General

The following management's discussion and analysis ("MD&A") of the financial condition and results of operations of ZTEST Electronics Inc. ("ZTEST" or the "Company") constitutes management's review of the factors that affected the Company's interim condensed consolidated financial and operating performance for the six months ended December 31, 2012. The MD&A was prepared as of February 26, 2013 and should be read in conjunction with the unaudited interim condensed consolidated financial statements of the Company for the six months ended December 31, 2012, and the audited consolidated financial statements for the year ended June 30, 2012, including the notes thereto. Unless otherwise stated, all amounts discussed herein are denominated in Canadian dollars.

Additional information about the Company can be found at www.sedar.com.

The Company

The Company operates a single business segment involving the design, development, and assembly of printed circuit boards. The management of the Company, which has not changed since the preceding fiscal year end, is comprised of the following individuals:

Name	Position(s)
Wojciech Drzazga	Director and CEO
John Perreault [1]	Director and President
K. Michael Guerreiro [1] [2]	Director
Mike Hiscott [1] [2]	Director
Michael D. Kindy	VP Finance & CFO
William R. Johnstone	Secretary

(1) Denotes member of audit committee
(2) Denotes member of compensation committee

Corporate Performance

The 2013 fiscal year continues to be a growth year for the Company. Revenues for the second quarter are 32.7% greater than they were one year previously and, including the more modest growth realized in the first quarter, are 21.5% greater on a year-to-date basis. This revenue growth also continues to translate into positive cash flow from operations which amounted to $217,113 for the quarter and $380,069 for the six month period.

The Company was profitable for the fourth consecutive quarter and for the fifth time in the past six quarters. As a result of this profitability the Company has almost eliminated its deficiency in assets, has increased its capital under management. A private placement completed in February 2013 will further enhance the capital under management and will move the Company into a positive equity position.

The Company also continued to reduce its debt burden with the repayment of $81,308 in long-term debt during the quarter. This included an optional pre-payment where the Company received a $16,000 debt reduction in exchange for a $15,000 cash payment. At December 31, 2012 the total long-term debt has been reduced to $826,207 representing a reduction of $346,734, or almost 30%, in the past 12 months. The reduction in the debt burden enhances profitability through reduced financing costs and will ultimately improve cash flow as debts mature and monthly payments are no longer required.

The reduction and repayment of long-term debt is beneficial but does not occur without challenges. The Company currently has 5 long-term debt instruments outstanding. One of these debts, which is non-interest bearing and has a carrying value of $39,600, matured a number of years ago, no repayment has occurred, and no means of settlement has yet been reached with the creditor. The other four instruments are being repaid, sometimes in advance of their repayment terms and three of these debts now have maturities of 12 months or less. As a result of these impending maturities the Company has a requirement to make payments of $720,229 over the next twelve months. This not only resulted in a substantial decline in the Company's working capital position but continues to exert pressure on the Company's cash management practices.

Corporate Performance - continued

The approaching maturities have been a focal point of the Company's cash management practices for quite some time now and are the principle reason why the Company continues to accumulate cash and to make pre-payments on the debts whenever there has been a measurable benefit to doing so. Management will continue to stress its cash management practices with the objective to have the Company in position to settle these obligations as they become due.

Management will continue striving to maximize revenues, to minimize expenses, to optimize its cash utilization, and to maximize the benefits derived for its stakeholders. The following data may provide some additional insights relative to the Company's operating performance and financial position:

	For the fiscal years ended:		
	June 12	June 11	June 10
Total Revenues	4,571,417	4,010,068	3,837,630
Net income (loss) income from operations	390,936	(178,066)	266,210
Per share	0.055	(0.031)	0.051
Net income (loss) for the year	392,778	(180,359)	380,613
Per share	0.056	(0.031)	0.072
Total assets	2,340,853	2,106,570	2,255,703
Total long-term financial liabilities	698,648	1,051,125	1,352,187
Total liabilities	2,416,943	2,575,438	2,786,454

	For the three month periods ended:				
	Dec. 12	Sept. 12	June 12	Mar. 12	Dec. 11
Total Revenues	1,113,223	1,072,656	1,289,855	1,483,588	839,112
Net income (loss) from operations	31,955	6,132	42,073	279,280	(17,116)
Per share - basic	0.004	0.004	0.006	0.040	(0.002)
Net income (loss) for the period	33,336	8,789	44,015	279,280	(17,216)
Per share - basic	0.005	0.004	0.006	0.040	(0.002)
Total assets	2,133,002	2,252,523	2,340,853	2,652,994	2,122,488
Total long-term financial liabilities	66,478	602,565	698,648	785,338	902,553
Total liabilities	2,141,525	2,299,246	2,416,943	2,773,099	2,521,873

