERS

The Audit Committee:

a. invites the Company's external auditors, the CFO, and such other persons as deemed appropriate by the Audit Committee to attend meetings of the Audit Committee;

b. reports material decisions and actions of the Audit Committee to the Board, together with such recommendations as the Committee may deem appropriate;

c. has the power to conduct or authorize investigations into any matter within the scope of its responsibilities;

d. has the right to engage independent counsel and other advisors as it determines necessary to carry out its duties and the right to set the compensation for any advisors employed by the Audit Committee;

e. has the right to communicate directly with the CFO and other members of Management who have responsibility for the internal and external audit process, as well as to communicate directly with the internal and external auditors; and

f. pre-approves non-audit services to be performed by the external auditors.

COMPOSITION

The Audit Committee is composed of a minimum of three directors, all of whom meet the independence and experience requirements and have relevant skills and/or experience in the Audit Committee's areas of responsibility as required by the securities laws applicable to the Company, including those of any stock exchange on which the Company's securities are traded.

Appointment of Committee Members and Vacancies

Members of the Audit Committee are appointed or confirmed by the Board annually and hold office at the pleasure of the Board. The Board fills any vacancy on, or any additional members to, the Audit Committee.

Committee Chair

The Board appoints a Chair for the Audit Committee.

STRUCTURE AND OPERATIONS

Meetings

The Chair of the Audit Committee or the Chair of the Board or any two of its members may call a meeting of the Audit Committee. The Audit Committee meets at least four times each fiscal year, and at such other times during each year as it deems appropriate.

Quorum

A majority of the members appointed to the Audit Committee constitutes a quorum.

Notice of Meetings

The Chair of the Audit Committee arranges to provide notice of the time and place of every meeting in writing (including by facsimile) to each member of the Audit Committee at least two (2) business days prior to the time fixed for such meeting, provided, however, that a member may in any manner waive a notice of a meeting. Attendance of a member at a meeting constitutes a waiver of notice of the meeting, except where a member attends a meeting for the express purpose of objecting to the transaction of any business on the grounds that the meeting is not lawfully called. The Chair also ensures that an agenda for the meeting and all required materials for review by the members of the Audit Committee are delivered to the members with sufficient time for their review, or that such requirement is waived.

Absence of Committee Chair

If the Chair of the Audit Committee is not present at any meeting of the Audit Committee, the other members of the Audit Committee will be chose a Chair to preside at the meeting.

Secretary of Committee

At each meeting the Audit Committee appoints a secretary who need not be a director of the Company.

Attendance of the Company's Officers at Meetings

The Chair of the Audit Committee or any two members of the Audit Committee may invite one or more officers of the Company to attend any meeting of the Audit Committee.

Delegation

The Audit Committee may, in its discretion and where permitted by National Instrument 52-110 – Audit Committees, delegate all or a portion of its duties and responsibilities to a subcommittee, management or, to the extent otherwise permitted by applicable plans, laws or regulations, to any other body or individual.

Procedure and Records

Subject to any statute or constating documents of the Company, the Audit Committee determines its own procedures at meetings and may conduct meetings by telephone and keeps records of its proceedings.

COMPLAINTS

The Audit Committee has established a Whistle Blower Policy which sets out the procedures for:

a. the receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls, or auditing matters; and

b. the confidential, anonymous submission to the Company of concerns regarding questionable accounting or auditing matters.

The Audit Committee reviews the Whistle Blower Policy annually.

REPORTING AND ASSESSMENT

The Audit Committee reports to the Board of Directors, and on an annual basis, presents to the Board a Committee Annual Report consisting of the Audit Committee's review of its charter, the Committee's and its Chair's performance over the past year, and any recommendations the Audit Committee makes in respect thereto.



Fortuna Silver Mines Inc.

Years ended December 31, 2012 and 2011

Consolidated Financial Statements

March 19, 2013

(All amounts in US$'000's unless otherwise stated)

Deloitte LLP
2800 - 1055
Dunsmuir Street
4 Bentall Centre
P.O. Box 49279
Vancouver BC V7X
1P4
Canada

Tel: 604-669-4466
Fax: 778-374-0496
www.deloitte.ca

Independent Auditor's Report

To the Board of Directors and Shareholders of
Fortuna Silver Mines Inc.

We have audited the accompanying consolidated financial statements of Fortuna Silver Mines Inc., which comprise the consolidated statements of financial position as at December 31, 2012 and December 31, 2011 and the consolidated statements of income, statements of changes in equity, comprehensive income and cash flows for the years then ended and a summary of significant accounting policies and other explanatory
information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards and the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Fortuna Silver Mines Inc. as at December 31, 2012 and December 31, 2011 and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board.

(Signed) Deloitte LLP

Independent Registered Chartered Accountants
March 19, 2013
Vancouver, Canada

FORTUNA SILVER MINES INC.
CONSOLIDATED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31,
(Expressed in thousands of US Dollars, except for share and per share amounts)

	Notes	2012	2011

Sales	**19**	**$**	**161,020**	$	110,104
Cost of sales	**20**		**90,358**		49,030
Mine operating earnings			**70,662**		60,974
Other expenses					
Selling, general and administrative expenses	**11 a), 11 b), 21**		**20,541**		19,840
Exploration and evaluation costs	**22**		**777**		1,715
Net loss (gain) on commodity contracts			**339**		(481)
Gain on disposal of mineral properties, plant and equipment			**(50)**		(59)
Write-off of mineral properties, plant and equipment	**9 a), 9 b)**		**3,887**		-
Impairment of mineral properties, plant and equipment	**9 d)**		**-**		1,894
Operating income			**45,168**		38,065
Finance items					
Interest income			**620**		830
Interest expense			**(562)**		(560)
Net finance income	**23**		**58**		270
Income before tax			**45,226**		38,335
Income taxes	**14**		**13,763**		18,802
Net income for the year		**$**	**31,463**	$	19,533
Earnings per Share -Basic	**15 e)i**	**$**	**0.25**	$	0.16
Earnings per Share - Diluted	**15 e)ii**	**$**	**0.25**	$	0.16
Weighted average number of shares outstanding - Basic	**15 e)i**		**123,584,611**		123,295,063
Weighted average number of shares outstanding - Diluted	**15 e)ii**		**125,232,663**		124,711,984

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

FORTUNA SILVER MINES INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
FOR THE YEARS ENDED DECEMBER 31,
(Expressed in thousands of US Dollars)

	Notes		**2012**		2011
Net income for the year		**$**	**31,463**	$	19,533
Other comprehensive income (loss)					
Transfer of unrealized loss to realized (loss) upon reduction of net investment, net of nil taxes			**(895)**		-
Unrealized (loss) gain on translation of net investment, net of nil taxes			**(376)**		751
Unrealized gain (loss) on translation to presentation currency on foreign operations			**2,224**		(79)
Other comprehensive income			**953**		672
Total comprehensive income for the year		**$**	**32,416**	$	20,205

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

FORTUNA SILVER MINES INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31,
(Expressed in thousands of US Dollars)

	Notes		**2012**		2011
OPERATING ACTIVITIES					
Net income for the year		**$**	**31,463**	$	19,533
Items not involving cash					

Depletion and depreciation			**21,372**		9,421
Accretion of provisions			**232**		173
Income taxes			**13,763**		18,802
Share-based payments			**1,703**		3,682
Unrealized gain on commodity contracts			**(17)**		(116)
Write-off of mineral properties			**3,887**		-
Impairment of mineral properties, plant and equipment			**-**		1,894
Gain on disposal of mineral properties, plant and equipment			**(50)**		(59)
Accrued interest on long term loans receivable and payable			**(25)**		24
Other			**20**		-
			72,348		53,354
Changes in non-cash working capital items					
Accounts receivable and other assets			**(6,971)**		(3,292)
Prepaid expenses			**(45)**		(315)
Due from related parties			**31**		(35)
Inventories			**(1,567)**		(7,273)
Trade and other payables			**718**		6,829
Due to related parties			**(155)**		169
Provisions			**(386)**		(201)
Cash provided by operating activities before interest and income taxes			**63,973**		49,236
Income taxes paid			**(10,703)**		(15,007)
Interest expense paid			**(31)**		(80)
Interest income received			**611**		837
Net cash provided by operating activities			**53,850**		34,986
INVESTING ACTIVITIES					
Purchase of short term investments			**(6,000)**		(49,671)
Redemptions in short term investments			**17,000**		53,406
Expenditures on mineral properties, plant and equipment			**(44,839)**		(76,676)
Advances of deposits on long term assets			**(9,752)**		(31,859)
Receipts of deposits on long term assets			**10,429**		35,424
Proceeds on disposal of mineral properties, plant and equipment			**116**		41
Net cash used in investing activities			**(33,046)**		(69,335)
FINANCING ACTIVITIES					
Proceeds from long term debt			**-**		18
Repayment of long term debt			**(800)**		(18)
Net proceeds on issuance of common shares			**738**		3,656
Repayment of finance lease obligations			**(844)**		(1,178)
Net cash (used in) provided by financing activities			**(906)**		2,478
Effect of exchange rate changes on cash and cash equivalents			**92**		303
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS			**19,898**		(31,871)
Cash and cash equivalents - beginning of year	**3**		**38,730**		70,298
CASH AND CASH EQUIVALENTS - END OF YEAR	**3**	**$**	**58,720**	$	38,730
Supplemental cash flow information	**16**				

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

FORTUNA SILVER MINES INC.
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
(Expressed in thousands of US Dollars)

	Notes		**2012**		2011
ASSETS					
CURRENT ASSETS					
Cash and cash equivalents	**3**	**$**	**58,720**	**$**	38,730
Short term investments	**4**		**6,019**		17,000
Derivative assets	**5**		**-**		70
Accounts receivable and other assets	**6**		**27,032**		19,167
Prepaid expenses			**1,268**		1,218
Due from related parties	**11 c)**		**5**		36
Inventories	**7**		**12,858**		11,291
Assets held for sale	**8, 19**		**51**		-

Total current assets			**105,953**		87,512
NON-CURRENT ASSETS					
Deposits on long-term assets	**6**		**2,694**		2,260
Deferred income tax assets	**14**		**113**		36
Mineral properties, plant and equipment	**9**		**207,503**		181,833
Total assets		**$**	**316,263**	**$**	271,641
LIABILITIES AND EQUITY					
CURRENT LIABILITIES					
Trade and other payables	**10**	**$**	**17,348**	**$**	17,155
Due to related parties	**11 c)**		**54**		205
Derivative liabilities	**5**		**-**		87
Provisions	**13**		**457**		727
Income tax payable	**14**		**200**		3,923
Current portion of leases and long term liabilities	**12**		**449**		1,512
Total current liabilities			**18,508**		23,609
NON-CURRENT LIABILITIES					
Leases and long term liabilities	**12**		**2,250**		2,764
Provisions	**13**		**9,970**		4,247
Deferred income tax liabilities	**14**		**21,042**		12,710
Non-controlling interest			**-**		-
Total liabilities			**51,770**		43,330
EQUITY					
Share capital			**187,807**		186,540
Share option and warrant reserve			**12,994**		10,495
Retained earnings			**59,344**		27,881
Accumulated other comprehensive income			**4,348**		3,395
Total equity			**264,493**		228,311
Total liabilities and equity		**$**	**316,263**	**$**	271,641
Contingencies and capital commitments	**24**				
Subsequent events	**25**				

APPROVED BY THE DIRECTORS:

"*Jorge Ganoza Durant*", Director — Jorge Ganoza Durant

"*Robert R. Gilmore*" , Director — Robert R. Gilmore

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

FORTUNA SILVER MINES INC.
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
FOR THE YEARS ENDED DECEMBER 31,
(Expressed in thousands of US Dollars, except for share amounts)

		Attributable to equity holders of the Company					
		Share Capital					
	Notes	Shares	Amount	Share Option and Warrant Reserve	Retained Earnings	Accumulated Other Comprehensive Income ("AOCI")	Total Equity
Balance – December 31, 2011		124,945,921	$ 186,540	$ 10,495	$ 27,881	$ 3,395	$ 228,311
Exercise of options		314,225	738	-	-	-	738
Issuance of shares for property	**15 a)**	8,605	51	-	-	-	51
Transfer of share option and warrant reserve on exercise of options		-	478	(478)	-	-	-
Share-based payments expense		-	-	2,977	-	-	2,977
Net income for the year		-	-	-	31,463	-	31,463
Transfer of unrealized loss to realized loss upon reduction of net investment, net of taxes		-	-	-	-	(895)	(895)
Unrealized loss on translation of net investment		-	-	-	-	(376)	(376)
Unrealized gain on translation to presentation currency on foreign operations		-	-	-	-	2,224	2,224
Total comprehensive income for the year					31,463	953	32,416
Balance – December 31, 2012		125,268,751	$187,807	$ 12,994	$ 59,344	$ 4,348	$ 264,493
Balance - December 31, 2010		122,497,465	$ 180,403	$ 11,116	$ 8,348	$ 2,723	$ 202,590
Issuance of shares under bought deal financing, net of issuance costs		-	(95)	-	-	-	(95)
Exercise of options		2,441,700	3,751	-	-	-	3,751
Issuance of shares for property	**15 a)**	6,756	30	-	-	-	30

Transfer of share option and warrant reserve on exercise of options	-	2,451	(2,451)	-	-	-
Share-based payments expense	-	-	1,830	-	-	1,830
Net income for the year	-	-	-	19,533	-	19,533
Unrealized gain on translation of net investment	-	-	-	-	751	751
Unrealized loss on translation to presentation currency on foreign operations	-	-	-	-	(79)	(79)
Total comprehensive income for the year				19,533	672	20,205
Balance – December 31, 2011	123,945,921	$ 186,540	$ 10,495	$ 27,881	$ 3,395	$ 228,311

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

1. Corporate Information

Fortuna Silver Mines Inc. ("Fortuna" or the "Company") is engaged in silver mining and related activities, in Latin America, including exploration, extraction, and processing. The Company operates the Caylloma silver/lead/zinc mine in southern Peru and the San Jose silver/gold mine in Mexico.

Fortuna is a publicly traded company incorporated and domiciled in Canada. Its common shares are listed on the New York Stock Exchange under the trading ticker symbol FSM, on the Toronto Stock Exchange and Lima Stock Exchange, both under the trading ticker symbol FVI, and on the Frankfurt Stock Exchange under the trading symbol F4S.F.

The Company's registered office is located at Suite 650, 200 Burrard Street, Vancouver, British Columbia, Canada, V6C 3L6.

2. Basis of Consolidation and Summary of Significant Accounting Policies

a) Statement of Compliance

These consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). The policies applied in these consolidated financial statements are based on IFRS issued and effective as at December 31, 2012. The Board of Directors approved these financial statements for issue on March 19, 2013.

b) Basis of Consolidation

These consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries: Minera Bateas S.A.C. ("Bateas"); Fortuna Silver (Barbados) Inc. ("Barbados"); Compania Minera Cuzcatlan SA ("Cuzcatlan"); Continuum Resources Ltd. ("Continuum"); Fortuna Silver Mines Peru S.A.C. ("FSM Peru"); and Fortuna Silver Mexico, S.A. de CV. ("FS Mexico").

All significant inter-company transactions, balances, revenues, and expenses have been eliminated upon consolidation.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

c) Revenue Recognition

Revenue arising from the sale of metal concentrates is recognized when title or the significant risks and rewards of ownership of the concentrates have been transferred to the buyer. The passing of title to the customer is based on the terms of the sales contract. Final commodity prices are set in a period subsequent to the date of sale based on a specified quotational period, either

one, two, or three months after delivery. The Company's metal concentrates are provisionally priced at the time of sale based on the prevailing market price.

Variations between the price recorded at the delivery date and the final price set under the sales contracts are caused by changes in market prices, and result in an embedded derivative in accounts receivable. The embedded derivative is recorded at fair value each period until final settlement occurs, with changes in fair value classified as provisional price adjustments and included in sales in the consolidated statement of income. Sales of metal concentrates are net of refining and treatment charges.

Revenues from metal concentrate sales are subject to adjustment upon final settlement of metals prices, weights, and assays as of a date that is typically one, two, or three months after the delivery date. Typically, the adjustment is based on an inspection of the concentrate by the customer and in certain cases an inspection by a third party. The Company records adjustments to revenues monthly based on quoted spot prices for the expected settlement period. Adjustments for weights and assays are recorded when results are determinable or on final settlement.

d) Cash and Cash Equivalents

Cash and cash equivalents are designated as fair value through profit or loss ("FVTPL"). Cash and cash equivalents include cash on hand, demand deposits, and money market instruments, with maturities from the date of acquisition of 90 days or less, which are readily convertible to known amounts of cash and are subject to insignificant changes in value. Transaction costs are expensed when incurred through profit or loss.

e) Mineral Properties, Plant and Equipment

Costs directly related to construction projects are capitalized to work-in-progress until the asset is available for use in the manner intended by management. Completed property, plant and equipment are recorded at cost, net of accumulated depreciation and accumulated impairments. Assets, other than capital work in progress, will be depreciated to their residual values over their estimated useful lives as follows:

Land and buildings		
Land	Not depreciated	
Mineral properties	Units of production	
Buildings, located at the mine	Life of mine	
Buildings, others	6 – 20 years	Straight line
Leasehold improvements	7 – 8 years	Straight line

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

e) Mineral Properties, Plant and Equipment (continued)

Plant and equipment		
Machinery and equipment	3 – 8 years	Straight line
Furniture and other equipment	3 – 13 years	Straight line
Transport units	4 – 5 years	Straight line
Capital work in progress	Not depreciated	

Equipment under finance lease is initially recorded at the present value of minimum lease payments at the inception of the lease and depreciated as above. Spare parts and components included in machinery and equipment, depending on the replacement period of the initial component, are depreciated over 8 to 18 months.

Borrowing costs attributed to the construction of qualifying assets are capitalized to mineral properties, plant and equipment and included in the carrying amounts of related assets until the asset is available for use in the manner intended by management.

Costs associated with commissioning activities on constructed plants are deferred from the date of mechanical completion of the facilities until the date the assets are ready for use in the manner intended by management.

On an annual basis, the depreciation method, useful economic life and the residual value of each component asset is reviewed, with any changes recognized prospectively over its remaining useful economic life.

i. Exploration and Evaluation Assets

Significant payments related to the acquisition of land and mineral rights are capitalized as incurred. Prior to acquiring such land or mineral rights, the Company makes a preliminary evaluation to determine that the property has significant potential to develop an economic ore body. The time between initial acquisition and full evaluation of a property's potential is dependent on many factors including: location relative to existing infrastructure, the property's stage of development, geological controls and metal prices.

The Company defers the cost of acquiring, maintaining its interest, exploring and developing mineral properties as exploration and evaluation assets when future inflow of economic benefits from the properties is probable and until such time as the properties are placed into development, abandoned, sold or considered to be impaired in value.

If a mineable ore body is discovered, exploration and evaluation costs are reclassified to mining properties. If no mineable ore body is discovered, such costs are expensed in the period in which it is determined the property has no future economic value.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

e) Mineral Properties, Plant and Equipment (continued)

i. Exploration and Evaluation Assets (continued)

Proceeds received from the sale of interests in evaluation and exploration assets are credited to the carrying value of the mineral properties, with any excess included in income as gain or loss on disposal of mineral properties, plant and equipment.

Write-downs due to impairment in value are charged to income. The cash-generating unit for assessing impairment is a geographic region and shall be no larger than the operating segment.

Exploration costs that do not relate to any specific property are expensed as incurred.

ii. Operational Mining Properties and Mine Development

For operating mines, all exploration within the mineral deposit is capitalized and amortized on a unit-of-production basis over proven and probable reserves and the portion of resources expected to be extracted economically as part of the production cost.

Costs of producing properties are amortized on a unit-of-production basis over proven and probable reserves and the portion of resources expected to be extracted economically, and costs of abandoned properties are written-off.

The company has made a change in estimate and commencing in the fourth quarter of 2012, the amortization on a unit-of-production basis will be over the portion of resources, in addition to the proven and probable reserves, expected to be extracted economically. The change in estimate is applied prospectively and impacts the depletion of the mineral deposit for the current and future periods.

iii. Commercial Production

Capital work in progress consists of expenditures for the construction of future mines and includes pre-production revenues and expenses prior to achieving commercial production. Commercial production is a convention for determining the point in time in which a mine and plant has completed the operational commissioning and has operational results that are expected to remain at a sustainable commercial level over a period of time, after which production costs are no longer capitalized and are reported as operating costs. The determination of when commercial production commences is based on several qualitative and quantitative factors including but not limited to the following:

- all major capital expenditures to bring the mine to the condition necessary for it to be capable of operating in the manner intended by management have been completed;
- the mine or mill is operating within eighty percent of design capacity;
- metallurgical recoveries are achieved within eighty percent of projections; and,
- the ability to sustain ongoing production of ore at a steady or increasing level.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

e) Mineral Properties, Plant and Equipment (continued)

iii. Commercial Production (continued)

On the commencement of commercial production, depletion of each mining property will be provided on a unit-of-production basis. Any costs incurred after the commencement of production are capitalized to the extent they give rise to a future economic benefit.

f) Asset Impairment

Assets are reviewed and tested for impairment when an indicator of impairment is considered to exist. An assessment of impairment indicators is performed at each reporting period or whenever indicators arise. Even with no indicators present, the Company will test an intangible asset with an indefinite useful life or an intangible asset not yet available for use for impairment at least once annually. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less cost to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest level for which there are separately identifiable cash inflows or cash generating units. These are typically individual mines or development projects. Brownfields exploration projects, located close to existing mine infrastructure, are assessed for impairment as part of the associated mine cash generating unit.

When the recoverable amount is assessed using pre-tax discounted cash flow techniques, the resulting estimates are based on detailed mine and/or production plans. For value in use, recent cost levels are considered, together with expected changes in costs that are compatible with the current condition of the business. The cash flow forecasts are based on best estimates of expected future revenues and costs, including the future cash costs of production, capital expenditure and reclamation and closures costs.

Where a fair value less cost to sell model is used the cash flow forecast includes net cash flows expected to be realized from extraction, processing and sale of mineral resources that do not currently qualify for inclusion in proven or probable reserves and the portion of resources expected to be extracted economically.

Where an impairment loss subsequently reverses, the carrying amount of the asset or cash-generating unit is increased to the revised estimate of recoverable amount, but not beyond the carrying amount that would have been determined had no impairment loss been recognized for the asset or cash-generating unit in prior years. A reversal of an impairment loss is recognized into earnings immediately.

g) Provisions

i. Decommissioning and restoration provisions

Future obligations to retire an asset, including dismantling, remediation and ongoing treatment and monitoring of the site related to normal operations are initially recognized and recorded as a liability based on estimated future cash flows discounted at the risk-free rate.

FORTUNA SILVER MINES INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011
(All amounts in US$'000's unless otherwise stated)

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

g) Provisions (continued)

i. Decommissioning and restoration provisions (continued)

The decommissioning and restoration provision ("DRP") is adjusted at each reporting period for changes to factors including the

expected amount of cash flows required to discharge the liability, the timing of such cash flows and the risk-free discount rate.

The liability is accreted to full value over time through periodic charges to income. This accretion of provisions is charged to finance costs in the consolidated statements of income.

The amount of the DRP initially recognized is capitalized as part of the related asset's carrying value and amortized to income. The method of amortization follows that of the underlying asset. The costs related to a DRP are only capitalized to the extent that the amount meets the definition of an asset and can bring about future economic benefit. For a closed site or where the asset which generated a DRP no longer exists, there is no longer future benefit related to the costs and as such, the amounts are expensed. For operating sites, a revision in estimates or a new disturbance will result in an adjustment to the liability with an offsetting adjustment to the capitalized retirement cost. For closed sites, adjustments to the DRP that are required as a result of changes in estimates are charged to income in the period in which the adjustment is identified.

ii. Environmental disturbance restoration provisions

During the operating life of an asset, events such as infractions of environmental laws or regulations may occur. These events are not related to the normal operation of the asset and are referred to as environmental disturbance restoration provisions ("EDRP"). The costs associated with an EDRP are accrued and charged to earnings in the period in which the event giving rise to the liability occurs. Any subsequent adjustments to an EDRP due to changes in estimates are also charged to earnings in the period of adjustment. These costs are not capitalized as part of the long-lived asset's carrying value.

iii. Other provisions

Provisions are recognized when a present legal or constructive obligation exists, as a result of past events, and it is probable that an outflow of resources that can be reliably estimated will be required to settle the obligation. Where the effect is material, the provision is discounted using an appropriate current market-based pre-tax discount rate.

h) Inventories

Inventories include metals contained in concentrates, stockpiled ore, materials, and supplies. The classification of metals inventory is determined by the stage in the production process. Product inventories are sampled for metal content and are valued based on the lower of actual production costs incurred or estimated net realizable value based upon the period ending prices of contained metal.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

h) Inventories (continued)

Ore stockpile and finished goods inventories are valued at the lower of production cost and net realizable value. Materials and supplies are valued at the lower of average cost and net realizable value. Production costs include all mine site costs.

i) Assets Held for Sale

A non-current asset is classified as held for sale when it meets the following criteria:

- the non-current asset is available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets; and,
- the sale of the non-current asset is highly probable. For the sale to be highly probable:
- the appropriate level of management must be committed to a plan to sell the asset;
- an active program to locate a buyer and complete the plan must have been initiated;
- the non-current asset or disposal group must be actively marketed for sale at a price that is reasonable in relation to its current fair value;
- the sale should be expected to qualify for recognition as a completed sale within one year from the date of classification as held for sale (with certain exceptions); and,
- actions required to complete the plan should indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.

Assets held for sale are not depreciated. When the sale of assets held for sale is expect to occur beyond one year, the assets are measured at the lower of its carrying amount and fair value less costs to sell. Any gain or loss from initial measurement and subsequent measurement are recorded in other comprehensive income but not in excess of cumulative impairment losses.

j) Income Taxes

Income tax expense consists of current and deferred tax expense. Income tax is recognized in the consolidated statement of income.

Current tax expense is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at period end, adjusted for amendments to tax payable with regards to previous years.

Deferred tax assets and liabilities are recognized for deferred tax consequences attributable to unused tax loss carry forwards, unused tax credits and differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using the enacted or substantially enacted tax rates expected to apply when the asset is realized or the liability settled.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

j) Income Taxes (continued)

The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income or loss in the period that substantive enactment occurs.

A deferred tax asset is recognized to the extent that it is probable that future taxable income will be available against which the asset can be utilized. To the extent that the Company does not consider it probable that deferred tax asset will be recovered, the deferred tax asset is reduced.

The following temporary differences do not result in deferred tax assets or liabilities:

- the initial recognition of assets or liabilities, not arising in a business combination, that does not affect accounting or taxable income;
- goodwill; and,
- investments in subsidiaries, associates and jointly controlled entities where the timing of reversal of the temporary differences can be controlled and reversal in the foreseeable future is not probable.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to the offset current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Company intends to settle its current tax assets and liabilities on a net basis.

k) Share-Based Payments

The fair value method of accounting is used for share-based payment transactions. Under this method, the cost of share options and other equity-settled share-based payment arrangements are recorded based on the estimated fair value at the grant date and charged to earnings over the vesting period. Where awards are forfeited because non-market based vesting conditions are not satisfied, the expense previously recognized is proportionately reversed in the period the forfeiture occurs.

