Excellon Resources Inc.

EXCELLON

*An Evolution in* **High-Grade Silver**


# 2012 Annual Report

# EXCELLON
## *An Evolution in* **High-Grade Silver**


**Excellon's 100%-owned La Platosa Mine in Durango is Mexico's highest-grade silver mine, with lead and zinc by-products making it one of the lowest cash cost silver mines in the country. In today's market, the Company is positioning itself to capitalize on undervalued projects by focusing on increasing La Platosa's profitable silver production and near term mineable resources.**

**Excellon has ongoing gold exploration programs on the DeSantis Project, located near Timmins, Ontario and the Beschefer Project, located in northwestern Quebec. Both projects are located in prolific gold producing areas, host gold mineralization and have significant discovery potential.**

*All financial figures in this Annual Report are reported in US dollars unless otherwise noted.*

## Contents



**Disclaimer**
This document contains "forward-looking statements" within the meaning of applicable Canadian securities legislation and applicable U.S. securities laws. Except for statements of historical fact relating to the Company, such forward-looking statements include, without limitation, statements regarding the future results of operations, performance and achievements of the Company, including potential property acquisitions, the timing, content, cost and results of proposed work programs, the discovery and delineation of mineral deposits/resources/reserves, geological interpretations, the potential of the Company's properties, proposed production rates, potential mineral recovery processes and rates, business plans and future operating revenues. Forward looking statements are made based on management's beliefs, estimates, assumptions and opinions on the date the statements are made. Although the Company believes that such statements are reasonable, it can give no assurance that such expectations will prove to be correct and the Company undertakes no obligation to forward-looking statements, except as may be required by law. Forward-looking statements are typically identified by words such as: believes, expects, anticipates, intends, estimates, targets, plans, postulates, and similar expressions, or are those which, by their nature, refer to future events. The Company cautions investors that any forward-looking statements by the Company are not guarantees of future results or performance, and that actual results may differ materially from those in forward-looking statements as a result of various risk factors, including, but not limited to, variations in the nature, quality and quantity of any mineral deposits that may be located, significant downward variations in the market price of any minerals produced (particularly silver), the Company's inability to obtain any necessary permits, consents or authorizations required for its activities, to produce minerals from its properties successfully or profitably, to continue its projected growth, to raise the necessary capital or to be fully able to implement its business strategies. A description of the risk factors applicable to the Company can be found in the Company's most recent Annual Information Form under "Description of the Business - Risk Factors". All of the Company's public disclosure filings may be accessed via www.sedar.com and readers are urged to review these materials, including the technical reports filed with respect to the Company's mineral properties, and particularly the latest NI 43 101 compliant technical report prepared by Roscoe Postle Associates Inc. with respect to the Platosa Property. This document is not, and is not to be construed in any way as, an offer to buy or sell securities in the United States.

**Cautionary Note to United States Investors Concerning Estimates of Measured, Indicated and Inferred Resources**
The terms "Measured", "Indicated" and "Inferred" Mineral Resources used or reference in this document are defined in accordance with Canadian 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") Standards on Mineral Resources and Mineral Reserves. The CIM standards differ significantly from standards in the United States. United States investors are advised that while such terms are recognized and required by Canadian regulations, the United States Securities and Exchange Commission does not recognize them. "Inferred Mineral Resources" have a great amount of uncertainty as to their existence, and 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 or that Mineral Resources will ever be upgraded to Mineral Reserves. Under Canadian rules, estimates of Inferred Mineral Resources may not form the basis of feasibility or other economic studies. United States investors are cautioned not to assume that all or any part of Indicated Mineral Resources will ever be converted into Mineral Reserves. United States investors are also cautioned not to assume that all or any part of an Inferred Mineral Resource exists or is economically or legally mineable, or that an Indicated Mineral Resource is economically or legally mineable.

**Cautionary Note to United States Investors regarding Adjacent or Similar Properties**
This document may also contain information with respect to adjacent or similar mineral properties in respect of which the Company has no interest or rights to explore or mine. The Company advises United States investors that the United States Securities and Exchange Commission's mining guidelines strictly prohibit information of this type in documents filed with the SEC. Readers are cautioned that the Company has no interest in or right to acquire any interest in any such properties, and that mineral deposits on adjacent or similar properties are not indicative of mineral deposits on the Company's properties.

# Letter to Shareholders

## Dear Shareholder

***We are pleased to look back over 2012 with you, a year in which we achieved significant success on the production, exploration and community relation fronts, albeit with significant struggles along the way. We intend to build on our successes and learn from the stresses of 2012.***

Our strategy going forward is to use our greatest strengths – our people, exceptionally high grade La Platosa silver mine, low cost production, cash flow and, most importantly, our Canadian ethics and values – to adapt to the market and operational difficulties currently faced by every exploration, development and mining company in the industry. **Our goal is to evolve from our foundation of high-grade silver into the next of Mexico's successful mid-tier producers.**

On the production front, despite operating for less than three quarters of the year, our La Platosa Mine produced 1.1 million ounces of silver, 5.7 million pounds of lead and 10.5 million pounds of zinc (1.6 million silver equivalent ounces) from 48,000 tonnes of ore grading 846 g/t silver, 6.75% lead and 11.81% zinc. La Platosa's ore grades remain amongst the highest in the silver industry, with our net cash costs of US$5.99 amongst the lowest. Rob Moore, our Chief Operating Officer, and Pablo Gurrola, our Mine Manager, deserve credit for this positive year of production as does the entire mining team at La Platosa and our mill operations team at Miguel Auza.

Our net income during the year was the second highest in Excellon's history and our revenues the third highest – again, in less than three quarters of production. We were on a record setting pace during the first two quarters of the year before production was halted in the early days of the third quarter. As of the end of the year, we had a strong financial position of US$11 million from cash, securities and trade receivables, all after funding significant expenditures during 2012, including: US$2.9 on the buy-back of 5.1 million shares; US$2.4 million to purchase the last royalty overhanging our production; and US$9 million on an aggressive exploration program in Mexico and Canada. Our new Chief Financial Officer, Rupy Dhadwar, has performed an excellent job since taking his role and we expect many positive contributions from him during 2013.

On the exploration front, we finally made the discovery that we and our shareholders have been waiting on for years – the first definitive indications that we are on the periphery of a major carbonate replacement deposit (CRD) system. In mid-2012, drill hole LP1019 intersected 55 metres of CRD-style mineralization grading 132 g/t silver, 3.1% lead, 1.8% zinc with anomalous gold only one kilometre north-northwest of our mining operation. Follow-up holes have continued to intersect CRD-style mineralization and we now believe that the "Source" of La Platosa's high grade silver/lead zinc mantos may be closer than we had previously theorized. Our Vice President Exploration, John Sullivan, and Exploration Manager, Rene Ramirez, deserve much credit for the intelligent perseverance required to make this discovery.

During 2012, we initiated a complete review of our community relations and corporate social responsibility (CSR) programs. Excellon has always been a contributor to the local communities, including providing health clinics and assessments at the mine with the aid of the mine's doctor, ambulance and facilities, donating to local sports teams, providing drought relief packages and providing scholarships. We continue to maintain and develop an excellent relationship with the local towns of Bermejillo and Mapimi and their surroundings, from which we draw the majority of our workforce and materials. During the year, we hired a well-respected external consultant to design and implement an IFC/World Bank compliant CSR program focused on education and health in these local towns. We also hired a Manager of Government and Community Relations, Sandra Magaña. Our 2013 program includes the purchase of computer equipment for certain schools, the building of facilities for others, cooperative reforestation programs, cultural festivals, the purchase of necessary medical equipment and improvements to existing infrastructure. We are very excited to see what Sandra can accomplish during the upcoming year.

Early in 2013, we joined the Mining Association of Canada, which represents many of Canada's leading mining companies and the highest standards of Canadian values and ethics in the industry. We look forward to learning from the Association's expertise and working to implement leading initiatives such as Toward Sustainable Mining in the coming years. We plan to keep our shareholders updated on our various CSR programs throughout the year, so please keep an eye on the website.

Despite these successes, market conditions during 2012 continued to be difficult. Since the beginning of 2011, though the Toronto Stock Exchange has retreated only 10%, metals stocks and exchanges have been severely impacted, with the TSX Venture Exchange down ~56%, the GDXJ (Market Vectors Junior Gold Miners) down ~63% and the Sprott Physical Silver Trust down ~52% from each of their respective early-2011 highs.

Until early July, Excellon was faring relatively well versus many of its peers and the market, retreating from a 50-day moving average of ~$1.08 in early 2011 to ~$0.57 in early July. Unfortunately, though we were well poised with our new CRD/Source discovery to enjoy the brief market and silver price rebound from mid-summer, we faced external challenges beyond our control during that period.

On July 5th, the workers of La Platosa elected a representative union. The union that lost the vote, the Los Mineros (which is affiliated with the United Steel Workers), quickly launched an illegal blockade of La Platosa with the support and advice of an NGO and the local Ejido La Sierrita. We lost 99 days of production and profitability to this illegal action and suffered a broad public campaign of misinformation. While Excellon has never faced such a challenge in its history, through these trials we redeveloped and strengthened the support of the local, state and federal governments and witnessed the formation of a grassroots movement, the Concerned Women of Bermejillo, which took action on behalf of the local communities most affected by the blockade and ultimately helped us regain access to the mine. We are sure that many of our shareholders spoke with Joanne Jobin, our Vice President Investor Relations, during this tremendously frustrating situation period and she was tireless in her communication efforts.

*"Moving into 2013, we are now ready to focus on our high-grade silver production, profitable cash flow and mine-life – all in the context of market volatility that is providing opportunities seldom seen in a generation."*

While we were challenged on a number of fronts by the Los Mineros, the NGO and Ejido during the year, we were consistently exonerated by each independent authority that reviewed the claims brought against us: the Mexican National Contact Point of the Organization for Economic Cooperation and Development (OECD), the environmental and labour authorities in Mexico and various other international and regulatory agencies. For a full background on the illegal blockade and related matters, we invite you to visit the Community section of our website.

Moving into 2013, we are now ready to focus on our high-grade silver production, profitable cash flow and mine-life – all in the context of market volatility that is providing opportunities seldom seen in a generation. The market valuations of many promising exploration, resource development and development stage projects continue to decrease in the absence of cash flow. We have therefore revised our business strategy to improve our market valuation by focusing on our relative advantages so that we can capitalize on these developing opportunities.

First, we are focused on increasing our high-grade/low cost production beyond the currently budgeted 200 tonnes per day, primarily by further optimizing existing production and increasing our mining workforce at La Platosa. Second, we are seeking custom milling opportunities and small scale acquisitions in Durango, Zacatecas and San Luis Potosi to better utilize our mill at Miguel Auza and, along with improvements in our production, increase our cash flow. Third, we have shifted our exploration to expand existing high-grade mantos resources that will be easily accessible through existing mine infrastructure. We will also continue exploration for Source-style mineralization going forward, though at a more measured pace.

The Board of Directors has also tabled a proposal to improve the investment attractiveness of Excellon's common shares on the market. At the upcoming Annual and Special Meeting of Shareholders, we will be requesting shareholder approval to consolidate the Company's shares on a five-for-one basis. The Board's proposal is founded on the conviction that La Platosa's strong cash flow will fund future growth in both production and mine life without requiring further equity financing. The Board is convinced that the proposed consolidation will contribute to immediate and long-term shareholder value by, among others:

- increasing the breadth and sophistication of the Company's eligible investor base;
- increasing trading volume in the stock through a broader investor base;
- increasing the valuation level and investment profile of the common shares as the Company should no longer be considered a "penny stock"; and
- aligning the nominal market price of the common shares with those of the Company's peers.



**The Board of Directors and Management urge shareholders to review the enclosed management information circular and vote your shares IN FAVOUR of the proposed consolidation.**

With the nomination of Ned Goodman and Joanne Ferstman for election to Excellon's Board of Directors, we have reached a pivotal point in our evolution and we continue to have one of the strongest boards in the junior mining industry. These well-known Canadian business leaders are founders and builders of internationally successful mining and financial companies and bring exceptional business, financial and capital market experience to the Board of Directors, which will in turn enhance our new business strategy over the coming years. These key nominees add to last year's appointment of Oliver Fernández and the high level Mexican business and government relationships that he brings to the table.

Excellon is an evolution in high-grade silver. We are focused on adapting to the current market and operational environments and capitalizing on the opportunities that both present to us. We look forward to building on 2012's successes and turning the challenges that we have faced into advantages. We hope you will be reading of a vastly improved Company in this letter next year – and it's our job to deliver on that hope.

We are sincerely grateful for those of our shareholders who stood by us during what was an extraordinarily difficult summer and we thank you for the many messages of support we received as we progressed through that situation. We have gained and continue to build on the support of community and government in Mexico and we trust that we can rely on yours, the Company's owners, during 2013 and in coming years.

**Peter A. Crossgrove**

*Executive Chairman,*
*Chief Executive Officer*

**Brendan Cahill**

*President*

March 26, 2013

# Management's Discussion and Analysis of Financial Results

*For the year ended December 31, 2012* March 26, 2013

***Excellon Resources Inc. (the "Company", or "Excellon") has prepared this Management's Discussion and Analysis of Financial Results ("MD&A") for the year ended December 31, 2012 in accordance with the requirements of National Instrument 51-102 ("NI 51-102"). This MD&A contains information as at March 26, 2013 and provides information on the operations of the Company for the year ended December 31, 2012 and 2011 and subsequent to the year end, and should be read in conjunction with the audited consolidated financial statements for the year ended December 31, 2012 and the related notes for the year then ended.***

***The Company prepares its consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and Interpretations of the International Financial Reporting Interpretations Committee ("IFRIC") which the Canadian Accounting Standards Board has approved for incorporation into Part I of the Handbook of the Canadian Institute of Chartered Accountants. The consolidated financial statements have been prepared under the historical cost method, except for certain financial instruments measured at fair value. The Company has consistently applied the accounting policies used in preparation of these consolidated financial statements throughout all the periods presented. All figures in this MD&A are in US dollars unless otherwise noted.***

## Description of Business

Excellon is exploring, developing and mining the high-grade silver-lead-zinc mineralization on its 40,864-hectare Platosa Property ("Platosa") located in northeastern Durango State, Mexico. The style of mineralization at Platosa resembles that of several of the world-class carbonate replacement deposits ("CRD") of Mexico.