	For the three month periods ended:				
	Sept. 11	June 11	Mar. 11	Dec. 10	Sept. 10
Total Revenues	959,862	957,817	820,976	1,112,951	1,118,324
Net income (loss) from operations	86,699	(100,165)	(117,154)	(51,768)	91,021
Per share - basic	0.012	(0.014)	(0.022)	(0.010)	0.017
Net income (loss) for the period	86,699	(98,320)	(117,154)	(51,768)	86,883
Per share - basic	0.012	(0.014)	(0.022)	(0.010)	0.017
Total assets	2,033,096	2,106,570	2,299,219	2,212,766	2,250,671
Total long-term financial liabilities	962,334	1,051,125	1,173,917	1,227,289	1,115,540
Total liabilities	2,415,265	2,575,438	2,712,514	2,639,707	2,694,540

There were no cash dividends paid or accrued during any of the periods noted above.

Results of Operations

For the six month period ended December 31, 2012 the Company has reported revenues of $2,185,879, including $1,113,223 generated during the three month period then ended. The figures reported for the corresponding periods ended December 31, 2011 were $1,798,974 and $839,112. The revenues for the three month period, which were $274,111, or 32.7%, greater than the prior year, resulted in improved profitability as the Company reported net income of $33,336 for the quarter as opposed to a loss of $17,216 at December 2011. In spite of this improvement, however, net income for the six month period still trails December 2011 levels. This is a result of a decline in gross margin percentage and increased operating expenses. The highlights from operations are discussed below.

Results of Operations - continued

The cost of product sales reported for the periods ended December 31 were as follows:

Six month periods:	Dec. 12	Dec. 11	Change
Raw materials and supplies consumed	$ 955,329	$ 552,317	$ 403,012
Labour costs incurred	363,511	383,555	(20,044)
Depreciation	74,993	85,627	(10,634)
Other costs	51,022	65,460	(14,438)
Net change in finished goods and work in process	(12,238)	13,634	(25,872)
Total cost of product sales	$ 1,432,617	$ 1,100,593	$ 332,024

Three month periods:	Dec. 12	Dec. 11	Change
Raw materials and supplies consumed	$ 488,261	$ 294,961	$ 193,300
Labour costs incurred	187,601	180,266	7,335
Depreciation	37,496	42,813	(5,317)
Other costs	25,316	25,788	(472)
Net change in finished goods and work in process	4,416	(7,109)	11,525
Total cost of product sales	$ 743,090	$ 536,719	$ 206,371

The Company actively promotes turnkey assembly, which incorporates the procurement of components and supplies, as a cost-effective alternative for its customers. The alternative is pure assembly where the customers must provide all materials. It seems that, at present, many customers concur as the cost of raw materials and supplies consumed continues to be much higher. Quarterly costs were more than 65% greater at December 2012 and costs for the six month period were almost 73% higher than they were at December 2011. The average mark-up on turnkey work however is lower than it is on pure assembly work so the increased costs help to explain the lower gross margin percentages being realized. The Company will continue to promote its turnkey service however it is at the customer's discretion and accordingly volumes will fluctuate from one period to the next independent from assembly volumes.

For the first time in a number of periods the Company experienced an increase in labour costs as the expense for the three month period ended December 2012 was 4.1% greater than for the same period one year earlier. Throughout the December 2011 period the Company was participating in a government sponsored work-share program which ended in April 2012 at which time the Company implemented a permanent reduction in its workforce. Lower labour costs have persisted since that time however an increase in overall assembly volume during the recent quarter, and the provision of some more labour-intensive assemblies, translated into the 4.1% cost increase. In spite of this recent increase, the costs for the six month period ended December 2012 remain approximately 5.2% lower than December 2011 levels. The savings realized in the first quarter of the year was attributed to increased efficiencies and lower labour demand. The Company will continue to monitor its labour requirements, to make every effort to match supply to demand, and to continue to benefit from efficiency enhancements whenever feasible.

The actual amount of labour costs included in the costs of products sold for the period is determined by combining the labour costs incurred with the net change in finished goods and work in process for the period. For the three month period ended December 31, 2012 this aggregate total is $192,017 which is significantly greater than the December 31, 2011 total of $173,157. These figures are indicative of the short-term increase in labour demand resulting from increased assembly volume and the provision of some more labour-intensive assemblies.