Share-based payment expense relating to cash-settled awards, including deferred and restricted share units is accrued over the vesting period of the units based on the quoted market value of Company's common shares. As these awards will be settled in cash, the expense and liability are adjusted each reporting period for changes in the underlying share price.

i. Stock Option Plan

The Company applies the fair value method of accounting for all stock option awards. Under this method, the Company recognizes a compensation expense for all stock options awarded to employees, based on the fair value of the options on the date of grant which is determined by using the Black-Scholes option pricing model. The fair value of the options is expensed over the graded vesting period of the options.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

k) Share-based Payments (continued)

ii. Deferred Share Unit ("DSU") Plan

The Company's DSU compensation liability is accounted for based on the number of units outstanding and the quoted market value of the Company's common shares at the financial position date. The year-over-year change in the deferred share unit compensation liability is recognized in income.

iii. Restricted Share Unit ("RSU") Plan

The Company's RSU compensation liability is accounted for based on the number of units outstanding and the quoted market value of the Company's common shares at the financial position date. The Company recognizes a compensation cost in operating income on a graded vesting basis for each RSU granted equal to the quoted market value of the Company's common shares at the date of which RSUs are awarded to each participant prorated over the performance period and adjusts for changes in the fair value until the end of the performance date. The cumulative effect of the change in fair value is recognized in income in the period of change.

l) Earnings per Share

Basic earnings per share is computed by dividing net income for the year by the weighted average number of common shares outstanding during the year.

The diluted earnings per share calculation is based on the weighted average number of common shares outstanding during the year, plus the effects of dilutive common share equivalents. This method requires that the dilutive effect of outstanding options issued should be calculated using the treasury stock method. This method assumes that all common share equivalents have been exercised at the beginning of the year (or at the time of issuance, if later), and that the funds obtained thereby were used to purchase common shares of the Company at the average trading price of the common shares during the year, but only if dilutive.

m) Foreign Currency Translation

The presentation currency of the Company is the United States Dollar ("US$").

The functional currency of each of the entities in the group is the US$, with the exception of the parent entity and certain holding companies which have a Canadian dollar functional currency.

Transactions in foreign currencies are initially recorded in the functional currency at the exchange rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange at each financial position date. Foreign exchange gains or losses on translation to the functional currency of an entity are recorded in income. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of the initial transaction.

FORTUNA SILVER MINES INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011
(All amounts in US$'000's unless otherwise stated)

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

m) Foreign Currency Translation (continued)

For entities with a functional currency different from the presentation currency of the Company, translation to the presentation currency is required. Assets and liabilities are translated at the rate of exchange at the financial position date. Revenue and expenses are translated at the average rate for the period. All resulting exchange differences are recognized in other comprehensive income.

n) Financial Instruments

i. Financial Assets

The Company classifies all financial assets as either fair value through profit or loss ("FVTPL"), held-to-maturity ("HTM"), loans and receivables, or available-for-sale "(AFS"). The classification is determined at initial recognition and depends on the nature and purpose of the financial asset.

a) Financial Assets at Fair Value Through Profit or Loss

Financial assets are classified as FVTPL when the financial asset is held-for-trading or it is a designated FVTPL on initial recognition. A financial asset is classified in this category if acquired principally for the purpose of selling in the short-term.

Financial assets classified as FVTPL are stated at fair value with any resulting gain or loss recognized in income or loss in the period in which they arise. Transaction costs related to financial assets classified as FVTPL are recognized immediately in net income (loss).

Derivatives are not being accounted for as hedges and are categorized as held-for-trading. Derivatives are initially recognized at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. Fair value of the Company's recognized commodity-based derivatives are based on the forward prices of the associated market index. Gains or losses are recorded in the consolidated statement of income.

b) Held-to-Maturity ("HTM")

HTM investments are recognized on a trade-date basis and are initially measured at fair value, including transaction costs. The Company does not have any assets classified as HTM investments.

c) Loans and Receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are initially measured at fair value, net of transaction costs and are classified as current or non-current assets based on their maturity date. They are carried at amortized cost less any impairment. The impairment loss of receivables is based on a review of all outstanding amounts at period end. Interest income is recognized by applying the effective interest rate, except for short term receivables when the recognition of interest would not be significant.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

n) Financial Instruments (continued)

i. Financial Assets (continued)

d) Available-For-Sale ("AFS") Assets

AFS financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories.

AFS financial assets are measured at fair value, determined by published market prices in an active market, except for investments in equity instruments that do not have quoted market prices in an active market which are measured at cost. Changes in fair value are recorded in other comprehensive income (loss) until realized through disposal or impairment. Investments classified as available-for-sale are written down to fair value through income whenever it is necessary to reflect prolonged or significant decline in the value of the assets. Realized gains and losses on the disposal of available-for-sale securities are recognized in the consolidated statement of income.

The Company does not have any assets classified as AFS.

e) Impairment of Financial Assets

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at each period end. Financial assets are impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted.

Objective evidence of impairment could include the following:

- significant financial difficulty of the issuer or counterparty;
- default or delinquency in interest or principal payments; or
- it has become probable that the borrower will enter bankruptcy or financial reorganization.

For financial assets carried at amortized cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of the estimated future cash flows, discounted at the financial asset's original effective interest rate.

The carrying amount of all financial assets at amortized cost, excluding trade receivables, is directly reduced by the impairment loss. The carrying amount of trade receivables is reduced through the use of an allowance account. When a trade receivable is considered uncollectable, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognized in income or loss.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

n) Financial Instruments (continued)

i. Financial Assets (continued)

f) Impairment of Financial Assets (continued)

With the exception of AFS equity instruments, if in a subsequent period, the amount of the impairment loss decreases and the decrease relates to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through income or loss. On the date of impairment reversal, the carrying amount of the financial asset cannot exceed its amortized cost had an impairment not been recognized.

g) Derecognition of Financial Assets

A financial asset is derecognized when:

- the contractual right of the asset's cash flows expire; or
- if the Company transfers the financial asset and substantially all risks and reward of ownership to another entity.

ii. Financial Liabilities

Derivatives are categorized as held-for-trading. Derivatives are initially recognized at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. Fair value of the Company's recognized commodity-based derivatives are based on the forward prices of the associated market index. Gains or losses are recorded in the consolidated statement of income.

Long term debt and other financial liabilities are recognized initially at the fair value, net of transaction costs incurred, and are subsequently stated at amortized cost. Any difference between the amounts originally received (net of transaction costs) and the redemption value is recognized in the consolidated statement of income over the period to maturity using the effective interest method.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

n) Financial Instruments (continued)

iii. Classification and Subsequent Measurements

The Company has designated each of its significant categories of financial instruments as follows:

Financial Instrument	Classification	Measurement
Cash and Cash Equivalents	FVTPL	Fair value
Short Term Investments	FVTPL	Fair value
Derivative Assets	FVTPL	Fair value
Trade Receivable from Concentrate Sales	FVTPL	Fair value
Other Accounts Receivables	Loans and receivables	Amortized cost
Due from Related Parties	Loans and receivables	Amortized cost
Long Term Receivables	Loans and receivables	Amortized cost
Trade and Other Payables	Other liabilities	Amortized cost
Due to Related Parties	Other liabilities	Amortized cost
Derivative Liabilities	FVTPL	Fair value
Income Tax Payable	Other liabilities	Amortized cost
Lease and Long Term Liabilities	Other liabilities	Amortized cost

iv. Effective Interest Method

The effective interest method calculates the amortized cost of a financial instrument and allocates interest income or expense over the corresponding period. The effective interest rate is the rate that discounts estimated future cash receipts or payments over the expected life of the financial instrument, or where appropriate, a shorter period, to the net carrying amount on initial recognition. Income or expense is recognized on an effective interest basis for instruments other than those financial instruments classified as FVTPL.

o) Segment Reporting

A geographical segment is a distinguishable component of the entity that is engaged in providing products or services within a particular economic environment and is subject to risks and returns that are different than those of segments operating in other economic environments.

The business operations comprise the mining and processing of silver-lead, zinc, and silver-gold and the sale of these products.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

p) Leases

A lease is a finance lease when substantially all of the risks and rewards incidental to ownership of the leased asset are transferred from the lessor to the lessee by the agreement. The leased assets are initially recorded at the lower of the fair value and the present value of the minimum lease payments and are depreciated over the shorter of the asset's useful lives and the term of the lease. Interest on the lease instalments is recognized as interest expense over the lease term using the effective interest method. Leases for land and buildings are recorded separately if the lease payments can be allocated accordingly.

Leases that do not transfer all the risks and rewards of ownership are classified as operating leases. Payments are recorded in the income statement using the straight line method over their estimated useful lives.

q) Share Capital

Common shares are classified as equity. Incremental costs directly attributable to the issue of shares are shown in equity as a deduction from the proceeds. Share-based payments including stock option plan, deferred share unit plan, and restricted share unit plan are discussed in Note 2. j).

r) Related Party Transactions

Parties are considered to be related if one party has the ability directly, or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control, related parties may be individuals or corporate entities. A transaction is considered to be a related party transaction when there is a transfer of resources or obligations between related parties.

s) Significant Accounting Judgments and Estimates

The preparation of consolidated financial statements requires management to make judgments and estimates that affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of expenses during the reporting period. Actual outcomes could differ from these judgments and estimates. The consolidated financial statements include judgments and estimates which, by their nature, are uncertain. The impacts of such judgments and estimates are pervasive throughout the consolidated financial statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and the revision affects both current and future periods.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

s) Significant Accounting Judgments and Estimates (continued)

Significant assumptions about the future and other sources of judgments and estimates that management has made at the statement of financial position date, that could result in a material adjustment to the carrying amounts of assets and liabilities, in the event that actual results differ from assumptions made, relate to, but are not limited to, the following:

i. Critical Judgments

- The analysis of the functional currency for each entity of the Company. In concluding that the United States dollar functional currency for its Peruvian and Mexican entities and the Canadian and Barbados entities have a Canadian dollar functional currency, management considered the currency that mainly influences the cost of providing goods and services in each jurisdiction in which the Company operates. As no single currency was clearly dominant the Company also considered secondary indicators including the currency in which funds from financing activities are denominated and the currency in which funds are retained.
- In concluding when commercial production has been achieved, the Company considered the following factors:
- all major capital expenditures to bring the mine to the condition necessary for it to be capable of operating in the manner intended by management have been completed;
- the mine or mill is operating as per design capacity and metallurgical recoveries were achieved; and,
- the ability to sustain ongoing production of ore at a steady or increasing level.
- The identification of reportable segments, basis for measurement and disclosure of the segmented information.
- The determination of estimated useful lives and residual values of tangible and long-lived assets and the measurement of depreciation expense.
- The identification of impairment indicators, cash generating units and determination of value in use and the write down of tangible and long lived assets.
- Measurement of financial instruments involve significant judgments related to interpretation of the terms of the instrument, identification, classification, impairment and the overall measurement to approximate fair values.

ii. Estimates

- the recoverability of amounts receivable which are included in the consolidated statements of financial position;
- the estimation of assay grades of metal concentrates sold in the determination of the carrying value of accounts receivable which are included in the consolidated statements of financial position and included as sales in the consolidated statements of income;
- the carrying value of the short term investments and the recoverability of the carrying value which are included in the consolidated statements of financial position;
- the determination of net realizable value of inventories on the consolidated statements of financial position;

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

s) Significant Accounting Judgments and Estimates (continued)

ii. Estimates (continued)

- the estimated useful lives of property, plant and equipment which are included in the consolidated statements of financial position and the related depreciation included in the consolidated statements of income;
- the determination of mineral reserves, carrying amount of mineral properties, and depletion of mineral properties included in the consolidated statements of financial position and the related depletion included in the consolidated statements of income;
- review of tangible and intangible assets carrying value, the determination of whether these assets are impaired and the measurement of impairment charges or reversals which are included in the consolidated statements of income;
- the determination of the fair value of financial instruments and derivatives included in the consolidated statements of financial position;
- the fair value estimation of share-based awards included in the consolidated statements of financial position and the inputs used in accounting for share-based compensation expense in the consolidated statements of income;
- the provision for income taxes which is included in the consolidated statements of income and composition of deferred income tax asset and liabilities included in the consolidated statement of financial position;
- the recognition of deferred income tax assets, amounts recorded for uncertain tax positions, the measurement of income tax expense and indirect taxes included in the consolidated statement of financial position;
- the inputs used in determining the net present value of the liability for provisions related to decommissioning and restoration included in the consolidated statements of financial position;
- the inputs used in determining the various commitments and contingencies accrued in the consolidated statements of financial position; and,
- the assessment of indications of impairment of each mineral properties and related determination of the net realizable value and write-down of those properties where applicable.

t) Significant Changes in Accounting Policies including Initial Adoption

IFRS 7 *Financial Instruments: Disclosures* (Amendment)
The amendment, effective for annual periods beginning on or after July 1, 2011, with early application permitted, requires additional quantitative and qualitative disclosures relating to transfers of financial assets, where: financial assets are derecognized in their entirety, but where the entity has a continuing involvement in them; financial assets that are not derecognized in their entirety. The Company has adopted the amendment to IFRS 7 and the amendment did not have a material impact on the Company's consolidated financial statements.

FORTUNA SILVER MINES INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011
(All amounts in US$'000's unless otherwise stated)

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

t) Significant Changes in Accounting Policies including Initial Adoption (continued)

IAS 12 *Income Taxes* (Amendment)
IAS 12 *Income Taxes*, amendments regarding Deferred Tax: Recovery of Underlying Assets introduces an exception to the existing principle for the measurement of deferred tax assets and liabilities arising on investment property measured at fair value, and the requirement that deferred tax on non-depreciable assets measured using the revaluation model in IAS 16 should always be measured on a sale basis. The amendment is effective for annual periods beginning on or after January 1, 2012. The Company has adopted the amendment to IAS 12 and the amendment did not have a material impact on the Company's consolidated financial statements.

u) New Accounting Standards

i) New Accounting Standards Impacting on or after July 1, 2012

IAS 1 *Presentation of Financial Statements* (Amendment)
The amendments to IAS 1 *Presentation of Financial Statements* retain the 'one or two statement' approach at the option of the entity and only revise the way other comprehensive income ("OCI") is presented: requiring separate subtotals for those elements which may be 'recycled' (e.g. cash-flow hedging, foreign currency translation), and those elements that will not (e.g. fair value through OCI items under IFRS 9) to the statement of income. In addition, the tax associated with items presented before tax to be shown separately for each of the two groups of OCI items (without changing the option to present items of OCI either before tax or net of tax).

ii) New Accounting Standards Impacting on or after January 1, 2013

On May 17, 2012, the IASB issued Annual Improvements to IFRSs: 2009-2011 Cycle, incorporating amendments to five IFRSs; **IFRS 1 *First-time Adoption of International Reporting Standards*, IAS 1 *Presentation of Financial Statements*, IAS 16 *Property, Plant and Equipment*, IAS 32 *Financial Statements: Presentation*, IAS 34 *Interim Financial Reporting***. The amendments are effective for annual periods beginning on or after January 1, 2013, with early application permitted, and must be applied retrospectively.

IFRS 1 *First-time Adoption of International Financial Reporting Standards* (Amendment)
IFRS 1 is amended to clarify the repeated application of IFRS 1 and the treatment of borrowing costs incurred on or after the date of transition to IFRSs. This is not applicable as the company has already transitioned to IFRS.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

u) New Accounting Standards (continued)

ii) New Accounting Standards Impacting on or after January 1, 2013 (continued)

IAS 1 *Presentation of Financial Statements* (Amendment)
IAS 1 is amended to clarify that only one comparative period - which is the preceding period - is required for a complete set of financial statements.

IAS 16 *Property, Plant, and Equipment* (Amendment)
IAS 16 is amended to clarify the classification of servicing equipment. Spare parts, stand-by equipment and servicing equipment should be classified as property, plant, and equipment when they meet the definition of property, plant, and equipment in IAS 16 and otherwise as inventory using IAS 2 *Inventories*.

IAS 32 *Financial Instruments: Presentation* (Amendment)
IAS 32 is amended to clarify that IAS 12 *Income Taxes* applies to the account for income taxes relating to distributions to holders of equity instruments and transaction costs of equity transactions.

IAS 34 Interim Financial Reporting (Amendment)
IAS 34 is amended to clarify that the total assets and total liabilities for a particular reportable segment would be separately disclosed in interim financial reporting only when the amounts are regularly provided to the chief operating decision maker and there has been a material change from the amounts disclosed in the last annual financial statements for the reportable segment.

The Company does not anticipate these amendments to have a significant impact on its consolidated financial statements.

IFRS 7 *Financial Instruments: Disclosures in Respect of Offsetting* (Amendment)
At its meeting on December 13-15, 2011, the IASB approved amendments to IFRS 7,*Financial Instruments*: Disclosures, with respect to offsetting financial assets and financial liabilities. The common disclosure requirements issued by the IASB and the FASB in December 2011 are intended to help investors and other users to better assess the effect or potential effect of offsetting arrangements on a company's financial position. Companies and other entities are required to apply the amendments for annual

reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. The required disclosures should be provided retrospectively. The Company does not anticipate this amendment to have a significant impact on its consolidated financial statements.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

u) New Accounting Standards (continued)

ii) New Accounting Standards Impacting on or after January 1, 2013 (continued)

IFRS 10 *Consolidated Financial Statements*

IFRS 10 *Consolidated Financial Statements* replaces the portion of IAS 27 *Consolidated and Separate Financial Statements* that addresses the accounting for consolidated financial statements, and SIC12 *Consolidation - Special Purpose Entities*. IFRS 10 establishes principles for the presentation and preparation of consolidated financial statements when an entity controls one or more entities. This standard (i) requires a parent entity (an entity that controls one or more other entities) to present consolidated financial statements; (ii) defines the principle of control, and establishes control as a basis for consolidation; (iii) sets out how to apply the principle of control whether an investor controls an investee and therefore must consolidate the investee; and (iv) sets out the accounting requirements for the preparation of consolidated financial statements. IFRS 10 is effective for annual periods beginning on or after January 1, 2013. The Company does not anticipate the application of IFRS 10 to have a significant impact on its consolidated financial statements.

IFRS 11 *Joint Arrangements*

IFRS 11 replaces IAS 31 *Interest in Joint Ventures* and SIC-13 *Jointly-Controlled Entities-Non-Monetary Contributions by Venturers.* This standard establishes the core principle that a party to a joint arrangement determines the type of joint arrangement in which it is involved by assessing its rights and obligations and accounts for those rights and obligations in accordance with that type of joint arrangement (joint operations or joint ventures). This standard is effective for annual periods on or after January 1, 2013.

IFRS 12 *Disclosure of Interests in Other Entities*

IFRS 12 combines the disclosure requirements for an entity's interest in subsidiaries, joint arrangements, associates and structured entities into one comprehensive disclosure standard. This standard requires the disclosure of information that enable users of financial statements to evaluate the nature of, and risks associated with, its interest in other entities and the effects of those interests on its financial position, financial performance and cash flows. This standard is effective for annual periods beginning on or after January 1, 2013.

The Company does not anticipate these amendments to have a significant impact on its consolidated financial statements.

FORTUNA SILVER MINES INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011
(All amounts in US$'000's unless otherwise stated)

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

u) New Accounting Standards (continued)

ii) New Accounting Standards Impacting on or after January 1, 2013 (continued)

IFRS 13 *Fair Value Measurement*

IFRS 13 *Fair Value Measurement* provides guidance on how to measure fair value, but does not change when fair value is required or permitted under IFRS. IFRS 13 defines fair value, sets out a single IFRS framework for measuring fair value and

requires disclosures about fair value measurements. IFRS 13 applies when another IFRS requires or permits fair value measurements or disclosures about fair value measurements (and measurements, such as fair value less costs to sell, based on fair value or disclosures about those measurements), except for: share-based payment transactions within the scope of IFRS 2 *Share-based Payment*; leasing transactions with the scope of IAS 17 *Leases*; measurements that have some similarities to fair value that are not fair value, such as net realizable value in IAS 2 *Inventories*; or value in use IAS 36 *Impairment of Assets*. This standard is effective for annual periods beginning on or after January 1, 2013. The Company does not anticipate the application of IFRS 13 to have a significant impact on its consolidated financial statements.

IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements*, and IFRS 12 *Disclosure of Interests in Other Entities: Transition Guidance*
The amendments provide additional transition relief, limiting the requirement to provide adjusted comparative information to only the preceding comparative period. For disclosures related to unconsolidated structured entities, the amendments will remove the requirement to present comparative information for periods before IFRS 12 is first applied. The effective date of the amendments is annual periods beginning on or after January 1, 2013, which is aligned with the effective date of IFRS 10, IFRS 11, and IFRS 12. The Company does not anticipate these amendments to have a significant impact on its consolidated financial statements.

IAS 19 *Employee Benefits*
On June 16, 2011, the IASB issued amendments to IAS 19, *Employee Benefits,* in order to improve the accounting for employment benefits.

The amendments make important improvements by:
- eliminating the option to defer the recognition of gains and losses, known as the 'corridor method' or the "deferral and amortization approach";
- streamlining the presentation of changes in assets and liabilities arising from defined benefit plans, including requiring re-measurements to be presented in OCI, thereby separating those changes from changes that many perceive to be the result of an entity's day-to-day operations;
- enhancing the disclosure requirements for defined benefit plans, providing better information about the characteristics of defined benefit plans and the risks that entities are exposed to through participation in those plans.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

u) New Accounting Standards (continued)

ii) New Accounting Standards Impacting on or after January 1, 2013 (continued)

IAS 19 *Employee Benefits (continued)*
The amendments are effective for financial years beginning on or after January 1, 2013. The Company does not anticipate the application of IFRS 13 to have a significant impact on its consolidated financial statements

IAS 27 *Separate Financial Statements*
IAS 27 has the objective of setting standards to be applied in accounting for investments in subsidiaries, jointly controlled entities, and associates when an entity elects, or is required by local regulations, to present separate (non-consolidated) financial statements. This standard is effective for annual periods beginning on or after January 1, 2013. This standard will not have an impact on the consolidated financial statements.

IAS 28 *Investments in Associates and Joint Ventures*
IAS 28 prescribes the accounting for investments in associates and to set the requirements for the application of the equity method when accounting for investments in associates and joint ventures. This standard is effective for annual periods beginning on or after January 1, 2013. This standard will not have an impact on the consolidated financial statements.

iii) New Accounting Standards Impacting on or after January 1, 2014

IAS 32 *Financial Instruments - Presentation in Respect of Offsetting* (Amendment)
The amendments to IAS 32 address inconsistencies in current practice when applying the requirements with regards to the offsetting of financial assets and financial liabilities. The amendments are effective for annual periods beginning on or after January 1, 2014 and are required to be applied retrospectively.

iv) New Accounting Standards Impacting on or after January 1, 2015

IFRS 9 *Financial Instruments - Classification and Measurement*

IFRS 9*, Financial Instruments:* IFRS 9 introduces the new requirements for the classification, measurement and de-recognition of financial assets and financial liabilities. The amendments are effective for annual periods beginning on or after January 1, 2015, with earlier application permitted.

t) Comparative figures

Certain comparative figures have been reclassified to conform to the presentation adopted for the current period. In particular: prepaid expenses are now reported separate from accounts receivable and other assets as prepaid expenses are not a financial instrument under IFRS 7; due from related parties are included separate from due to related parties as offsetting is not permitted under IAS 1; and, GST/HST and value added tax receivable are included with accounts receivable and other assets as permitted under IAS 1.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

t) Comparative figures (continued)

	Accounts receivable and other assets	**GST/HST and value added tax receivable**	**Prepaid expenses**	**Due from related parties**	**Due to related parties**
December 31, 2011	**$ 15,608**	**$ 4,777**	**$ -**	**$ -**	**$ 169**
Reclassifications	**3,559**	**(4,777)**	**1,218**	**36**	**36**
Adjusted December 31, 2011	**$ 19,167**	**-**	**$ 1,218**	**$ 36**	**$ 205**

3. Cash and Cash Equivalents

	December 31, 2012	December 31, 2011
Cash	**$ 18,038**	$ 25,652
Cash equivalents	**40,682**	13,078
	$ 58,720	$ 38,730

Cash and cash equivalents include cash on hand, demand deposits, and money market instruments, with maturities from the date of acquisition of 90 days or less.

4. Short Term Investments

	December 31, 2012	December 31, 2011
Held for trading short term investments	**$ 6,019**	$ 17,000

Short term investments include deposits with maturities from the date of acquisition of more than 90 days.

5. Derivative Assets and Derivative Liabilities

	December 31, 2012		December 31, 2011	
	Assets	**Liabilities**	Assets	Liabilities
Lead forward contracts	**$ -**	**$ -**	$ -	$ 53
Zinc forward contacts	**-**	**-**	70	-
Silver forward contracts	**-**	**-**	-	34
Total	**$ -**	**$ -**	$ 70	$ 87

The Company occasionally enters into forward commodity contracts as well as put and call option commodity arrangements to secure a minimum price level on part of its zinc and lead metal production. As at December 31, 2012, no such contracts are outstanding.

5. Derivative Assets and Derivative Liabilities (continued)

In 2011, the Company entered into short term forward and option contracts to fix the final settlement price of metal delivered in concentrates, where the final settlement price is yet to be set at a future quotational period according to contract terms. The forward sale and option contracts were settled against the arithmetic average of metal spot prices over the month in which the contract matures. No initial premium associated with these trades had been paid.

6. Accounts Receivable and Other Assets and Deposits on Long Term Assets

The current accounts receivables and other assets are comprised of the following:

		December 31, 2012		December 31, 2011
Current				
Trade receivables from concentrate sales	**$**	**15,158**	$	11,287
Current portion of long term receivables		**832**		891
Advances and other receivables		**3,637**		2,213
GST/HST and value added tax receivable		**7,405**		4,776
Accounts receivable and other assets	**$**	**27,032**	$	19,167

Deposits on long term assets include the non-current accounts receivable and other assets are comprised of the following:

		December 31, 2012		December 31, 2011
Non-Current				
Long term receivables	**$**	**1,557**	$	1,415
Less: current portion of long term receivables		**(832)**		(891)
Non-current portion of long term receivables		**725**		524
Deposits on equipment		**1,086**		1,167
Deposits paid to contractors		**744**		448
Other		**139**		121
Deposits on long term assets	**$**	**2,694**	$	2,260

As at December 31, 2012, the Company had $1,178 trade receivables (2011: $100) which were past due with no impairment. The Company's allowance for doubtful accounts is $nil for all reporting periods.

The aging analysis of these trade receivables from concentrate sales is as follows:

		December 31, 2012		December 31, 2011
0-30 days	**$**	**13,725**	$	9,518
31-60 days		**255**		911
61-90 days		**-**		758
over 90 days		**1,178**		100
	$	**15,158**	$	11,287

7. Inventories

	December 31, 2012	December 31, 2011

Concentrate stock piles	**$**	**2,918**	$	2,488
Ore stock piles		**3,391**		4,008
Materials and supplies		**6,549**		4,795
Total inventories	**$**	**12,858**	$	11,291

For the years ended December 31, 2012, $59,077 (2011: $31,655) of inventory was expensed in cost of sales and there has been no impairment during 2012 (2011: $nil).

8. Assets Held for Sale

Balance, December 31, 2011	$	-
Additions		63
Disposals		(12)
Total assets held for sale – December 31, 2012	**$**	**51**
Less current portion		**(51)**
Non current assets held for sale – December 31, 2012	**$**	**-**

As at December 31, 2012, the Company has $51 (2011: $nil) of equipment held for sale. Included in assets held for sale are a scoop and a front loader as the machinery is not being used in the mine operations and are expected to be sold within one year.