The ore mined is processed at the Company's mill located in Miguel Auza in Zacatecas State, Mexico. At Miguel Auza, the Company produces two concentrates: a silver-lead concentrate and a silver-zinc concentrate. Both concentrates are shipped to the port of Manzanillo where they are purchased by Consorcio Minero de Mexico Cormin Mex, S.A. de C.V., a Trafigura Group Company.

On October 25, 2011, the Company reported an updated Mineral Resource estimate for the Platosa Mine. The estimate was prepared as at July 31, 2011. The new Measured plus Indicated Mineral Resource estimate was 637,000 tonnes grading 836 g/t (24.4 oz/T) Ag, 8.95% Pb, 10.58% Zn. The new estimate confirmed that the Mineral Resource at Platosa had been maintained and expanded since the previous estimate.

**Platosa Project - Mineral Resource Estimate** (as of July 31, 2011)

| **Category** | **Tonnes** (t) | **Ag** (g/t) | **Ag** (oz/T) | **Pb** (%) | **Zn** (%) | **Contained Ag** (oz) | **Contained Pb** (lb) | **Contained Zn** (lb) |
|---|---|---|---|---|---|---|---|---|
| Measured | 88,000 | 1,064 | 31.0 | 9.14 | 11.99 | 3,016,000 | 17,760,000 | 23,301,000 |
| Indicated | 549,000 | 800 | 23.3 | 8.92 | 10.36 | 14,104,000 | 107,918,000 | 125,248,000 |
| M + I | 637,000 | 836 | 24.4 | 8.95 | 10.58 | 17,120,000 | 125,678,000 | 148,549,000 |
| Inferred | 69,000 | 1,011 | 29.5 | 11.35 | 11.34 | 2,241,000 | 17,254,000 | 17,247,000 |

Notes:
1. CIM guidelines were followed for the classification of Mineral Resources.
2. Mineral Resources are estimated at an incremental NSR cut-off value of US$200 per tonne.
3. NSR metal price assumptions: Ag US$25.00/oz, Pb US$1.15/lb, Zn US$1.15/lb.
4. Estimate is of Mineral Resources only and, because these do not constitute Mineral Reserves, they do not have any demonstrated economic viability.
5. National Instrument 43-101 compliant Mineral Resource estimate prepared by David Ross, P.Geo., of Roscoe Postle Associates Inc., independent geological and mining consultants of Toronto, Ontario. Prepared as at July 31, 2011.
6. Totals may not add correctly due to rounding.

## Mine Operations

Mined tonnage in the fourth quarter of 2012 was lower that of than that of the first two quarters of 2012 and the fourth quarter of 2011 due to an illegal blockade of the mine entrance, which commenced on July 8, 2012 and prevented mining until October 16, 2012. Despite production being halted for over 25% of the year, tonnage was only down by 19% from the prior year. For the year, silver grades increased by 6% and zinc and lead grades increased by 8% and 29% respectively. Metal recoveries during 2012 were significantly improved over the prior year.

Following are the Platosa Mine production statistics for the years indicated:

| | **2012** | 2011 |
|---|---|---|
| Tonnes of ore processed | **48,199** | 59,405 |
| Ore grades: | | |
| Silver (g/t) | **846** | 796 |
| Silver (oz/T) | **24.67** | 23.22 |
| Lead (%) | **6.75** | 6.24 |
| Zinc (%) | **11.81** | 9.17 |
| Recoveries: | | |
| Silver (%) | **93.4** | 88.9 |
| Lead (%) | **82.1** | 75.6 |
| Zinc (%) | **84.8** | 78.5 |
| Production: | | |
| Silver - (oz) | **1,081,165** | 1,312,146 |
| Silver equivalent ounces - (oz) | **1,550,964**(1) | 1,759,309(2) |
| Lead - (lb) | **5,731,160** | 6,529,018 |
| Zinc - (lb) | **10,450,813** | 8,674,527 |
| Sales: | | |
| Silver ounces - (oz) | **1,060,211** | 1,312,146 |
| Silver equivalent ounces - (oz) | **1,523,422**(1) | 1,759,309(2) |
| Lead - (lb) | **5,638,330** | 6,529,018 |
| Zinc - (lb) | **10,316,726** | 8,674,527 |
| Realized prices: | | |
| Silver - ($US/oz) | **31.03** | 34.16 |
| Lead - ($US/lb) | **0.91** | 0.98 |
| Zinc - ($US/lb) | **0.90** | 1.02 |

(1) Silver equivalent ounces in 2012 were established using prices of US$31 per oz, US$0.90 per lb, and US$0.90 per lb for silver, lead and zinc, respectively, and applied to the recovered metal content of the concentrates.
(2) Silver equivalent ounces in 2011 were established using prices of US$34 per oz, US$1.00 per lb, and US$1.00 per lb for silver, lead and zinc, respectively, and applied to the recovered metal content of the concentrates.

On July 5, 2012, a state government-supervised union election was held by the workers of La Platosa. Based on initial results, the Sindicato Nacional Minero Metalúrgico Napoleón Gómez Sada was selected by the workers of La Platosa to be the representative union of the mine. On July 8, 2012, an illegal blockade of the La Platosa Mine was commenced by an opposing union that had lost the election, the Sindicato Nacional de Trabajadores Mineros Metalúrgicos, Siderúrgicos y Similares de la República Mexicana, which is affiliated with the United Steelworkers Union, along with members of the local Ejido La Sierrita, both of which are advised by the non-governmental organization Proyecto de Derechos Económicos, Sociales y Culturales, A.C ("ProDESC"). The Company continued to produce concentrate until July 19, 2012 from stockpiled material that was already on site at Miguel Auza. The Company regained access to the Platosa site on August 29, 2012 but was unable to resume full production until October 16, 2012 due to delays in reissuing certain permits that had been suspended during the illegal blockade. Subsequently, milling resumed at the Miguel Auza flotation plant and deliveries of concentrate recommenced. The Company also incurred significant additional legal fees, consulting fees, and travel and accommodation costs in 2012.

## Cash Cost per Ounce of Silver Produced

As a result of the illegal blockade, production was halted from July 8, 2012 to October 16, 2012 and the Company was unable to realize certain costs efficiencies when production resumed during the fourth quarter. As a consequence the Company's cash cost was impacted. For the year, cash operating cost during the period in which the Platosa Mine was operating was $6.5M (2011 - $6.9M) for production of 1,081,165 ounces of silver (2011 - 1,312,146) resulting in a higher than ordinary course cash cost of US $5.99/oz (2011 - US $5.29/oz). The calculation of cash cost per ounce produced reflects the cost of production adjusted for by-product and various non-cash costs included in Cost of Sales. This calculation may differ from that used by other companies in the industry. The Company uses this measure internally to evaluate the underlying operating performance of the Company for the reporting periods presented. The table below presents the details of the calculation.

Reconciliation of Cash Cost per Ounce of Silver Produced, Net of By-Product Credits:

| | **2012** $000's | 2011 $000's |
|---|---|---|
| Cost of sales | **19,189** | 17,195 |
| Adjustments - increase/(decrease): | | |
| Depletion, depreciation and amortization | **(2,787)** | (2,411) |
| Inventory changes | **158** | (62) |
| Third party smelting and refining charges | **5,852** | 6,250 |
| Royalties | **(321)** | (543) |
| By-product credits (1) | **(12,598)** | (13,485) |
| Suspension-related costs (2) | **(3,020)** | – |
| Cash operating cost | **6,473** | 6,944 |
| Ounces of silver produced | **1,081,165** | 1,312,146 |
| **Cash operating cost per ounce of silver produced in US $/oz** | **5.99** | 5.29 |

(1) By-product credits comprise revenues from sales of lead and zinc.
(2) Production was suspended during the illegal blockade. Care-and-maintenance and other costs incurred during the suspension period that were not related to production have been excluded from total cash costs and the calculation of total cash cost per ounce produced.

Cash operating cost, net of by-product credits, is provided as additional information and is a non-IFRS measure that does not have a standardized meaning. This measure should not be considered in isolation or as a substitute for measures of performance prepared in accordance with generally accepted accounting principles and is not necessarily indicative of operating expenses as determined under generally accepted accounting principles. This measure is intended to provide investors with information about the cash generating capabilities of the Company's operations and the Company uses this information for the same purpose. This analysis excludes capital expenditures and income taxes.

## Exploration

### Mexico

#### *Platosa Property*

This Platosa property covers 40,864 ha and the initial concessions and private lands were acquired by the Company in 1996. The Platosa Mine exploits a series of typical, although very high-grade, distal CRD silver, lead, zinc manto deposits located strategically within the prolific Mexican CRD Belt. It is the Company's belief, and diamond drilling results to early 2013 continue to confirm, that the Platosa Property holds considerable potential for the discovery of additional high-grade manto mineralization and for the discovery of large-tonnage, though lower grade, proximal CRD mineralization. CRDs are epigenetic, intrusion-related, high-temperature, sulphide-dominant, lead-zinc-silver-copper-gold-rich deposits that commonly occur in clusters associated with major regional geologic features. The Mexican CRD Belt is perhaps the world's best developed CRD cluster and Platosa lies in the centre of the northwest-southeast-trending axis of the largest deposits of the belt.

Several features make CRDs highly desirable mining targets. These include:

- **Size** - Proximal CRDs average 10 to 15 million tonnes of ore and the largest range up to 50 million tonnes;
- **Grade** - Ores are typically polymetallic with metal contents ranging from 2-12% lead; 2-18% zinc, 60-600 g/t silver, up to 2% copper and 6 g/t gold; and
- **Deposit morphology** - Individual CRD orebodies within the overall deposit are continuous and average 0.5 to 2 million tonnes in size, with some up to 20 million tonnes. They are typically metallurgically straight-forward and given that they are limestone-hosted, the environmental impact of tailings disposal is generally minimal.

CRD orebodies take the form of lenses or elongate to elongated-tabular bodies referred to as mantos or chimneys depending on whether they are horizontal or steeply inclined. A spectrum of CRD orebodies exists, ranging from distal manto and medial chimney massive sulphide bodies to proximal sulphide-rich skarns associated with unmineralized or porphyry-type intrusive bodies. Transitions of orebody morphology and mineralogy, and alteration zoning can be used in exploration to trace mantos into chimneys, sulphides into skarn, or skarn into stock contact deposits.

During the illegal blockade of the Platosa property, it was not possible to carry out any drilling, however, drilling resumed in early September with three rigs and in late September a fourth rig was added. A fifth rig was added in January. Since resumption of drilling, exploration efforts have focussed on following up on increasingly encouraging results in the search for the source of the high-grade, massive sulphide Platosa mantos at Rincon del Caido (“Rincon”), approximately one kilometre (“km”) NW of the known mantos.

In general, recent exploration at Platosa has focused on two target types.

The first target is located in an irregularly-shaped area extending roughly 1.5 km from the Platosa Mine. In this area the primary objective is as follows:

- To further add to the known distal-style, high-grade CRD Mineral Resources and to discover new mantos by drilling the geological, structural and geophysical targets developed by the Company’s previous drilling and geotechnical surveys. This follows on the success in adding mineralization to the 6A/6B Manto and the discovery of the Pierna Manto, both during 2010. Early in 2012 additional high-grade manto sulphides were discovered in the 6A Manto area. The Company expects that this mineralization will add to its Mineral Resource base in the future.

The second area encompasses the vast majority of the remainder of the property, including a portion of the first area. Within this area the objectives are as follows:

- To pursue the potential for larger-volume medial and proximal CRD mineralization, referred to as the Source. Geological evidence of this potential has been found in several drill holes completed since 2008 including hole EX10-LP763 drilled in 2010 in the Rincon del Caido area approximately 1.0 km NW of the Guadalupe Manto and more recently in holes EX12-LP986, LP995, LP1008 and in particular LP1019, which early in Q3 again intersected strong geologic evidence of a proximal environment. Hole LP1019 also intersected a significant width of sulphide mineralization as discussed further below. Following the resumption of drilling in September, drilling for the Source continued in the immediate Rincon area and the corridor linking Rincon with the massive sulphide mantos of the mine. Drilling is ongoing in this corridor as of the date of this report. Depending on progress at Rincon and other factors the Company may direct a portion of its drilling to a renewed search for additional distal high-grade massive sulphide mantos later in 2013; and

- Continue to employ geophysical methods with demonstrated success as targeting tools. To this end a Natural Source and Controlled Source Audio Magnetotelluric ("NSAMT" and "CSAMT") ground geophysical survey was completed in Q2. It was carried out over several areas, including Rincon del Caido, believed to host structures that may be favourable locations for the discovery of large-tonnage proximal CRD deposits. This type of survey has demonstrated its effectiveness at Platosa in the past and it was while testing NSAMT-interpreted structures in 2005 and 2006 that the Guadalupe and Guadalupe South mantos were discovered. The results have been incorporated into the Company's target-generation data base. In addition a downhole mis-a-la-masse electrical geophysical was carried out in two of the Rincon holes late in 2012. The results of this survey suggest the presence of sulphide mineralization for some distance from the centre of the immediate Rincon area although these results do not allow provide no quantitative information.

Diamond drilling for the Source continued to encounter success once drilling resumed late in the third quarter and into the first quarter of 2013. Four drill rigs were working at Rincon in the immediate vicinity of hole LP1019 until year end and a fifth was added in January. Hole LP1019 encountered several intervals of semi-massive to massive sulphides within 55.46 m of pyroxene and garnet-rich skarn at Rincon, 1.0 km NW of the Platosa Mine. The skarn occurs at a marble-hornfels contact and the entire 55.46 m assayed 132 g/t (3.8 oz/T) Ag, 3.13% Pb, 1.74% Zn and 0.075 g/t Au. Five strongly mineralized, higher-grade intervals were identified within the 55.46 m. This was the first time persistently anomalous gold had been intersected at Platosa and the discovery clearly suggested increasing proximity to the Source of the high-grade Platosa mantos. The hole provided the clearest evidence to date of a near-Source environment. The Company continues to believe it may be traceable to the large-tonnage proximal CRD deposit that has been the ultimate object of the Company's exploration program since it acquired the Platosa property in 1996.