Depreciation costs are calculated as a percentage of the carrying value of equipment which has been declining as depreciation charges exceed new additions. Only $1,690 has been spent on equipment enhancements so far this year and none of that was in the most recent three month period. This would indicate that it is reasonable to anticipate that this expense will continue to decline in the immediate future. The Company continually monitors its equipment requirements and makes acquisitions and enhancements when it is prudent to do so according to a cost-benefit analysis. Based upon the assessed capacity, capability, and reliability of the existing equipment there are no immediate plans for major acquisitions or enhancements.

Results of Operations - continued

Other costs of product sales include repairs and maintenance, stencils and tooling, packaging, and freight costs net of amounts recovered. Each of these costs is incurred on an as-needed basis and without any specific correlation with revenues which can lead to fluctuations from one period to the next. Each of these costs is constantly monitored and is within management expectations so they will not be further elaborated upon.

Selling, general and administrative expenses for the periods ended December 31 were as follows:

Six month periods:	Dec. 12	Dec. 11	Change
Employee and consultant compensation	$ 399,144	$ 342,827	$ 56,317
Occupancy costs	132,918	130,725	2,193
Professional fees	32,366	27,484	4,912
Bad debts	-	8,047	(8,047)
Regulatory fees	21,338	8,184	13,154
Other costs	39,493	35,588	3,905
Total selling, general and administrative	$ 625,259	$ 552,855	$ 72,434

Three month periods:	Dec. 12	Dec. 11	Change
Employee and consultant compensation	$ 197,348	$ 173,385	$ 23,963
Occupancy costs	64,679	56,207	8,472
Professional fees	14,710	14,500	210
Bad debts	-	-	-
Regulatory fees	6,047	5,444	603
Other costs	26,482	22,096	4,386
Total selling, general and administrative	$ 309,266	$ 271,632	$ 37,634

As expected, the increase in employee and consultant compensation realized in the first quarter persisted through the second quarter. This increase encompasses the impact from the termination of the work-share program described previously, increased director fees, and increased compensation rates. There was no reduction in administrative personnel when the work-share program ended so costs returned to previous levels and then increased due to annual salary adjustments.

Occupancy costs consist primarily of rent and utility charges for the Company's operating facility. The base rental charges are $905 per quarter greater in the current year than they were for the periods ended December 2011 thereby accounting for most of the year to date increase. The utility and additional rents arising from common area costs have fluctuated such that an increase during the second quarter offset the reduction realized in the first quarter.

Professional fees, which include a pro-rated portion of estimated annual audit fees as well as the cost of legal services, are virtually identical for the three month periods. The costs for the six month period ended December 2012 remain higher than for the corresponding period ended December 31, 2011 as a result of incremental legal fees arising from the conversion of the Class A shares to common shares and the Company's annual shareholder meeting each of which occurred during the first quarter.

For the first time in many periods, the Company incurred a bad debt during the first quarter of its 2012 fiscal year. There has been no recurrence of this event since that time as demonstrated by the absence of this expense for the other periods presented. The Company has a very strong history of collecting on each of its accounts and does not anticipate the recurrence of this cost.

Regulatory fees include all stock exchange and transfer agent fees incurred. The fees for the three month periods are highly similar, as a result of recurring transactions, but the costs associated with having held a shareholders' meeting September 2012 continue to cause the year-to-date figures to be higher during the current year. There were no similar costs incurred during the periods ended December 2011.

Results of Operations - continued

The remaining elements of SG&A are individually insignificant and represent less than 5% of total SG&A for the periods presented. These expenses are continuously monitored by management and do not warrant detailed investigation or elaboration.

The Company's debt load continues to decline which results in lower costs of financing. The financing costs are comprised of interest on long-term debt, other interest expense, and loan guarantee fees as follows:

Six month periods:	Dec. 12	Dec. 11	Change
Interest expense – long term (cash based)	$ 38,462	$ 54,577	$ (16,115)
Interest expense – long term (accretion)	12,668	9,864	2,804
Interest expense – other	297	307	(10)
Loan guarantee fees	4,800	4,800	-
Total financing expenses	$ 56,227	$ 69,548	$ (13,321)