9. Mineral Properties, Plant and Equipment

	Mineral Properties Non-Depletable (Mario, Don Mario, Tlacolula)	Mineral Properties Depletable (Caylloma, San Jose, Taviche)	Machinery and Equipment	Land, Buildings, and Leasehold Improvements	Furniture and Other Equipment	Transport Units	Equipment under Finance Lease	Capital Work in Progress	Total
Year ended December 31, 2012									
Opening carrying amount	$ 7,311	$ 105,668	$ 17,316	$ 37,452	$ 3,185	$ 135	$ 2,520	$ 8,246	$ 181,833
Additions	2,566	24,849	5,384	138	1,462	129	653	15,778	50,959
Disposals	-	-	(1,097)	-	(22)	(5)	-	(50)	(1,174)
Write-off of mineral properties	(3,887)	-	-	-	-	-	-	-	(3,887)
Depletion and depreciation	-	(12,327)	(3,000)	(4,449)	(629)	(73)	(705)	-	(21,183)
Reclassification	(5,030)	5,030	444	2,653	(12)	-	-	(3,085)	-
Adjustment on currency translation	-	953	-	2	-	-	-	-	955
Closing carrying amount	**$ 960**	**$ 124,173**	**$ 19,047**	**$ 35,796**	**$ 3,984**	**$ 186**	**$ 2,468**	**$ 20,889**	**$ 207,503**
As at December 31, 2012									
Cost	$ 960	$ 157,054	$ 27,092	$ 44,004	$ 5,694	$ 539	$ 5,124	$ 20,889	$ 261,356
Accumulated depletion and depreciation	-	(32,881)	(8,045)	(8,208)	(1,710)	(353)	(2,656)	-	(53,853)
Closing carrying amount	**$ 960**	**$ 124,173**	**$ 19,047**	**$ 35,796**	**$ 3,984**	**$ 186**	**$ 2,468**	**$ 20,889**	**$ 207,503**

9. Mineral Properties, Plant and Equipment (continued)

	Mineral Properties Non-Depletable (Mario, Don Mario, Taviche, Tlacolula)	Mineral Properties Depletable (Caylloma, San Jose*)	Machinery and Equipment	Land, Buildings, and Leasehold Improvements	Furniture and Other Equipment	Transport Units	Equipment under Finance Lease	Capital Work in Progress	Total
Year ended December 31, 2011									
Opening carrying amount	$ 49,129	$ 33,608	$ 6.897	$ 7,013	$ 3,177	$ 112	$ 2,893	$ 14,534	$ 117,363
Additions	6,258	30,091	5,429	729	2,032	131	500	33,837	79,007
Disposals	-		(1,532)	-	(33)	-	-	-	(1,565)
Depletion and depreciation	-	(6,107)	(1,847)	(1,820)	(334)	(97)	(873)	-	(11,078)
Impairment charge	-		(1,688)	(195)	-	(11)	-	-	(1,894)
Reclassification	(48,076)	48,076	10,057	31,725	(1,657)	-	-	(40,125)	-
Closing carrying amount	**$ 7,311**	**$ 105,668**	**$ 17,316**	**$ 37,452**	**$ 3,185**	**$ 135**	**$ 2,520**	**$ 8,246**	**$ 181,833**
As at December 31, 2011									
Cost	7,311	125,667	$ 22,870	$ 41,212	$ 4,296	$ 520	$ 4,674	$ 8,246	$ 214,796
Accumulated depletion and depreciation	-	(19,999)	(5,554)	(3,760)	(1,111)	(385)	(2,154)	-	(32,963)
Closing carrying amount	**$ 7,311**	**$ 105,668**	**$ 17,316**	**$ 37,452**	**$ 3,185**	**$ 135**	**$ 2,520**	**$ 8,246**	**$ 181,833**

*Commercial production began on September 1, 2011 for San Jose.

As at December 31, 2012, the non-depletable mineral properties includes the Tlacolula property (2011: Mario, Don Mario, Tlacolula, and Taviche) as the Mario and Don Mario properties were abandoned and written off in 2012.

Mineral properties includes bonuses paid of $nil (2011: $1,350) which were paid upon commissioning of the San Jose mine. The bonus paid in 2011 comprises of $1,113 paid to key management and $237 paid to a company controlled by a director.

9. Mineral Properties, Plant and Equipment (continued)

a) Mario Property

In May 2011, the Company entered into an agreement to acquire a 100% interest in the Mario Property, located in the Department of Junin in central Peru. Under the terms of the agreement, the Company is granted the exclusive right and option to purchase an undivided 100% interest in the Mario Property subject to the following payments:

1. $500 on signing of agreement;
2. $500 on or before six months from the signing of the agreement;
3. $500 on or before 12 months from the signing of the agreement; and,
4. $2,500 on or before 24 months from the signing of the agreement.

The transfer of the property to the Company is subject to a 1% net smelter return ("NSR") royalty on production from the property payable to Crocodile Gold ("Crocodile"). The Company shall have the right to purchase the NSR royalty from Crocodile at any time during the five-year period following the final option payment for the sum of $3,000. The property is also subject to a 2% NSR royalty on production payable to Teck Cominco and a 0.5% NSR royalty on production payable to Socrate Capital Inc., with each royalty in turn subject to certain buy-back provisions. As at May 14, 2012, $1,000 had been paid under the agreement.

During the second quarter of 2012, upon completion of a 7,000 meter Phase I drill program at the Mario and Don Mario Properties ("Mario project"), the Company determined the program was not successful in demonstrating the potential to meet the minimum target size established for the project and the Company abandoned its interest in the Mario property resulting in a write-off of $3,627.

b) Don Mario Property

The Company entered into an option agreement, effective July 20, 2011, to acquire 100% interest in the Don Mario property, with Consorcio Empresarial Agmin S.A.C.("AGMIN"). Under the terms of the mining assignment and option to purchase mineral rights agreement ("agreement"), the Company is required to make the following payments:

1. $200 on signing the agreement;
2. $300 after 12 months from signing the agreement;
3. $500 after 24 months from signing the agreement; and,
4. $2,000 after 36 months from signing the agreement.

Under the terms of the agreement, once the option is exercised and the technical report is prepared under National Instrument 43-101 and published, if the pre-feasibility study indicates that the property contains more than five million silver equivalent ounces, the Company would further pay AGMIN, one dollar for each additional resource and reserves indicated in the pre-feasibility report. The Company has the option to buy-out the additional pay-out for a further $3,000, subject to certain conditions.

9. Mineral Properties, Plant and Equipment (continued)

b) Don Mario Property (continued)

As at May 14, 2012, $200 had been paid under the agreement. The Don Mario property is part of the overall Mario project and as the Phase 1 drill program at the Mario Property was not successful, the Company abandoned its interest in the Don Mario Property resulting in a write-off of $260.

c) Tlacolula Property

Pursuant to an agreement dated September 14, 2009, as amended December 18, 2012, the Company, through its wholly owned subsidiary, Cuzcatlan, was granted an option (the "Option") to acquire a 60% interest (the "Interest") in the Tlacolula silver project ("property") located in the State of Oaxaca, Mexico from Radius Gold Inc.'s wholly owned subsidiary, Radius (Cayman) Inc. ("Radius") (a related party by way of directors in common with the Company described further in Note 11).

The Company can earn the Interest by spending $2,000, which includes a commitment to drill 1,500 meters within 12 months after Cuzcatlan has received a permit to drill the property and making staged annual payments totalling $250 cash and providing $250 in common shares of the Company to Radius according to the following schedule:

- Ø $20 cash and $20 cash equivalent in shares upon stock exchange approval;
- Ø $30 cash and $30 cash equivalent in shares by January 15, 2011;
- Ø $50 cash and $50 cash equivalent in shares by January 15, 2012;
- Ø $50 cash and $50 cash equivalent in shares by the January 15, 2013; and,
- Ø $100 cash and $100 cash equivalent in shares within 90 days after Cuzcatlan has completed the first 1,500 meters of drilling on the property.

Upon completion of the cash payments and share issuances, and incurring the exploration expenditures as set forth above, the Company will be deemed to have exercised the Option and acquired a 60% interest in the property, whereupon a joint venture will be formed to further develop the property on the basis of the Company owning 60% and Radius 40%.

On January 15, 2010, the transaction was approved by the TSX Venture Exchange, The Company has issued 7,813 common shares at a fair market value of $2.56 per share and paid $20 cash according to the terms of the option agreement.

On January 14, 2011, the Company issued 6,756 common shares of the Company, at a fair market value of $4.44 per share and paid $30 cash according to the terms of the option agreement.

On January 13, 2012, the Company issued 8,605 common shares of the Company, at a fair market value of $5.81 per share and paid $50 cash according to the terms of the option agreement.

9. Mineral Properties, Plant and Equipment (continued)

c) Tlacolula Property (continued)

As at December 31, 2012, the Company had issued a total of 23,174 common shares of the Company, with a fair market value of $100 and paid $100 cash according to the terms of the option agreement.

Subsequent to December 31, 2012, on January 15, 2013, the Company issued 11,415 common shares of the Company, at a fair market value of $4.38 per share and on January 14, 2013 paid $50 cash according to the terms of the option agreement.

d) Taviche Property

In 2010, the Company included the idle plant in Taviche as part of the San Jose mine plant as it was more likely than not that the idle plant could be used to treat excess ore from San Jose or from surrounding areas where the company was conducting exploration. On September 1, 2011, the San Jose mine plant commenced commercial production and in the fourth quarter of 2011, achieved an average of 955 tonnes milled per day with the San Jose plant having sufficient capacity for the production. In the fourth quarter of 2011, management reassessed the usability of the idle plant and in conjunction, obtained an independent third party appraisal of various assets acquired under an asset purchase agreement dated 2007 related to the Taviche property.

Management used the fair value less cost to sell method to determine the recoverable amount of the idle plant. Based upon an independent appraisal of the assets, which is in accordance with fair value less cost to sell, the Company took an impairment

charge, in 2011, of $1.89 million that comprised of the following impairments: $1.08 million on the tailing dam, $0.14 million on the mine infrastructure, and $0.67 million on equipment, machinery, and buildings. As at December 31, 2011, the net book value of assets related to the Taviche property for machinery and equipment amounted to $0.36 million.

e) Taviche Oeste Concessions

Subsequent to December 31, 2012, on February 4, 2013, the Company, through its wholly owned subsidiary, Cuzcatlan, acquired, through an option agreement (the "Option") with Plata Pan American S.A. de C.V. ("Plata") (a wholly owned subsidiary of Pan American Silver Corp.), a 55% undivided interest in 6,254 hectare Taviche Oeste Concessions ("concessions") immediately surrounding the San Jose Mine in Oaxaca, Mexico. The Company made a cash payment of $4.0 million. Once a production decision is made to develop ore from the concessions, the Company, through its wholly owned subsidiary, Cuzcatlan, will purchase the remaining 45% undivided interest in the property for $6.0 million. Plata will retain a 2.5% net smelter royalty on ore production from this property.

f) San Luisito Concessions

Subsequent to December 31, 2012, in February 2013, the Company through its wholly owned subsidiary, Cuzcatlan, acquired, was granted an option (the "Option"), with a third party, on concessions in the San Luisito Project, Sonora, Mexico and made a cash payment of $50. Further payments due are as follows : August 26, 2013 $150, February 24, 2014 $400, February 24, 2015 $1,000, February 26, 2016 $1,400, and February 26, 2017 $12,000. The third party will retain a 2% net smelter royalty on ore produced from this property.

10. Trade and Other Payables

	December 31, 2012	December 31, 2011
Trade accounts payable	**$ 11,114**	$ 8,799
Payroll payable	**4,238**	5,809
Restricted share unit payable	**648**	1,204
Other payables	**1,348**	1,343
	$ 17,348	$ 17,155

11. Related Party Transactions

a) Purchase of Goods and Services

The Company entered into the following related party transactions:

	Years ended December 31,	
Transactions with related parties	**2012**	2011
Salaries and wages [1,2]	**$ 135**	$ 173
Other general and administrative expenses [2]	**308**	292
Leasehold improvements [2]	**23**	93
	$ 466	$ 558

[1] Salaries and wages includes employees' salaries and benefits charged to the Company based on a percentage of the
estimated hours worked for the Company

[2] Radius Gold Inc. ("Radius") has directors in common with the Company and shares office space, and is reimbursed for salaries, wages, general administration costs, and leasehold improvements incurred on behalf of the Company to June 30, 2012. Gold Group Management Inc. ("Gold Group"), which is owned by a director in common with the Company, provides various administrative, management, and other related services effective July 1, 2012.

In January 2012, the Company issued 8,605 (2011: 6,756) common shares, at a fair market value of $5.81 (2011: $4.44) per share and paid $50 (2011: $30) cash to Radius, under the option to acquire a 60% interest in Tlacolula silver project located in the State of Oaxaca, Mexico.

In October 2012, the Company entered into a services agreement, effective July 1, 2012, with Gold Group Management Inc. ("Gold Group"), which is owned by a director in common with the Company. The services agreement provides that Gold Group

provides various administrative, management and other related services.

Subsequent to December 31, 2012 to March 19, 2013 the Company issued 11,415 common shares of the Company, at a fair market value of $4.38 per share and paid $50 cash to Radius, under the option to acquire a 60% interest in the Tlacolula silver project located in the State of Oaxaca, Mexico.

11. Related Party Transactions (continued)

b) Key Management Compensation

Key management includes all persons named or performing the duties of Vice-President, Chief Financial Officer, President, Chief Executive Officer, and non-executive Directors of the Company. The compensation paid and payable to key management for services is shown below:

	Years ended December 31,	
	2012	2011
Salaries and other short term employee benefits	**$ 2,789**	$ 3,492
Directors fees	**388**	333
Consulting fees	**180**	416
Share-based payments	**1,629**	4,398
	$ 4,986	$ 8,639

The share-based payments includes the change in the DSU and RSU fair value over each reporting period and payments made under the DSU and RSU plans and the non-cancellation of share options.

Consulting fees includes fees paid to two non-executive directors in both 2012 and 2011.

c) Year end Balances arising from Purchases of Goods/Services

Amounts due from related parties	**December 31, 2012**	December 31, 2011
Owing from a director and officer [3]	**$ -**	$ 36
Owing from a company with common director [3]	**5**	-
	$ 5	$ 36

[3] Owing from a director includes non-interest bearing advances to company controlled by a director of the company at December 31, 2012 and to director and officers at December 31, 2011.

Amounts due to related parties	**December 31, 2012**	December 31, 2011
Owing to a company(ies) with common directors [4]	**$ 54**	$ 205

[4] 2012 Owing to Radius Gold Inc. ("Radius") and Gold Group Management Inc. ("Gold Group") whom have directors in common with the Company and 2011 to Radius.

On October 10, 2012, the Company paid Gold Group Management Inc., which is owned by a director in common with the Company, a retainer of $61 representing three months deposit under a services agreement effective July 1, 2012.

12. Leases and Long Term Liabilities

Leases and long term liabilities are comprised of the following:

	December 31, 2012	December 31, 2011
Obligations under finance lease (a)	**$ 676**	**$** 866
Long term liability (b)	**19**	771
Deferred share units (Note 15 c))	**2,004**	2,639
	2,699	4,276
Less: current portion		
Obligations under finance lease	**449**	741
Long term liability	**-**	771
Current portion of leases and long term liabilities	**449**	1,512
Leases and long term liabilities, non-current	**$ 2,250**	**$** 2,764

a) Obligations under Finance Lease

The following is a schedule of the Company's future minimum lease payments. These are related to the acquisition of mining equipment, and vehicles, and buildings.

Obligations under Finance Lease	December 31, 2012	December 31, 2011
Not later than 1 year	**$ 469**	763
Less: future finance charges on finance lease	**(20)**	(22)
	449	741
Later than 1 year but less than 5 years	**231**	126
Less: future finance charges on finance lease	**(4)**	(1)
	227	125
Present value of finance lease payments	**$ 676**	$ 866

b) **Long Term Liabilities**

In May 2008, the Company acquired the Monte Alban II concession for which a payment of $800 was due May 2012. This liability is non-interest bearing and the principal was paid during the second quarter of 2012.

The Company's Mexican operation is required to provide a seniority premium to all employees as required under Mexican labor law. This liability is calculated using actuarial techniques and discounting the benefit using the Projected Unit Credit Method with the following assumptions: a discount rate of 7.50%, wages increases ranging from 4.5% to 5.0%, minimum wage increase of 4.0%, and a long term inflation rate of 4.0%. During the year ended December 31, 2012, $20 (2011: $nil) has been recognized as an expense, respectively.

13. Provisions

A summary of the Company's provisions for other liabilities and charges is presented below:

	Decommissioning and Restoration Liability		
	Caylloma Mine	**San Jose Mine**	**Total**
Total provisions – December 31, 2010	$ 3,298	$ 1,583	$ 4,881
Increase to existing provisions	119	7	126
Accretion of provisions	138	35	173
Foreign exchange differences	142	(147)	(5)
Cash payments	(201)	-	(201)
Total provisions – December 31, 2011	$ 3,496	$ 1,478	$ 4,974
Less: current portion	(501)	(226)	(727)
Non current - December 31, 2011	$ 2,995	$ 1,252	$ 4,247
Total provisions - December 31, 2011	**$ 3,496**	**$ 1,478**	**$ 4,974**
Increase to existing provisions	**3,954**	**1,680**	**5,634**
Accretion of provisions	**124**	**108**	**232**
Foreign exchange differences	**(129)**	**102**	**(27)**

Cash payments		**(386)**	**-**	**(386)**
Total provisions – December 31, 2012	**$**	**7,059**	**$ 3,368**	**$ 10,427**
Less: current portion		**(111)**	**(346)**	**(457)**
Non current – December 31, 2012	**$**	**6,948**	**$ 3,022**	**$ 9,970**

In view of the uncertainties concerning environmental reclamation, the ultimate cost of reclamation activities could differ materially from the estimated amount recorded. The estimate of the Company's decommissioning and restoration liability relating to the Caylloma and San Jose mine is subject to change based on amendments to laws and regulations and as new information regarding the Company's operations becomes available.

Future changes, if any, to the estimated liability as a result of amended requirements, laws, regulations, operating assumptions, estimated timing and amount of obligations may be significant and would be recognized prospectively as a change in accounting estimate. Any such change would result in an increase or decrease to the liability and a corresponding increase or decrease to the mineral properties, plant and equipment balance.

14. Income Tax

a) Income tax expense differs from the amount that would be computed by applying the Canadian statutory income tax rate of 25.00% (2011: 26.50%) to income before income taxes. The reasons for the differences are as follows:

		December 31, 2012	December 31, 2011
Income before tax	**$**	**45,226**	$ 38,335
Statutory income tax rate		**25.00%**	26.50%
Expected income tax	**$**	**11,307**	$ 10,159
Items non-deductible for income tax purposes		**1,155**	1,401
Difference between Canadian and foreign tax rates		**2,354**	1,376
Effect of change in tax rates		**(796)**	620
Impact of foreign exchange on tax assets and liabilities		**(1,580)**	3,271
Impact of Mexican inflation on tax values		**(193)**	(16)
Other items		**(70)**	704
Unused tax losses and tax offsets not recognized in tax asset		**1,586**	1,287
Total income taxes	**$**	**13,763**	$ 18,802
Represented by:			
Current income tax	**$**	**5,508**	$ 14,607
Deferred income tax		**8,255**	4,195
	$	**13,763**	$ 18,802

The effective tax rate for the years ended December 31, 2012 and 2011 was 30.43% and 49.05%, respectively. The change in the effective tax rate was primarily attributable to the geographical mix of income, fluctuations in exchange rates for foreign currency, the impact of foreign exchange on the tax basis on non-monetary assets, and the non-recognition of tax benefits.

Effective January 1, 2012, the Canadian Federal corporate tax rate decreased from 16.5% to 15.0% and the British Columbia provincial tax remained the same at 10%. The overall reduction in tax rates has resulted in a decrease in the Company's statutory tax rate from 26.50% to 25.00%.

In 2009, the Mexican government approved tax reform that includes a 2% increase in the income tax rate in Mexico from 28% to 30% for a three-year period starting in 2010.

The Mexican corporate tax rate was scheduled to be reduced from 30% to 29% on January 1, 2013 and then to 28% on January 1, 2014. However, newly enacted legislation maintains the 2012 rate of 30% through the end of 2013, with a reduction to 29% on January 1, 2014 and an additional reduction to 28% on January 1, 2015.

Income taxes payable of $200 (December 31, 2011: $3,923) relates to current taxes.

14. Income Tax (continued)

b) The tax effected items that give rise to significant portions of the deferred income tax assets and deferred income tax liabilities at December 31, 2012 and 2011 are presented below:

		December 31, 2012		December 31, 2011
Deferred income tax assets:				
Non-capital losses	**$**	**2,431**	$	12,544
Provisions and other		**4,059**		2,059
Other		**78**		5
Mineral properties, plant and equipment		**-**		296
Net deferred income tax assets		**6,568**		14,904
Deferred income tax liabilities:				
Mineral properties – Peru	**$**	**(14,314)**	$	(11,790)
Mineral properties – Mexico		**(3,452)**		(5,640)
Equipment		**(9,731)**		(10,148)
Total deferred income tax liabilities	**$**	**(27,497)**	$	(27,578)
Net deferred income tax liabilities	**$**	**(20,929)**	$	(12,674)
Classification				
Non-current assets	**$**	**113**	$	36
Non-current liabilities		**(21,042)**		(12,710)
Net deferred income tax liabilities	**$**	**(20,929)**	$	(12,674)

c) The Company recognizes tax benefits on losses or other deductible amounts generated in countries where the probable criteria for the recognition of deferred tax assets has been met. The Company's unrecognized deductible temporary differences and unused tax losses for which no deferred tax asset is recognized consist of the following amounts:

		December 31, 2012		December 31, 2011
Non-capital losses	**$**	**47,124**	$	38,503
Provisions and other		**2,652**		3,841
Share issue cost		**1,947**		2,913
Investment in subsidiaries		**1,283**		56
Mineral properties, plant and equipment		**1,467**		1,532
Unrecognized deductible temporary differences	**$**	**54,473**	$	46,845

FORTUNA SILVER MINES INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011
(All amounts in US$'000's unless otherwise stated)

14. Income Tax (continued)

c) (continued)

The Company's unrecognized taxable temporary difference consists of the following amounts:

		December 31, 2012		December 31, 2011
Withholding tax	**$**	**505**	$	147
Unrecognized taxable temporary difference	**$**	**505**	$	147

The Company's tax losses have the following expiry dates:

			Expiry date
Non-capital losses, expiring as follows:			
Canada	$	43,906	2013 - 2032
Mexico		11,321	2016 - 2032
	$	**55,227**	

15. Share Capital

a) Unlimited Common Shares Without Par Value

During the year ended December 31, 2012, the Company issued 8,605 (2011: 6,756) common shares, at a fair market value of $5.81 (2011: $4.44) per share to Radius Gold, under the option to acquire a 60% interest in Tlacolula silver project located in the State of Oaxaca, Mexico. (Refer to Note 9. c)).

Subsequent to December 31, 2012 to March 19, 2013, the Company issued 11,415 common shares of the Company, at a fair market value of $4.38 per share and paid $50 cash to Radius, under the option to acquire a 60% interest in the Tlacolula silver project located in the State of Oaxaca, Mexico. (Refer to Note 9. c)).

b) Share Options

Shareholder approval of the Company's Stock Option Plan (the "Plan"), dated April 11, 2011, was obtained at the Company's annual general meeting held on May 26, 2011. The Plan provides that the number of common shares of the Company issuable under the Plan, together with all of the Company's other previously established or proposed share compensation arrangements, may not exceed 12,200,000 shares, which equals 9.92% of the current total number of issued and outstanding common shares of the Company, as at April 11, 2011.

Option pricing models require the input of highly subjective assumptions including the estimate of the share price volatility, risk-free interest rate and expected life of the options. Changes in the subjective input assumptions can materially affect the fair value estimate.

15. Share Capital (continued)

b) Share Options (continued)

The following is a summary of share option transactions:

	December 31, 2012		December 31, 2011	
	Shares (in 000's)	**Weighted average exercise price (CAD$)**	Shares (in 000's)	Weighted average exercise price (CAD$)
Outstanding at beginning of the year	**3,876**	**$ 2.83**	4,551	$ 1.51
Granted	**2,613**	**4.18**	1,792	4.46
Exercised	**(314)**	**2.35**	(2,442)	1.55
Forfeited	**(50)**	**4.46**	(25)	4.46
Expired	**(8)**	**4.46**	-	-
Outstanding at end of the year	**6,117**	**$ 3.42**	3,876	$ 2.83
Vested and exercisable at end of the year	**3,081**	**$ 2.63**	2,557	$ 1.99

During the year ended December 31, 2012, 2,612,459 share purchase options were granted with exercise prices ranging from CAD$3.79 to CAD$6.67 with terms ranging from three and five years, respectively. The vesting of 2,047,542 share purchase options are as follows: 50% after twelve months of grant date and a further 50% after twenty four months of grant date. The vesting of 184,138 share purchase options are as follows: 33.33% after twelve months of grant date, a further 33.33% after twenty four months of grant date, and a further 33.34% after thirty six months of grant date. The vesting of 380,779 share purchase options are as follows: 33.33% after twelve months of grant date, a further 33.33% after twenty-four months of grant date, and a further 33.34% after thirty-six months of grant date.

During the year ended December 31, 2012, 49,628 share purchase options were forfeited, 41,542 share purchase options were accelerated to expire March 30, 2012, and 8,271 share purchase options expired unexercised.

Subsequent to December 31, 2012, 25,000 share purchase options were accelerated to expire March 31, 2013 from January 11, 2017.

Subsequent to December 31, 2012 to March 19, 2013, 25,000 share purchase options were exercised at CAD$0.85 resulting in issued and outstanding shares of 125,305,166.

The share-based payment charge of $2,977 (2011: $1,830) covering option grants, forfeitures, and accelerated vesting recognized for the year ended December 31, 2012 has been determined under the fair value method using the Black-Scholes option pricing model with the following assumptions:

15. Share Capital (continued)

b) Share Options (continued)

	Years ended December 31,	
	2012	2011
Risk-free interest rate	**1.00% to 1.62%**	**1.91%**
Expected stock price volatility	**55.93% to 58.36%**	**56.48%**
Expected term in years	**3**	**3**
Expected dividend yield	**0%**	**0%**
Expected forfeiture rate	**4.15%**	**1.38%**

The expected volatility assumption is based on the historical volatility of the Company's Canadian dollar common share price on the Toronto Stock Exchange.

The following table summarizes information related to stock options outstanding and exercisable at December 31, 2012:

Exercise price in CAD$	Number of outstanding share purchase options (in 000's)	Weighted average remaining contractual life of outstanding share purchase options (years)	Weighted average exercise price on outstanding share purchase options CAD$	Exercisable share purchase options (in 000's)	Weighted average exercise price on exercisable share purchase options CAD$
$0.80 to $0.99	781	5.8	$ 0.84	781	$ 0.84
$1.00 to $1.99	660	3.4	1.53	660	1.53
$2.00 to $6.67	4,676	2.4	4.11	1,640	3.92
$0.80 to $4.46	6,117	3.0	$ 3.42	3,081	$ 2.63

The weighted average remaining life of vested share purchase options at December 31, 2012 was 3.3 years (2011: 4.9 years).

c) Deferred Share Units ("DSU") Cost

During 2010, the Company implemented a DSU plan which allows for up to 1% of the number of shares outstanding from time to time to be granted to eligible directors. All grants under the plan are fully vested upon credit to an eligible directors' account.

During the year ended December 31, 2011, the Company granted 48,824 DSU with a market value of CAD$232, at the date of grant, to a director, and 93,544 DSU with a market value of CAD$473, at the date of grant, to a director, with vesting subject to the commissioning of the San Jose mine, which occurred on September 1, 2011. During the year ended December 31, 2011, 70,000 DSU were settled in cash for $5.36 per unit for a total payment of $375.