Between April 23, 2012 and January 17, 2013 the Company issued six press releases covering Platosa drilling results. During that period a total of 12 holes intersected important Source-style sulphide mineralization. The mineralization is found in a skarnified-marble unit located at or close to its contact with an impervious hornfels unit at a depth of between 500 and 600 m vertical and at some distance above the contact of the marble with underlying granite. Of particular interest is the presence of persistent anomalous gold in these intersections, the first time such values have been found at Platosa. These values plus the particular style of the sulphides and the alteration encountered in the host rocks leads Company geologists to believe that the intersections are on the edge of the Source itself. In addition, narrow widths of highly anomalous bismuth and anomalous copper have been found in certain of the Rincon holes. The sulphide mineralization demonstrates multi-stage, pyrite-rich, massive to semi-massive textures that clearly overprint earlier pyroxene and garnet-rich skarn. The multi-stage characteristics are similar to those shown by the sulphides being mined from the Platosa mantos, although there are distinct compositional differences reflected by much higher pyrite content, the appearance of anomalous chalcopyrite and much darker-coloured sphalerite. The consistently anomalous gold, bismuth (8,280 ppm over 1.0 m in LP1023A and 1,685 ppm over 2.6 m in LP1024) and copper (0.23% over 1.1 m in LP1024 and 0.12% over 8.1 m in LP1025) combined with the overall skarn mineralogy indicate that this area is still somewhat distal to the Source itself, but may lie along a feeder system leading from the Source. The Source may lie between Rincon and the high-grade Platosa mantos, or farther to the northwest. The assay intervals mentioned in the Source holes are core widths. Mineralization banding lies at highly-variable angles to core axes and more geometric information is still required to confidently estimate true thicknesses. Results for several of the Rincon holes are shown in the table below and assay results summarized in the press releases can be viewed on the Company's website or under the Company's profile on SEDAR at www.sedar.com.

| Location | DDH No. | Interval From (m) | Interval To (m) | Interval Width (m)* | Silver (g/t) | Silver (oz/T) | Lead (%) | Zinc (%) | Gold (g/t) |
|---|---|---|---|---|---|---|---|---|---|
| Rincon del Caido | LP1019 | 516.70 | 572.16 | 55.46 | 132 | 3.8 | 3.13 | 1.74 | 0.075 |
| | Incl. | 546.83 | 549.80 | 2.97 | 236 | 6.9 | 7.18 | 5.46 | 0.146 |
| | and | 562.73 | 566.00 | 3.27 | 264 | 7.7 | 10.41 | 7.59 | 0.041 |
| | LP1023A | 513.00 | 515.00 | 2.00 | 610 | 17.8 | 3.08 | 0.11 | 0.571 |
| | and | 525.65 | 569.05 | 43.40 | 146 | 4.3 | 2.76 | 1.85 | 0.216 |
| | incl. | 530.60 | 536.40 | 5.80 | 381 | 11.1 | 10.63 | 11.51 | 0.354 |
| | LP1030 | 498.90 | 509.23 | 10.33 | 185 | 5.4 | 5.22 | 5.58 | 0.478 |
| | and | 579.27 | 581.02 | 1.75 | 444 | 13.0 | 8.81 | 5.97 | 0.067 |
| | and | 590.04 | 596.72 | 6.68 | 409 | 11.9 | 10.23 | 8.37 | 0.114 |
| | LP1038 | 491.80 | 499.05 | 7.25 | 21 | 0.6 | 0.74 | 3.57 | 13.066 |
| | incl. | 497.10 | 499.05 | 1.95 | 72 | 2.1 | 2.40 | 11.74 | 39.430 |

### *Miguel Auza Property*

The Miguel Auza property encompasses 41,498 ha and lies on the eastern flank of the Fresnillo Mexican Silver Trend some 150-200 km north of Fresnillo and Zacatecas City, both of which areas have and continue to be the source of a large percentage of Mexican silver, lead and zinc production. The property covers numerous high- and low-sulphide epithermal veins carrying Ag, Au, Pb, and Zn. The property has been the site of a large amount of historic mining since the time of the Spaniards and as recently as 2008 when Silver Eagle Mines Inc., through its Mexican subsidiary, carried out mining and milling on the Calvario Vein system.

The Company carried out a modest exploration program at Miguel Auza between the fall of 2009 and the fall of 2010 and while certain areas were highlighted as meriting further early stage exploration work, a decision was made to concentrate exploration activities at Platosa. The Company periodically reviews the potential of Miguel Auza, including the potential of the Miguel Auza Mine, which has been closed since December 2008.

## Canada and Other

In Q4 the Company continued work on its gold exploration projects in the Abitibi Belt of northeastern Ontario and northwestern Quebec. In addition it continued to weigh its options with respect to its El Condor gold property in southeastern Ecuador. El Condor is located within 3 km of Kinross's Fruta del Norte gold deposit, on which a feasibility study is in progress.

### *DeSantis Property, Northeastern Ontario*

The Company holds a 51% interest and may increase this interest to 100%, subject to a Net Smelter Returns ("NSR") royalty ranging from 1.5% to 3.5% by portion of the original DeSantis property, located five kilometres southwest of downtown Timmins, pursuant to an option agreement dated February 1, 2010 with International Prospectors and Explorers Inc. ("IEP"). In addition, the Company has an option to earn a 100% interest, subject to a 2% NSR royalty, in the contiguous DeSantis West property pursuant to an option agreement dated April 13, 2010 with a group of Timmins area prospectors. Collectively, these two properties are referred to as the DeSantis Property. The Company has the option to earn the additional 49% interest in the DeSantis portion of the property by issuing an additional 540,000 shares to IEP by April 24, 2013. Excellon has the option to earn a 100% interest in the DeSantis West portion of the property by making an additional C$20,000 payment and issuing an additional 48,600 Excellon shares to the owners by April 13, 2013. The Company has the option to buyout portions of each of NSRs on the overall property.

The property is located along the Destor-Porcupine Tectonic Zone ("DPZ"), the main structure controlling gold deposits in the Timmins gold camp, approximately 11 km west of the Dome Mine, owned by Goldcorp Inc. and 14 km east of Lake Shore Gold Corp.'s Timmins Mine. The property covers approximately 5 km of strike length within highly prospective volcanosedimentary stratigraphy on the north side of the DPZ, including the past producing DeSantis Mine. Gold deposits in the Timmins camp occur in a variety of forms, but virtually all can be related to structural controls associated with major deformation zones, the foremost being the DPZ.

The DeSantis Property hosts at least five known gold-bearing zones, all of which are located near the area of historic underground mining on the property. The DeSantis Mine produced 35,800 ounces of gold from 178,650 tonnes of ore, which graded 6.2 g/t Au during its intermittent production history.

A major exploration effort on the property was undertaken in the mid-1980s by a Noranda Inc. - Stan West Mining Corp. joint venture. Focussed on deeper portions of the Albitite Zone, this advanced exploration program rehabilitated the No. 2 Shaft, several of the lowest underground levels, and completed test mining and underground drilling from those levels. Resultant from that work and the work of others, a historic resource estimate for the Albitite Zone is 65,500 tonnes grading 7.85 g/t Au, while the Hydrothermal Alteration Zone was estimated to contain 117,000 tonnes grading 9.09 g/t Au. These resource estimates, while considered relevant, are historic in nature, do not have currently demonstrated economic viability and should not be relied upon.

Lateegra completed 15 diamond drill holes on the property in 2010 prior to the involvement of the Company. These holes were directed at evaluating the known gold mineralization within the Hydrothermal Alteration and Albitite Zones that are situated within 400 metres of the DeSantis No. 2 Shaft. The presence of gold was confirmed in certain of the holes and in addition gold was found in holes that tested the historic Arsenopyrite and Green Carbonate Zones, both in proximity to the Albitite Zone. Recent gold discoveries at Lake Shore's Thunder Creek and 144 Zones occur near the contact of volcanic sequences with Porcupine metasedimentary rocks and in shear zones proximal to porphyritic intrusions within the Porcupine metasedimentary sequence. A similar geological setting may exist in the poorly exposed and largely untested northern portion of the DeSantis Property.

In 2011, the Company completed 22 additional drill holes. This campaign focussed on expansion of the Hydrothermal Alteration Zone, as well as the Albitite Zone, and tested reconnaissance targets located elsewhere on the property.

Results from the first 10 holes of the 2011 campaign included an intersection of 3.63 g/t Au over 23.17 m including 14.25 g/t Au over 1.17 m in drill hole DS11-020A. Assay results for the first 10 holes completed during 2011 are summarized in an October 18, 2011 press release, which can be viewed on the Company's website or under the Company's profile on SEDAR at www.sedar.com. The remainder of the holes completed during 2011, while intersecting favourable geology, alteration and occasional quartz veining did not intersect noteworthy gold mineralization.

Between January and April 2012, three additional drill holes were completed, one on a reconnaissance target on the western portion of the property, one as follow-up within the Hydrothermal Alteration Zone and one at depth testing the down-dip extension of the Albitite Zone. The first two intersected quartz veining but returned only low gold values over narrow widths, however, hole DS12-004 intersected 1.74 g/t Au over 12.00 m including 10.39 g/t Au over 1.50 m on the down-dip extension of the Albitite Zone. The quoted intersections are core widths and may not represent true thicknesses.

In mid-October 2012 the Company completed a comprehensive program of geotechnical compilation, relogging and sampling of recent and historic drill core and reviewing the property in a regional context. Based on the results of this work a 5,000 m follow-up drilling program began in late October. Drilling is focused on following up on promising previous results and the testing of undrilled areas east of and below the known Albitite Zone. In addition geophysical and geology targets are being tested in a series of holes on portions of the property that have seen little or no previous work such as the volcanic-sedimentary contact referred to above. As of the date of this report, while certain holes have intersected interesting geology and alteration there have been no material assay results obtained.

***Beschefer Property, Northwestern Quebec***

The Company holds a 100% interest (subject to a 3% NSR) in the property, which is located within the Abitibi Greenstone Belt approximately 60 km northeast of the Casa Berardi Mine, 80 km east-southeast of the Detour Mine and 12 km east of the past producing Selbaie Mine. The Company has the option to buy out 1.75% NSR of the 3% NSR royalty for $1.5 million. The Selbaie Mine produced 57.5 million tonnes grading 0.56 g/t Au, 38 g/t Ag, 0.87% Cu, and 1.85% Zn over its mine life. The property has little or no bedrock exposure and is muskeg-covered such that drilling is most effectively performed during freezing conditions.

Gold mineralization, the B-14 Zone, was discovered in 1995 by Billiton Canada Inc. and apart from a short program by SOQUEM , the property has seen limited exploration since then. The gold mineralization is hosted within a typical Archean volcanic 'greenstone' assemblage and is typical of other shear zone-hosted mesothermal gold deposits in that it is hosted within mylonite, highly sheared and altered rock, which also contains increased quartz veining and pyrite. As previously reported, Lateegra carried out 1,523 m of diamond drilling in five holes in early 2011, primarily on the B-14 Zone, prior to the involvement of the Company. Results included 3.80 g/t Au over 4.35 m including 13.85 g/t Au over 0.30 m in hole BE11-001 and 12.4 g/t Au over 3.78 m including 63.5 g/t Au over 0.43 m in hole BE11-003.

Between January and late March 2012, the Company completed 33 additional holes on the property. Drilling focused on expansion of the B-14 Zone, as well as exploration targets elsewhere on the property. Results included 4.54 g/t Au over 7.80 m including 9.16 g/t Au over 1.35 m in hole BE12-006, 13.07 g/t Au over 8.75 m including 58.5 g/t Au over 1.50 m in hole BE12-014 and 10.50 g/t Au over 1.50 m and 3.56 g/t Au over 6.06 m, both in hole BE12-030. The quoted intersections are core widths and may not represent true thicknesses.

Assay results for all the Company's 2012 drill holes are summarized in press releases issued in March, April and May 2012 and can be viewed on the Company's website or under the Company's profile on SEDAR at www.sedar.com.

The Company's 2011 and 2012 drilling results confirmed that the B-14 Zone has the potential to host a gold resource. In mid-December 2012 the Company completed a comprehensive program of geotechnical compilation, relogging and sampling of recent and historic drill core and reviewing the property in a regional context. Based on the results of this work a 5,000 m follow-up drilling program began in early February 2013. Drilling is primarily focused on expanding the B-14 Zone. In addition historic geophysical targets on portions of the property, which have seen little or no work and may represent structures with gold potential are being tested by a small number of holes. As of the date of this report while various holes have intersected interesting geology, alteration and varying amounts of pyrite mineralization there have been no material assay results obtained.

## Qualified Person

Mr. John Sullivan, BSc., PGeo., Excellon's Vice President of Exploration has acted as the Qualified Person, as defined in NI 43-101, with respect to the disclosure of the scientific and technical information contained in this MD&A.

Mr. Sullivan is an economic geologist with over 35 years of experience in the mineral industry. Prior to joining Excellon in 2007, he was a senior geologist at a Toronto-based international geological and mining engineering consulting firm where he evaluated properties and prepared NI 43-101 reports on gold and base metal projects in Canada and internationally. In addition, he has held senior positions with two large Canadian mining companies where he directed major exploration programs, managed field offices, and evaluated projects in Canada, Europe, Africa and Latin America. Mr. Sullivan is not independent of Excellon, as he is an officer of the Company.

## Risk and Uncertainties

The Company is exposed to many risks in conducting its business, including but not limited to: metal price risk since the Company derives its revenues from the sale of silver, lead and zinc; foreign exchange risk since the Company reports in United States dollars but operates in jurisdictions that use other currencies; the inherent risk of uncertainties in estimating Mineral Resources; political risk associated with operating in foreign jurisdictions, environmental risks and risks associated with labour relations issues. Further factors affecting the Company are described in the Annual Information Form on SEDAR (www.sedar.com).