Three month periods:	Dec. 12	Dec. 11	Change
Interest expense – long term (cash based)	$ 18,324	$ 26,360	$ (8,036)
Interest expense – long term (accretion)	3,782	4,932	(1,150)
Interest expense – other	148	149	(1)
Loan guarantee fees	2,400	2,400	-
Total financing expenses	$ 24,654	$ 33,841	$ (9,187)

Interest expense – long term includes the cash-based interest charges, the amount incurred based upon the face value of the debts, plus accretion of the difference between the face values and the carrying amounts. The reduction in the cash-based interest charges, which are 29.5% lower for the six month period, and 30.5% lower for the three month period, reflects the positive impact of management's efforts to reduce long-term debt. As at December 31, 2012 the face value of long-term debt was $843,535 and the carrying value was $826,207. In contrast the face value at December 31, 2011 was $1,213,256 and the carrying value was $1,172,941. It is anticipated that long-term debt will continue to decline resulting in further reduction in interest expense.

The Company has an operating loan facility in place with its financial institution whereby it can borrow up to $250,000. While this loan was not drawn upon the Company is still required to pay a guarantee fee of $800 per month to an individual that provided a guarantee as additional security for this loan. The current loan facility and the corresponding guarantee are scheduled to expire in May 2013.

Liquidity

The Company has reported a working capital deficiency in the amount of $666,091 as at December 31, 2012. It has been noted for a number of periods now that the impending maturity of long-term debt was going to put significant pressure on working capital. This is highly evident in the second quarter as the current portion of long-term debt rose by $457,561 and working capital declined by the very similar value of $459,443. The correlation between these figures for the six month period is not quite as precise as the current portion of long-term debt rose by $469,425 while working capital decreased by $489,404. The increase in the current portion of long-term debt is primarily attributable to two debentures which mature December 2013 and, despite the working capital position, the Company anticipates being able to settle each of its long-term obligations as they mature. This expectation may seem more rational when one considers that there is $776,792 (June 2012 - $781,656) in current liabilities which are not secured, bear no interest or other carrying charges, no payments have been made since the 2007 fiscal year, and there are no current repayment terms. The $4,864 decline in these stagnant liabilities arose from writing down a liability that originated in 2000 to its current cash value of $Nil.

Liquidity

The Company utilizes long term debt as a means of financing new equipment acquisitions and of settling other obligations whenever suitable terms can be negotiated. The Company's short-term financing requirements, if any, are now expected to be met through the bank operating line.

In addition to satisfying the cost of operations the Company must also address the settlement of the following amounts as at December 31, 2012:

	Due by Dec. 2013	Due by Dec. 2015	Due by Dec. 2017	Due after Dec. 2017	Total Due
Repurchase of preferred shares [1, 2]	$ 665,501	$ -	$ -	$ -	$ 665,501
Settlement of dividends payable [1]	263,337	-	-	-	263,337
Debenture [1]	39,600	-	-	-	39,600
Other long-term debt [3]	735,829	68,106	-	-	803,935
Operating leases	87,824	181,986	201,904	347,448	819,162
Total	$ 1,792,091	$ 250,092	$ 201,904	$ 347,448	$ 2,591,535

(1) Each of these amounts were past due as at December 31, 2012

(2) The repurchase price includes $473,855 reported as an element of current liabilities plus $191,646 in paid up capital that is reported as an element of share capital.

(3) Other long-term debt includes three obligations for which their carrying value is lower than their face values. The unaudited condensed interim consolidated financial statements as at December 31, 2012 report these obligations based upon their carrying values while the figures reported above represent the non-discounted cash payments to be made.

Capital Resources

The Company has access to a $250,000 revolving line of credit from its financial institution. The loan, which has not been drawn upon, bears interest at the prime lending rate plus 0.5%, is due upon demand, matures May 13, 2013, and is secured by a general security agreement covering the assets of Permatech Electronics Corporation and by the personal guarantee of an individual that is not related to the Company. The Company issued 500,000 share purchase warrants to the guarantor with each warrant entitling them to acquire one common share of the Company at a price of $0.135 until the earlier of May 18, 2013 and the date when the guarantee is removed. The guarantor is also to be paid a fee of $800 per month and will receive interest, based upon the amount drawn from time to time on this line of credit, equal to 10% less the interest at prime plus 0.5% that is payable to the Company's financial institution.

There were no financing transactions completed during the six month period ended December 31, 2012 however the Company did complete a private placement financing on February 4, 2013. This placement resulted in the issuance of 2,200,000 units at $0.08 per unit for gross proceeds of $176,000. Each unit was comprised of 1 common share and ½ share purchase warrant with the shares restricted from trading until June 5, 2013. Each full warrant entitles the holder to acquire one additional common share for $0.10 until February 4, 2016. The Company paid a cash finders' fee of $10,560 in respect of this offering.