15. Share Capital (continued)

c) Deferred Share Units ("DSU") Cost (continued)

During the year ended December 31, 2012, there were no DSU grants or settlements in cash. As at December 31, 2012, there are 481,465 (2011: 481,465) DSU outstanding with a fair value of $2,004 (2011: $2,639).

d) Restricted Share Units ("RSU") Cost

During 2010, the Company implemented a RSU plan for certain employees or officers. The RSU entitle employees or officers to a cash payment after the end of a performance period of up to two years following the date of the award. The RSU payment will be an amount equal to the fair market value of the Company's common share on the five trading days immediately prior to the end of the performance period multiplied by the number of RSU held by the employee.

During the year ended December 31, 2011, the Company granted 155,674 RSU with a market value of CAD$788, at the date of grant, to a director, with vesting subject to the commissioning of the San Jose mine, which occurred on September 1, 2011.

During the year ended December 31, 2012, there were no RSU grants and the Company paid $583 (2011: $736) on 109,557 (2011: 109,557) RSU to directors and officers of the Company. As at December 31, 2012, there are 155,674 (2011: 265,231) RSU outstanding with a fair value of $648 (2011: $1,204). Refer to Note 10.

e) Earnings per Share

i. Basic

Basic earnings per share is calculated by dividing the income for the year by the weighted average number of shares outstanding during the year.

The following table sets forth the computation of basic earnings per share:

		Years ended December 31,		
		2012		2011
Income available to equity owners	**$**	**31,463**	$	19,533
Weighted average number of shares (in '000's)		**123,585**		123,295
Earnings per share - basic	**$**	**0.25**	$	0.16

15. Share Capital (continued)

e) Earnings per Share (continued)

ii. Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of shares outstanding to assume conversion of all potentially dilutive shares. The following table sets forth the computation of diluted earnings per share:

		Years ended December 31,		
		2012		2011
Income available to equity owners	**$**	**31,463**	$	19,533
Weighted average number of shares ('000's)		**123,585**		123,295
Incremental shares from share options		**1,648**		1,417

Weighted average diluted shares outstanding ('000's)		**125,233**		124,712
Earnings per share - diluted	**$**	**0.25**	$	0.16

For the year ended December 31, 2012, excluded from the calculation were 184,138 (2011: $nil) anti-dilutive options with an exercise price of CAD$6.67 (2011: $nil).

16. Supplemental Cash Flow Information

	Note	Years ended December 31, 2012	2011
Non-cash Investing and Financing Activities:			
Issuance of shares on purchase of mineral properties, property, plant and equipment	**9 c)**	**$ 50**	$ 30

17. Capital Disclosure

The Company's objectives when managing capital are to provide shareholder returns through maximization of the profitable growth of the business and to maintain a degree of financial flexibility relevant to the underlying operating and metal price risks while safeguarding the Company's ability to continue as a going concern.

The capital of the Company consists of equity and available credit facility, net of cash. The Board of Directors does not establish a quantitative return on capital criteria for management. The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets.

The management of the Company believes that the capital resources of the Company as at December 31, 2012, are sufficient for its present needs for at least the next 12 months. The Company is not subject to externally imposed capital requirements.

The Company's overall strategy with respect to capital risk management remained unchanged during the year.

18. Management of Financial Risk

The Company is exposed to certain financial risks, including currency risk, credit risk, liquidity risk, interest risk, and price risk. The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework and reviews the Company's policies on an ongoing basis.

a) Fair Value of Financial Instruments

The carrying value of cash and cash equivalents, short term investments, derivative assets, trade receivable from concentrate sales, other accounts receivables, due from related parties, trade and other payables, due to related parties, and derivative liabilities approximate their fair value due to the relatively short periods to maturity and the terms of these financial instruments. Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument.

The amortized value of long term receivables approximates their fair value as these are measured at the amortized cost using the effective interest method. The fair value of the lease and long term liabilities is $2,723 as at December 31, 2012.

The analysis of financial instruments that are measured subsequent to initial recognition at fair value can be categorized into Levels 1 to 3 based upon the degree to which the fair value is observable.

- Level 1 - inputs to the valuation methodology are quoted (unadjusted) for identical assets or liabilities in active markets.
- Level 2 - inputs to valuation methodology include quoted market prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 - inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The Company has classified the determination of fair value of trade receivable from concentrate sales, and derivatives as Level 2, as the valuation method used by the Company includes an assessment of assets in quoted markets with significant observable inputs.

	Financial assets (liabilities) at fair value as at December 31, 2012			
	Level 1	**Level 2**	**Level 3**	**Total**
Cash and cash equivalents	**$ 58,720**	**$ -**	**$ -**	**$ 58,720**
Short term investments	**6,019**	**-**	**-**	**6,019**
Trade receivable from concentrate sales	**-**	**15,158**	**-**	**15,158**
	$ 64,739	**$ 15,158**	**$ -**	**$ 79,897**

There were no changes in the levels during the year ended December 31, 2012.

18. Management of Financial Risk (continued)

a) Fair Value of Financial Instruments (continued)

	Financial assets (liabilities) at fair value as at December 31, 2011			
	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	$ 38,730	$ -	$ -	$ 38,730
Short term investments	17,000	-	-	17,000
Trade receivable from concentrate sales	-	11,287	-	11,287
Derivatives assets	-	70	-	70
Derivatives liabilities	-	(87)	-	(87)
	$ 55,730	$ 11,270	$ -	$ 67,000

There were no changes in the levels during the year ended December 31, 2011.

Accounts receivable includes trade receivable from concentrate sales, provisional price adjustments, and final price adjustments. The fair value of accounts receivable resulting from provisional pricing reflect observable market commodity prices. Resulting fair value changes to accounts receivable are through sales. Transactions involving accounts receivable are with counterparties the Company believes are creditworthy. As such, these accounts receivable are classified within Level 2 of the fair value hierarchy.

Derivatives are carried at their fair value, which is determined based on internal valuation models that reflect observable forward market commodity prices. Resulting fair value changes to derivatives are through net gain (loss) on commodity contracts. Transactions involving derivatives are with counterparties the Company believes to be creditworthy.

During the year ended December 31, 2012, there have been no changes in the classification of financial assets and liabilities in Levels 1, 2, and 3 of the hierarchy.

b) Currency Risk

The Company is exposed to the financial risk related to the fluctuation of foreign exchange rates. The Company operates in Canada, Peru and Mexico and a portion of its expenses are incurred in Canadian dollars, nuevo soles, and Mexican pesos. A significant change in the currency exchange rates between the United States dollar relative to the other currencies could have a material effect on the Company's income, financial position, or cash flows. The Company has not hedged its exposure to currency fluctuations.

18. Management of Financial Risk (continued)

b) Currency Risk (continued)

As at December 31, 2012, the Company is exposed to currency risk through the following assets and liabilities denominated in Canadian dollars, nuevo soles and Mexican pesos (all amounts are expressed in thousands of Canadian dollars, thousands of nuevo soles or thousands of Mexican pesos):

	December 31, 2012			December 31, 2011		
	Canadian Dollars	**Nuevo Soles**	**Mexican Pesos**	Canadian Dollars	Nuevo Soles	Mexican Pesos
Cash and cash equivalents	**$ 4,231**	**S/. 1,389**	**$ 6,136**	$ 18,457	S/. 1,396	$ 1,758
Short term investments	**6,000**	**-**	**-**	-	-	-
Accounts receivable and other assets	**77**	**3,097**	**98,147**	42	5,657	58,939
Due from related parties	**-**	**-**	**-**	-	4,434	-
Trade and other payables	**(1,225)**	**(12,300)**	**(49,779)**	(1,580)	(17,993)	(24,310)
Due to related parties	**(54)**	**-**	**-**	(209)	-	-
Provisions, current	**-**	**(284)**	**(4,502)**	-	(1,351)	(3,163)
Income tax payable	**-**	**(326)**	**-**	-	(10,581)	-
Leases and long term liabilities	**(1,998)**	**-**	**(245)**	(2,691)	-	-
Provisions	**-**	**(19,560)**	**(39,323)**	-	(8,079)	(17,494)
Total	**$ 7,031**	**S/. (27,984)**	**$ 10,434**	$ 14,019	S/. (26,517)	$ 15,730
Total US$ equivalent	**$ 7,053**	**$ (10,970)**	**$ 802**	$ 13,745	$ (9,832)	$ 1,125

Based on the above net exposure as at December 31, 2012, and assuming that all other variables remain constant, a 10% depreciation or appreciation of the US dollar against the above currencies would result in an increase or decrease, as follows: impact to other comprehensive income of $784 (2011: $1,527) and a net loss of $1,130 (2011: net loss $967).

c) Credit Risk

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations. The Company's cash and cash equivalents and short term investments are held through large Canadian, international and foreign national financial institutions. These investments mature at various dates within one year. All of the Company's trade accounts receivables from concentrate sales are held with large international metals trading companies.

The Company holds derivative contracts with financial institutions and in this regard is exposed to counterparty risk. The Company mitigates this risk by transacting only with reputable financial institutions to minimize credit risk.

The Company's maximum exposure to credit risk as at December 31, 2012 is as follows:

18. Management of Financial Risk (continued)

c) Credit Risk (continued)

	December 31, 2012	December 31, 2011
Cash and cash equivalents	**$ 58,720**	$ 38,730
Short term investments	**6,019**	17,000
Accounts receivable and other assets	**27,032**	19,167
Derivative assets	**-**	70
Due from related parties	**5**	36
	$ 91,776	$ 75,003

The carrying amount of financial assets recorded in the financial statements represents the Company's maximum exposure to credit risk. The Company believes it is not exposed to significant credit risk and overall, the Company's credit risk has not declined significantly from the prior year.

d) 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 by continuing to monitor forecasted and actual cash flows. The Company has in place a planning and budgeting process to help determine the funds required to support the Company's normal operating requirements on an ongoing basis and its development plans. The Company strives to maintain sufficient liquidity to meet its short term business requirements, taking

into account its anticipated cash flows from operations, its holdings of cash, short term investments, and its committed liabilities.

The Company expects the following maturities of its financial liabilities (including interest), finance leases, and other contractual commitments:

	Expected payments due by period as at December 31, 2012				
	Less than 1 year	1 - 3 years	4 - 5 years	After 5 years	Total
Trade and other payables	$ 17,348	$ -	$ -	$ -	$ 17,348
Due to related parties	54	-	-	-	54
Income tax payable	200	-	-	-	200
Long term liabilities	469	2,254	-	-	2,723
Operating leases	702	1,305	886	147	3,040
Provisions	528	519	459	11,333	12,839
	$ 19,301	**$ 4,078**	**$ 1,345**	**$ 11,480**	**$ 36,204**

Operating leases includes leases for office premises, computer and other equipment used in the normal course of business. Refer to Note 24 c) for details of operating leases.

18. Management of Financial Risk (continued)

d) Liquidity Risk (continued)

In 2010, the Company entered into a credit agreement with the Bank of Nova Scotia for a $20 million senior secured revolving credit facility ("credit facility") to be refinanced or repaid on or within two and one-half years or before February 6, 2013. The credit facility is secured by a first ranking lien on Bateas and its assets and bears interest and fees at prevailing market rates. In the event that utilization under the credit facility is less than $10 million, a commitment fee of 1.50% per annum is payable quarterly on the unutilized portion of the available credit facility. No funds have been drawn from this credit facility.

Subsequent to December 31, 2012, in February 2013 the Bank of Nova Scotia extended the credit facility maturity date to February 6, 2013 and then to February 27, 2013. On March 15, 2013, the Bank of Nova Scotia extended the credit facility maturity date to March 28, 2013. No funds were drawn from this credit facility.

e) Interest Rate Risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The risk that the Company will realize a loss as a result of a decline in the fair value is limited because the balances are generally held with major financial institutions in demand deposit accounts.

A 10% change in interest rates would cause a $nil change in income on an annualized basis.

f) Metal Price Risk

The Company is exposed to metals price risk with respect to silver, gold, zinc, lead, and copper sold through its mineral concentrate products. The Company mitigates this risk by implementing price protection programs for some of its zinc and lead production through the use of derivative instruments. As a matter of policy, the Company does not hedge its silver production.

19. Segmented Information

All of the Company's operations are within the mining sector, conducted through operations in three countries. Due to geographic and political diversity, the Company's mining operations are decentralized whereby management are responsible for achieving specified business results within a framework of global policies and standards. Country corporate offices provide support infrastructure to the mine in addressing local and country issues including financial, human resources, and exploration support.

19. Segmented Information (continued)

Products are silver, gold, lead, zinc and copper produced from mines in Peru and Mexico, as operated by Bateas and Cuzcatlan, respectively. Segments have been aggregated where operations in specific regions have similar products, production processes, types of customers and economic environment.

The Company's operating segments are based on the reports reviewed by the senior management group that are used to make strategic decisions. The Chief Executive Officer considers the business from a geographic perspective considering the performance of the Company's business units. The segment information for the reportable segments for the years ended December 31, 2012 and 2011 are as follows:

Reportable Segments	**Corporate**	**Bateas**	**Cuzcatlan**	**Total**
Year ended December 31, 2012				
Sales to external customers	**$ -**	**$ 83,697**	**$ 77,323**	**$ 161,020**
Silver-gold concentrates	**$ -**	**$ -**	**$ 77,323**	**$ 77,323**
Silver-lead concentrates	**$ -**	**$ 68,616**	**$ -**	**$ 68,616**
Zinc concentrates	**$ -**	**$ 15,081**	**$ -**	**$ 15,081**
Sales to internal customers	**$ 8,379**	**$ -**	**$ -**	**$ 8,379**
Cost of sales*	**$ -**	**$ 51,231**	**$ 39,127**	**$ 90,358**
Depletion and depreciation**	**$ 284**	**$ 8,961**	**$ 12,127**	**$ 21,372**
Selling, general and administrative expenses*	**$ 13,594**	**$ 3,337**	**$ 3,610**	**$ 20,541**
Exploration and evaluation costs	**$ 777**	**$ -**	**$ -**	**$ 777**
Write-off of mineral properties	**$ -**	**$ 3,887**	**$ -**	**$ 3,887**
Other material non-cash items	**$ 2**	**$ (1)**	**$ (51)**	**$ (50)**
Interest income	**$ 156**	**$ 394**	**$ 70**	**$ 620**
Interest expense	**$ 300**	**$ 154**	**$ 108**	**$ 562**
Income (loss) before tax	**$ (14,514)**	**$ 25,396**	**$ 34,344**	**$ 45,226**
Income taxes	**$ 272**	**$ 6,521**	**$ 6,970**	**$ 13,763**
Income (loss) for the year	**$ (14,786)**	**$ 18,875**	**$ 27,374**	**$ 31,463**
Capital expenditures	**$ 525**	**$ 29,566**	**$ 20,868**	**$ 50,959**

* cost of sales and selling, general and administrative expenses includes depletion and depreciation
** included in cost of sales or selling, general and administrative expenses

FORTUNA SILVER MINES INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011
(All amounts in US$'000's unless otherwise stated)

19. Segmented Information (continued)

Reportable Segments	**Corporate**	**Bateas**	**Cuzcatlan**	**Total**
Year ended December 31, 2011				
Sales to external customers	$ -	$ 97,740	$ 12,264	$ 110,004
Silver-gold concentrates	$ -	$ -	$ 12,264	$ 12,264
Silver-lead concentrates	$ -	$ 80,689	$ -	$ 80,689
Zinc concentrates	$ -	$ 15,290	$ -	$ 15,290
Copper concentrates	$ -	$ 1,761	$ -	$ 1,761
Sales to internal customers	$ 5,961	$ -	$ -	$ 5,961
Cost of sales*	$ -	$ 42,236	$ 6,794	$ 49,030
Depletion and depreciation**	$ 100	$ 7,053	$ 2,268	$ 9,421
Selling, general and administrative expenses*	$ 14,352	$ 3,920	$ 1,568	$ 19,840
Exploration and evaluation costs	$ 1,715	$ -	$ -	$ 1,715
Other material non-cash items	$ 1	$ 10	$ (70)	$ (59)
Impairment of mineral properties, plant and equipment	$ -	$ -	$ 1,894	$ 1,894
Interest income	$ 494	$ 297	$ 39	$ 830
Interest expense	$ 306	$ 219	$ 35	$ 560
Income (loss) before tax	$ (15,881)	$ 52,133	$ 2,083	$ 38,335
Income taxes	$ 183	$ 15,804	$ 2,815	$ 18,802

Income (loss) for the year	$ (16,064)	$ 36,329	$ (732)	$ 19,533
Capital expenditures	$ 814	$ 25,066	$ 53,127	$ 79,007

* cost of sales and selling, general and administrative expenses includes depletion and depreciation
** included in cost of sales or selling, general and administrative expenses

Reportable Segments	**Corporate**	**Bateas**	**Cuzcatlan**	**Total**
As at December 31, 2012				
Assets held for sale	**$ -**	**$ 51**	**$ -**	**$ 51**
Total assets	**$ 19,412**	**$ 127,778**	**$ 169,073**	**$ 316,263**
Total liabilities	**$ 5,466**	**$ 27,710**	**$ 18,594**	**$ 51,770**
As at December 31, 2011				
Total assets	$ 27,878	$ 112,746	$ 131,017	$ 271,641
Total liabilities	$ 5,729	$ 29,793	$ 7,808	$ 43,330

19. Segmented Information (continued)

The segment information by geographical region for the years ended December 31, 2012 and 2011 are as follows:

Reportable Segments	**Canada**	**Peru**	**Mexico**	**Other**	**Total**
Year ended December 31, 2012					
Sales to external customers	**$ -**	**$ 83,697**	**$ 77,323**	**$ -**	**$ 161,020**
Silver-gold concentrates	**$ -**	**$ -**	**$ 77,323**	**$ -**	**$ 77,323**
Silver-lead concentrates	**$ -**	**$ 68,616**	**$ -**	**$ -**	**$ 68,616**
Zinc concentrates	**$ -**	**$ 15,081**	**$ -**	**$ -**	**$ 15,081**
Year ended December 31, 2011					
Sales to external customers	$ -	$ 97,740	$ 12,264	$ -	$ 110,004
Silver-gold concentrates	$ -	$ -	$ 12,264	$ -	$ 12,264
Silver-lead concentrates	$ -	$ 80,689	$ -	$ -	$ 80,689
Zinc concentrates	$ -	$ 15,290	$ -	$ -	$ 15,290
Copper concentrates	$ -	$ 1,761	$ -	$ -	$ 1,761

Reportable Segments	**Canada**	**Peru**	**Mexico**	**Other**	**Total**
As at December 31, 2012					
Non current assets	**$ 3,132**	**$ 84,531**	**$ 122,647**	**$ -**	**$ 210,310**
As at December 31, 2011					
Non current assets	$ 3,004	$ 68,105	$ 113,020	$ -	$ 184,129

For the years ended December 31, 2012, six (2011: three) customers, respectively, represented 100% of total sales to external customers as follows:

External Sales by Customer and Region	**Years ended December 31, 2012**		2011	
Customer 1	**$ 1,391**	**2%**	$ 95,978	98%
Customer 2	**75,136**	**89%**	1,762	2%
Customer 3	**6,675**	**8%**	-	0%
Customer 4	**495**	**1%**	-	0%
Bateas/Peru	**$ 83,697**	**100%**	$ 97,740	100%
% of total sales	**52%**		89%	
Customer 1	**$ 2,333**	**3%**	$ 12,264	100%
Customer 2	**74,990**	**97%**	-	0%
Cuzcatlan/Mexico	**$ 77,323**	**100%**	$ 12,264	100%
% of total sales	**48%**		11%	
Consolidated	**$ 161,020**	**100%**	$ 110,004	100%
% of total sales	**100%**		100%	

20. Cost of Sales

The cost of sales for the years ended December 31, 2012 and 2011 are as follows:

	Years ended December 31,					
	2012			2011		
	Caylloma	**San Jose**	**Total**	Caylloma	San Jose	Total
Direct mining costs [1]	**$40,879**	**$27,511**	**$68,390**	$ 33,995	$ 4,654	$ 38,649
Depletion and depreciation	**8,861**	**11,616**	**20,477**	6,919	2,140	9,059
Royalty expenses	**1,491**	**-**	**1,491**	1,322	-	1,322
	$51,231	**$39,127**	**$90,358**	$ 42,236	$ 6,794	$ 49,030

[1] Direct mining costs includes salaries and other short term benefits, contractor charges, energy, consumables and production related costs.

21. Selling, General and Administrative expenses

The selling, general and administrative expenses for the years ended December 31, 2012 and 2011 are as follows:

	Years ended December 31,	
	2012	2011
Salaries and benefits	**$ 12,213**	$ 12,168
Corporate administration	**2,172**	3,409
Audit, legal and professional fees	**4,461**	2,915
Filing and listing fees	**236**	467
Director's fees	**564**	519
Depreciation	**895**	362
	$ 20,541	$ 19,840

22. Exploration and Evaluation Costs

The exploration and evaluation costs for the years ended December 31, 2012 and 2011 are as follows:

	Years ended December 31,	
	2012	2011
Share-based payments	**$ 52**	$ -
Salaries, wages and benefits	**506**	931
Direct costs	**219**	784
	$ 777	$ 1,715

23. Net Finance Income

The net finance income for the years ended December 31, 2012 and 2011 are as follows:

	Years ended December 31,	
	2012	2011
Finance income		
Interest income on FVTPL financial assets	**$ 620**	$ 830
Total finance income	**620**	830
Finance expenses		

Interest expense		**30**		81
Standby and commitment fees		**300**		306
Accretion of provisions (Note 13)		**232**		173
Total finance expense		**562**		560
Net finance income	**$**	**58**	$	270

24. Contingencies and Capital Commitments

a) Bank Letter of Guarantee

The Caylloma mine closure plan was approved in November 2009 with total closure costs of $3,587 of which $1,756 is subject to annual collateral in the form of a letter of guarantee, to be awarded each year in increments of $146 over 12 years based on the estimated life of the mine.

Scotiabank Peru, a third party, has established a bank letter of guarantee on behalf of Bateas in favor of the Peruvian mining regulatory agency in compliance with local regulation associated with the approved Bateas' mine closure plan, for the sum of $585. This bank letter of guarantee expires 360 days from December 2012.

Banco Bilbao Vizcaya Argentaria, S.A. had also established bank letters of guarantee totalling $54 to provide an annual guarantee associated with an office lease contract and truck rentals. These bank letters of guarantee were renewed in June 2011 with expiry 360 days to June 2012. This guarantee expired in June 2012.

b) Capital Commitments

As at December 31, 2012, $5,613 of capital commitments not disclosed elsewhere in the consolidated financial statements, and forecasted to be expended within one year, includes the following: $4,280 mine and tailing dam development at the San Jose property; and, $1,333 for the tailings dam transport system, concentrator plant, electrical infrastructure renewal, and camp infrastructure at Caylloma.

24. Contingencies and Capital Commitments (continued)

c) Other Commitments

The Company has a contract to guarantee power supply at its Caylloma mine. Under the contract, the seller is obligated to deliver a "maximum committed demand" (for the present term this stands at 3,500 Kw) and the Company is obligated to purchase subject to exemptions under provisions of "Force Majeure". The contract is automatically renewed every two years for a period of 10 years and expiring in 2017. Renewal can be avoided without penalties by notification 10 months in advance of renewal date.

Tariffs are established annually by the energy market regulator in accordance with applicable regulations in Peru.

The Company acts as guarantor to finance lease obligations held by two of its mining contractors. These finance lease contracts are related to the acquisition of mining equipment deployed at the Caylloma mine. As at December 31, 2012, these obligations amounted to $13 and mature in 2013.

On May 24, 2010, the Company entered into a seven year office premise lease located in Peru. The annual rent payable on 1,717 rentable square meters for office space, is as follows:

- year one $289;
- year two $297;
- year three $306; and,
- years four through seven the lease is subject a minimum annual increase of 3% or the Consumer Price Index published by Bureau of Labor Statistics of the United States Department of Labor, whichever is higher.

The lease also includes the use of additional space for mini-warehouse and parking spots, the obligation for which is $58 per annum for the first year and is subject to an annual increase of 3% as stated above until the end of the lease. During 2011, the Company provided a security deposit of $44.

24. Contingencies and Capital Commitments (continued)

c) Other Commitments (continued)

On September 30, 2012, the Company entered into an one year office premise lease in Mexico effective September 30, 2012, with an annual lease obligation of $16.

The expected payments due by period as at December 31, 2012 are as follows:

	Expected payments due by period as at December 31, 2012				
	Less than 1 year	1 - 3 years	4 -5 years	After 5 years	Total
Office premises – Canada	$ 148	$ 443	$ 306	$ 147	$ 1,044
Office premises – Peru	373	781	580	-	1,734
Office premises – Mexico	14	-	-	-	14
Total office premises	**$ 535**	**$ 1,224**	**$ 886**	**$ 147**	**$ 2,792**
Computer equipment – Peru	149	64	-	-	213
Computer equipment – Mexico	18	17	-	-	35
Total computer equipment	**$ 167**	**$ 81**	**$ -**	**$ -**	**$ 248**
Total operating leases	**$ 702**	**$ 1,305**	**$ 886**	**$ 147**	**$ 3,040**

d) **Other Contingencies**

The Company is subject to various investigations, claims and legal and tax proceedings covering matters that arise in the ordinary course of business activities. Each of these matters is subject to various uncertainties and it is possible that some of these matters may be resolved unfavorably to the Company. Certain conditions may exist as of the date the financial statements are issued, which may result in a loss to the Company. In the opinion of management none of these matters are expected to have a material effect on the results of operations or financial conditions of the Company.

During the year ended December 31, 2012, the Ministry of Mining and Energy (MEM) in Peru made an update to the approved Mining Environmental Liabilities List. The Company is currently in the process of evaluating its mining concessions which are currently included on the list and as at the date of the issuance of the financial statements an estimate of liability cannot be determined.

25. Subsequent events up to March 19, 2013

Subsequent to December 31, 2012, in February 2013 the Bank of Nova Scotia extended the credit facility maturity date to February 6, 2013 and then to February 27, 2013. On March 15, 2013, the Bank of Nova Scotia extended the credit facility maturity date to March 28, 2013. No funds were drawn from this credit facility.

FORTUNA
SILVER MINES INC.

CORPORATE OFFICE:
Suite 650-200 Burrard Street
Vancouver, BC Canada V6C 3L6

Tel: +1.604.484.4085
Fax: +1.604.484.4029

MANAGEMENT HEAD OFFICE:
Piso 5, Av. Jorge Chávez #154
Miraflores, Lima - Perú

Tel: +51.1.616.6060, ext.2

TRADING SYMBOL:
NYSE: FSM
TSX: FVI
BVL: FVI
Frankfurt: F4S.F
info@fortunasilver.com
WWW.FORTUNASILVER.COM

MANAGEMENT'S DISCUSSION AND ANALYSIS

FOR THE

YEAR ENDED DECEMBER 31, 2012

As at March 19, 2013

(Dollar amounts expressed in US dollars, unless otherwise indicated)

FORTUNA SILVER MINES INC.
Management's Discussion and Analysis
For the year ended December 31, 2012
(Dollar amounts expressed in US dollars, unless otherwise indicated)

Management's Discussion and Analysis ("MD&A") is intended to help the reader understand the significant factors that have affected Fortuna Silver Mines Inc. and its subsidiaries' ("Fortuna" or the "Company") performance and such factors that may affect its future performance. This MD&A, which has been prepared as of March 19, 2013, should be read in conjunction with the Company's audited consolidated financial statements for year ended December 31, 2012 and the related notes contained therein. The Company reports its financial position, financial performance and cash flows in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). This MD&A refers to various non-GAAP financial measures, such as cash cost per tonne of processed ore, cash cost per ounce of payable silver, total production cost per tonne, adjusted net income, operating cash flow per share before change in working capital items, income taxes, and interest income, used by the Company to manage and evaluate operating performance and ability to generate cash and are widely reported in the silver mining industry as benchmarks for performance, but do not have a standardized meaning and may differ from methods used by other companies with similar descriptions. The Company believes that certain investors use these non-GAAP financial measures to evaluate the Company's performance. Accordingly, non-GAAP financial measures should not be considered in isolation or as a substitute for measures of performance prepared in accordance with IFRS. To facilitate a better understanding of these measures as calculated by the Company, we have provided detailed descriptions and reconciliations as required.