## Overall Performance

Mined tonnage for 2012 of 48,199 tonnes were significantly far lower than the 59,405 tonnes mined in 2011 due to the previously referenced illegal blockade and subsequent permitting delays, which halted production from July 8, 2012 until October 16, 2012. Consequently, production of silver in 2012 was 1.1 million ounces as compared to 1.3 million in 2011. The overall silver grade of ore processed in 2012 improved to 846 g/t compared to 796 g/t for the prior year. The overall recovery of silver at 93.4% in 2012 was a significant improvement from 88.9% for 2011. Recoveries for lead and zinc improved to 82.1% and 84.8% respectively, an overall increase of 8.4% from the prior year.

The silver price in 2012 averaged $31.15 per ounce on the London Metal Exchange (2011 - $35.12) while the Company realized an average price of $31.03 per ounce sold (2011 - $34.16). Sales declined in 2012 to $36.3 million as compared to $48.0 million in 2011, a result of production being halted due to the illegal blockade previously referenced.

As at December 31, 2012 cash and cash equivalents on hand were $1.4 million, marketable securities were $4.2 million and trade receivables were $5.5 million as compared to $22.3 million cash and cash equivalents and accounts receivables of $0.5 million at December 31, 2011. The Company has now resumed full production and expects that cash balances will increase in 2013 reflecting the continuing strength of the mine operations.

## Results of Operations

Financial statement highlights for the year ended December 31, 2012 and 2011 are as follows *(in thousands of US dollars):*

| | **2012**<br>$ | 2011<br>$ |
|---|---|---|
| Revenue | **36,273** | 48,010 |
| Cost of sales | **(19,189)** | (17,195) |
| Gross profit | **17,084** | 30,815 |
| Expenses: | | |
| Corporate administration | **(7,338)** | (8,405) |
| Exploration | **(9,907)** | (6,067) |
| Other | **685** | (5,096) |
| Income tax refund (expense) | **7,884** | (6,814) |
| Net income for the year | **8,408** | 4,433 |



Overall, the Company recorded a net income of $8.4 million compared to $4.4 million in the previous year.

Despite losing over three months production and having a lower net realizable price of silver at $31.03 (2011 - $34.16), revenues for 2012 were $36.3 million compared to $48.0 million in 2011.

While lower tonnages were processed in 2012, the mine incurred care-and-maintenance costs and was unable to utilize production cost efficiencies increasing cost of sales in 2012 to $19.2 million (2011 - $17.2 million) As a result, gross profit margin decreased from 64% in 2011 to 47% in 2012.

Exploration cost increased to $9.9 million (2011 - $6.1 million) as the Company invested its resources into drilling with up to four rigs on the Platosa property.

Corporate administrative expenses represent administrative costs incurred in Canada. Management compensation and stock based compensation are the largest component.

A future tax asset of $8.4 million was recognized in 2012 as the Company was able to utilize its tax loss carry-forwards based on a tax planning reorganization in the year.

Other expenses include unrealized foreign exchange gains of the Company. In 2012, the decrease in the expense is due to the strengthening of the peso relative to the USD since 2011, which resulted in an unrealized foreign exchange gain on an intercompany loan that is foreign to the functional currency of a reporting entity. The loan is not treated as long-term investment as the loan is expected to be repaid in the near future, at which time the gain or loss will be realized.

## Outlook

***Exploration:***

The Platosa exploration program continues to meet with considerable success. Planned expenditures for 2013 are $11.0 million, approximately 90% of which will be for diamond drilling. The budgeted expenditures will be split between the continued search for the high-tonnage proximal source of the manto mineralization in the Rincon del Caido area and the renewed search for additional high-grade massive sulphide mineralization in the vicinity of the known mantos. Some of the manto holes will be drilled to the contact of the carbonate package with the underlying felsic intrusive contact to determine whether a Source environment is present outside of the Rincon-Mantos Corridor. Two rigs will be deployed for manto holes, a third to Rincon del Caido and the Company plans to drill 58,000 m for the year.

In Canada the Company has drilling programs underway on its DeSantis gold property in Timmins and on the Beschefer gold project in northwestern Quebec. Both projects are expected to amount to 5,000 m of drilling and should be completed in early spring.

***Operations:***

The Company has projected 72,000 tonnes of ore mined and silver production of 1.5 million ounces (silver equivalent ounces of 2.2 million) for 2013. The Company's cash costs in 2013 are projected to be US$5.50 to $6.50 per ounce, net of by-products. Increased development activities, deeper mining depths and increasing water pumping capacity will put upward pressure on operating costs in 2013. The Company has made significant investment in water control procedures and will continue in 2013 to manage the underground water flows with increased pumping capacity and the previously installed watertight control doors in key operating areas of the mine in order to facilitate the expected tonnage production.

The Company plans to spend approximately $1.8 million in growth capital expenditures to develop and expand the mine and $1.1 million in sustaining capital in 2013.

The Company expects to fund all expenditures for 2013 from cash generated from operations at La Platosa, reflecting the robustness of the mine and its operations, and expects to maintain a strong financial position in 2013.

## Summary of Quarterly Results

The following table sets forth selected quarterly information for the last eight quarters *(in thousands of US dollars except for per share amounts).*

| Quarter ended | December 31, 2012 | September 30, 2012 | June 30, 2012 | March 31, 2012 |
|---|---|---|---|---|
| Revenue | $ 9,113 | $ 60 | $ 13,994 | $ 13,106 |
| Income (loss) before income taxes | $ (1,821) | $ (5,523) | $ 1,283 | $ 6,585 |
| Net income (loss) | $ 6,660 | $ (4,350) | $ 478 | $ 5,620 |
| Earnings (loss) per share - basic | $ 0.02 | $ (0.02) | $ 0.00 | $ 0.02 |
| - diluted | $ 0.02 | $ (0.02) | $ 0.00 | $ 0.02 |

| Quarter ended | December 31, 2011 | September 30, 2011 | June 30, 2011 | March 31, 2011 |
|---|---|---|---|---|
| Revenue | $ 14,009 | $ 11,174 | $ 15,442 | $ 7,385 |
| Income (loss) before income taxes | $ 1,401 | $ (450) | $ 9,419 | $ 877 |
| Net income (loss) | $ (3,101) | $ (976) | $ 8,055 | $ 455 |
| Earnings (loss) per share - basic | $ (0.01) | $ 0.00 | $ 0.03 | $ 0.00 |
| - diluted | $ (0.01) | $ 0.00 | $ 0.03 | $ 0.00 |

Quarterly revenue fluctuations are a function of metal prices and the volume of ore mined as well as ore grades. The Company has a policy of expensing exploration costs, which creates volatility in earnings.

## Liquidity and Capital Resources

As at December 31, 2012, the Company's cash and cash equivalents were $1.4 million (December 31, 2011 - $22.3 million), and working capital was $15.3 million (December 31, 2011 - $18.8 million). As at December 31, 2012, the Company's trade receivables were $5.5 million (December 31, 2011 - $0.5 million). The Company also invested $5.0 million in marketable securities of the Sprott Physical Silver Trust to hold units reflecting an underlying investment in 134,732 ounces of silver. The only source of funds available to the Company is cash flow generated by the Platosa Mine. The Company plans to spend a total of $2.9 million in capital expenditures for 2013.

## Off-Balance Sheet Arrangements

The Company does not have any off-balance sheet arrangements.

## Related Party Transactions

The corporate secretary of the Company is a partner in a firm that provides legal services to the Company. During the year, the Company incurred legal services of $182,000 (2011 - $162,000) with an outstanding payable balance of $18,000 at December 31, 2012 (December 31, 2011 - $30,000).

**Common share data (as at March 26, 2013)**

| | |
|---|---|
| Common shares outstanding | 274,960,967 |
| Stock options granted | 12,693,264 |
| Total | 287,654,231 |

## Internal Control over Financial Reporting and Disclosure Controls and Procedures

Management has designed and implemented internal controls over financial reporting ("ICFR") to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

Management has designed disclosure controls and procedures ("DC&P") to provide a reasonable assurance that (i) material information relating to the Company is made known to them by others, particularly during the period in which the annual filings are being prepared and (ii) information required to be disclosed by the Company in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time periods specified in securities legislation.

## Additional Sources of Information

Additional disclosures pertaining to the Company, including its most recent audited and unaudited interim financial statements, management information circular, material change reports, press releases and other information, are available on the SEDAR website at www.sedar.com or on the Company's website at www.excellonresources.com.

*This MD&A contains "forward-looking statements" within the meaning of applicable Canadian securities legislation and applicable U.S. securities laws. Except for statements of historical fact relating to the Company, such forward-looking statements include, without limitation, statements regarding the future results of operations, performance and achievements of the Company, including potential property acquisitions, the timing, content, cost and results of proposed work programs, the discovery and delineation of mineral deposits/resources/reserves, geological interpretations, the potential of the Company's properties, proposed production rates, potential mineral recovery processes and rates, business plans and future operating revenues. Forward looking statements are made based on management's beliefs, estimates, assumptions and opinions on the date the statements are made. Although the Company believes that such statements are reasonable, it can give no assurance that such expectations will prove to be correct and the Company undertakes no obligation to update forward-looking statements. Forward-looking statements are typically identified by words such as: believes, expects, anticipates, intends, estimates, targets, plans, postulates, and similar expressions, or are those which, by their nature, refer to future events. The Company cautions investors that any forward-looking statements by the Company are not guarantees of future results or performance, and that actual results may differ materially from those in forward-looking statements as a result of various risk factors, including, but not limited to, variations in the nature, quality and quantity of any mineral deposits that may be located, significant downward variations in the market price of any minerals produced (particularly silver), the Company's inability to obtain any necessary permits, consents or authorizations required for its activities, to produce minerals from its properties successfully or profitably, to continue its projected growth, to raise the necessary capital or to be fully able to implement its business strategies. A description of the risk factors applicable to the Company can be found in the Company's most recent Annual Information Form under "Description of the Business - Risk Factors". All of the Company's public disclosure filings may be accessed via www.sedar.com and readers are urged to review these materials, including the technical reports filed with respect to the Company's mineral properties, and particularly the latest NI 43-101-compliant technical report prepared by Roscoe Postle Associates Inc. with respect to the Platosa Property. This document is not, and is not to be construed in any way as, an offer to buy or sell securities in the United States.*

## Cautionary Note to United States Investors Concerning Estimates of Measured, Indicated and Inferred Resources

*The terms "Measured", "Indicated" and "Inferred" Mineral Resources used or reference in this MD&A are defined in accordance with Canadian 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") Standards on Mineral Resources and Mineral Reserves. The CIM standards differ significantly from standards in the United States. United States investors are advised that while such terms are recognized and required by Canadian regulations, the United States Securities and Exchange Commission does not recognize them. "Inferred Mineral Resources" have a great amount of uncertainty as to their existence, and 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 or that Mineral Resources will ever be upgraded to Mineral Reserves. Under Canadian rules, estimates of Inferred Mineral Resources may not form the basis of feasibility or other economic studies other than a Preliminary Economic Assessment ("PEA"). United States investors are cautioned not to assume that all or any part of Indicated Mineral Resources will ever be converted into Mineral Reserves. United States investors are also cautioned not to assume that all or any part of an Inferred Mineral Resource exists or is economically or legally mineable, or that an Indicated Mineral Resource is economically or legally mineable.*

## Cautionary Note to United States Investors regarding Adjacent or Similar Properties

*This MD&A may also contain information with respect to adjacent or similar mineral properties in respect of which the Company has no interest or rights to explore or mine. The Company advises United States investors that the United States Securities and Exchange Commission's mining guidelines strictly prohibit information of this type in documents filed with the SEC. Readers are cautioned that the Company has no interest in or right to acquire any interest in any such properties, and that mineral deposits on adjacent or similar properties are not indicative of mineral deposits on the Company's properties.*

# Management's Responsibility for Financial Reporting

The management of Excellon Resources Inc. is responsible for the integrity and fair presentation of the accompanying consolidated financial statements.

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and reflect management's best estimates and judgements.

Management is responsible for establishing and maintaining adequate internal control over financial reporting. Management has developed and maintains a system of internal controls to obtain reasonable assurance that the Company's assets are safeguarded, transactions are authorized and financial information is reliable. Any system of internal control over financial reporting has inherent limitations, including the possibility of circumvention and overriding of controls, and therefore, can provide only reasonable assurance with respect to financial statement preparation and presentation. Management concludes that at December 31, 2012, the Company's internal control over financial reporting was effective. The Board of Directors oversees management's responsibility for financial reporting and internal control systems through an Audit Committee, which is composed entirely of independent directors. The Audit Committee of the Board of Directors has met with the Company's independent auditors to review the scope and results of the annual audit and to review the consolidated financial statements and related financial reporting matters prior to submitting the consolidated financial statements to the Board for approval. The Audit Committee also reviews the quarterly financial statements and recommends them for approval to the Board of Directors, reviews with management the Company's systems of internal control and approves the scope of the independent auditors audit and non-audit work.

The consolidated financial statements have been audited by PricewaterhouseCoopers LLP, Chartered Accountants, Licensed Public Accountants. Their report outlines the scope of their examination and opinion on the consolidated financial statements.

*"signed"*

**Peter A. Crossgrove**
*Chief Executive Officer*

*"signed"*

**Rupy Dhadwar**
*Chief Financial Officer*

March 26, 2013

# Independent Auditor's Report

To the Shareholders of Excellon Resources Inc.

We have audited the accompanying consolidated financial statements of Excellon Resources Inc., which comprise the Consolidated Statements of Financial Position as at December 31, 2012 and 2011 and the Consolidated Statements of Income and Comprehensive Income, Consolidated Statements of Changes in Equity, and the Consolidated Statements of Cash Flow for the years ended December 31, 2012 and 2011, and the related notes, collectively referred to as the 'financial statements'.

### 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, 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. 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 audit 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 Excellon Resources Inc. as at December 31, 2012 and 2011 and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers LLP

Chartered Accountants, Licensed Public Accountants

March 26, 2013

# Consolidated Statements of Financial Position

*(in thousands of U.S. dollars)*

| | December 31, 2012 $ | December 31, 2011 $ |
|---|---|---|
| **Assets** | | |
| **Current assets** | | |
| Cash and cash equivalents | **1,369** | 22,262 |
| Marketable securities (note 5) | **4,152** | – |
| Trade receivables | **5,467** | 548 |
| Income taxes receivable | **3,122** | – |
| Inventories (note 6) | **2,022** | 1,459 |
| Other current assets | **1,555** | 1,030 |
| | **17,687** | 25,299 |
| **Non-current assets** | | |
| Long term investments | **20** | 71 |
| Property, plant and equipment (note 7) | **20,972** | 21,154 |
| Mineral rights (note 8) | **24,405** | 20,719 |
| Deferred income tax assets (note 14) | **8,059** | – |
| **Total assets** | **71,143** | 67,243 |
| **Liabilities** | | |
| **Current liabilities** | | |
| Trade payables | **2,377** | 2,503 |
| Income taxes payable (note 14) | **–** | 3,970 |
| | **2,377** | 6,473 |
| **Non-current liabilities** | | |
| Provisions (note 9) | **1,637** | 1,429 |
| Deferred income tax liabilities (note 14) | **–** | 331 |
| **Total liabilities** | **4,014** | 8,233 |
| **Equity** | | |
| Share capital (note 10) | **77,453** | 77,797 |
| Contributed surplus | **9,329** | 9,639 |
| Accumulated other comprehensive income | **1,810** | 1,445 |
| Deficit | **(21,463)** | (29,871) |
| **Total equity** | **67,129** | 59,010 |
| **Total liabilities and equity** | **71,143** | 67,243 |

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

Approved by the Board

**"Timothy J. Ryan"**
*Director*

**"Alan R. McFarland"**
*Director*

# Consolidated Statements of Income and Comprehensive Income

*For the year ended December 31, 2012 and 2011 (in thousands of U.S. dollars, except per share data)*

| | **December 31, 2012 $** | December 31, 2011 $ |
|---|---|---|
| Revenues | **36,273** | 48,010 |
| Cost of Sales (note 11a) | **(19,189)** | (17,195) |
| | **17,084** | 30,815 |
| Corporate administrative expenses (note 11b) | **(7,338)** | (8,405) |
| Exploration | **(9,907)** | (6,067) |
| Other income (expenses) (note 11c) | **777** | (5,065) |
| **Income before financing and tax** | **616** | 11,278 |
| Finance income | **18** | 1 |
| Finance costs | **(110)** | (32) |
| **Net finance costs** | **(92)** | (31) |
| **Income before income tax** | **524** | 11,247 |
| Income tax recovery (expense) (note 14) | **7,884** | (6,814) |
| **Net income** | **8,408** | 4,433 |
| **Other comprehensive income (loss)** | | |
| Unrealized gain (loss) on available for sale securities | **(51)** | 22 |
| Foreign currency translation differences | **416** | (48) |
| **Total other comprehensive income (loss)** | **365** | (26) |
| **Total comprehensive income** | **8,773** | 4,407 |
| **Earnings per share** | | |
| Basic | **$0.03** | $0.02 |
| Diluted | **$0.03** | $0.02 |
| **Weighted average number of shares** | | |
| Basic | **276,826,514** | 261,539,534 |
| Diluted | **277,447,537** | 263,327,008 |

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

# Consolidated Statements of Changes in Equity

*For the year ended December 31, 2012 and 2011*

| | Share capital $ | Contributed surplus $ | Accumulated other comprehensive income $ | Deficit $ | Total equity $ |
|---|---|---|---|---|---|
| **Balance - January 1, 2011** | 55,937 | 7,655 | 1,471 | (34,304) | 30,759 |
| Net income | – | – | – | 4,433 | 4,433 |
| Total other comprehensive income (loss) | – | – | (26) | – | (26) |
| Total comprehensive income (loss) | – | – | (26) | 4,433 | 4,407 |
| Employee share options: | | | | | |
| Value of services recognized | 1,146 | 1,489 | – | – | 2,635 |
| Proceeds on issuing shares | 1,710 | – | – | – | 1,710 |
| Share payment for acquisition (note 8) | 18,400 | 694 | – | – | 19,094 |
| Share payment for mineral rights (note 8) | 855 | – | – | – | 855 |
| Repurchased shares | (251) | (199) | – | – | (450) |
| **Balance - December 31, 2011** | 77,797 | 9,639 | 1,445 | (29,871) | 59,010 |
| **Balance - January 1, 2012** | 77,797 | 9,639 | 1,445 | (29,871) | 59,010 |
| Net income | – | – | – | 8,408 | 8,408 |
| Total other comprehensive income (loss) | – | – | 365 | – | 365 |
| Total comprehensive income (loss) | – | – | 365 | 8,408 | 8,773 |
| Employee share options: | | | | | |
| Value of services recognized | 29 | 1,100 | – | – | 1,129 |
| Proceeds on issuing shares | 42 | – | – | – | 42 |
| Share payment for mineral rights | 1,062 | – | – | – | 1,062 |
| Repurchased shares | (1,477) | (1,410) | – | – | (2,887) |
| **Balance - December 31, 2012** | 77,453 | 9,329 | 1,810 | (21,463) | 67,129 |

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

# Consolidated Statements of Cash Flow

*For the year ended December 31, 2012 and 2011*

| | **December 31, 2012 $** | December 31, 2011 $ |
|---|---|---|
| **Cash flow provided by (used in)** | | |
| **Operating activities** | | |
| Net income for the year | **8,408** | 4,433 |
| Adjustments for: | | |
| Depletion, depreciation and amortization | **2,893** | 2,499 |
| Deferred income tax | **(8,390)** | 544 |
| Share-based compensation | **1,129** | 2,635 |
| Post-employment benefits | **59** | (628) |
| Rehabilitation provision - accretion | **75** | 34 |
| Rehabilitation provision - change of estimate | **(34)** | 824 |
| Unrealized loss on marketable securities | **848** | – |
| Unrealized loss (gain) on foreign intercompany loans | **(1,457)** | 3,319 |
| Write-down of property, plant and equipment | **100** | 1,273 |
| Changes in items of working capital: | | |
| Trade receivables | **(4,919)** | 1,407 |
| Income taxes payable | **(7,092)** | 6,451 |
| Inventories | **(563)** | (76) |
| Other current assets | **(525)** | 275 |
| Trade payables | **(126)** | (453) |
| **Net cash provided by (used in) operating activities** | **(9,594)** | 22,537 |
| **Investing activities** | | |
| Purchase of marketable securities | **(5,000)** | – |
| Purchase of property, plant and equipment | **(2,777)** | (4,145) |
| Proceeds from sale of processing equipment | **1,744** | – |
| Purchase of royalty interests | **(2,400)** | – |
| Purchase of mineral rights | **(390)** | – |
| Net cash acquired on acquisitions | **–** | 786 |
| **Net cash provided by (used in) investing activities** | **(8,823)** | (3,359) |
| **Financing activities** | | |
| Proceeds on issuance of shares | **42** | 1,710 |
| Shares repurchased from market | **(2,887)** | (450) |
| **Net cash provided by (used in) financing activities** | **(2,845)** | 1,260 |
| **Effect of exchange rate changes on cash and cash equivalents** | **369** | (154) |
| **Increase (decrease) in cash and cash equivalents** | **(20,893)** | 20,284 |
| **Cash and cash equivalents - Beginning of the year** | **22,262** | 1,978 |
| **Cash and cash equivalents - End of the year** | **1,369** | 22,262 |
| Interest | **35** | – |
| Cash paid for income tax | **6,600** | 1,144 |

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

# Notes to the Consolidated Financial Statements

*December 31, 2012 and 2011 (in thousands of US Dollars)*

## 1. General Information

Excellon Resources Inc. and its subsidiaries (together the Company or Excellon) is involved in the exploration, development and extraction of high-grade silver-lead-zinc metals in Mexico and the exploration of gold in properties in Canada.

Excellon is domiciled in Canada and incorporated under the laws of the province of Ontario. The address of its principal office is 20 Victoria Street, Suite 900, Toronto, Ontario, M5C 2N8, Canada.

## 2. Basis Of Presentation

### a. Statement of compliance

The Company prepares its consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and Interpretations of the International Financial Reporting Interpretations Committee ("IFRIC") which the Canadian Accounting Standards Board has approved for incorporation into Part I of the Handbook of the Canadian Institute of Chartered Accountants. The consolidated financial statements have been prepared under the historical cost method, except for certain financial instruments measured at fair value. The Company has consistently applied the accounting policies used in preparation of these consolidated financial statements throughout all the periods presented. Critical accounting estimates and judgments used by management in the preparation of these consolidated financial statements are presented in note 4.

All financial information presented in USD has been rounded to the nearest thousand unless otherwise stated.

The consolidated financial statements were approved by the Board of Directors for issue on March 26, 2013.

## 3. Significant Accounting Policies

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements.

### a. Consolidation

#### *i. Subsidiaries*

Subsidiaries are entities controlled by the Company where control is achieved when the Company has the power to govern the financial and operating policies of the entity. Control is normally achieved through ownership, directly or indirectly, of more than 50 percent of the voting power. The Company owns directly and indirectly 100% of all the subsidiaries. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by the Company.

*ii. Transactions eliminated on consolidation*

Intercompany transactions, balances, income and expenses are eliminated in preparing the consolidated financial statements.

## b. Segment reporting

The Company has two reportable segments based on a geographical basis. During the year, the consolidated entity operated in Mexico and Canada.

The Mexican operation is principally engaged in the acquisition, exploration, evaluation, and development of mining properties. The Platosa property is in commercial production and is earning revenue through the sale of silver-lead concentrate and silver-zinc concentrate to a single customer that accounts for 100% of revenues.

The Canadian operations are principally engaged in the acquisition, exploration and evaluation of mining properties in Ontario and Quebec.

Non-current assets located at the corporate office in Canada are minor in relation to the total.

## c. Foreign currency transactions and translation

*i. Transactions and balances*

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or valuation where items are remeasured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at period-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the consolidated statements of income.

All foreign exchange gains and losses are presented in the statement of income within 'other expenses'.

*ii. Translation*

The results and financial position of all the Company entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- Assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- Income and expenses for each statement of income and comprehensive income are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the rate on the dates of the transactions);
- All resulting exchange differences have been recognized in other comprehensive income and accumulated as a separate component of equity in accumulated other comprehensive income.

## d. Financial instruments



Financial assets and liabilities are recognized when the company becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the company has transferred substantially all risks and rewards of ownership. Financial liabilities are derecognized when the obligation specified in the contract is discharged, cancelled or expires.

The Company’s financial instruments primarily consist of cash and cash equivalents (classified as loans and receivables), trade receivable (classified as loans and receivables), trade payable (classified as other financial liabilities). The fair values of these financial instruments approximate their carrying values. Initial and subsequent measurement and recognition of changes in the value of financial instruments depends on their initial classification:

Loans and receivables and other financial liabilities are initially measured at fair value and subsequently measured at amortized cost. Amortization of premiums or discounts and losses due to impairment are included in current period net income (loss).

Held for trading financial instruments are measured at fair value. All gains and losses are included in net income (loss) for the period in which they arise.

Available-for-sale investments are recognized initially at fair value plus transaction costs and are subsequently carried at fair value. Gains or losses arising from remeasurement are recognized in other comprehensive income. When an available-for-sale investment is sold or impaired, the accumulated gains or losses are moved from accumulated other comprehensive income to the statement of income and are included in “other gains and osses (net)”. Available-for-sale investments are classified as non-current, unless an investment matures within twelve months, or management expects to dispose of it within twelve months.

Financial assets and liabilities are offset and the net amount presented in the consolidated balance sheet when, and only when, the Company has a legal right to offset the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

**e. Cash and Cash equivalents**

Cash and cash equivalents consist of cash on hand, bank deposits and highly liquid short-term investments with a maturity date of three months or less when acquired.

**f. Inventories**

Silver-lead and silver-zinc in concentrate and ore stockpiles are physically measured or estimated and valued at the lower of cost or net realizable value. Net realizable value is the estimated selling price, less estimated costs of completion and costs of selling final product.

Cost is determined by the weighted average method and comprises direct purchase costs and an appropriate portion of fixed and variable overhead costs, including depreciation and amortisation, incurred in converting materials into finished goods. The cost of production is allocated to joint products using a ratio of spot prices by volume at each month end. Separately identifiable costs of conversion of each metal are specifically allocated.

Materials and supplies are valued at the lower of cost or net realizable value. Any provision for obsolescence is determined by reference to specific items. A regular review is undertaken to determine the extent of any provision for obsolescence by comparing those item to their replacement costs.



When inventories have been written down to net realizable value, the Company makes a new assessment of net realizable value in each subsequent period. If the circumstances that caused the write-down no longer exist, the remaining amount of the write-down is reversed.

**g. Property, plant and equipment**

Property, plant and equipment are carried at cost less accumulated depreciation and any impairment charges.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate assets (major components) of property, plant and equipment.

The cost of replacing a part of an item of property, plant and equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Company, and its cost can be measured reliably. The carrying amount of the replaced part is derecognized. The costs of the day-to-day servicing of property, plant and equipment are recognized in profit or loss as incurred.

Depreciation is recorded over the useful life of the asset, or over the remaining life of the mine, if shorter, as follows:

- Mining properties - on a units-of-production basis;
- Associated mining equipment - 3-10 years on a straight line basis;
- Buildings - 20 years on a straight line basis; and
- Processing equipment - 4-8 years on a straight line basis.

Depreciation charges on a unit-of-production basis are based on indicated and inferred mineral resources.

The method of amortization, estimates of residual values and useful lives are reassessed at least at each financial year-end, and any change in estimate is taken into account in the determination of future depreciation charges.

**h. Exploration and evaluation expenditures**

Acquisitions of mineral rights are capitalized. Subsequent exploration and evaluation costs related to an area of interest are expensed as incurred on a project-by-project basis pending determination of indicated resources. Upon determination of indicated resources, further development costs are capitalized.

The capitalized costs are presented as either tangible or intangible development assets according to the nature of the assets acquired. When a licence is relinquished or a project is abandoned, the related costs are immediately recognized in profit or loss.

**i. Development expenditure**

Development expenditures incurred by or on behalf of the Company are accumulated separately for each area of interest in which an indicated resource has been identified. Such expenditures comprise costs directly attributable to the construction of a mine and the related infrastructure.

General and administrative costs are allocated to a development asset only to the extent that those costs can be related directly to development activities in the relevant area of interest.

Once a development decision has been taken, the development expenditure is classified under property, plant and equipment as "development properties".