This document contains forward-looking statements. Please refer to the cautionary language under the heading "Cautionary Statement on Forward-Looking Statements".

Index **Page**

Business of the Company 2
2012 Highlights 2
2013 Outlook and Guidance 3
Results of Operations 5
Property Option Agreements 11
Annual Financial Results 12
Quarterly Information 16
Fourth Quarter 2012 Financial Results 18
Non-GAAP Financial Measures 21
Adjusted Net Income (non-GAAP financial measure) 21
Operating cash flow per share before change in working capital items (non-GAAP financial measure) 21

Cash cost per ounce of payable silver and cash cost per tonne of processed ore (non-GAAP financial measure) 21
Liquidity and Capital Resources 24
Off-Balance Sheet Arrangements 29
Related Party Transactions *(expressed in $'000's)* 29
Significant Accounting Judgments and Estimates 31
Financial Instruments and Related Risks *(expressed in $'000's)* 33
Derivatives 36
Significant Accounting Policy 36
Significant Changes in Accounting Policies including Initial Adoption 37
New Accounting Standards 37
Other Data 41
Share Position and Outstanding Warrants and Options 41
Other Risks and Uncertainties 42
Controls and Procedures 42
Cautionary Statement on Forward-Looking Statements 42

Business of the Company

Fortuna is engaged in silver mining and related activities, in Latin America, including exploration, extraction, and processing. The Company operates the Caylloma silver/lead/zinc mine ("Caylloma") in southern Peru and the San Jose silver/gold mine ("San Jose") in Mexico.

Fortuna is a publicly traded company incorporated and domiciled in Canada. Its common shares are listed on the New York Stock Exchange under the trading ticker symbol FSM, on the Toronto Stock Exchange and Lima Stock Exchange, both under the trading ticker symbol FVI, and on the Frankfurt Stock Exchange under the trading symbol F4S.F.

The Company's registered office is located at Suite 650, 200 Burrard Street, Vancouver, British Columbia, Canada, V6C 3L6.

The financial results include the accounts of the Company and its wholly owned subsidiaries: Minera Bateas S.A.C. ("Bateas"); Fortuna Silver (Barbados) Inc. ("Barbados"); Compania Minera Cuzcatlan SA ("Cuzcatlan"); Continuum Resources Ltd. ("Continuum"); Fortuna Silver Mines Peru S.A.C. ("FSM Peru"); and Fortuna Silver Mexico, S.A. de CV. ("FS Mexico").

2012 Highlights

Full Year Financial and Operating Highlights

Net income for the year ended December 31, 2012 ("2012") increased by 62% to $31.5 million, compared to $19.5 million for the year ended December 31, 2011 ("2011"). The increase, in spite of an 11% lower silver price, reflects the contribution of San Jose in its first full year of production, and a lower effective income tax rate.

Cash generated by operating activities, before changes in working capital, increased by 59% to $62.2 million attributed to San Jose's strong cash margins and a lower cash tax rate.

Basic earnings per share for the year rose by 56% to $0.25 (2011: $0.16). Operating cash flow per share, before changes in working capital items, increased by 56% to $0.50 (2011: $0.32) (Refer to non-GAAP financial measures).

In 2012, sales were comprised of silver and gold, 67% and 17%, respectively, compared to the prior year of 65% and 6%, respectively.

Silver production increased by 60% to 3,987,757 ounces (2011: 2,486,655 ounces) and gold production rose by 199% to 20,699 ounces (2011: 6,917 ounces), exceeding annual guidance by 8% for silver and 19% for gold.

Consolidated cash cost per ounce of payable silver, net of by-product credits, was $5.96, compared to $0.25 in 2011. The higher cost was primarily at Caylloma, due to higher unit cash costs, higher refining charges, and lower by-product credits. (Refer to non-GAAP financial measures).

Fourth Quarter Highlights and Recent Developments

Fourth quarter net income was $8.5 million, compared to a net loss of $1.8 million a year ago. Cash generated by operating activities, before changes in working capital, increased by 35% over the prior period to $11.9 million. The increase in net income and cash generation was driven by higher sales at San Jose, lower effective income tax rate, and lower cash tax rate.

Basic earnings per share for Q4 2012 improved to $0.07, compared to a $0.01 loss per share in Q4 2011. Operating cash flow per share, before change in working capital items, increased by 43% to $0.10, compared to $0.07 in Q4 2011 (Refer to non-GAAP financial measures).

Compared to the third quarter of 2012, cash generated by operating activities, before changes in working capital, decreased by $8.1 million to $11.9 million primarily due to lower sales of $5.9 million driven by lower final sales adjustments of $3.5 million, changes in concentrate inventory, and lower head grades at San Jose, and to higher unit cash cost at Caylloma with an impact of $1.3 million.

Silver production increased by 11% to 1,010,730 ounces (Q4 2011: 913,803 ounces), while gold production rose by 5% to 4,368 ounces (Q4 2011: 4,153 ounces).

Consolidated cash cost per ounce of payable silver, net of by-product credits, was $8.85, compared to $5.20 in Q4 2011, due to higher cash cost per ounce at both Caylloma and San Jose. The main increase comes from San Jose, where unit costs were much lower in Q4 2011 as low cost development ore were consumed by the plant during the first quarter of commercial production. Compared to Q3 2012, consolidated cash cost per ounce of payable silver, net of by-product credits increased by 44% in Q4 2012 due to lower silver and gold head grades at San Jose.

Management Change

The Company appointed Robert Brown as Vice-President, Corporate Development effective August 1, 2012.

Mine Accident

It is with great sorrow the Company informs that on January 2, 2013, an electrical accident claimed the life of a contractor at the San Jose mine.

2013 Outlook and Guidance

Production Guidance

For 2013, the Company forecasts production of 4.4 million ounces of silver and 23,300 ounces of gold, an increase of 10% and 13%, respectively over 2012, or 5.7 million silver equivalent ounces (using $30/oz silver and $1,700/oz gold).

Mine	Silver (M ox)	Gold (k oz)	CAPEX ($ millions)	Cash Cost (*) ($/t)
San Jose, Mexico	2.4	20.6	22.0	70.4
Caylloma, Peru	2.0	2.7	30.7	96.0
Total	**4.4**	**23.3**	**52.7**	**-**

(CAPEX refers to capital expenditure)

For 2013, the Company projects zinc and lead production of 25.1 million pounds and 19.4 million pounds, respectively, an increase over 2012 of 9% and 12%, respectively.

Cash cost quarterly guidance

Mine	Q1 ($/t)	Q2 ($/t)	Q3 ($/t)	Q4 ($/t)	2013 ($/t)	2013 ($/0z)
San Jose	76	78	67	65	70	2.90
Caylloma	96	97	95	95	96	7.70
Consolidated						5.00

***Note:** Cash cost per tonne ("$/t") includes all on-site direct and indirect production costs, community relations expenses, concentrate transportation and corporate management fees. It excludes government royalties and workers participation. Cash cost per ounce ("$/oz") is net of by-product credits.

Cash cost at San Jose for 2013 is expected to decrease by 5% over the 2012 cost of $74.10 per tonne, as mine throughput rises on completion of development activities. Cash cost at Caylloma for 2013 is expected to increase by 10% over the 2012 cost of $87.28 per tonne, due to higher wages, contractor tariffs, and operational items such as higher ground support in level 6 of the Animas and Bateas veins, and increased diesel energy generation. The forecast for 2013 incorporates certain cost containment measures taken by the Company, such as investments required to eliminate energy restrictions from the power grid.

San Jose Mine

In 2013, San Jose is expected to process 451,000 tonnes of ore grading 186 g/t silver and 1.60 g/t gold. Capital expenditures for the year are estimated to be $22.0 million. The mill expansion to 1,500 tonnes per day ("tpd") from 1,000 tpd is on track to be commissioned at the beginning of third quarter. Major capital expenditures include:

- Mine development: $5.7 million
- Plant expansion: $9.1 million
- Tailings dam expansion: $4.4 million

Caylloma Mine

Caylloma is expected to process 464,100 tonnes of ore grading 170 g/t silver and 0.40 g/t gold in 2013. Capital expenditures are estimated to be $30.7 million, including the following major items:

- Mine development: $7.6 million
- Camp infrastructure: $8.6 million
- Tailings dam expansion: $3.6 million
- Power grid: $4.8 million

Brownfields Exploration

The Company´s brownfields exploration budget for 2013 is estimated at $14.2 million: $7.5 million will be spent at San Jose and $6.7 million at Caylloma.

Results of Operations

Consolidated Metal Production

	QUARTERLY RESULTS						YEAR TO DATE RESULTS					
	Three months ended December 31,						Years ended December 31,					
	2012			2011			2012			2011		
Consolidated Metal Production	**Caylloma**	**San Jose**	**Consolidated**	Caylloma	San Jose	Consolidated	**Caylloma**	**San Jose**	**Consolidated**	Caylloma	San Jose	Consolidated
Silver (Oz)	**519,549**	**491,181**	**1,010,730**	536,426	377,377	913,803	**2,038,579**	**1,949,178**	**3,987,757**	2,008,488	478,167	2,486,655
Gold (Oz)	**514**	**3,854**	**4,368**	591	3,562	4,153	**2,781**	**17,918**	**20,699**	2,393	4,524	6,917
Lead (000's lb)	**4,936**	**-**	**4,936**	4,396	-	4,396	**17,886**	**-**	**17,886**	19,678	-	19,678
Zinc (000's lb)	**6,135**	**-**	**6,135**	5,688	-	5,688	**22,396**	**-**	**22,396**	23.425	-	23,425
Copper (000's lb)	**-**	**-**	**-**	-	-	-	**48**	**-**	**48**	36	-	36
Production cash cost (US$/oz Ag)*	**9.30**	**8.38**	**8.85**	6.48	3.34	5.20	**8.07**	**3.76**	**5.96**	(0.78)	4.69	0.25

* Net of by-product credits

Silver and gold production for the year ended December 31, 2012, totaled 3,987,757 ounces and 20,699 ounces, respectively, exceeding by 8% and 19%, respectively, the Company's production guidance for 2012. When compared to the previous year, silver and gold production increased by 60% and 199%, respectively, as San Jose contributed its first full year of production after commissioning in September 2011.

Consolidated cash cost per ounce of payable silver

Consolidated cash cost per ounce of payable silver for 2012, net of by-product credits, was $5.96 (2011: $0.25) (Refer to non-GAAP financial measures for reconciliation of cash cost to the cost of sales). The higher cost was primarily at Caylloma, which increased from negative $0.78 per ounce in 2011 to $8.07 per ounce in 2012, due to higher unit cash costs (up $4.57), higher refining charges (up $1.24), and lower by-product credits (down $3.04) for an overall increase of $8.85 per ounce. This increase is in line with our forecast for 2012 (See Caylloma Mine Review and San Jose Mine Review for more detail).

Consolidated cash cost per ounce of payable silver in Q4 2012, net of by-product credits, was $8.85, compared to $5.20 in Q4 2011, due to higher cash cost per ounce at both Caylloma and San Jose. The main increase comes from San Jose, where unit costs were much lower in Q4 2011, as the mine completed its commissioning phase and started its first full quarter of commercial production. Cash cost per ounce at Caylloma was higher due to higher unit costs and refining charges. Compared to Q3 2012, consolidated cash cost per ounce increased 44% due mainly to lower silver and gold head grades at San Jose of 7% and 20%, respectively.

During the fourth quarter of 2012, the Company identified through its internal control procedures an inconsistency in San Jose's reported cash cost per ounce of payable silver. The adjusted San Jose cash cost per ounce of payable silver is as follows: Q1 2012 $0.83, Q2 2012 $0.82, and Q3 2012 $4.81. The adjusted consolidated cash cost per ounce of payable silver is as follows: Q1 2012 $3.96, Q2 2012 $4.75, and Q3 2012 $6.15. The Company deems the adjustments not to be material. (Refer to non-GAAP financial measures).

San Jose Mine Review

San Jose is an underground silver-gold mine located in southern Mexico in the State of Oaxaca. Its commercial product is silver-gold concentrate. Commercial production commenced on September 1, 2011. The table below shows the main variables used by management to measure the operating performance of the mine: throughput, grade, recovery, metal production, and unit costs.

	San Jose Mine	
	2012	2011

Mine Production	YTD	Q4	Q3	Q2	Q1	YTD	Q4	Q3
Tonnes milled	**369,022**	**98,348**	**91,607**	**92,011**	**87,056**	116,410	87,884	28,526
Average tonnes milled per day	**1,055**	**1,107**	**1,048**	**1,034**	**989**	954	955	951
Silver								
Grade (g/t)	**188**	**177**	**191**	**187**	**198**	150	159	124
Recovery %	**88**	**88**	**89**	**88**	**85**	85	84	89
Production (oz)	**1,949,178**	**491,181**	**502,835**	**486,297**	**468,865**	478,167	377,377	100,790
Gold								
Grade (g/t)	**1.74**	**1.39**	**1.73**	**1.96**	**1.92**	1.43	1.48	1.25
Recovery %	**87**	**88**	**89**	**88**	**84**	85	85	84
Production (oz)	**17,918**	**3,854**	**4,501**	**5,065**	**4,498**	4,524	3,562	962
Unit Costs								
Production cash cost (US$/oz Ag)*	**3.76**	**8.38**	**4.81**	**0.82**	**0.83**	4.69	3.34	9.72
Production cash cost (US$/tonne)	**74.10**	**82.82**	**80.59**	**66.50**	**65.46**	50.73	47.16	61.70
Unit Net Smelter Return (US$/tonne)	**209.70**	**198.53**	**213.44**	**207.45**	**223.07**	155.56	160.93	154.58

* Net of by-product credits

During 2012, silver and gold production at San Jose was 15% and 19%, respectively, above annual production guidance. The increased production resulted from mining higher grade ore ahead of schedule on level 1350, which contributed approximately 47% of mined ore in the period, or 160% above plan. By accelerating completion of the main access ramp and preparing levels 1350 and 1300 ahead of plan, we added operational flexibility to the mine that will help to sustain production in the face of potential ore variability and to secure the ramp-up of production to 1,500 tpd by the third quarter of 2013. Mine preparation peaked in Q4 2012 at 1,127 meters of underground development, compared to 614 meters, on average, during the first three quarters of the year. In Q4 2012, silver and gold head grades decreased compared to the first nine months of 2012 because of higher production of lower grade development ore from level 1300.

In its first full year of operation, the San Jose processing plant performed within design parameters, with silver and gold recoveries of 88% and 87%, respectively, and average ore throughput of 1,055 tpd.

Cash cost per tonne of processed ore for 2012 was $74.10, or 6% above forecast as a result of accelerated mine preparation in the fourth quarter and certain non-recurring items. Cash cost per payable ounce of silver for 2012 was $3.76, net of by-product credits.

Cash cost per tonne for Q4 2012 was $82.82, or 76% above Q4 2011. The increase is mainly because of the high volume of lower cost development ore treated during Q4 2011, as the mine completed its commissioning phase and started its first full quarter of operations. Cash cost per tonne in Q4 2012 was 12% above the full year due, in part, to the acceleration of mine preparation in Q4 2012. Cash cost per payable ounce of silver in Q4 2012 was 151% above the same period a year ago because of lower unit costs in Q4 2011, as explained above. Cash cost per payable ounce of silver in Q4 2012 was $8.38, or 74% above Q3 2012, due to lower head grades in Q4 2012 (Refer to 2013 Outlook and Guidance for cost estimates for 2013).

Cash cost per ounce of payable silver and cash cost per tonne of processed ore are non-GAAP financial measures (Refer to non-GAAP financial measures for reconciliation of cash cost to the cost of sales).

On October 2012, the Company, working in collaboration with state and community authorities, completed the final two kilometers of a thirteen kilometer, eight inch diameter water pipeline connecting the Ocotlan water treatment plant with the San Jose mine site. The pipeline is delivering approximately 20% of the make-up water currently required for the San Jose mill.

Capital expenditures at San Jose in 2012 were $14.3 million, which is lower than the $30.8 million budgeted mainly due to the postponement of the dore plant project.

Caylloma Mine Review

Caylloma is an underground silver-lead-zinc mine located in southern Peru, in the Arequipa department. Its commercial products are a silver-lead and zinc concentrates. The table below shows the main variables used by management to measure the operating performance of the mine.

	Caylloma Mine									
	2012					2011				
Mine Production	YTD	Q4	Q3	Q2	Q1	YTD	Q4	Q3	Q2	Q1
Tonnes milled	**462,222**	**115,522**	**117,386**	**115,870**	**113,444**	448,866	116,363	115,574	111,992	104,937
Average tonnes milled per day	**1,266**	**1,256**	**1,306**	**1,295**	**1,260**	1,264	1,307	1,270	1,273	1,206
Silver										
Grade (g/t)	**177**	**176**	**181**	**181**	**171**	171	177	186	162	158
Recovery %	**77**	**79**	**77**	**76**	**78**	81	81	81	82	82
Production (oz)	**2,038,579**	**519,549**	**524,906**	**509,897**	**484,227**	2,008,488	536,426	559,959	474,979	437,124

Gold										
Grade (g/t)	**0.40**	**0.34**	**0.44**	**0.42**	**0.39**	0.36	0.35	0.35	0.38	0.37
Recovery %	**47**	**40**	**51**	**50**	**45**	46	45	43	47	48
Production (oz)	**2,781**	**514**	**847**	**780**	**640**	2,393	591	563	638	601
Lead										
Grade (%)	**1.99**	**2.17**	**1.97**	**1.85**	**1.98**	2.15	1.85	2.11	2.28	2.36
Recovery %	**88**	**90**	**87**	**86**	**90**	93	92	92	94	92
Production (000's lb)	**17,886**	**4,936**	**4,452**	**4,055**	**4,443**	19,678	4,396	4,960	5,276	5,046
Zinc										
Grade (%)	**2.56**	**2.78**	**2.55**	**2.49**	**2.43**	2.68	2.47	2.58	2.80	2.87
Recovery %	**86**	**87**	**85**	**84**	**88**	88	90	88	89	87
Production (000's lb)	**22,396**	**6,135**	**5,615**	**5,325**	**5,321**	23,425	5,688	5,815	6,177	5,745
Copper										
Production (000's lb)	**48**	**-**	**-**	**48**	**-**	36	-	-	-	36
Unit Costs										
Production cash cost (US$/oz Ag)*	**8.07**	**9.30**	**7.43**	**8.49**	**6.99**	(0.78)	6.48	(0.48)	(4.59)	(5.93)
Production cash cost (US$/tonne)	**87.28**	**96.80**	**85.14**	**85.55**	**81.58**	69.12	79.68	69.96	63.49	62.50
Unit Net Smelter Return (US$/tonne)	**183.29**	**196.29**	**180.94**	**172.95**	**183.63**	221.01	190.95	248.63	234.61	208.58

*** Net of by-product credits**

Silver production for 2012 at Caylloma increased just 1% year over year because of a decrease in metallurgical recoveries of 5%, despite higher ore production (up 3%) and silver head grades (up 4%). Metallurgical recoveries were affected in 2012 by the high oxide content of ore mined in level 6 of the Animas vein, which contributed 30% of ore production during the year. In Q4 2012, the Company implemented recommendations to improve metallurgical recoveries following extensive testing conducted over several months. Positive results were achieved in November and December 2012, with silver recoveries improving to 80%, which are expected to reach 82% in 2013. Lower lead and zinc head grades and recoveries resulted in a year-over-year reduction in lead and zinc production of 9% and 4%, respectively.

Cash cost per tonne at Caylloma for 2012 was $87.28 per tonne of processed ore, an increase of 26% from 2011, but only 1% higher than forecast. The increase resulted mainly from higher contractor tariffs and labor costs. Cash cost per payable ounce of silver for 2012 was $8.07, net of by-product credits, compared to negative $0.78 in the prior year.

Cash cost per tonne for Q4 2012 was $96.80, or 21% above Q4 2011. Throughout the first three quarters of 2012, cost per tonne remained steady and below projections, however, higher costs for some items originally budgeted for 2013 were incurred in Q4 2012, resulting in costs rising 13% compared to forecast. These increases, which are reflected in the 2013 Outlook and Guidance, relate to milder inflation in contractor and transport tariffs and wages, operational items such as higher ground support in level 6 of the Animas and Bateas veins, and increased diesel energy generation as a result of constraints in the power grid. Cash cost per payable ounce of silver in Q4 2012 was $9.30, net of by-product credits, compared to $6.48 in Q4 2011.

Several cost containment initiatives were or are being implemented to help offset cost pressures. These mainly relate to changes in mining methods of high-grade narrow veins that will result in less mine preparation, the concentration of operations under one single contractor, ceasing production at minor peripheral veins, and the ongoing energy project to increase access to energy from the power grid.

Capital expenditures at Caylloma were $16.8 million in 2012, compared to $25.0 million budgeted for the year. The lower expenditures were due mainly to reducing the scope and postponing refurbishment of the processing plant, postponing until 2013 the energy project, and delaying moderately the mine camp project. The new tailings facility was successfully commissioned in January 2013.

Caylloma Mine and San Jose Mine Concentrates

The table below shows the production and balance of commercial end-products at each of our operating mines.

	QUARTERLY RESULTS				**YEAR TO DATE RESULTS**			
	Three months ended December 31,				**Years ended December 31,**			
	2012		2011		**2012**		2011	
Mine Concentrates	**Caylloma**	**San Jose**	Caylloma	San Jose	**Caylloma**	**San Jose**	Caylloma	San Jose
Silver Gold								
Opening Inventory (t)	**0**	**424**	0	538	**0**	**730**	0	0
Production (t)	**0**	**2,723**	0	2,277	**0**	**9,647**	0	2,958
Sales (t)	**0**	**2,682**	0	2,084	**0**	**9,915**	0	2,228
Adjustment (t)	**0**	**2**	0	0	**0**	**3**	0	0
Closing Inventory (t)	**0**	**466**	0	730	**0**	**466**	0	730
Zinc								
Opening Inventory (t)	**589**	**0**	273	0	**305**	**0**	258	0
Production (t)	**5,351**	**0**	4,964	0	**19,588**	**0**	20,569	0
Sales (t)	**5,435**	**0**	4,920	0	**19,394**	**0**	20,490	0
Adjustment (t)	**15**	**0**	-12	0	**23**	**0**	-32	0
Closing Inventory (t)	**521**	**0**	305	0	**521**	**0**	305	0
Lead								

Opening Inventory (t)	**261**	**0**	232	0	**255**	**0**	191	0
Production (t)	**4,155**	**0**	3,599	0	**14,803**	**0**	15,767	0
Sales (t)	**4,011**	**0**	3,590	0	**14,820**	**0**	15,760	0
Adjustment (t)	**37**	**0**	14	0	**204**	**0**	58	0
Closing Inventory (t)	**443**	**0**	255	0	**443**	**0**	255	0
Copper								
Opening inventory (t)	**9**	**0**	4	0	**4**	**0**	29	0
Production (t)	**0**	**0**	0	0	**97**	**0**	80	0
Sales (t)*	**0**	**0**	0	0	**0**	**0**	104	0
Adjustment (t)	**-9**	**0**	0	0	**-101**	**0**	-1	0
Closing Inventory (t)	**0**	**0**	4	0	**0**	**0**	4	0

*** Copper concentrate sold as lead concentrate**

Property Option Agreements

Mario and Don Mario Properties ("Mario project")

During the second quarter of 2012, upon completion of a 7,000 meter Phase I drill program at the Mario and Don Mario Properties ("Mario project"), the Company determined the program was not successful in demonstrating the potential to meet the minimum target size established for the project and the Company abandoned its interest in the Mario property resulting in a write-off of $3.9 million.

Tlacolula Property

Pursuant to an agreement dated September 14, 2009, as amended December 18, 2012, the Company, through its wholly owned subsidiary, Cuzcatlan, was granted an option (the "Option") to acquire a 60% interest (the "Interest") in the Tlacolula silver project ("property") located in the State of Oaxaca, Mexico from Radius Gold Inc.'s wholly owned subsidiary, Radius (Cayman) Inc. ("Radius").

The Company can earn the Interest by spending $2.0 million, which includes a commitment to drill 1,500 meters within 12 months after Cuzcatlan has received a permit to drill the property and making staged annual payments totalling $0.25 million cash and providing $0.25 million in common shares of the Company to Radius according to the following schedule:

- Ø $0.02 million cash and $0.02 million cash equivalent in shares upon stock exchange approval;
- Ø $0.03 million cash and $0.03 million cash equivalent in shares by January 15, 2011;
- Ø $0.05 million cash and $0.05 million cash equivalent in shares by January 15, 2012;
- Ø $0.05 million cash and $0.05 million cash equivalent in shares by the January 15, 2013; and,
- Ø $0.10 million cash and $0.10 million cash equivalent in shares within 90 days after Cuzcatlan has completed the first 1,500 meters of drilling on the property.

Upon completion of the cash payments and share issuances, and incurring the exploration expenditures as set forth above, the Company will be deemed to have exercised the Option and acquired a 60% interest in the property, whereupon a joint venture will be formed to further develop the property on the basis of the Company owning 60% and Radius 40%.

As at December 31, 2012, the Company had issued 23,174 common shares of the Company, with a fair market value of $0.10 million and paid $0.10 million cash according to the terms of the option agreement.

Subsequent to December 31, 2012, on January 15, 2013, the Company issued 11,415 common shares of the Company, at a fair market value of $4.38 per share and on January 14, 2013 paid $0.05 million cash according to the terms of the option agreement.

Taviche Property

In 2010, the Company included the idle plant in Taviche as part of the San Jose mine plant as it was more likely than not that the idle plant could be used to treat excess ore from San Jose or from surrounding areas where the company was conducting exploration. On September 1, 2011, the San Jose mine plant commenced commercial production and in the fourth quarter of 2011, achieved an average of 955 tonnes milled per day with the San Jose plant having sufficient capacity for the production. In the fourth quarter of 2011, management reassessed the usability of the idle plant and in conjunction, obtained an independent third party appraisal of various assets acquired under an asset purchase agreement dated 2007 related to the Taviche property.

Management used the fair value less cost to sell method to determine the recoverable amount of the idle plant. Based upon an independent appraisal of the assets, which is in accordance with fair value less cost to sell, the Company took an impairment charge, in 2011, of $1.89 million that comprised of the following impairments: $1.08 million on the tailing dam, $0.14 million on the mine infrastructure, and $0.67 million on equipment, machinery, and buildings. As at December 31, 2011, the net book value of assets related to the Taviche property for machinery and equipment amounted to $0.36 million.

Taviche Oeste Concessions

Subsequent to December 31, 2012, on February 4, 2013, the Company, through its wholly owned subsidiary, Cuzcatlan, acquired, through an option agreement (the "Option") with Plata Pan American S.A. de C.V. ("Plata") (a wholly owned subsidiary of Pan American

Silver Corp.), a 55% undivided interest in 6,254 hectare Taviche Oeste Concessions ("concessions") immediately surrounding the San Jose Mine in Oaxaca, Mexico. The Company made a cash payment of $4.0 million. Once a production decision is made to develop ore from the concessions, the Company, through its wholly owned subsidiary, Cuzcatlan, will purchase the remaining 45% undivided interest in the property for $6.0 million. Plata will retain a 2.5% net smelter royalty on ore production from this property.