A development property is reclassified as a "mining property" at the end of the commissioning phase, when the mine is capable of operating in the manner intended by management.

No depreciation is recognized in respect of development properties until they are reclassified as "mining properties".

Each development property is tested for impairment in accordance with the policy in note 3 m ii Impairment.

**j. Mining properties**

When further development expenditures are incurred in respect of a mining property after the commencement of production, such expenditures are carried forward as part of the mining property when it is probable that additional future economic benefits associated with the expenditure will flow to the consolidated entity. Otherwise such expenditures are classified as a cost of production.

Depreciation is charged using the units-of-production method. The units-of-production basis results in a depreciation charge proportional to the depletion of indicated and inferred resources.

Mine properties are tested for impairment in accordance with the policy in note 3 m ii Impairment.

### k. Decommissioning and site rehabilitation provision

The Company records the present value of estimated costs of legal and constructive obligations required to restore operating locations in the period in which the obligation is incurred. The nature of these restoration activities includes dismantling and removing structures, rehabilitating mines and tailings dams, dismantling operating facilities, closure of plant and waste sites, and restoration, reclamation and re-vegetation of affected areas.

The obligation is attributable to development when the asset is installed or the environment is disturbed at the production location. Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a discount rate that reflects the current market assessments of the time value of money. When the liability is initially recognized, the present value of the estimated cost is capitalised by increasing the carrying amount of the related mining asset.

The periodic unwinding of the discount applied in establishing the net present value of provisions due to the passage of time is recognized in the consolidated statement of income as a finance cost. Changes in the rehabilitation estimate attributable to development will be recognized as additions or charges to the corresponding assets and rehabilitation liability when they occur.

### l. Mineral Rights

Mineral rights are carried at cost and amortized using a units-of-production method based on the resources that exist in the location that has access to such rights.

Methods of amortization and estimated useful lives are reassessed annually and any change in estimate is taken into account in the determination of future amortization charges.

### m. Impairment

#### *i. Financial assets*

A financial asset not carried at fair value through profit or loss is assessed at each reporting date to determine whether there is objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

#### *ii. Non-financial assets*

The carrying amounts of the Company's non-financial assets, other than inventories and deferred tax assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset or CGU recoverable amount is estimated. Recoverability of assets or CGU (mine operation) to be held and used are measured by a comparison of the carrying value of the asset to the recoverable amount, which is the higher of value in use and fair value less costs to sell.

For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets.

An impairment loss is recognized if the carrying amount of an asset or the CGU exceeds its estimated recoverable amount. Impairment losses are recognized in profit or loss.

Impairment losses recognized in respect of the CGU are allocated to reduce the carrying amount of long-lived assets in the unit on a pro rata basis.

Non-financial assets that have been impaired in prior periods are tested for possible reversal of impairment whenever events or changes in circumstances indicate that the impairment has reversed. If the impairment has reversed, the carrying amount of the asset is increased to its recoverable amount but not beyond the carrying amount that would have been determined had no impairment loss been recognized for the asset in the prior periods. A reversal of an impairment loss is recognized into earnings immediately.

**n. Future employee Benefits**

Employees of the Company's Mexican mines are entitled by local labor laws to employee leaving indemnities, generally based on each employee's length of service, employment category and remuneration.

The cost of these retirement benefits is determined using the projected unit credit method. Current service cost and any past service cost are recognized in the same line item in the statements of income as the related compensation cost. Changes in actuarial assumptions used to determine the accrued benefit obligation are recognized in full in the period in which they occur, in the statements of income.

The most significant assumptions used in accounting for post employment benefits are the discount rate, the mortality and the life of mine assumptions. The discount rate is used to determine the net present value of future liabilities. Each year, the unwinding of the discount on those liabilities is charged to the Company's income statement as the interest cost. The life of mine and mortality assumptions are used to project the future stream of benefit payments, which is then discounted to arrive at a net present value of liabilities. The values attributed to the liabilities are assessed in accordance with the advice of independent qualified actuaries.

**o. Current and deferred income tax**

The tax expense for the period comprises current and deferred tax. Tax is recognized in the statement of income and comprehensive income, except to the extent that it relates to items recognized in other comprehensive income or directly in equity. In this case the tax is also recognized in other income or directly in equity, respectively.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in the countries where the Company's subsidiaries operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is recognized, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit nor loss. Deferred income tax is provided on temporary differences arising on investments in subsidiaries except in the case of a subsidiary where timing of the reversal of the temporary difference is controlled by the Company and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred income tax is determined on a non discount basis using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognized only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

The Company recognizes neither the deferred tax asset regarding the temporary difference on the rehabilitation liability, nor the corresponding deferred tax liability regarding the temporary difference on the rehabilitation asset.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

**i. Royalties**

Royalties, resource rent taxes and revenue-based taxes are accounted for under taxes when they have the characteristics of an income tax. This is considered to be the case when they are imposed under Government authority and the amount payable is based on taxable income - rather than based on quantity produced or as a percentage of revenue - after adjustment for temporary differences. For such arrangements, current and deferred tax is provided on the same basis as described above for other forms of taxation. Obligations arising from royalty arrangements that do not satisfy these criteria are recognized as current provisions and included in cost of sales. The royalties incurred by the Company are considered not to meet the criteria to be treated as part of income tax.

**p. Share-based payments**

***i. Share-based payment transactions***

Employees (including directors and senior executives) of the Company receive a portion of their remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity instruments ("equity-settled transactions").

In situations where equity instruments are issued to non-employees and some or all of the goods or services received by the Company, as consideration cannot be specifically identified, they are measured at fair value of the share-based payment. Otherwise, share-based payments are measured at the fair value of goods or services received.

***ii. Equity-settled transactions***

The costs of equity-settled transactions with employees are measured by reference to the fair value at the date on which they are granted using the Black-Scholes option-pricing model.

The costs of equity-settled transactions are recognized, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ("the vesting date"). The cumulative expense is recognized for equity-settled transactions at each reporting date until the vesting date reflects the Company's best estimate of the number of equity instruments that will ultimately vest. The profit or loss charge or credit for a period represents the movement in cumulative expense recognized as at the beginning and end of that period and the corresponding amount is represented in contributed surplus. No expense is recognized for awards that do not ultimately vest.



Where the terms of an equity-settled award are modified, the minimum expense recognized is the expense as if the terms had not been modified. An additional expense is recognized for any modification, which increases the total fair value of the share-based payment arrangement, or is otherwise beneficial to the employee as measured at the date of modification.

The dilutive effect of outstanding options is reflected as additional dilution in the computation of earnings per share.

**q. Revenue recognition**

Company policy requires all production to be sold under contract. Revenue is only recognized on individual shipments when persuasive evidence exists that the following criteria are satisfied:

- The significant risks and rewards of ownership of the product have been transferred to the buyer;
- Neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold has been retained;
- The amount of revenue can be measured reliably;
- It is probable that the economic benefits associated with the sale will flow to the Company; and
- The costs incurred or to be incurred in respect of the sale can be measured reliably.

Satisfaction of these conditions depends on the terms of trade with individual customers. Generally the risks and rewards are considered to have transferred to the customer when title and insurable risk of loss transfer.

Certain products are sold on a 'provisional pricing' basis where the sale price received by the group is subject to a final adjustment at the end of a period that may be up to 60 days after delivery to the customer. The final sale price is based on the market price on the quotational date in the contract of sale. Sales are initially recognized when the revenue recognition criteria have been satisfied, using market prices at that date. At each reporting date the provisionally priced shipment is marked to market based on the forward selling price for the quotational point specified in the contract until that point is reached. Revenue is only recognized on this basis where the forward selling price can be reliably measured.

Many of the Company's sales are subject to an adjustment based on inspection of the shipment by the customer. In such cases, revenue is recognized based on the group's best estimate of the grade at the time of shipment, and any subsequent adjustments are recorded against revenue when advised.

**r. Earnings per share**

Basic earnings per share ("EPS") is calculated by dividing the net income (loss) for the period attributable to equity owners of Excellon by the weighted average number of common shares outstanding during the period.

Diluted EPS is calculated by adjusting the weighted average number of common shares outstanding for dilutive instruments. The number of shares included with respect to options, warrants and similar instruments is computed using the treasury stock method. Excellon's potentially dilutive common shares comprise stock options granted to employees and warrants.

**s. Accounting standards issued but not yet applied**

IFRS 9, Financial Instruments was issued by the IASB and will replace IAS 39, Financial Instruments: Recognition and Measurement. IFRS 9 retains but simplifies the mixed measurement model and establishes two primary measurement categories for financial assets: amortized cost and fair value through profit or loss. IFRS 9 also replaces the models for measuring equity instruments. Such instruments are either recognized at fair value through profit or loss or at fair value through other comprehensive income (loss). Where equity instruments are measured at fair value through other comprehensive income (loss), dividends are recognized in profit or loss to the extent that they do not clearly represent a return of investment; however, other gains and losses (including impairments) associated with such instruments remain in accumulated comprehensive income (loss) indefinitely. Requirements for financial liabilities are included in IFRS 9 and they largely carry forward existing requirements from IAS 39, except that fair value changes due to credit risk for liabilities designated at fair value through profit and loss are generally recorded in other comprehensive income (loss). IFRS 9 is effective for annual periods beginning on or after January 1, 2015. The Company is currently evaluating the impact of IFRS 9 on its consolidated financial statements.

IFRS 10, Consolidated Financial Statements was issued by the IASB to replace IAS 27, Consolidated and Separate Financial Statement and SIC-12, Consolidation - Special Purpose Entities. IFRS 10 requires an entity to consolidate an investee when it has power over the investee, is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Under existing IFRS, consolidation is required when an entity has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. IFRS 10 is effective for annual periods beginning on or after January 1, 2013. The Company is currently evaluating the impact of IFRS 10 on its consolidated financial statements.

IFRS 11, Joint Arrangements supersedes IAS 31, Interests in Joint Ventures, and SIC-13, Jointly Controlled Entities - Non-monetary Contributions by Venturers. IFRS 11 requires a venturer to classify its interest in a joint arrangement as a joint venture or joint operation. Joint ventures will be accounted for using the equity method of accounting whereas for a joint operation the venturer will recognize its share of the assets, liabilities, revenue and expenses of the joint operation. Under existing IFRS, entities have the choice to proportionately consolidate or equity account for interests in joint ventures. IFRS 11 is effective for annual periods beginning on or after January 1, 2013. The Company is currently evaluating the impact of IFRS 11 on its consolidated financial statements.

IFRS 12 Disclosures of Interests in Other Entities was issued by the IASB to create a comprehensive disclosure standard to address the requirements for subsidiaries, joint arrangements and associates including the reporting entity's involvement with other entities. It also includes the requirements for unconsolidated structured entities. IFRS 12 is effective for annual periods beginning on or after January 1, 2013. The Company is currently evaluating the impact of IFRS 12 on its consolidated financial statements.

IFRS 13, Fair Value Measurement is a comprehensive standard for fair value measurement and disclosure requirements for use across all IFRS standards. The new standard clarifies that fair value is the price that would be received to sell an asset, or paid to transfer a liability in an orderly transaction between market participants, at the measurement date. It also establishes disclosures about fair value measurement. Under existing IFRS, guidance on measuring and disclosing fair value is dispersed among the specific standards requiring fair value measurements and does not always reflect a clear measurement basis or consistent disclosures. IFRS 13 is effective for annual periods beginning on or after January 1, 2013. The Company is currently evaluating the impact of IFRS 13 on its consolidated financial statements.

The company plans to adopt these IFRS accounting standards when these standards become effective, if applicable.

## 4. Significant Accounting Estimates and Judgements

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Company's accounting policies. The following areas involve a higher degree of judgement or are areas where assumptions and estimates are significant to the consolidated financial statements. Actual results may differ significantly from these estimates included in the consolidated financial statements.

*i.* ***Valuation of mining properties and other long lived assets***

Mining properties and other long-lived assets are reviewed and evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. Common indicators of impairment in the mining industry include:

- A significant deterioration in expected future commodity prices;
- A significant adverse movement in foreign exchange rates;
- A significant increase in production costs;
- A large cost overrun during the development and construction of a new mine;
- A significant increase in the expected cost of dismantling assets and restoring the site;
- A significant reduction in the mineral content of ore reserves/resources;
- Serious mine accidents;
- A significant increase in market interest rates; and
- Adverse changes in government regulations and environmental law, including a significant increase in the taxes payable by the mine.

As at December 31, 2012 the Company determined that there were no indicators of impairment in carrying values of mining properties or any other long lived assets or cash generating units ("CGU").

*ii.* ***Useful economic life of property, plant and equipment***

The cost less the residual value of each item of property, plant and equipment is amortized over its useful economic life. Amortization is charged to cost of production over the shorter of the estimated lives of the individual assets or the life of mine using the units-of-production method. Amortization commences when assets are available for use. Land is not amortized.

The assets useful lives, expected units-of-production and methods of amortization are reviewed and adjusted if appropriate at each fiscal year end.

*iii.* ***Decommissioning and site rehabilitation provision***

The Company records any decommissioning and site rehabilitation obligation as a long-term liability in the period in which the related environmental disturbance occurs, based on the net present value of the estimated future costs (note 9). This obligation is adjusted at the end of each fiscal period to reflect the passage of time and changes in the estimated future costs underlying the obligation. In determining this obligation, management must make a number of assumptions about the amount and timing of future cash flows and discount rate to be used.

The undiscounted estimate of the asset retirement obligation ("ARO") has been discounted to its present value at a risk free rate which represents the 10 year Government of Canada bond rate and an estimate of the Company's pricing in the market to obtain debt. Assuming that all other variables remain constant, a one percent change in the discount rate would result in the liability change of approximately $112. The estimate also assumes a long term inflation rate. Assuming all other variables remain constant, a one percent change in the long term inflation rate would result in the liability change of approximately $111. Assuming all other variables remain constant, a 10% change in the undiscounted estimate of the ARO would result in the liability change of approximately $133.