San Luisito Concessions

Subsequent to December 31, 2012, in February 2013, the Company, through its wholly owned subsidiary, Cuzcatlan, was granted an option (the "Option") with a third party on concessions in the San Luisito Project, Sonora, Mexico and made a cash payment of $0.05 million. Further payments due are as follows: August 26, 2013 $0.15 million, February 24, 2014 $0.40 million, February 24, 2015 $1.0 million, February 26, 2016 $1.4 million, and February 26, 2017 $12 million. The third party will retain a 2% net smelter royalty on ore produced from this property.

Annual Financial Results

	Years Ended December 31,		
Expressed in $000's, except per share data	**2012**	2011	2010
Sales	**161,020**	110,004	74,506
Mine operating earnings	**70,662**	60,974	39,212
Operating income	**45,168**	38,065	27,728
Net income	**31,463**	19,533	16,003
Earnings per share, basic	**0.25**	0.16	0.15
Earnings per share, diluted	**0.25**	0.16	0.14
Total assets	**316,983**	271,642	233,871
Leases and long term liabilities	**2,250**	2,764	3,166

For the year ended December 31, 2012, net income increased by 62% to $31.5 million, compared to $19.5 million in 2011. Mine operating earnings increased by 16% to $70.7 million (2011: $61.0 million) and cash flow from operations, before changes in working capital, rose by 59% to $62.2 million (2011: $39.1 million).

The increase in net income reflects the contribution of San Jose, which commenced commercial operations in September 2011, and a lower effective tax rate, which reduced income taxes by $5.0 million. The full benefit of San Jose was tempered by lower sales and operating margins at Caylloma than in 2011. Caylloma was affected by higher treatment and refining charges and lower base metals sold (down $5.5 million), by lower prices for and, in turn, sales of silver and base metals (down $12.5 million), and an increase in unit cash cost year over year of 26%. However, cash flow from operations before changes in working capital, increased, as did cash flow margins (cash flow from operations, before changes in working capital, over sales), which increased to 39% in 2012 from 36% in 2011 as a result of strong margins at San Jose and a lower cash tax rate. The latter effect relates mainly to San Jose, which incurred no taxes during the year ended December 31, 2012.

Basic earnings per share increased by 56% to $0.25 in 2012, compared to $0.16 in 2011. Operating cash flow per share, before change in working capital items, increased by 56% to $0.50 (2011: $0.32) (Refer to non-GAAP financial measures).

Sales for 2012 increased by 46% to $161.0 million (2011: $110.0 million) primarily because of the contribution from San Jose of $77.3 million (2011: $12.3 million). In respect to metals, higher sales of silver and gold (up 71% and 303%, respectively) were partially offset by lower prices for silver, lead, and zinc (down 11%, 15%, and 12%, respectively), higher consolidated refining charges ($2.06/oz compared to $1.83/oz) and lower lead and zinc sales (down 9% and 5%, respectively).

Net realized prices are calculated from provisional sales, based on contained metals in concentrate sold, before government royalties and after deductions, treatment, and refining charges. Treatment charges are allocated to the base metals in Caylloma and to gold in San Jose. Final pricing for all concentrates takes place one month after the month of sale.

	YEAR TO DATE RESULTS Years ended December 31,					
	2012			2011		
Sales and Realized Prices	**Caylloma**	**San Jose**	**Consolidated**	Caylloma	San Jose	Consolidated
Provisional Sales (US$)	**82,226,303**	**79,161,972**	**161,388,274**	97,518,505	12,665,147	110,183,652
Adjustments (US$)*	**1,470,935**	**(1,839,272)**	**(368,338)**	221,116	(400,610)	(179,495)
Sales (US$)	**83,697,237**	**77,322,699**	**161,019,936**	97,739,620	12,264,536	110,004,157
Silver						
Provisional Sales (oz)	**1,975,984**	**1,984,902**	**3,960,886**	1,976,301	338,852	2,315,153
Realized Price (US$/oz)**	**30.98**	**30.84**	**30.91**	35.00	31.95	34.83
Net Realized Price (US$/oz)***	**26.96**	**27.83**	**27.40**	31.91	26.29	31.09
Gold						
Provisional Sales (oz)	**2,452**	**18,524**	**20,976**	2,130	3,069	5,199

Realized Price (US$/oz)**	**1,667.47**	**1,657.14**	**1,648.83**	1,560.59	1,680.93	1,631.39
Net Realized Price (US$/oz)***	**1,321.92**	**1,291.80**	**1,295.32**	1,116.09	1,224.19	1,179.90
Lead						
Provisional Sales (000's lb)	**17,662**	**-**	**17,662**	19,460	-	19,460
Realized Price (US$/lb)**	**0.94**	**-**	**0.94**	1.10	-	1.10
Net Realized Price (US$/lb)***	**0.63**	**-**	**0.63**	0.86	-	0.86
Zinc						
Provisional Sales (000's lb)	**22,049**	**-**	**22,049**	23,107	-	23,107
Realized Price (US$/lb)**	**0.88**	**-**	**0.88**	1.00	-	1.00
Net Realized Price (US$/lb)***	**0.66**	**-**	**0.66**	0.66	-	0.66
Copper						
Provisional Sales (000's lb)	**-**	**-**	**-**	47	-	47
Realized Price (US$/lb)**	**-**	**-**	**-**	4.25	-	4.25
Net Realized Price (US$/lb)***	**-**	**-**	**-**	2.65	-	2.65

*** Adjustments consists of mark-to-market and final price adjustments, and final assay adjustments**
**** Based on provisional sales before final price adjustments**
*****Net after payable metal deductions, treatment, and refining charges**
Treatment charges are allocated to the base metals in Caylloma and to gold in San Jose.

Cost of sales for 2012 increased by 84% to $90.4 million (2011: $49.0 million). The increase is primarily attributable to the contribution by San Jose of $39.1 million (2011: $6.8 million) as results for San Jose in 2012 reflect a full year versus four months in 2011, and to a 26% higher unit production cash costs per tonne of processed ore at Caylloma (Refer to non-GAAP financial measures for reconciliation of cash cost to the cost of sales).

	Expressed in $ millions					
	Years ended December 31,					
	2012			2011		
	Caylloma	**San Jose**	**Total**	Caylloma	San Jose	Total
Direct mining costs [1]	**$ 40.9**	**$ 27.5**	**$ 68.4**	$ 34.0	$ 4.7	$ 38.6
Depletion and depreciation	**8.9**	**11.6**	**20.5**	6.9	2.1	9.1
Royalty expenses	**1.5**	**-**	**1.5**	1.3	-	1.3
	$ 51.3	**$ 39.1**	**$ 90.4**	$ 42.2	$ 6.8	$ 49.0

[1] Direct mining costs includes salaries and other short term benefits, contractor charges, energy, consumables and production related costs.

Selling, general and administrative expenses for 2012 increased by 4% to $20.5 million (2011: $19.8 million). The increase is primarily attributable to an increase of $2.4 million in Cuzcatlan general and administrative expenses as commercial production at San Jose commenced September 1, 2011, to a $1.6 million increase in corporate general and administrative expenses as a result of higher salaries and professional fees related to the growth of the Company, and offset by a $2.6 million decrease in share-based payments. The decrease in share-based payments is attributed to the decline in the fair value of restricted share units and deferred share units. Shared-based payments related to vesting of granted instruments, excluding the mark-to-market effect, amounted to $3.2 million during the year.

Selling, general and administrative expenses consist primarily of corporate office and subsidiary expenses such as salaries and other payroll related costs for executive, administrative, legal, financial, information technology, human and organizational development, and procurement functions, as well as professional service fees.

	Expressed in $ millions	
	Year ended December 31,	
	2012	2011
Corporate general and administrative expenses	**$ 11.6**	$ 10.0
Bateas general and administrative expenses	**3.2**	3.4
Cuzcatlan general and administrative expenses	**3.3**	0.9
Foreign exchange	**(0.1)**	0.1
Share-based payments	**2.2**	4.8
Workers' participation	**0.3**	0.6
	$ 20.5	$ 19.8

Exploration and evaluation costs for 2012 decreased to $0.8 million (2011: $1.7 million).

	Expressed in $ millions	
	Year ended December 31,	
	2012	2011
Share-based payments	**$ 0.1**	$ -
Salaries, wages, and benefits	**0.5**	0.9
Direct costs	**0.2**	0.8
	$ 0.8	$ 1.7

Net loss (gain) on commodity contract for 2012 was $0.3 million loss compared to a $0.5 million gain in 2011. The loss is related to short term contracts used to fix the final settlement price on metal contained in concentrate delivered throughout the period.

Write-off of mineral properties costs for 2012 was $3.9 million (2011: nil) and relates to the write-off of exploration costs for the Mario project.

Impairment of mineral properties, plant and equipment for 2012 was nil. This compares to an impairment charge in 2011 of $1.9 million related to the Taviche property comprised of: $1.1 million on the tailings dam, $0.1 million on mine infrastructure, and $0.7 million on equipment, machinery, and buildings.

Interest income for 2012 decreased by 25% to $0.6 million (2011: $0.8 million) primarily due to a reduction in cash balances.

Interest expense for 2012 remained unchanged at $0.6 million (2011: $0.6 million). Expenses for 2012 result from the accretion of the decommissioning and restoration of the San Jose property, offset by a reduction in interest on leases.

Income taxes for the year decreased by 27% to $13.8 million (2011: $18.8 million). The effective tax rate for the years ended December 31, 2012 and 2011 was 30.43% and 49.05%, respectively. The change in the effective tax rate was primarily attributable to the geographical mix of income and the impact of foreign exchange on the tax basis on non-monetary assets.

The income tax provision comprised $5.5 million (2011: $14.6 million) of current income tax expense arising mainly from our Peruvian operations and $8.3 million (2011: $4.2 million) of deferred income tax expense arising from our Peruvian and Mexican operations.

Quarterly Information

The following table provides information for the eight fiscal quarters ended December 31, 2012:

	Quarters ended							
Expressed in $000's, except per share data	**31-Dec-12**	30-Sep-12	30-Jun-12	31-Mar-12	31-Dec-11	30-Sep-11	30-Jun-11	31-Mar-11
Sales	**37,895**	43,835	38,689	40,601	31,047	32,543	24,528	21,886
Mine operating earnings	**13,264**	19,239	17,078	21,081	13,265	19,811	14,847	13,052
Operating income	**7,976**	12,262	8,397	16,533	4,436	14,886	10,667	8,076
Net income (loss)	**8,472**	8,026	3,854	11,111	(1,756)	10,309	6,199	4,781
Earnings per share, basic	**0.07**	0.06	0.03	0.09	(0.01)	0.08	0.05	0.04
Earnings per share, diluted	**0.07**	0.06	0.03	0.09	(0.01)	0.08	0.05	0.04
Total assets	**316,983**	304,612	288,686	280.825	271,641	270,289	253,350	242,566
Leases and long term liabilities	**2,250**	2,766	1,658	2,237	2,764	2,873	2,988	3,384

Sales growth from Q1 2011 to Q4 2012 reflects the surge in silver price since the beginning of 2010 and the commencement of commercial production at San Jose starting in September 2011.

The following table provides the realized prices from sales for the past eight quarters and the years ended December 31, 2012 and 2011:

Realized Prices from Sales

	2012					2011				
	YTD	**Q4**	**Q3**	**Q2**	**Q1**	YTD	Q4	Q3	Q2	Q1
Silver										
Realized Prices Silver (US$/oz)**										
Caylloma	**30.98**	**32.56**	**29.96**	**29.40**	**32.19**	35.00	32.09	38.33	37.88	30.94
San Jose	**30.84**	**32.73**	**30.29**	**28.89**	**31.90**	31.95	31.57	37.96	-	-
Consolidated	**30.91**	**32.64**	**30.11**	**29.12**	**32.05**	34.83	31.98	38.70	37.88	30.94
Net Realized Prices Silver (US$/oz)***										
Caylloma	**26.96**	**28.30**	**26.06**	**25.66**	**27.99**	31.91	28.58	35.28	34.86	28.26
San Jose	**27.83**	**29.71**	**27.35**	**26.02**	**28.63**	26.29	25.95	31.59	-	-
Consolidated	**27.40**	**29.01**	**26.67**	**25.86**	**28.30**	31.09	27.59	35.15	34.86	28.26
Gold										
Realized Prices Gold (US$/oz)**										
Caylloma	**1,667.47**	**1,714.36**	**1,660.62**	**1,603.01**	**1,680.97**	1,560.59	1,694.98	1,682.50	1,487.72	1,380.01
San Jose	**1,657.14**	**1,707.87**	**1,667.93**	**1,598.37**	**1,663.73**	1,680.93	1,675.70	1,763.44	-	-
Consolidated	**1,648.83**	**1,718.91**	**1,661.73**	**1,598.54**	**1,656.09**	1,631.39	1,673.38	1,703.29	1,487.72	1,380.01
Net Realized Prices Gold (US$/oz)***										
Caylloma	**1,321.92**	**1,206.60**	**1,382.27**	**1,318.12**	**1,332.77**	1,116.08	1,245.13	1,153.99	1,063.98	1,000.52
San Jose	**1,291.80**	**1,279.55**	**1,288.74**	**1,269.71**	**1,333.49**	1,224.19	1,221.05	1,273.67	-	-
Consolidated	**1,295.32**	**1,271.81**	**1,302.14**	**1,274.62**	**1,333.40**	1,179.90	1,224.79	1,185.07	1,063.98	1,000.52

Lead										
Realized Prices Lead (US$/lb)**										
Caylloma	**0.94**	**1.00**	**0.90**	**0.90**	**0.95**	1.10	0.91	1.13	1.17	1.18
Consolidated	**0.94**	**1.00**	**0.90**	**0.90**	**0.95**	1.10	0.91	1.13	1.17	1.18
Net Realized Prices Lead (US$/lb)***										
Caylloma	**0.63**	**0.68**	**0.62**	**0.58**	**0.63**	0.86	0.67	0.89	0.92	0.94
Consolidated	**0.63**	**0.68**	**0.62**	**0.58**	**0.63**	0.86	0.67	0.89	0.92	0.94
Zinc										
Realized Prices Zinc (US$/lb)**										
Caylloma	**0.88**	**0.89**	**0.86**	**0.88**	**0.92**	1.00	0.86	1.01	1.03	1.09
Consolidated	**0.88**	**0.89**	**0.86**	**0.88**	**0.92**	1.00	0.86	1.01	1.03	1.09
Net Realized Prices Zinc (US$/lb)***										
Caylloma	**0.66**	**0.65**	**0.65**	**0.67**	**0.68**	0.66	0.57	0.67	0.68	0.71
Consolidated	**0.66**	**0.65**	**0.65**	**0.67**	**0.68**	0.66	0.57	0.67	0.68	0.71

** Based on provisional sales before final price adjustments
***Net after payable metal deductions, treatment, and refining charges
Treatment charges are allocated to base metals in Caylloma and to gold in San Jose

Fourth Quarter 2012 Financial Results

During Q4 2012, the Company generated net income of $8.5 million, compared to a net loss in the prior year of $1.8 million. Mine operating earnings remained at $13.3 million (Q4 2011: $13.3 million) while cash flow from operations, before changes in working capital, increased by 35% to $11.9 million (Q4 2011: $8.8 million).

The higher net income resulted mainly from higher sales at San Jose, lower income taxes in the quarter comprising a $6.4 million reduction of deferred tax provision, and a one-time $1.9 million write-off of the Taviche idle plant that was recorded in the prior year. The full contribution of San Jose was curtailed by a $1.3 million negative final assay adjustment to sales and by higher costs related to accelerated mine preparation prior to the mine's expansion. Mine operating earnings remained flat due to lower results from Caylloma, which were affected by higher depletion and depreciation charges, an inventory build-up, and a rise in unit cash cost, reflecting the trend of our cost guidance for 2013.

The increase in cash flow from operations, before changes in working capital, reflects the positive contribution of San Jose to cash margins as well as lower cash tax rate in the period.

Basic earnings per share for Q4 2012 was $0.07 (Q4 2011: $0.01 loss). Operating cash flow per share, before change in working capital items, was $0.10 (Q4 2011: $0.07) (Refer to non-GAAP financial measures).

Sales for Q4 2012 increased by 22% to $37.9 million (Q4 2011: $31.0 million). The increase is due primarily to the contribution from San Jose of $16.7 million (Q4 2011: $11.4 million). In respect to metals, the sales increase was driven by higher provisional sales of silver, gold, and zinc, up 11%, 21%, and 12%, respectively, and partially offset by $1.3 million of negative assay adjustments at San Jose.

Net realized prices are calculated from provisional sales, based on contained metals in concentrate sold, before government royalties and after deductions, treatment, and refining charges. Treatment charges are allocated to the base metals in Caylloma and to gold in San Jose. Final pricing for all concentrates takes place one month after the month of sale.

	QUARTERLY RESULTS					
	Three months ended December 31,					
	2012			2011		
Sales and Realized Prices	**Caylloma**	**San Jose**	**Consolidated**	Caylloma	San Jose	Consolidated
Provisional Sales (US$)	**20,980,783**	**18,707,113**	**39,687,896**	21,742,179	11,792,088	33,534,267
Adjustments (US$)*	**223,218**	**(2,016,662)**	**(1,793,444)**	(2,086,580)	(400,610)	(2,487,190)
Sales (US$)	**21,204,001**	**16,690,451**	**37,894,452**	19,655,599	11,391,478	31,047,077
Silver						
Provisional Sales (oz)	**466,492**	**469,858**	**936,350**	526,096	318,593	844,689
Realized Price (US$/oz)**	**32.56**	**32.73**	**32.64**	32.09	31.57	31.98
Net Realized Price (US$/oz)***	**28.30**	**29.71**	**29.01**	28.58	25.95	27.59
Gold						
Provisional Sales (oz)	**440**	**3,710**	**4,150**	530	2,886	3,416
Realized Price (US$/oz)**	**1,714.36**	**1,707.87**	**1,718.91**	1,694.98	1,675.70	1,673.38
Net Realized Price (US$/oz)***	**1,206.60**	**1,279.55**	**1,271.81**	1,245.13	1,221.05	1,224.79
Lead						
Provisional Sales (000's lb)	**4,698**	**-**	**4,698**	4,340	-	4,340
Realized Price (US$/lb)**	**1.00**	**-**	**1.00**	0.91	-	0.91

Net Realized Price (US$/lb)***	**0.68**	**-**	**0.68**	0.67	-	0.67
Zinc						
Provisional Sales (000's lb)	**6,223**	**-**	**6,223**	5,565	-	5,565
Realized Price (US$/lb)**	**0.89**	**-**	**0.89**	0.86	-	0.86
Net Realized Price (US$/lb)***	**0.65**	**-**	**0.65**	0.57	-	0.57

*** Adjustments consists of mark-to-market and final price adjustments, and final assay adjustments**
**** Based on provisional sales before final price adjustments**
*****Net after payable metal deductions, treatment, and refining charges**
Treatment charges are allocated to the base metals in Caylloma and to gold in San Jose.

Cost of sales for Q4 2012 increased by 39% to $24.6 million, compared to $17.8 million in Q4 2011. The increase is primarily attributable to higher concentrate sales and unit cash costs at both San Jose and Caylloma. Refer to non-GAAP financial measures for reconciliation of cash cost to the cost of sales.

	Expressed in $ millions					
	Three months ended December 31,					
	2012			2011		
	Caylloma	**San Jose**	**Total**	Caylloma	San Jose	Total
Direct mining costs [1]	**$ 11.3**	**$ 8.1**	**$ 19.4**	$ 9.6	$ 4.0	$ 13.6
Depletion and depreciation	**2.8**	**2.0**	**4.8**	1.8	2.0	3.8
Royalty expenses	**0.4**	**-**	**0.4**	0.4	-	0.4
	$ 14.5	**$ 10.1**	**$ 24.6**	$ 11.8	$ 6.0	$ 17.8

[1] Direct mining costs includes salaries and other short term benefits, contractor charges, energy, consumables and production related costs.

Selling, general and administrative expenses for Q4 2012 decreased by 12% to $5.1 million (Q4 2011: $5.9 million). The decrease is primarily attributable to lower share-based payments of $0.9 million and foreign exchange of $0.3 million, offset by higher general and administrative expenses in Cuzcatlan ($0.1 million) and corporate general and administrative expenses ($0.3 million), mainly as a result of higher salaries and professional fees related to growth of the Company. The decrease in share-based payments is attributed to the decrease in the fair value of restricted share units and deferred share units. Shared-based payments related to vesting of granted instruments, excluding the mark-to-market effect, amounted to $1.0 million during the quarter.

Selling, general and administrative expenses consist primarily of corporate office and subsidiary expenses such as salaries and other payroll related costs for executive, administrative, legal, financial, information technology, human and organizational development, and procurement functions, as well as professional service fees.

	Expressed in $ millions	
	Three months ended December 31,	
	2012	2011
Corporate general and administrative expenses	**$ 3.2**	$ 2.9
Bateas general and administrative expenses	**0.8**	0.8
Cuzcatlan general and administrative expenses	**0.8**	0.7
Foreign exchange	**(0.1)**	0.2
Share-based payments	**0.3**	1.2
Workers' participation	**0.1**	0.1
	$ 5.1	$ 5.9

Exploration and evaluation costs for Q4 2012 decreased by 75% to $0.2 million (Q4 2011: $0.6 million).

	Expressed in $ millions	
	Three months ended December 31,	
	2012	2011
Salaries, wages, and benefits	**0.1**	0.3
Direct costs	**0.1**	0.3
	$ 0.2	$ 0.6

Net loss on commodity contract for Q4 2012 was nil compared to a loss of $0.4 million in Q4 2011, which is related to short term contracts used to fix the final settlement price on metal contained in concentrate delivered throughout the period.

Interest income for Q4 2012 remained flat at $0.2 million (Q4 2011: $0.2 million), as cash balances were reduced.

Interest expense for Q4 2012 remained unchanged at $0.1 million (Q4 2011: $0.1 million).

Income taxes for Q4 2012 decreased by 108% to a recovery of $0.5 million (Q4 2011: $6.2 million expense). The change was primarily attributable to the impact of foreign exchange on the tax basis on non-monetary assets.

Income tax provision is comprised of $1.7 million (Q4 2011: $1.9 million) of current income tax expense, arising mainly from our Peruvian operations, and a $2.2 million recovery (Q4 2011: $4.3 million expense) of deferred income tax arising from our Peruvian and Mexican operations.

Non-GAAP Financial Measures

Adjusted Net Income (non-GAAP financial measure)

	Expressed in $ millions	
	Years ended December 31,	
	2012	2011
NET INCOME FOR THE YEAR	**$ 31.5**	$ 19.5
Items of note, net of tax		
Mark-to-Market effect on derivatives	**-**	(0.1)
Write-off of mineral properties	**2.6**	-
Impairment of mineral properties, plant and equipment	**-**	1.3
ADJUSTED NET INCOME FOR THE YEAR (1)	**$ 34.1**	$ 20.7

(1) A non-GAAP financial measure

Operating cash flow per share before change in working capital items (non-GAAP financial measure)

	Expressed in $'000's (except per share measures)			
	Three months ended December 31,		Years ended December 31,	
	2012	2011	**2012**	2011
Net income for the period	**$ 8,472**	$ (1,755)	**$ 31,463**	$ 19,533
Items not involving cash	**4,392**	13,680	**40,885**	33,821
	$ 12,864	$ 11,925	**$ 72,348**	$ 53,354
Income taxes paid	**(1,141)**	(3,274)	**(10,703)**	(15,007)
Interest expense paid	**(8)**	(21)	**(31)**	(80)
Interest income received	**150**	155	**611**	837
Cash generated by operating activities before changes in working capital	**$ 11,865**	$ 8,785	**$ 62,225**	$ 39,104
Divided by				
Weighted average number of shares ('000's)	**124,412**	124,090	**123,585**	123,295
Operating cash flow per share before change in working capital items (1)	**$ 0.10**	$ 0.07	**$ 0.50**	$ 0.32

(1) A non-GAAP financial measure

Cash cost per ounce of payable silver and cash cost per tonne of processed ore (non-GAAP financial measure)

Cash cost per ounce of payable silver and cash cost per tonne of processed ore are key performance measures that management uses to monitor performance. In addition, cash costs are presented as they represent an industry standard method of comparing certain costs on a per unit basis but do not have a standardized meaning and may differ from methods used by other companies with similar descriptions. Management believes that certain investors use these non-GAAP financial measures to evaluate the Company's performance. These performance measures have no meaning under International Financial Reporting Standards ("IFRS") and, therefore, amounts presented may not be comparable to similar data presented by other mining companies.

The following tables present a reconciliation of cash costs per tonne of processed ore and cash cost per ounce of payable silver to the cost of sales in the consolidated financial statements for the past eight quarters and the years ended December 31, 2012 and 2011.

Consolidated Mine Cash Cost	Expressed in $'000's									
	2012					2011				
	YTD	**Q4**	**Q3**	**Q2**	**Q1**	YTD	Q4	Q3	Q2	Q1
Cost of sales (1)	**90,358**	**24,631**	**24,596**	**21,611**	**19,520**	49,030	17,782	12,732	9,682	8,834
Add / (Subtract)										
Change in concentrate inventory	**430**	**394**	**(872)**	**(320)**	**1,228**	2,142	415	1,168	(4)	563
Depletion and depreciation in concentrate inventory	**23**	**(41)**	**227**	**233**	**(396)**	(717)	(207)	(403)	22	(129)
Government royalties and mining taxes	**(1,491)**	**(399)**	**(320)**	**(170)**	**(602)**	(1,322)	(385)	(463)	(260)	(214)
Workers participation	**(1,153)**	**(379)**	**(428)**	**52**	**(398)**	(3,141)	(436)	(1,132)	(852)	(721)
Depletion and depreciation	**(20,477)**	**(4,879)**	**(5,826)**	**(5,374)**	**(4,398)**	(9,060)	(3,752)	(2,056)	(1,478)	(1,774)
Cash cost (A)	**67,690**	**19,327**	**17,377**	**16,032**	**14,954**	36,932	13,417	9,846	7,110	6,559
Cash cost (A)	**67,690**	**19,327**	**17,377**	**16,032**	**14,954**	36,932	13,417	9,846	7,110	6,559
Add / (Subtract)										

By-product credits	**(52,899)**	**(12,878)**	**(13,359)**	**(13,388)**	**(13,274)**	(40,644)	(11,184)	(10,207)	(9,720)	(9,533)
Refining charges	**7,790**	**2,051**	**1,986**	**1,849**	**1,904**	4,308	2,242	1,015	541	510
Cash cost applicable per payable ounce (B)	**22,581**	**8,500**	**6,004**	**4,493**	**3,584**	596	4,475	654	(2,069)	(2,464)
Payable ounces of silver production (C)	**3,788,369**	**960,194**	**976,355**	**946,384**	**905,436**	2,352,759	860,566	625,696	451,230	415,267
Cash cost per ounce of payable silver ($/oz) (B/C)	**5.96**	**8.85**	**6.15**	**4.75**	**3.96**	0.25	5.20	1.05	(4.59)	(5.93)

(1) Includes depletion, depreciation, distribution, community relations, government royalties and mining taxes, and workers participation.

San Jose Mine Cash Cost — **Expressed in $'000's**

	2012					2011		
	YTD	**Q4**	**Q3**	**Q2**	**Q1**	YTD	Q4	Q3
Cost of sales (1)	**39,126**	**10,090**	**11,184**	**10,147**	**7,705**	6,794	6,005	789
Add / (Subtract)								
Change in concentrate inventory	**(269)**	**115**	**(384)**	**(957)**	**957**	1,936	323	1,613
Depletion and depreciation in concentrate inventory	**146**	**16**	**150**	**338**	**(358)**	(684)	(195)	(489)
Workers participation	**(41)**	**(41)**	**-**	**-**	**-**	-	-	-
Depletion and depreciation	**(11,616)**	**(2,035)**	**(3,567)**	**(3,409)**	**(2,605)**	(2,141)	(1,988)	(153)
Cash cost (A)	**27,346**	**8,145**	**7,383**	**6,119**	**5,699**	5,905	4,145	1,760
Total processed ore (tonnes) (B)	**369,022**	**98,348**	**91,607**	**92,011**	**87,056**	116,410	87,885	28,525
Cash cost per tonne of processed ore ($/t) (A/B)	**74.10**	**82.82**	**80.59**	**66.50**	**65.46**	50.73	47.16	61.70
Cash cost (A)	**27,346**	**8,145**	**7,383**	**6,119**	**5,699**	5,905	4,145	1,760
Add / (Subtract)								
By-product credits	**(23,146)**	**(4,916)**	**(5,800)**	**(6,432)**	**(5,998)**	(5,539)	(4,313)	(1,226)
Refining charges	**2,757**	**679**	**717**	**693**	**668**	1,718	1,341	377
Cash cost applicable per payable ounce (C)	**6,957**	**3,908**	**2,300**	**380**	**369**	2,084	1,173	911
Payable ounces of silver production (D)	**1,851,718**	**466,622**	**477,694**	**461,981**	**445,421**	444,695	350,960	93,735
Cash cost per ounce of payable silver ($/oz) (B/C)	**3.76**	**8.38**	**4.81**	**0.82**	**0.83**	4.69	3.34	9.72
Mining cost per tonne	**33.43**	**40.36**	**35.51**	**28.84**	**28.26**	17.37	15.03	24.57
Milling cost per tonne	**17.96**	**17.84**	**20.10**	**15.76**	**18.15**	14.64	15.16	13.07
Indirect cost per tonne	**15.53**	**15.99**	**17.47**	**14.24**	**14.37**	11.54	11.33	12.12
Community relations cost per tonne	**2.09**	**3.52**	**2.33**	**2.29**	**0.02**	4.47	2.27	11.24
Distribution cost per tonne	**5.09**	**5.11**	**5.18**	**5.37**	**4.66**	2.71	3.37	0.70
Total production cost per tonne	**74.10**	**82.82**	**80.59**	**66.50**	**65.46**	50.73	47.16	61.70

(1) Includes depletion, depreciation, distribution, community relations, government royalties and mining taxes, and workers participation.

Caylloma Mine Cash Cost — **Expressed in $'000's**

	2012					2011				
	YTD	**Q4**	**Q3**	**Q2**	**Q1**	YTD	Q4	Q3	Q2	Q1
Cost of sales (1)	**51,232**	**14,541**	**13,412**	**11,464**	**11,815**	42,236	11,777	11,943	9,682	8,834
Add / (Subtract)										
Change in concentrate inventory	**699**	**279**	**(488)**	**637**	**271**	206	92	(445)	(4)	563
Depletion and depreciation in concentrate inventory	**(123)**	**(57)**	**77**	**(105)**	**(38)**	(33)	(12)	86	22	(129)
Government royalties and mining taxes	**(1,491)**	**(399)**	**(320)**	**(170)**	**(602)**	(1,322)	(385)	(463)	(260)	(214)
Workers participation	**(1,112)**	**(338)**	**(428)**	**52**	**(398)**	(3,141)	(436)	(1,132)	(852)	(721)
Depletion and depreciation	**(8,861)**	**(2,844)**	**(2,259)**	**(1,965)**	**(1,793)**	(6,919)	(1,764)	(1,903)	(1,478)	(1,744)
Cash cost (A)	**40,344**	**11,182**	**9,994**	**9,913**	**9,255**	31,027	9,272	8,086	7,110	6,559
Total processed ore (tonnes) (B)	**462,222**	**115,522**	**117,386**	**115,870**	**113,444**	448,866	116,363	115,574	111,992	104,937
Cash cost per tonne of processed ore ($/t) (A/B)	**87.28**	**96.80**	**85.14**	**85.55**	**81.58**	69.12	79.68	69.96	63.49	62.50
Cash cost (A)	**40,344**	**11,182**	**9.994**	**9.913**	**9,255**	31,027	9,272	8,086	7,110	6,559
Add / (Subtract)										
By-product credits	**(29,753)**	**(7,962)**	**(7,559)**	**(6,956)**	**(7,276)**	(35,105)	(6,871)	(8,981)	(9,720)	(9,533)
Refining charges	**5,033**	**1,372**	**1,269**	**1,156**	**1,236**	2,590	901	638	541	510
Cash cost applicable per payable ounce (C)	**15,624**	**4,592**	**3,704**	**4,113**	**3,215**	(1,488)	3,302	(257)	(2,069)	(2,464)
Payable ounces of silver production (D)	**1,936,651**	**493,572**	**498,661**	**484,403**	**460,015**	1,908,064	509,606	531,961	451,230	415,267
Cash cost per ounce of payable silver ($/oz) (B/C)	**8.07**	**9.30**	**7.43**	**8.49**	**6.99**	(0.78)	6.48	(0.48)	(4.59)	(5.93)

Mining cost per tonne	**39.78**	**40.04**	**39.76**	**40.64**	**38.67**	32.05	38.02	31.84	28.71	29.23
Milling cost per tonne	**14.05**	**15.69**	**14.13**	**12.66**	**13.73**	11.54	12.49	11.64	10.86	11.12
Indirect cost per tonne	**24.83**	**27.82**	**24.29**	**25.13**	**22.00**	18.80	21.92	19.80	17.44	15.70
Community relations cost per tonne	**1.46**	**4.61**	**0.43**	**0.48**	**0.32**	0.67	1.01	0.59	0.28	0.78
Distribution cost per tonne	**7.16**	**8.64**	**6.53**	**6.64**	**6.86**	6.06	6.24	6.09	6.20	5.67
Total production cost per tonne	**87.28**	**96.80**	**85.14**	**85.55**	**81.58**	69.12	79.68	69.96	63.49	62.50

(1) Includes depletion, depreciation, distribution, community relations, government royalties and mining taxes, and workers participation.

Liquidity and Capital Resources

Full Year Liquidity and Capital Resources

The capital of the Company consists of equity and available credit facility, net of cash. The Board of Directors does not establish a quantitative return on capital criteria for management. The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets.

The Company's cash and cash equivalents as at December 31, 2012 totalled $58.7 million (2011: $38.7 million), and short term investments totalled $6.0 million (2011: $17.0 million).

The $20.0 million increase (2011: $31.9 million decrease) in cash and cash equivalents at December 31, 2012 is due to the cash provided by operating activities of $53.9 million, net cash used in investing activities of $33.0 million and net cash used in financing activities of $0.9 million, and the effect of exchange rate changes on cash and cash equivalents of $0.1 million. Compared to 2011, the Company's expenditures on mineral properties, plant and equipment declined by $31.8 million and redemptions of short term investments declined by $36.4 million and cash provided by operating activities increased by $18.9 million attributable to the commissioning of San Jose mine on September 1, 2011.

Working capital for the year increased $23.5 million to $87.4 million reflecting increases inaccounts receivable and other assets of $7.9 million, prepaid expenses of $0.1 million, inventories of $1.6 million, assets held for sale of $0.1 million, and decreases in due to related parties of $0.2 million, derivative liabilities of $0.1 million, provisions of $0.3 million, income tax payable of $3.7 million, current portion of long term liabilities of $1.1 million; offset by decreases in short term investments of $11.0 miilion, derivative assets of $0.1 million, due from related parties and increases in trade and other payables of 0.2 million.

During the year ended December 31, 2012, cash generated by operating activities before changes in non-cash working capital items, income taxes paid, and interest income paid and received was $62.2 million (2011: $39.1 million). Changes in non-cash working capital items amounted to $8.4 million (2011: $4.1 million), and income taxes paid and interest income paid and received amounted to $10.1 million (2011: $14.3 million), resulting in net cash provided by operating activities of $53.9 million (2011: $35.0 million).

Cash used by the Company for the year ended December 31, 2012, in investing activities totalled $33.0 million (2011: $69.3 million) comprised of $11.0 million (2011: $3.7 million) net redemptions of short term investments, $0.7 million (2011: $3.6 million) net receipts on deposits on long term assets, $0.1 million (2011: nil) proceeds on disposal of mineral properties, plant and equipment, and offset by $44.8 million (2011: $76.7 million) expenditures on mineral properties, plant and equipment.

During the year ended December 31, 2012, cash used by financing activities totalled $0.9 million (2011: provided $2.5 million) with net repayment of long term debt of $0.8 million (2011: nil), repayment of finance lease obligations of $0.8 million (2011: $1.2 million), and offset by net proceeds on the issuance of common shares of $0.7 million (2011: $3.7 million).

Fourth Quarter Liquidity and Capital Resources

During Q4 2012, cash generated by operating activities before changes in non-cash working capital items, income taxes paid, and interest income paid and received was $11.9 million (Q4 2011: $8.8 million). Changes in non-cash working capital items amounted to $5.7 million (Q4 2011: $1.2 million), and income taxes paid and interest income paid and received amounted to $1.0 million (Q4 2011: $3.1 million), resulting in net cash provided by operating activities of $17.6 million (Q4 2011: $7.6 million).

Cash used by the Company in Q4 2012 for investing activities totalled $19.2 million (Q4 2011: $31.9 million), with $15.8 million (Q4 2011: $16.2 million) for expenditures on mineral properties, plant and equipment, $0.6 million (Q4 2011: $0.6 million net advances) in net receipts on deposits on long term assets, and $4.0 million (Q4 2011: $15.0 million) for net purchases of short term investments.

During Q4 2012, cash used by financing activities was $0.1 million, compared to $2.0 million provided by such activities in Q4 2011, and included repayment of finance lease obligations of $0.1 million (Q4 2011: $0.2 million), offset by net proceeds on the issuance of common shares of nil (Q4 2011: $2.2 million).

In 2010, the Company entered into a credit agreement with the Bank of Nova Scotia for a $20 million senior secured revolving credit facility ("credit facility") to be refinanced or repaid on or within two and one-half years or before February 6, 2013. The credit facility is secured by a first ranking lien on Bateas and its assets and bears interest and fees at prevailing market rates. In the event that utilization under the credit facility is less than $10 million, a commitment fee of 1.50% per annum is payable quarterly on the unutilized portion of

the available credit facility. No funds have been drawn from this credit facility.

In February 2013, the Bank of Nova Scotia extended the credit facility maturity date to February 6, 2013 and then to February 27, 2013. On March 15, 2013, the Bank of Nova Scotia extended the credit facility maturity date to March 28, 2013. No funds were drawn from this credit facility.

The Company has raised funds from two prospectus financings in 2010. The details of the expected use of proceeds and actual use of proceeds are discussed below.

Prospectus February 18, 2010 Closed March 2, 2010

	San Jose Project Financing Expressed in CAD $ millions		
	Expected Use of Proceeds*	Actual Use of Proceeds**	Variance
Mine development	$ 6.7	$ 11.2	$ (4.5)
Processing plant	16.6	30.4	(13.8)
Tailings dam	1.9	4.4	(2.5)
Water and Infrastructure	3.0	3.5	(0.5)
Energy supply	-	2.5	(2.5)
Construction management	-	2.5	(2.5)
Total	**$ 28.2**	**$ 54.5**	**$ (26.3)**

*excludes over-allotment
**US CAD FX rate at 1.0

Prospectus December 17, 2010 Closed December 23, 2010

	San Jose Project Financing** Expressed in CAD $ millions		
	Expected Use of Proceeds*	Actual Use of Proceeds**	Variance
Planned expansion	$ 14.5	$ -	$ 14.5
Exploration programs	5.5	11.4	(5.9)
Working Capital	17.7	26.3	(8.6)
Total	**$ 37.7**	**$ 37.7**	**$ -**

*excludes over-allotment
** funds to be utilized post development

Management believes that the Company's current operational requirements and capital projects can be funded from existing cash and cash equivalents, cash generated from operations, and the available credit facility. If future circumstances dictate an increased cash requirement and we elect not to delay, limit, or eliminate some of our plans, we may raise additional funds through debt financing, the issuance of hybrid debt-equity securities, or additional equity securities. If the Company needs to access the capital markets for additional financial resources, managements believes the Company will be able to do so at prevailing market rates.

Contractual Obligations

The Company expects the following maturities of its financial liabilities (including interest), finance leases, and other contractual commitments:

	Expressed in $ millions Expected payments due by period as at December 31, 2012				
	Less than 1 year	1 - 3 years	4 -5 years	After 5 years	Total
Trade and other payables	$ 17.3	$ -	$ -	$ -	$ 17.3
Due to related parties	0.1	-	-	-	0.1
Income tax payable	0.2	-	-	-	0.2
Long term liabilities	0.5	2.3	-	-	2.8
Operating leases	0.7	1.3	0.9	0.1	3.0
Provisions	0.5	0.5	0.5	11.3	12.8
	$ 19.3	**$ 4.1**	**$ 1.4**	**$ 11.4**	**$ 36.2**

Capital Commitments (expressed in $'000's)

As at December 31, 2012, $5,613 of capital commitments not disclosed elsewhere in the consolidated financial statements, and forecasted to be expended within one year, includes the following: $4,280 mine and tailing dam development at the San Jose property; and, $1,333 for the tailings dam transport system, concentrator plant, electrical infrastructure renewal, and camp infrastructure at Caylloma.

Other Commitments (expressed in $'000's)

The Company has a contract to guarantee power supply at its Caylloma mine. Under the contract, the seller is obligated to deliver a "maximum committed demand" (for the present term this stands at 3,500 Kw) and the Company is obligated to purchase subject to exemptions under provisions of "Force Majeure". The contract is automatically renewed every two years for a period of 10 years and expiring in 2017. Renewal can be avoided without penalties by notification 10 months in advance of renewal date.

Tariffs are established annually by the energy market regulator in accordance with applicable regulations in Peru.

The Company acts as guarantor to finance lease obligations held by two of its mining contractors. These finance lease contracts are related to the acquisition of mining equipment deployed at the Caylloma mine. As at December 31, 2012, these obligations amounted to $13 and mature in 2013.

On May 24, 2010, the Company entered into a seven year office premise lease located in Peru. The annual rent payable on 1,717 rentable square meters for office space is as follows:

- year one $289;
- year two $297;
- year three $306; and,
- years four through seven, the lease is subject a minimum annual increase of 3% or the Consumer Price Index published by Bureau of Labor Statistics of the United States Department of Labor, whichever is higher.

The lease also includes the use of additional space for mini-warehouse and parking spots, the obligation for which is $58 per annum for the first year and is subject to an annual increase of 3% as stated above until the end of the lease. During 2011, the Company provided a security deposit of $44.

On September 30, 2012, the Company entered into a one year office premise lease in Mexico effective September 30, 2012, with an annual lease obligation of $16.

The expected payments due by period as at December 31, 2012 are as follows:

	Expected payments due by period as at December 31, 2012				
	Less than 1 year	1 - 3 years	4 -5 years	After 5 years	Total
Office premises – Canada	$ 148	$ 443	$ 306	$ 147	$ 1,044
Office premises – Peru	373	781	580	-	1,734
Office premises – Mexico	14	-	-	-	14
Total office premises	**$ 535**	**$ 1,224**	**$ 886**	**$ 147**	**$ 2,792**
Computer equipment – Peru	149	64	-	-	213
Computer equipment – Mexico	18	17	-	-	35
Total computer equipment	**$ 167**	**$ 81**	**$ -**	**$ -**	**$ 248**
Total operating leases	**$ 702**	**$ 1,305**	**$ 886**	**$ 147**	**$ 3,040**

Other Contingencies

The Company is subject to various investigations, claims and legal and tax proceedings covering matters that arise in the ordinary course of business activities. Each of these matters is subject to various uncertainties and it is possible that some of these matters may be resolved unfavorably to the Company. Certain conditions may exist as of the date the financial statements are issued, which may result in a loss to the Company. In the opinion of management none of these matters are expected to have a material effect on the results of operations or financial conditions of the Company.

During the year ended December 31, 2012, the Ministry of Mining and Energy (MEM) in Peru made an update to the approved Mining Environmental Liabilities List. The Company is currently in the process of evaluating its mining concessions which are currently included on the list and as at the date of the issuance of the financial statements an estimate of liability cannot be determined.

Guarantees and Indemnifications (expressed in $'000's)

The Company may provide guarantees and indemnifications in conjunction with transactions in the normal course of operations. These are recorded as liabilities when reasonable estimates of the obligations can be made. Indemnifications that the Company has provided include obligation to indemnify:

- Ø directors and officers of the Company and its subsidiaries for potential liability while acting as a director or officer of the Company, together with various expenses associated with defending and settling such suits or actions due to association with the Company;
- Ø certain vendors of acquired company for obligations that may or may not have been known at the date of the transaction; and,
- Ø the dollar value cannot be reasonably estimated.

The Caylloma mine closure plan was approved in November 2009 with total closure costs of $3,587 of which $1,756 is subject to annual collateral in the form of a letter of guarantee, to be awarded each year in increments of $146 over 12 years based on the estimated life of the mine.

Scotiabank Peru, a third party, has established a bank letter of guarantee on behalf of Bateas in favor of the Peruvian mining regulatory agency in compliance with local regulation associated with the approved Bateas' mine closure plan, for the sum of $585. This bank letter of guarantee expires 360 days from December 2012.

Banco Bilbao Vizcaya Argentaria, S.A. had also established bank letters of guarantee totalling $54 to provide an annual guarantee associated with an office lease contract and truck rentals. These bank letters of guarantee were renewed in June 2011 with expiry 360 days to June 2012. This guarantee expired in June 2012.

Off-Balance Sheet Arrangements

The Company does not have any off-balance sheet arrangements or commitments that are expected to have a current or future effect

on our financial condition, results of operations, liquidity, capital expenditures, or capital resources that are material to investors, other than those disclosed in this MD&A and the consolidated financial statements and the related notes.

Related Party Transactions *(expressed in $'000's)*

a) Purchase of Goods and Services

The Company entered into the following related party transactions:

Transactions with related parties	Expressed in $'000's Years ended December 31, 2012	2011
Salaries and wages [1,2]	**$ 135**	$ 173
Other general and administrative expenses [2]	**308**	292
Leasehold improvements [2]	**23**	93
	$ 466	$ 558

[1] Salaries and wages includes employees' salaries and benefits charged to the Company based on a percentage of the estimated hours worked for the Company.

[2] Radius Gold Inc. ("Radius") has directors in common with the Company and shares office space, and is reimbursed for salaries, wages, general and administration costs, and leasehold improvements incurred on behalf of the Company to June 30, 2012. Gold Group Management Inc. ("Gold Group"), which is owned by a director in common with the Company, provides various administrative, management, and other related services effective July 1, 2012.

In January 2012, the Company issued 8,605 (2011: 6,756) common shares, at a fair market value of $5.81 (2011: $4.44) per share and paid $50 (2011: $30) cash to Radius, under the option to acquire a 60% interest in Tlacolula silver project located in the State of Oaxaca, Mexico.

In October 2012, the Company entered into a services agreement, effective July 1, 2012, with Gold Group Management Inc. ("Gold Group"), which is owned by a director in common with the Company. The services agreement provides that Gold Group provides various administrative, management and other related services.

Subsequent to December 31, 2012, on January 14, 2013 the Company issued 11,415 common shares of the Company, at a fair market value of $4.38 per share and paid $50 cash to Radius, under the option to acquire a 60% interest in the Tlacolula silver project located in the State of Oaxaca, Mexico.

b) Key Management Compensation

Key management includes all persons named or performing the duties of Vice-President, Chief Financial Officer, President, Chief Executive Officer, and non-executive Directors of the Company. The compensation paid or payable to key management for services is shown below:

	Expressed in $'000's Years ended December 31, 2012	2011
Salaries and other short term employee benefits	**$ 2,789**	$ 3,492
Directors fees	**388**	333
Consulting fees	**180**	416
Share-based payments	**1,629**	4,398
	$ 4,986	$ 8,639

The share-based payments includes the change in the deferred share unit ("DSU") and restricted share unit ("RSU") fair value over each reporting period and payments made under the DSU and RSU plans and the non-cancellation of share options.

Consulting fees includes fees paid to two non-executive directors in both 2012 and 2011.

c) Year end Balances arising from Purchases of Goods/Services

Amounts due from related parties	Expressed in $'000's December 31, 2012	December 31, 2011
Owing from a director and officer [3]	**$ -**	$ 36
Owing from a company with common director [3]	**5**	-
	$ 5	$ 36

[3] Owing from a director includes non-interest bearing advances to company controlled by a director of the company at December 31, 2012 and to director and officers at December 31, 2011.

Amounts due to related parties	Expressed in $'000's December 31, 2012	December 31, 2011

Owing to a company(ies) with common directors [4]	**$**	**54**	$	205

[4] 2012 Owing to Radius Gold Inc. ("Radius") and Gold Group Management Inc. ("Gold Group") whom have directors in common with the Company and 2011 to Radius.

On October 10, 2012, the Company paid Gold Group Management Inc., which is owned by a director in common with the Company, a retainer of $61 representing three months deposit under a services agreement effective July 1, 2012.

Significant Accounting Judgments and Estimates

The preparation of these consolidated financial statements requires management to make judgments and estimates that affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of expenses during the reporting period. Actual outcomes could differ from these judgments and estimates. The consolidated financial statements include judgments and estimates which, by their nature, are uncertain. The impacts of such judgments and estimates are pervasive throughout the consolidated financial statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and the revision affects both current and future periods. Significant assumptions about the future and other sources of judgments and estimates that management has made at the statement of financial position date, that could result in a material adjustment to the carrying amounts of assets and liabilities, in the event that actual results differ from assumptions made, relate to, but are not limited to, the following:

i. Critical Judgments

- The analysis of the functional currency for each entity of the Company. In concluding that the United States dollar functional currency for its Peruvian and Mexican entities and the Canadian and Barbados entities have a Canadian dollar functional currency, management considered the currency that mainly influences the cost of providing goods and services in each jurisdiction in which the Company operates. As no single currency was clearly dominant the Company also considered secondary indicators including the currency in which funds from financing activities are denominated and the currency in which funds are retained.
- In concluding when commercial production has been achieved, the Company considered the following factors:

- all major capital expenditures to bring the mine to the condition necessary for it to be capable of operating in the manner intended by management have been completed;
- the mine or mill is operating within eighty percent of design capacity;
- metallurgical recoveries are achieved within eighty percent of projections; and,
- the ability to sustain ongoing production of ore at a steady or increasing level.
- The identification of reportable segments, basis for measurement and disclosure of the segmented information.
- The determination of estimated useful lives and residual values of tangible and long-lived assets and the measurement of depreciation expense.
- The identification of impairment indicators, cash generating units and determination of value in use and the write down of tangible and long lived assets.
- Measurement of financial instruments involve significant judgments related to interpretation of the terms of the instrument, identification, classification, impairment and the overall measurement to approximate fair values.

ii. Estimates

- the recoverability of amounts receivable which are included in the consolidated statements of financial position;
- the estimation of assay grades of metal concentrates sold in the determination of the carrying value of accounts receivable which are included in the consolidated statements of financial position and included as sales in the consolidated statements of income;
- the carrying value of the short term investments and the recoverability of the carrying value which are included in the consolidated statements of financial position;
- the determination of net realizable value of inventories on the consolidated statements of financial position;
- the estimated useful lives of property, plant and equipment which are included in the consolidated statements of financial position and the related depreciation included in the consolidated statements of income;
- the determination of mineral reserves, carrying amount of mineral properties, and depletion of mineral properties included in the consolidated statements of financial position and the related depletion included in the consolidated statements of income;
- review of tangible and intangible assets carrying value, the determination of whether these assets are impaired and the measurement of impairment charges or reversals which are included in the consolidated statements of income;
- the determination of the fair value of financial instruments and derivatives included in the consolidated statements of financial position;
- the fair value estimation of share-based awards included in the consolidated statements of financial position and the inputs used in accounting for share-based compensation expense in the consolidated statements of income;
- the provision for income taxes which is included in the consolidated statements of income and composition of deferred income tax asset and liabilities included in the consolidated statement of financial position;
- the recognition of deferred income tax assets, amounts recorded for uncertain tax positions, the measurement of income tax expense and indirect taxes included in the consolidated statement of financial position;
- the inputs used in determining the net present value of the liability for provisions related to decommissioning and restoration included in the consolidated statements of financial position;

- the inputs used in determining the various commitments and contingencies accrued in the consolidated statements of financial position; and,
- the assessment of indications of impairment of each mineral properties and related determination of the net realizable value and write-down of those properties where applicable.

Financial Instruments and Related Risks *(expressed in 000's)*

The Company is exposed to certain financial risks, including currency risk, credit risk, liquidity risk, interest risk, and price risk. The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework and reviews the Company's policies on an ongoing basis.

a) Fair Value of Financial Instruments

The carrying value of cash and cash equivalents, short term investments, derivative assets, trade receivable from concentrate sales, other accounts receivables, due from related parties, trade and other payables, due to related parties, and derivative liabilities approximate their fair value due to the relatively short periods to maturity and the terms of these financial instruments. Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument.

The amortized value of long term receivables approximates their fair value as these are measured at the amortized cost using the effective interest method. The fair value of the lease and long term liabilities is $2,723 as at December 31, 2012.

The analysis of financial instruments that are measured subsequent to initial recognition at fair value can be categorized into Levels 1 to 3 based upon the degree to which the fair value is observable.

- Level 1 - inputs to the valuation methodology are quoted (unadjusted) for identical assets or liabilities in active markets.
- Level 2 - inputs to valuation methodology include quoted market prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 - inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The Company has classified the determination of fair value of trade receivable concentrate sales, and derivatives as Level 2, as the valuation method used by the Company includes an assessment of assets in quoted markets with significant observable inputs.

Expressed in $'000's

Financial assets (liabilities) at fair value as at December 31, 2012				
	Level 1	**Level 2**	**Level 3**	**Total**
Cash and cash equivalents	**$ 58,720**	**$ -**	**$ -**	**$ 58,720**
Short term investments	**6,019**	**-**	**-**	**6,019**
Trade receivable from concentrate sales	**-**	**15,158**	**-**	**15,158**
	$ 64,739	**$ 15,158**	**$ -**	**$ 79,897**

There were no changes in the levels during the year ended December 31, 2012.

Expressed in $'000's

Financial assets (liabilities) at fair value as at December 31, 2011				
	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	$ 38,730	$ -	$ -	$ 38,730
Short term investments	17,000	-	-	17,000
Trade receivable from concentrate sales	-	11,287	-	11,287
Derivatives assets	-	70	-	70
Derivatives liabilities	-	(87)	-	(87)
	$ 55,730	$ 11,270	$ -	$ 67,000

There were no changes in the levels during the year ended December 31, 2011.

Accounts receivable includes trade receivable from concentrate sales, provisional price adjustments, and final price adjustments. The fair value of accounts receivable resulting from provisional pricing reflect observable market commodity prices. Resulting fair value changes to accounts receivable are through sales. Transactions involving accounts receivable are with counterparties the Company believes are creditworthy. As such, these accounts receivable are classified within Level 2 of the fair value hierarchy.