*iv.* ***Calculation of share-based compensation expense***



The amount expensed for stock-based compensation is based on the application of a recognized option valuation formula, which is highly dependent on the expected volatility of the Company's registered shares and the expected life of the options. The Company uses an expected volatility rate for its shares based on past stock trading data, adjusted for future expectations, and actual volatility may be significantly different. While the estimate of stock-based compensation can have a material impact on the operating results reported by the Company, it is a non-cash charge and as such has no impact on the Company's cash position or future cash flows.

*v. Determination of reserves and resources*

The Company uses the services of experts to estimate the indicated and inferred resources of its mineral properties in Mexico. These experts express an opinion based on certain technological and legal information as prepared by management as being current, complete and accurate as of the date of their calculations and in compliance with National Instrument 43-101. These estimated resources are used in the evaluation of potential impairment of asset carrying values, the useful lives of assets, amortization rates and the timing of cash flows.

*vi. Income taxes*

Income taxes are calculated using the liability method of tax accounting. Under this method, current income taxes are recognized for the estimated income taxes payable for the current period. Deferred income tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and on unclaimed losses carried forward and are measured using the substantially enacted tax rates that are expected to be in effect when the differences are expected to reverse or losses are expected to be utilized. Deferred tax assets are recorded to recognize tax benefits only to the extent that, based on available evidence, including forecasts, it is probable that they will be realized.

## 5. Marketable Securities

The Company invested $5,000 in the Sprott Physical Silver Trust to hold units reflecting an underlying investment in ounces of silver. These securities have been classified as a "held for trading financial instrument" during the year. An unrealized loss of $848 was recorded in income in recognition of a decrease in value as at December 31, 2012.

## 6. Inventories

| | **2012**<br>**$** | 2011<br>$ |
|---|---|---|
| Ore | **29** | 450 |
| Concentrate | **578** | – |
| Production spares | **1,415** | 1,009 |
| | **2,022** | 1,459 |

## 7. Property, Plant And Equipment

| | Mining properties $ | Mining equipment $ | Processing equipment $ | Assets under construction $ | Total $ |
|---|---|---|---|---|---|
| At January 1, 2011 | | | | | |
| Cost | 20,443 | 8,778 | 7,127 | 3,968 | 40,316 |
| Accumulated depreciation | (12,566) | (2,628) | (1,317) | – | (16,511) |
| | 7,877 | 6,150 | 5,810 | 3,968 | 23,805 |
| **Year ended December 31, 2011** | | | | | |
| Opening net book value | 7,877 | 6,150 | 5,810 | 3,968 | 23,805 |
| Additions | 1,957 | 837 | – | 1,351 | 4,145 |
| Reclassification | 367 | 280 | 1,784 | (2,431) | – |
| Disposals | – | (41) | – | (28) | (69) |
| Depreciation | (625) | (841) | (865) | – | (2,331) |
| Write-down | – | – | – | (1,273) | (1,273) |
| Exchange differences | (1,322) | (945) | (36) | (820) | (3,123) |
| Closing net book value | 8,254 | 5,440 | 6,693 | 767 | 21,154 |
| At December 31, 2011 | | | | | |
| Cost | 20,584 | 8,636 | 8,814 | 767 | 38,801 |
| Accumulated depreciation | (12,330) | (3,196) | (2,121) | – | (17,647) |
| | 8,254 | 5,440 | 6,693 | 767 | 21,154 |
| **Year ended December 31, 2012** | | | | | |
| Opening net book value | 8,254 | 5,440 | 6,693 | 767 | 21,154 |
| Additions | 1,115 | 856 | 38 | 768 | 2,777 |
| Reclassification | – | 864 | 185 | (1,049) | – |
| Disposals | – | (3) | (1,741) | – | (1,744) |
| Depreciation | (615) | (1,066) | (1,023) | – | (2,704) |
| Write-down | – | – | (100) | – | (100) |
| Exchange differences | 546 | 409 | 587 | 47 | 1,589 |
| Closing net book value | 9,300 | 6,500 | 4,639 | 533 | 20,972 |
| At December 31, 2012 | | | | | |
| Cost | 22,810 | 10,928 | 7,685 | 533 | 41,956 |
| Accumulated depreciation | (13,510) | (4,428) | (3,046) | – | (20,984) |
| | 9,300 | 6,500 | 4,639 | 533 | 20,972 |

## 8. Mineral Rights

| | Platosa (Mexico) $ | Beschefer (Canada) $ | Desantis (Canada) $ | Total $ |
|---|---|---|---|---|
| At January 1, 2011 | | | | |
| Cost | 2,547 | – | – | 2,547 |
| Accumulated depreciation | (577) | – | – | (577) |
| | 1,970 | – | – | 1,970 |
| **Year ended December 31, 2011** | | | | |
| Opening net book value | 1,970 | – | – | 1,970 |
| Additions (1) | – | 8,163 | 10,960 | 19,123 |
| Depreciation | (168) | – | – | (168) |
| Exchange differences | (206) | – | – | (206) |
| Closing net book value | 1,596 | 8,163 | 10,960 | 20,719 |
| At December 31, 2011 | | | | |
| Cost | 2,255 | 8,163 | 10,960 | 21,378 |
| Accumulated depreciation | (659) | – | – | (659) |
| | 1,596 | 8,163 | 10,960 | 20,719 |
| **Year ended December 31, 2012** | | | | |
| Opening net book value | 1,596 | 8,163 | 10,960 | 20,719 |
| Additions | 2,400 | 648 | 804 | 3,852 |
| Depreciation | (189) | – | – | (189) |
| Exchange differences | 222 | (81) | (118) | 23 |
| Closing net book value | 4,029 | 8,730 | 11,646 | 24,405 |
| At December 31, 2012 | | | | |
| Cost | 4,927 | 8,730 | 11,646 | 25,303 |
| Accumulated depreciation | (898) | – | – | (898) |
| | 4,029 | 8,730 | 11,646 | 24,405 |

(1) On August 5, 2011 the Company completed the purchase of the net assets of Lateegra Gold Corp. ("Lateegra"). An aggregate of 50,056,999 common shares of Lateegra were exchanged for 27,030,787 common shares of Excellon representing an exchange ratio of one Lateegra share being equal to 0.54 Excellon share. The fair value of the net assets acquired were as follows:

| | August 5, 2011 $ |
|---|---|
| Cash and cash equivalents | 1,191 |
| Trade receivables | 127 |
| Other current assets | 38 |
| Long term investments | 51 |
| Mineral rights | 18,266 |
| Trade payables | (174) |
| Net assets acquired | 19,499 |

Acqusition cost is comprised of the following

| | $ |
|---|---|
| Share capital issuance | 18,400 |
| Options and warrants issuance | 694 |
| Legal and professional fees | 405 |
| | 19,499 |

## 9. Provisions

| | Post - retirement benefits (1) $ | Rehabilitation provision $ | Total $ |
|---|---|---|---|
| At January 1, 2011 | | | |
| Opening balance | 987 | 388 | 1,375 |
| **Year ended December 31, 2011** | | | |
| Opening balance | 987 | 388 | 1,375 |
| Change in estimate | (628) | 824 | 196 |
| Accretion for the year | – | 34 | 34 |
| Exchange differences | (131) | (45) | (176) |
| Closing Balance | 228 | 1,201 | 1,429 |
| **Year ended December 31, 2012** | | | |
| Opening balance | 228 | 1,201 | 1,429 |
| Change in estimate | 59 | (34) | 25 |
| Accretion for the year | – | 75 | 75 |
| Exchange differences | 18 | 90 | 108 |
| Closing Balance | 305 | 1,332 | 1,637 |

(1) Post-retirement benefits: The Company provides post retirement benefits supplements as well as leaving indemnities to employees at the Mexican operations. Under Mexican Labour Law, the Company provides statutorily mandated severance benefits to its employees terminated under certain circumstances. Such benefits consist of a one-time payment of three months wages plus 20 days wages for each year of service payable upon involuntary termination without just cause.

Key financial assumptions used in the above estimate include an annual discount rate of 6.5% (2011 - 7%), annual salary and minimum wage increase rate of 3.5% (2011 - 3.5%) and the life of the mine of ten years.

## 10. Share Capital

| | Number of shares (000's) | $ |
|---|---|---|
| **Year ended December 31, 2011** | | |
| Opening balance | 247,873 | 55,937 |
| Shares issued on exercise of stock options | 3,165 | 2,856 |
| Shares issued on Lateegra acquisition | 27,031 | 18,400 |
| Shares issued on Beschefer agreement | 1,080 | 855 |
| Share purchase buyback | (852) | (251) |
| Balance at December 31, 2011 | 278,297 | 77,797 |
| **Year ended December 31, 2012** | | |
| Opening balance | 278,297 | 77,797 |
| Shares issued on exercise of stock options | 84 | 71 |
| Shares issued on Beschefer agreement | 1,080 | 648 |
| Shares issued on Desantis agreement | 842 | 414 |
| Share purchase buyback | (5,124) | (1,477) |
| Balance at December 31, 2012 | 275,179 | 77,453 |



### SHARE OPTION PROGRAM (EQUITY-SETTLED)

The Company has a share option program that entitles directors, officers, employees and consultants to purchase shares in the Company. Under the program, the Company may grant options for up to 10% of the common shares issued and outstanding. Under the program, the exercise price of each option may not be less than the market price of the Company's common shares on the date of grant, and an option's maximum term is five years. Options may be granted by the board of directors at any time and may vest immediately upon grant.

***Disclosure of share option program***

The number and weighted average exercise prices of share options are as follows:

| | **2012** | | 2011 | |
|---|---|---|---|---|
| | **Weighted Average Exercise Price (CAD)** | **Options** | Weighted Average Exercise Price (CAD) | Options |
| Outstanding at January 1 | **$ 1.07** | **13,764,952** | $ 1.18 | 12,844,272 |
| Granted | **$ 0.54** | **2,000,000** | $ 0.67 | 6,198,400 |
| Exercised | **$ 0.50** | **(83,334)** | $ 0.53 | (3,165,000) |
| Expired | **$ 2.10** | **(2,139,968)** | $ 1.54 | (1,669,385) |
| Forfeited | **$ 0.68** | **(1,294,666)** | $ 0.90 | (443,335) |
| Outstanding at December 31 | **$ 0.85** | **12,246,984** | $ 1.07 | 13,764,952 |
| Exercisable at December 31 | **$ 0.90** | **10,168,638** | $ 1.15 | 10,818,270 |

The options outstanding at December 31, 2012 have an exercise price in the range of CAD $0.19 to CAD $3.18 (2011 - CAD $0.19 to CAD $5.21) and a weighted average remaining contractual life of 2.61 years (2011 - 2.69 years).

The weighted average share price at the date of exercise for share options exercised in 2012 was CAD $0.62 (2011 - CAD $0.94).

***Inputs for measurement of grant date fair values***

The grant date fair value of the share option program was measured based on the Black-Scholes formula. Expected volatility is estimated by considering historic average share price volatility. The inputs used in the measurement of the fair values at grant date of the share option program are the following:

| **Weighted average** | **2012** | 2011 |
|---|---|---|
| Fair value at grant date | **$ 0.40** | $ 0.42 |
| Share price at grant date | **$ 0.54** | $ 0.79 |
| Exercise price | **$ 0.85** | $ 0.67 |
| Risk free interest rate | **1.31%** | 1.58% |
| Expected life of options in years | **2.61** | 2.92 |
| Expected volatility | **92.28%** | 81.04% |
| Expected dividend yield | **0.00%** | 0.00% |
| Estimated forfeiture rate | **4.97%** | 2.99% |

***Share-based compensation expense***

Compensation expense is recognized over the vesting period of the grant and the corresponding entry is recorded in equity as contributed surplus. Share-based compensation expense is comprised of the following costs:

| | **2012** $ | 2011 $ |
|---|---|---|
| Share options granted in 2009 | **–** | 132 |
| Share options granted in 2010 | **227** | 687 |
| Share options granted in 2011 | **448** | 1,816 |
| Share options granted in 2012 | **455** | – |
| | **1,130** | 2,635 |

**WARRANTS**

During the year, all outstanding warrants expired, unexercised.

### *Disclosure of warrants*

The number and weighted average exercise prices of warrants are as follows:

| | 2012 Weighted Average Exercise Price (CAD) | 2012 Warrants | 2011 Weighted Average Exercise Price (CAD) | 2011 Warrants |
|---|---|---|---|---|
| Outstanding at January 1 | **0.82** | **3,928,662** | – | – |
| Granted during the period | **–** | **–** | 0.86 | 6,244,650 |
| Expired during the period | **0.82** | **(3,928,662)** | 0.92 | (2,315,988) |
| Outstanding at December 31 | **–** | **–** | 0.82 | 3,928,662 |
| Exercisable at December 31 | **–** | **–** | 0.82 | 3,928,662 |

### *Inputs for measurement of grant date fair values*

The grant date fair value of the warrants was measured based on the Black-Scholes formula. Expected volatility is estimated by considering historic average share price volatility. The inputs used in the measurement of the fair values at grant date of the warrants are the following:

| Weighted average | | 2012 | | 2011 |
|---|---|---|---|---|
| Fair value at issue date | **$** | **–** | $ | 0.07 |
| Share price at issue date | **$** | **–** | $ | 0.67 |
| Exercise price | **$** | **–** | $ | 0.86 |
| Risk free interest rate | | **–** | | 1.47% |
| Expected life of warrants in years | | **–** | | 0.46 |
| Expected volatility | | **–** | | 68.51% |
| Expected dividend yield | | **–** | | 0.00% |
| Estimated forfeiture rate | | **–** | | 2.99% |

## 11. Expense By Nature

### (a) Cost of sales is comprised of the following:

| | 2012 $ | 2011 $ |
|---|---|---|
| Direct mining and milling costs (1) | **16,081** | 14,241 |
| Depletion, depreciation and amortization | **2,787** | 2,411 |
| Royalties | **321** | 543 |
| **Cost of sales** | **19,189** | 17,195 |

(1) Cost of sales consists of direct mining and milling costs; which include personnel, general and administrative, fuel and electricity, maintenance and repair costs as well as operating supplies, external services, third party smelting, refining and transport fees. Care and maintenance costs incurred at the mine during the illegal blockade have been included in cost of sales.

### (b) Corporate administrative expenses consist of the following:

| | 2012 $ | 2011 $ |
|---|---|---|
| Office and overhead costs | **3,025** | 2,810 |
| Salaries and wages | **3,078** | 3,033 |
| Share based compensation | **1,130** | 2,474 |
| Depletion, depreciation and amortization | **105** | 88 |
| **Corporate administrative expenses** | **7,338** | 8,405 |

### (c) Other (income) expenses consist of the following:

| | **2012** **$** | 2011 $ |
|---|---|---|
| Impairment of long term assets | **100** | 1,273 |
| Unrealized loss (gain) on marketable securities | **851** | – |
| Foreign exchange loss (gain) | **(1,728)** | 3,792 |
| **Other expenses (income)** | **(777)** | 5,065 |

## 12. Compensation Of Key Management

Key management includes the Company's directors and officers. Compensation awarded to key management included:

| | **2012** **$** | 2011 $ |
|---|---|---|
| Salaries and short-term employee benefits | **2,399** | 2,272 |
| Share-based payments | **1,126** | 1,656 |
| | **3,525** | 3,928 |

## 13. Related Parties

The corporate secretary of the Company is a partner in a firm that provides legal services to the Company. During the year, the Company incurred legal services of $182 (2011 - $162) with an outstanding payable balance of $18 at December 31, 2012 (December 31, 2011 - $30).

## 14. Income Tax

The Company's provision for (recovery of) income taxes differs from the amount computed by applying the combined Canadian federal and provincial income tax rates to income before income tax as a result of the following:

| | **2012** **$** | 2011 $ |
|---|---|---|
| **Statutory tax rates** | **26.50%** | 28.25% |
| Income taxes computed at the statutory rates | **139** | 3,177 |
| Non-deductible items | **(1,014)** | 773 |
| Change in tax benefit not recognized | **(7,080)** | 2,283 |
| Foreign tax differentials, rate changes and other | **71** | 581 |
| **Provision for income taxes (recovery)** | **(7,884)** | 6,814 |

The enacted or substantially enacted tax rate in Canada (26.50% in 2012) and Mexico (30.00% in 2012) where the company operates is applied in the tax provision calculation. The Canadian tax rate decreased from 28.25% in 2011 to 26.50% in 2012 due to reductions in the enacted Federal and Ontario rates.

Provision for (recovery of) income taxes consists of the following:

| | **2012** **$** | 2011 $ |
|---|---|---|
| Current income taxes | **506** | 6,270 |
| Deferred income taxes (recovery) | **(8,390)** | 544 |
| | **(7,884)** | 6,814 |

The following table the Company's reflects deferred income tax assets (liabilities):

| | 2012<br>$ | 2011<br>$ |
|---|---|---|
| Non-capital losses carried forward | **6,232** | – |
| Resource related assets | **62** | – |
| Property, plant and equipment | **2,057** | – |
| Prepaid expenses, deposits and other | **543** | 364 |
| Deferred income tax assets | **8,894** | 364 |
| Deferred income and other | **(743)** | (34) |
| Accrued revenue | **(92)** | (661) |
| Net deferred income tax assets (liabilities) | **8,059** | (331) |

The following temporary differences and non-capital losses have not been recognized in the consolidated financial statements:

| | 2012<br>$ | 2011<br>$ |
|---|---|---|
| Non-capital losses carried forward | **33,278** | 51,528 |
| Capital losses | **5,601** | 5,703 |
| Resource related deductions | **15,824** | 9,335 |
| Share issuance costs | **494** | 874 |
| Property, plant and equipment | **309** | 8,489 |
| Prepaid expenses, deposits and other | **968** | 2,110 |
| | **56,474** | 78,039 |

As at December 31, 2012, the Company has non-capital losses to be carried forward and applied against taxable income of future years. The non-capital losses have expiry dates as follows:

| | 2012<br>$ | 2011<br>$ |
|---|---|---|
| 2014 | **2,032** | 2,197 |
| 2015 | **496** | 460 |
| 2016 | **194** | 2,643 |
| 2017 | **6,098** | 6,861 |
| 2018 | **13,376** | 11,587 |
| 2019 | **560** | 485 |
| 2020 and thereafter | **32,260** | 27,295 |
| | **55,016** | 51,528 |

As at December 31, 2012, the Company has Canadian capital losses of $11,201 (2011 - $11,405) that may be carried forward indefinitely and applied against capital gains of future years.

As a December 2012, $nil (2011 - $nil) was recognized as a deferred tax liability for taxes that would be payable on the unremitted earnings of certain of the Company's subsidiaries as the Company has determined that undistributed profits of its subsidiaries will not be distributed in the foreseeable future; and the investments are not held for resale and are expected to be recouped by continued use of these operations by the subsidiaries. The amount of temporary differences not booked for these unremitted earnings at December 31, 2012 is $17,964 (2011 - $21,425).

## 15. Financial Instruments

Fair Values of non-derivative financial instruments

All financial assets and financial liabilities, other than derivatives, are initially recognized at the fair value of consideration paid or received, net of transaction costs as appropriate, and subsequently carried at fair value or amortized cost, as indicated in the tables below.

The financial assets and liabilities are presented by class in the following table at their carrying values, which generally approximate to the fair values due to their short period to maturity:

| | 2012<br>$ | 2011<br>$ |
|---|---|---|
| **Financial assets** | | |
| Loans and receivables | | |
| Cash and cash equivalents | **1,369** | 22,262 |
| Trade receivables | **5,467** | 548 |
| Fair value through profit and loss | | |
| Marketable securities | **4,152** | – |
| Available for sale investments | | |
| Long term investments | **20** | 71 |
| | **11,008** | 22,881 |
| **Financial liabilities** | | |
| Other liabilities | **2,377** | 2,503 |
| Trade payables | **2,377** | 2,503 |

The carrying values of cash and cash equivalents, trade receivables and other liabilities approximate their fair value. The methods and assumptions used in estimating the fair value of other financial assets and liabilities are as follows:

***Embedded derivatives***

Revenues from the sale of metals produced since the commencement of commercial production are based on provisional prices at the time of shipment. Variations between the price recorded at the time of sale and the actual final price received from the customer are caused by changes in market prices for metals sold and result in an embedded derivative in accounts receivable. The embedded derivative is recorded at fair value each reporting period until settlement occurs, with the changes in fair value recorded to revenues. For the year ended December 31, 2012, the Company recorded $8,387 (2011 - $11,476) in revenues from provisionally priced sales on the statement of income (loss) and comprehensive income (loss). As at December 31, 2012, the Company has recorded embedded derivatives in the amount of $4,130 (2011 - $138) in trade receivables.

***Fair Value Hierarchy***

The Company values financial instruments carried at fair value using quoted market prices, where available. Quoted market prices represent a Level 1 valuation. When quoted market prices are not available, the Company maximizes the use of observable inputs within valuation models. When all significant inputs are observable, the valuation is classified as Level 2. Valuations that require the significant use of unobservable inputs are considered Level 3.

The Company had no level 3 instruments for the years ended December 31, 2012 and 2011.

***Risk management policies and hedging activities***

The Company is sensitive to changes in commodity prices, foreign exchange and interest rates. The Company's board of directors has overall responsibility for the establishment and oversight of the Company's risk management framework. Although the Company has the ability to address its price-related exposures through the use of options, futures and forward contracts, it does not generally enter into such arrangements. Similarly, derivative financial instruments are not used to reduce these financial risks.

***Economic dependence***

The Company's sole customer is Consorcio Minero de Mexico Cormin Mex S.A. de C/V (a subsidiary within the Trafigura group of companies) ("Trafigura") accounting for 100% of sales of $36,273 (2011 - $48,010). An amount of $1,763 is included in the trade receivables from Trafigura as at December 31, 2012 (December 31, 2011 - $138).

***Credit risk***

Credit risk is the risk of unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations. The Company's credit risk is primarily attributable to cash and cash equivalents. Management believes the credit risk on cash and cash equivalents is very low since the Company's cash and cash equivalents balance are held at large international financial institutions with strong credit ratings.

The Company is exposed to credit risk from its customer, Trafigura. Accounts receivable are subject to normal industry credit risks and are considered low.

***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's approach to managing liquidity is to ensure that it will have sufficient liquidity to meet its liabilities when due. To the extent the Company does not believe it has sufficient liquidity to meet these obligations, management will consider securing additional funds through equity or debt transactions. Accounts payable excluding accrued liabilities are due within 90 days or less. In addition, the company is obligated to make annual payments of US $561 under a surface rights lease with the Ejido La Sierrita. These annual payments are subject to a CPI adjustment and the final payment is in 2037.

***Currency risk***

The Mexican peso (MXN) and the Canadian dollar are the functional currencies of the Company and as a result currency exposures arise from transactions and balance in currencies other than the functional currencies. The Company's potential currency exposures comprise:

- translational exposure in respect of non-functional currency monetary items

***Translational exposure in respect of non-functional currency monetary items***

Monetary items, including financial assets and liabilities, denominated in currencies other than the functional currency of an operation are periodically revalued to the functional currency equivalents as at that date, and the associated unrealized gain or loss is taken to the income statement to reflect this risk.

The principal non-functional currency to which the Company is exposed is the United States dollar (USD). Based on the Company's net financial assets and liabilities in USD as at December 31, 2012, a weakening of the USD against the MXN and CAD functional currencies by 1% with all other variables held constant, would increase/(decrease) net loss and equity by approximately $100.



***Transactional exposure in respect of non-functional currency expenditure and revenues***

Certain operating and capital expenditures are is incurred by some operations in currencies other than their functional currency. To a lesser extent, certain sales revenue is earned in currencies other than the functional currency of operations, and certain exchange control restrictions may require that funds be maintained in currencies other than the functional currency of the operation.

At December 31, 2012, there are no forward exchange contracts outstanding to manage short-term foreign currency cash flows relating to operating activities.

***Commodity price risk***

The nature of the Company's operations results in exposure to fluctuations in commodity prices. Management continuously monitors commodity prices of silver, lead and zinc.

The Company is particularly exposed to the risk of movements in the price of silver. Declining market prices for silver could have a material effect on the Company's profitability, and the Company's policy is not to hedge its exposure to silver. The London Silver Spot price average, in USD per ounce, was $31.15 in 2012 (2011 - $35.12). The Company estimates that an increase (decrease) in the commodity prices by 10% in 2012 with all other variables held constant would have resulted in an increase (decrease) in net income of approximately $4,000.

***Interest rate risk***

Cash and cash equivalents earn interest at floating rates dependent upon market conditions.

## 16. Capital Management

The Company's objectives of capital management are intended to safeguard the entity's ability to continue as a going concern and to continue the exploration and extraction of ore from its mining properties.

The capital of the Company consists of the items included in shareholders' equity. Risk and capital management are monitored by the board of directors. The Company manages the capital structure and makes adjustments depending on economic conditions. Funds have been primarily secured through issuances of equity capital. The Company invests all capital that is surplus to its immediate needs in short-term, liquid and highly rated financial instruments, such as cash and other short-term deposits, all held with major financial institutions. Significant risks are monitored and actions are taken, when necessary, according to the Company's approved policies.

## 17. Segment Reporting

The Chief Operating Decision Maker (CODM) is the Company's Board of Directors. The CODM monitors the operating results of segments separately in order to allocate resources between segments and to assess performance.

| | Canada | | Mexico | |
|---|---|---|---|---|
| | **2012 $** | 2011 $ | **2012 $** | 2011 $ |
| Property, plant and equipment | **8** | 44 | **20,964** | 20,482 |
| Capital expenditures | **–** | (19) | **(2,777)** | (3,723) |
| Mineral Rights | **20,376** | 19,123 | **4,029** | 1,596 |
| Total assets | **25,717** | 30,039 | **45,426** | 37,204 |
| | | | | |
| Revenue | **–** | – | **36,273** | 48,010 |
| Cost of sales | **–** | – | **(19,189)** | (17,195) |
| Corporate Administrative expenses | **(7,338)** | (8,405) | **–** | – |
| Exploration | **(2,798)** | (858) | **(7,109)** | (5,209) |
| Other expenses | **(1,077)** | (280) | **1,854** | (4,785) |
| Net Finance costs | **(17)** | – | **(75)** | (31) |
| Income tax | **–** | 43 | **7,884** | (6,857) |
| Net income (loss) | **(11,230)** | (9,500) | **19,638** | 13,933 |

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# Investor Information

**Directors:**

**Peter A Crossgrove,**
*Executive Chairman*

**Andre Y. Fortier** 1, 2, 3 Chair, 4

**Timothy J. Ryan** 1 Chair, 2, 3

**Alan R. McFarland** 1, 2 Chair, 4

**Thor E. Eaton** 1, 2, 3, 4 Chair

**Oliver Fernandez** 1, 4

**Ned Goodman**:
*Standing for Election to the Board of Directors*
**Joanne Ferstman**:
*Standing for Election to the Board of Directors*
**Brendan Cahill**, *President and Chief Executive Officer:*
*Standing for Election to the Board of Directors*

**Committees:**
1. Audit Committee
2. Nominating & Corporate Governance Committee
3. Compensation Committee
4. Health, Safety & Environmental Committee

**Officers/Management**

**Peter A Crossgrove**,
*Executive Chairman*

**Brendan Cahill**,
*President and Chief Executive Officer*

**Rupy Dhadwar**,
*Chief Financial Officer*

**Rob Moore**,
*Chief Operating Officer*

**John Sullivan**,
*VP Exploration*

**Joanne Jobin**,
*VP Investor Relations*

**Legal Advisors:**

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**Transfer Agent:**

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**Timmins Exploration Office**

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Timmins, Ontario P4N 7C3

T: 704 168 1900

**Shareholder Information**
*As at December 31, 2012*

| | |
|---|---|
| Listed: TSX | **EXN** |
| Shares O/S | **275,179,467** |
| Shares F/D | **287,426,451** |
| Treasury/Cash: | **$1.4M** |
| Market Cap: | $**154M** |

**Share price**
*(May 2012- April 2013)*


**Annual and Special Meeting of Shareholders**

The Annual and Special Meeting of Shareholders will take place on Tuesday, April 30, 2013 at 10:00 am at the TMX Broadcast Centre, located at The Exchange Tower, 130 King Street West, Toronto, Ontario, Canada, M5X 1J2.

TSX:**EXN**

EXCELLON

www.excellonresources.com