Derivatives are carried at their fair value, which is determined based on internal valuation models that reflect observable forward market commodity prices. Resulting fair value changes to derivatives are through net gain (loss) on commodity contracts. Transactions involving derivatives are with counterparties the Company believes to be creditworthy.

During the year ended December 31, 2012, there have been no changes in the classification of financial assets and liabilities in Levels 1, 2, and 3 of the hierarchy.

b) Currency Risk

The Company is exposed to the financial risk related to the fluctuation of foreign exchange rates. The Company operates in Canada, Peru and Mexico and a portion of its expenses are incurred in Canadian dollars, nuevo soles, and Mexican pesos. A significant change in the currency exchange rates between the United States dollar relative to the other currencies could have a material effect on the Company's income, financial position, or cash flows. The Company has not hedged its exposure to currency fluctuations.

As at December 31, 2012, the Company is exposed to currency risk through the following assets and liabilities denominated in Canadian dollars, nuevo soles and Mexican pesos (all amounts are expressed in thousands of Canadian dollars, thousands of nuevo soles or thousands of Mexican pesos):

	Expressed in '000's					
	December 31, 2012			December 31, 2011		
	Canadian Dollars	**Nuevo Soles**	**Mexican Pesos**	Canadian Dollars	Nuevo Soles	Mexican Pesos
Cash and cash equivalents	**$ 4,231**	**S/. 1,389**	**$ 6,136**	$ 18,457	S/. 1,396	$ 1,758
Short term investments	**6,000**	**-**	**-**	-	-	-
Accounts receivable and other assets	**77**	**3,097**	**98,147**	42	5,657	58,939
Due from related parties	**-**	**-**	**-**	-	4,434	-
Trade and other payables	**(1,225)**	**(12,300)**	**(49,779)**	(1,580)	(17,993)	(24,310)
Due to related parties	**(54)**	**-**	**-**	(209)	-	-
Provisions, current	**-**	**(284)**	**(4,502)**	-	(1,351)	(3,163)
Income tax payable	**-**	**(326)**	**-**	-	(10,581)	-
Leases and long term liabilities	**(1,998)**	**-**	**(245)**	(2,691)	-	-
Provisions	**-**	**(19,560)**	**(39,323)**	-	(8,079)	(17,494)
Total	**$ 7,031**	**S/. (27,984)**	**$ 10,434**	$ 14,019	S/. (26,517)	$ 15,730
Total US$ equivalent	**$ 7,053**	**$ (10,970)**	**$ 802**	$ 13,745	$ (9,832)	$ 1,125

Based on the above net exposure as at December 31, 2012, and assuming that all other variables remain constant, a 10% depreciation or appreciation of the US dollar against the above currencies would result in an increase or decrease, as follows: impact to other comprehensive income of $784 (2011: $1,527) and a net loss of $1,130 (2011: $967).

c) Credit Risk

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations. The Company's cash and cash equivalents and short term investments are held through large Canadian, international and foreign national financial institutions. These investments mature at various dates within one year. All of the Company's trade accounts receivables are held with large international metals trading companies.

The Company holds derivative contracts with financial institutions and in this regard is exposed to counterparty risk. The Company mitigates this risk by transacting only with reputable financial institutions to minimize credit risk.

The Company's maximum exposure to credit risk at December 31, 2012 is as follows:

	Expressed in '000's	
	December 31, 2012	December 31, 2011
Cash and cash equivalents	**$ 58,720**	$ 38,730
Short term investments	**6,019**	17,000
Accounts receivable and other assets	**27,032**	19,167
Derivative assets	**-**	70
Due from related parties	**5**	36
	$ 91,776	$ 75,003

The carrying amount of financial assets recorded in the financial statements represents the Company's maximum exposure to credit risk. The Company believes it is not exposed to significant credit risk and overall, the Company's credit risk has not declined significantly from the prior year.

d) 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 by continuing to monitor forecasted and actual cash flows. The Company has in place a planning and budgeting process to help determine the funds required to support the Company's normal operating requirements on an ongoing basis and its development plans. The Company strives to maintain sufficient liquidity to meet its short term business requirements, taking into account its anticipated cash flows from operations, its holdings of cash, short term investments, and its committed liabilities.

(Refer to Contractual Obligations for the expected payments due as at December 31, 2012.)

Derivatives

	Expressed in $ millions			
	December 31, 2012		December 31, 2011	
	Assets	**Liabilities**	Assets	Liabilities
Lead forward contracts	**$ -**	**$ -**	$ -	$ 0.1
Zinc forward contracts	**-**	**-**	0.1	-
Silver forward contracts	**-**	**-**	-	-
Total	**$ -**	**$ -**	$ 0.1	$ 0.1

The Company occasionally enters into forward commodity contracts as well as put and call option commodity arrangements to secure a minimum price level on part of its zinc and lead metal production. As at the end of the period no such contracts are outstanding.

In 2011, the Company entered into short term forward and option contracts to fix the final settlement price of metal delivered in concentrates, where the final settlement price is yet to be set at a future quotational period according to contract terms. The forward sale and option contracts were settled against the arithmetic average of metal spot prices over the month in which the contract matures. No initial premium associated with these trades had been paid.

Significant Accounting Policy

Operational Mining Properties and Mine Development

For operating mines, all exploration within the mineral deposit is capitalized and amortized on a unit-of-production basis over proven and probable reserves and the portion of resources expected to be extracted economically as part of the production cost.

Costs of producing properties are amortized on a unit-of-production basis over proven and probable reserves and the portion of resources expected to be extracted economically, and costs of abandoned properties are written-off.

The company has made a change in estimate and commencing in the fourth quarter of 2012, the amortization on a unit-of-production basis will be over the portion of resources, in addition to the proven and probable reserves, expected to be extracted economically. The change in estimate is applied prospectively and impacts the depletion of the mineral deposit for the current and future periods.

Significant Changes in Accounting Policies including Initial Adoption

IFRS 7 *Financial Instruments: Disclosures* (Amendment)
The amendment, effective for annual periods beginning on or after July 1, 2011, with early application permitted, requires additional quantitative and qualitative disclosures relating to transfers of financial assets, where: financial assets are derecognized in their entirety, but where the entity has a continuing involvement in them; financial assets that are not derecognized in their entirety. The Company has adopted the amendment to IFRS 7 and the amendment did not have a material impact on the Company's consolidated financial statements.

IAS 12 *Income Taxes* (Amendment)
IAS 12 *Income Taxes*, amendments regarding Deferred Tax: Recovery of Underlying Assets introduces an exception to the existing principle for the measurement of deferred tax assets and liabilities arising on investment property measured at fair value, and the requirement that deferred tax on non-depreciable assets measured using the revaluation model in IAS 16 should always be measured on a sale basis. The amendment is effective for annual periods beginning on or after January 1, 2012. The Company has adopted the amendment to IAS 12 and the amendment did not have a material impact on the Company's consolidated financial statements.

New Accounting Standards

The Company is currently assessing the impact of adopting the new accounting standards, noted below, on our consolidated financial statements.

The following standards and amendments to existing standards have been published and are mandatory for the Company's annual accounting periods beginning on or after July 1, 2012 or later:

i) New Accounting Standards Impacting on or after July 1, 2012

IAS 1 *Presentation of Financial Statements* (Amendment)
The amendments to IAS 1 *Presentation of Financial Statements* retain the 'one or two statement' approach at the option of the entity and only revise the way other comprehensive income ("OCI") is presented: requiring separate subtotals for those elements which may be 'recycled' (e.g. cash-flow hedging, foreign currency translation), and those elements that will not (e.g. fair value through OCI items under IFRS 9) to the statement of income. In addition, the tax associated with items presented before tax to be shown separately for each of the two groups of OCI items (without changing the option to present items of OCI either before tax or net of tax).

ii) New Accounting Standards Impacting on or after January 1, 2013

On May 17, 2012, the IASB issued Annual Improvements to IFRSs: 2009-2011 Cycle, incorporating amendments to five IFRSs;**IFRS 1** ***First-time Adoption of International Reporting Standards*****, IAS 1** ***Presentation of Financial Statements*****, IAS 16** ***Property, Plant and Equipment*****, IAS 32** ***Financial Statements: Presentation*****, IAS 34** ***Interim Financial Reporting***. The amendments are effective for annual periods beginning on or after January 1, 2013, with early application permitted, and must be applied retrospectively.

IFRS 1 ***First-time Adoption of International Financial Reporting Standards*** (Amendment)
IFRS 1 is amended to clarify the repeated application of IFRS 1 and the treatment of borrowing costs incurred on or after the date of transition to IFRSs. This is not applicable as the company has already transitioned to IFRS.

IAS 1 ***Presentation of Financial Statements*** (Amendment)
IAS 1 is amended to clarify that only one comparative period - which is the preceding period - is required for a complete set of financial statements.

IAS 16 ***Property, Plant, and Equipment*** (Amendment)
IAS 16 is amended to clarify the classification of servicing equipment. Spare parts, stand-by equipment and servicing equipment should be classified as property, plant, and equipment when they meet the definition of property, plant, and equipment in IAS 16 and otherwise as inventory using IAS 2 *Inventories*.

IAS 32 ***Financial Instruments: Presentation*** (Amendment)
IAS 32 is amended to clarify that IAS 12 *Income Taxes* applies to the account for income taxes relating to distributions to holders of equity instruments and transaction costs of equity transactions.

IAS 34 Interim Financial Reporting (Amendment)
IAS 34 is amended to clarify that the total assets and total liabilities for a particular reportable segment would be separately disclosed in interim financial reporting only when the amounts are regularly provided to the chief operating decision maker and there has been a material change from the amounts disclosed in the last annual financial statements for the reportable segment.

The Company does not anticipate these amendments to have a significant impact on its consolidated financial statements.

IFRS 7 ***Financial Instruments: Disclosures in Respect of Offsetting*** (Amendment)
At its meeting on December 13-15, 2011, the IASB approved amendments to IFRS 7,*Financial Instruments*: Disclosures, with respect to offsetting financial assets and financial liabilities. The common disclosure requirements issued by the IASB and the FASB in December 2011 are intended to help investors and other users to better assess the effect or potential effect of offsetting arrangements on a company's financial position. Companies and other entities are required to apply the amendments for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. The required disclosures should be provided retrospectively. The Company does not anticipate this amendment to have a significant impact on its consolidated financial statements.

IFRS 10 ***Consolidated Financial Statements***
IFRS 10 *Consolidated Financial Statements* replaces the portion of IAS 27 *Consolidated and Separate Financial Statements* that addresses the accounting for consolidated financial statements, and SIC12 *Consolidation - Special Purpose Entities*. IFRS 10 establishes principles for the presentation and preparation of consolidated financial statements when an entity controls one or more entities. This standard (i) requires a parent entity (an entity that controls one or more other entities) to present consolidated financial statements; (ii) defines the principle of control, and establishes control as a basis for consolidation; (iii) sets out how to apply the principle of control whether an investor controls an investee and therefore must consolidate the investee; and (iv) sets out the accounting requirements for the preparation of consolidated financial statements. IFRS 10 is effective for annual periods beginning on or after January 1, 2013. The Company does not anticipate the application of IFRS 10 to have a significant impact on its consolidated financial statements.

IFRS 11 ***Joint Arrangements***
IFRS 11 replaces IAS 31 *Interest in Joint Ventures* and SIC-13 *Jointly-Controlled Entities-Non-Monetary Contributions by Venturers.* This standard establishes the core principle that a party to a joint arrangement determines the type of joint arrangement in which it is involved by assessing its rights and obligations and accounts for those rights and obligations in accordance with that type of joint arrangement (joint operations or joint ventures). This standard is effective for annual periods on or after January 1, 2013.

IFRS 12 ***Disclosure of Interests in Other Entities***
IFRS 12 combines the disclosure requirements for an entity's interest in subsidiaries, joint arrangements, associates and structured entities into one comprehensive disclosure standard. This standard requires the disclosure of information that enable users of financial statements to evaluate the nature of, and risks associated with, its interest in other entities and the effects of those interests on its

financial position, financial performance and cash flows. This standard is effective for annual periods beginning on or after January 1, 2013.

The Company does not anticipate these amendments to have a significant impact on its consolidated financial statements.

IFRS 13 *Fair Value Measurement*

IFRS 13 *Fair Value Measurement* provides guidance on how to measure fair value, but does not change when fair value is required or permitted under IFRS. IFRS 13 defines fair value, sets out a single IFRS framework for measuring fair value and requires disclosures about fair value measurements. IFRS 13 applies when another IFRS requires or permits fair value measurements or disclosures about fair value measurements (and measurements, such as fair value less costs to sell, based on fair value or disclosures about those measurements), except for: share-based payment transactions within the scope of IFRS 2 *Share-based Payment*; leasing transactions with the scope of IAS 17 *Leases*; measurements that have some similarities to fair value that are not fair value, such as net realizable value in IAS 2 *Inventories*; or value in use IAS 36 *Impairment of Assets*. This standard is effective for annual periods beginning on or after January 1, 2013. The Company does not anticipate the application of IFRS 13 to have a significant impact on its consolidated financial statements.

IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements*, and IFRS 12 *Disclosure of Interests in Other Entities: Transition Guidance*

The amendments provide additional transition relief, limiting the requirement to provide adjusted comparative information to only the preceding comparative period. For disclosures related to unconsolidated structured entities, the amendments will remove the requirement to present comparative information for periods before IFRS 12 is first applied. The effective date of the amendments is annual periods beginning on or after January 1, 2013, which is aligned with the effective date of IFRS 10, IFRS 11, and IFRS 12. The Company does not anticipate these amendments to have a significant impact on its consolidated financial statements.

IAS 19 *Employee Benefits*

On June 16, 2011, the IASB issued amendments to IAS 19, *Employee Benefits,* in order to improve the accounting for employment benefits.

The amendments make important improvements by:

- eliminating the option to defer the recognition of gains and losses, known as the 'corridor method' or the "deferral and amortization approach";
- streamlining the presentation of changes in assets and liabilities arising from defined benefit plans, including requiring re-measurements to be presented in OCI, thereby separating those changes from changes that many perceive to be the result of an entity's day-to-day operations;
- enhancing the disclosure requirements for defined benefit plans, providing better information about the characteristics of defined benefit plans and the risks that entities are exposed to through participation in those plans.

The amendments are effective for financial years beginning on or after January 1, 2013. The Company does not anticipate the application of IFRS 13 to have a significant impact on its consolidated financial statements

IAS 27 *Separate Financial Statements*

IAS 27 has the objective of setting standards to be applied in accounting for investments in subsidiaries, jointly controlled entities, and associates when an entity elects, or is required by local regulations, to present separate (non-consolidated) financial statements. This standard is effective for annual periods beginning on or after January 1, 2013. This standard will not have an impact on the consolidated financial statements.

IAS 28 *Investments in Associates and Joint Ventures*

IAS 28 prescribes the accounting for investments in associates and to set the requirements for the application of the equity method when accounting for investments in associates and joint ventures. This standard is effective for annual periods beginning on or after January 1, 2013. This standard will not have an impact on the consolidated financial statements.

iii) New Accounting Standards Impacting on or after January 1, 2014

IAS 32 *Financial Instruments - Presentation in Respect of Offsetting* (Amendment)

The amendments to IAS 32 address inconsistencies in current practice when applying the requirements with regards to the offsetting of financial assets and financial liabilities. The amendments are effective for annual periods beginning on or after January 1, 2014 and are required to be applied retrospectively.

iv) New Accounting Standards Impacting on or after January 1, 2015

IFRS 9 *Financial Instruments - Classification and Measurement*

IFRS 9*, Financial Instruments:* IFRS 9 introduces the new requirements for the classification, measurement and de-recognition of

financial assets and financial liabilities. The amendments are effective for annual periods beginning on or after January 1, 2015, with earlier application permitted.

Other Data

Additional information related to the Company is available for viewing atwww.sedar.com and the Company's website at www.fortunasilver.com.

Share Position and Outstanding Warrants and Options

The Company's outstanding share position as at March 19, 2013 is 125,305,166 common shares. In addition, 6,091,610 incentive stock options are currently outstanding as follows:

Type of Security	No. of Shares	Exercise Price (CAD$)	Expiry Date
Incentive Stock Options:	1,663,651	$4.46	June 8, 2014
	2,047,542	$4.03	May 29, 2015
	200,000	$1.35	February 5, 2016
	50,000	$2.29	March 30, 2016
	10,000	$1.75	May 8, 2016
	2,500	$0.85	July 5, 2016
	225,000	$1.55	July 5, 2016
	225,000	$1.66	July 10, 2016
	10,000	$0.85	January 11, 2017
	350,000	$2.22	January 11, 2017
	184,138	$6.67	February 20, 2017
	38,000	$0.85	June 27, 2017
	380,779	$3.79	July 31, 2017
	25,000	$0.85	October 24, 2017
	250,000	$0.85	October 5, 2018
	230,000	$0.85	November 5, 2018
	200,000	$0.83	July 6, 2019
TOTAL OUTSTANDING OPTIONS	**6,091,610**		

Other Risks and Uncertainties

There have been no major changes from the reported risks factors outlined in the Annual Information Form for the financial year ended December 31, 2012.

Controls and Procedures

Disclosure Controls and Procedures

The Company's management, with the participation of the Chief Executive Officer and the Chief Financial Officer, have evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in the rules of the SEC and the Canadian Securities Administrators ("CSA") as of December 31, 2012, and have concluded that such disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Securities Exchange Act of 1934 and Canadian securities laws is (i) recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and Canadian securities laws and (ii) accumulated and communicated to them Company's management, including its principal executive officer and principal financial officer, to allow timely decisions regarding required disclosure.

Internal Control over Financial Reporting

The Company's management, with the participation of its CEO and CFO, are responsible for establishing a system of internal control over financial reporting to provide reasonable assurance regarding the reliability and integrity of the Company's financial information and the preparation of its financial statements in accordance with IFRS as issued by the IASB.

The Company's management, including its CEO and CFO, believe that due to its inherent limitations, internal control over financial reporting may not prevent or detect misstatements on a timely basis. Also, projection of any evaluation of the effectiveness of internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

There has been no change in the Company's internal control over financial reporting that occurred during the year that has materially affected, or is reasonably likely to materially affect, its internal control over financial reporting.

Management concludes that, as of December 31, 2012, the Company's internal control over financial reporting was effective and no material weaknesses were identified.

Cautionary Statement on Forward-Looking Statements

Certain statements contained in this MD&A and any documents incorporated by reference into this MD&A constitute forward-looking statements within the meaning of the U.S. Private Securities Litigation Reform Act of 1995 and Section 21E of the United States Securities Exchange Act of 1934, as amended, and forward-looking information within the meaning of applicable Canadian securities legislation (collectively, "forward-looking statements"). Forward-looking statements express or involve discussions with respect to predictions, expectations, beliefs, plans, projections, objectives, assumptions or future events or performance (often, but not always, identified using words or phrases such as "expects", "is expected", "anticipates", "believes", "plans", "projects", "estimates", "assumes", "intends", "strategies", "targets", "goals", "forecasts", "objectives", "budgets", "schedules", "potential" or variations thereof or stating that certain actions, events or results "may", "could", "would", "might" or "will" be taken, occur or be achieved, or the negative of any of these terms and similar expressions) and are not statements of historical fact. Forward-looking statements relate to, among other things:

- mineral "reserves" and "resources" as they involve the implied assessment, based on estimates and assumptions that the reserves and resources described exist in the quantities predicted or estimated and can be profitably produced in the future;
- timing of the completion of construction activities at the Company's properties and their completion on budget;
- production rates at the Company's properties;
- cash cost estimates;
- timing to achieve full production capacity at the Company's properties;
- timing for completion of infrastructure upgrades related to the Company's properties;
- timing for delivery of materials and equipment for the Company's properties; and
- the sufficiency of the Company's cash position and its ability to raise equity capital or access debt facilities.

Forward-looking statements are necessarily based upon a number of estimates and assumptions that, while considered reasonable by the Company as at the date of such statements, are inherently subject to significant business, economic, social, political and competitive uncertainties and contingencies and other factors that could cause actual results or events to differ materially from those projected in the forward-looking statements. The estimates and assumptions of the Company contained or incorporated by reference in this MD&A which may prove to be incorrect, include, but are not limited to, (1) that all required third party contractual, regulatory and governmental approvals will be obtained for the development, construction and production of its properties, (2) there being no significant disruptions affecting operations, whether due to labor disruptions, supply disruptions, power disruptions, damage to equipment or otherwise; (3) permitting, development, expansion and power supply proceeding on a basis consistent with the Company's current expectations; (4) currency exchange rates being approximately consistent with current levels; (5) certain price assumptions for silver, lead, zinc and copper; (6) prices for and availability of natural gas, fuel oil, electricity, parts and equipment and other key supplies remaining consistent with current levels; (7) production forecasts meeting expectations; (8) the accuracy of the Company's current mineral resource and reserve estimates; (9) labor and materials costs increasing on a basis consistent with the Company's current expectations; and (10) assumptions made and judgments used in engineering and geological interpretation.

In addition, there are known and unknown risk factors which could cause the Company's actual results, performance or achievements to differ materially from any future results, performance or achievements expressed or implied by the forward-looking statements. Known risk factors include, risks associated with project development; the need for additional financing; operational risks associated with mining and mineral processing; changes in national and local government legislation, taxation, controls, regulations and political or economic developments in Canada, Mexico, the United States, Peru or other countries in which the Company does or may carry on business; the possibility of cost overruns or unanticipated expenses; fluctuations in silver, lead, zinc and copper prices; title matters; uncertainties and risks related to carrying on business in foreign countries; environmental liability claims and insurance; reliance on key personnel; currency exchange rate fluctuations; competition; and other risks and uncertainties, including those described in the "Risks and Uncertainties" section in the MD&A and in the "Risk Factors" section in the Company's Annual Information Form for the financial year ended December 31, 2011 filed with the Canadian Securities Administrators and the U.S. Securities and Exchange Commission and available at www.sedar.com and www.edgar.gov.

Although the Company has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in forward-looking statements, there may be other factors that cause actions, events or results not to be as anticipated, estimated or intended. These forward-looking statements are made as of the date of this MD&A. There can be no assurance that forward looking statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, readers are cautioned not to place undue reliance on forward-looking statements. Except as required by law, the Company does not assume the obligation to revise or update these forward looking statements after the date of this document or to revise them to reflect the occurrence of future unanticipated events.

EXHIBIT 23.1

CONSENT OF INDEPENDENT REGISTERED CHARTERED ACCOUNTANTS

We consent to the use of our report dated March 19, 2013 relating to the consolidated financial statements of Fortuna Silver Mines Inc. appearing in this Annual Report on Form 40-F of Fortuna Silver Mines Inc. for the year ended December 31, 2012.

/s/ Deloitte LLP

Independent Registered Chartered Accountants
Vancouver, Canada
April 1, 2013

EXHIBIT 99.5

MINE SAFETY DISCLOSURE

During the year ended December 31, 2012, Fortuna Silver Mines Inc. (the "Company") had one mine-related fatality at its Caylloma Mine, Peru.

As the Company's mines are located outside the United States, the Company has no other mine safety disclosures to be made in response to Section 1503(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act for the year ended December 31, 2012.

EXHIBIT 99.6

CONSENT OF ERIC N. CHAPMAN

CONSENT OF AUTHOR

I hereby consent to the use of my name, Eric N. Chapman, and reference to my name, the technical report entitled “Fortuna Silver Mines Inc.: Caylloma Property, Caylloma District, Peru” dated as of March 22, 2013 (the “Caylloma Report”) evaluating the Caylloma Property of Fortuna Silver Mines Inc. (the “Company”), the technical report entitled “Fortuna Silver Mines Inc.: San Jose Property, Oaxaca, Mexico” dated as of March 22, 2013 evaluating the San Jose Property of the Company (together with the Caylloma Report, the “Reports”), and the information contained in the Reports as described or incorporated by reference in the Company’s Annual Report on Form 40-F for the year ended December 31, 2012 filed with the United States Securities and Exchange Commission.

Dated the 1st day of April, 2013.

“Eric N. Chapman”
Eric N. Chapman, P.Geo., C. Geol. (FGS)

EXHIBIT 99.7

CONSENT OF THOMAS KELLY

CONSENT OF AUTHOR

I hereby consent to the use of my name, Thomas Kelly, and reference to my name, the technical report entitled “Fortuna Silver Mines Inc.: Caylloma Property, Caylloma District, Peru” dated as of March 22, 2013 (the “Caylloma Report”) evaluating the Caylloma Property of Fortuna Silver Mines Inc. (the “Company”), the technical report entitled “Fortuna Silver Mines Inc.: San Jose Property, Oaxaca, Mexico” dated as of March 22, 2013 evaluating the San Jose Property of the Company (together with the Caylloma Report, the “Reports”), and the information contained in the Reports as described or incorporated by reference in the Company’s Annual Report on Form 40-F for the year ended December 31, 2012 filed with the United States Securities and Exchange Commission.

Dated the 1st day of April, 2013.

“Thomas Kelly”
Thomas Kelly, E.M. Fellow AusIMM, Registered Member SME

EXHIBIT 99.8

CONSENT OF THOMAS VEHRS

CONSENT OF EXPERT

I hereby consent to the use of my name, Thomas Vehrs, and reference to my name, and the technical information contained in the Annual Information Form of Fortuna Silver Mines Inc. (the "Company") for the year ended December 31, 2012 described or incorporated by reference in the Company's Annual Report on Form 40-F for the year ended December 31, 2012 filed with the United States Securities and Exchange Commission.

Dated the 1st day of April, 2013.

"Thomas Vehrs"
Thomas Vehrs, Ph.D., Registered Member SME

EXHIBIT 99.9

CERTIFICATION PURSUANT TO RULE 13a-14 OR 15d-14 OF THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Jorge Ganoza Durant, certify that:

1. I have reviewed this annual report on Form 40-F of Fortuna Silver Mines Inc. (the "issuer");

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this report;

4. The issuer's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the issuer and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the issuer's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the issuer's internal control over financial reporting; and

5. The issuer's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the issuer's auditors and the audit committee of the issuer's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the issuer's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the issuer's internal control over financial reporting.

Dated: April 1, 2013

"Jorge Ganoza Durant"

Name: Jorge Ganoza Durant
Title: President, Chief Executive Officer & Director
(principal executive officer)

EXHIBIT 99.10

CERTIFICATION PURSUANT TO RULE 13a-14 OR 15d-14 OF THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Luiz Ganoza Durant, certify that:

1. I have reviewed this annual report on Form 40-F of Fortuna Silver Mines Inc. (the "issuer");

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this report;

4. The issuer's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the issuer and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the issuer's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the issuer's internal control over financial reporting; and

5. The issuer's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the issuer's auditors and the audit committee of the issuer's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the issuer's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the issuer's internal control over financial reporting.

Dated: April 1, 2013

"Luis Ganoza Durant"
Name: Luiz Ganoza Durant
Title: Chief Financial Officer
(principal financial officer)

EXHIBIT 99.11

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the annual report of Fortuna Silver Mines Inc. (the "Company") on Form 40-F for the fiscal year ended December 31, 2012, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Jorge Ganoza Durant, President, Chief Executive Officer & Director of the Company, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: April 1, 2013

"Jorge Ganoza Durant"
Name: Jorge Ganoza Durant
Title: President, Chief Executive Officer & Director
(principal executive officer)

EXHIBIT 99.12

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the annual report of Fortuna Silver Mines Inc. (the "Company") on Form 40-F for the fiscal year ended December 31, 2012, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Luis Ganoza Durant, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: April 1, 2013

"Luis Ganoza Durant"

Name: Luiz Ganoza Durant
Title: Chief Financial Officer
(principal financial officer)