Related Party Transactions

The Company has participated in a number of transactions with the Company's Officers, Directors, their spouses, and companies that are considered related as a consequence of the involvement of one or more of these individuals. All revenues, expenses and period end balances with the related parties are at exchange amounts established and agreed to by the related parties. All transactions with related parties are in the normal course of operations and have been carried out on the same terms as those accorded to unrelated parties.

The following balances were due to the related parties defined above as at the following dates:

	2012		2011	
	Dec. 31	June 30	Dec. 31	June 30
Loan payable at prime + 8% [1]	99,959	111,845	122,129	131,540

(1) This is the face value of this obligation. It is reported in the financial statements at a discounted value.

Related Party Transactions - continued

The following income and expense items have arisen as a result of transactions involving the related parties defined above:

	2012		2011	
	Dec. 31	June 30	Dec. 31	June 30
Interest expense – long term	6,492	14,433	7,633	21,030

The following stock options have been issued to Directors and/or Officers of the Company and remain outstanding as at the date of this document:

Description	Expiry Date	Number of Common shares
Stock options @ $0.10 per share	Nov. 30, 2015	900,000
Stock options @ $0.10 per share	Sept. 14, 2017	300,000

Convertible Instruments and Other Securities

The Company has the following securities issued and outstanding:

Share capital	Quantity	Amount
Balance, December 31, 2011 and June 30, 2012	7,062,488	$ 21,773,391
Common shares issued in exchange for Class A shares	99,454	8,951
Common shares	7,161,942	21,782,342
Paid in capital of preferred shares		191,646
Balance December 31, 2012	7,161,942	21,973,988
Issued February 4, 2013	2,200,000	176,000
Less: cash finders' fees paid		(10,560)
Balance as at the date of this document	9,361,942	$ 22,139,428

Preferred shares	Quantity	Amount
Series A preferred shares	166,667	$ 160,000
Series C preferred shares	288,858	505,501
		665,501
Less: amount accounted for as paid in capital		(191,646)
Liability element of preferred shares		$ 473,855

In addition to the shares issued and outstanding the Company has issued stock options as incentives to various parties. The following list itemizes the common shares that have been reserved to satisfy the conversions and exercise of options along with the expiry date associated therewith.

Reserved shares	Expiry Date	Number of Common shares
Warrants @ $0.135 per share (1)	May 2013	500,000
Stock options @ $0.10 per share	Nov. 2015	900,000
Warrants @ $0.10 per share	Mar 2016	900,000
Stock options @ $0.10 per share	Dec. 2017	300,000
Shares reserved as at December 31, 2012		2,600,000
Warrants @ $0.10 per share	Feb. 2016	1,100,000
Shares reserved as at the date of this document		3,700,000

(1) These warrants will expire on the earlier of May 18, 2013 and the date that the Company eliminates the guarantee that the holder has provided as security for the Company's line of credit. These warrants are also subject to claw-back provisions as may be imposed by the TSX Venture Exchange.

Convertible Instruments and Other Securities - continued

Fully diluted position	Number of Common shares
Shares issued	7,161,942
Shares reserved	2,600,000
Fully diluted as at December 31, 2012	9,761,942
Shares issued February 4, 2013	2,200,000
Reserved for warrants February 4, 2013	1,100,000
Fully diluted as at the date of this document	13,061,942

Additional disclosures relative to stock options are as follows:

	Common Shares Under Option	Weighted Average Price/Option	Weighted Average Expiry Date
Beginning of period	900,000	$ 0.10	Nov. 30, 2015
Issued during period	300,000	$ 0.10	Sept. 14, 2017
End of period and date of this document	1,200,000	$ 0.10	May 11, 2016

While all stock options are held by related parties the Company has no ability to cause them to be exercised.

Additional disclosures relative to share purchase warrants are as follows:

	Number of Warrants	Weighted Average Price per Warrant	Weighted Average Expiry Date
Beginning and end of period	1,400,000	$ 0.113	Mar. 18, 2015
Issued February 4, 2013	1,100,000	0.100	Feb. 4, 2016
As at date of this document	2,500,000	$ 0.107	Aug. 7, 2015

Changes in Accounting Policy

The accounting policies followed by the Company are established in accordance with International Financial Reporting Standards (IFRS) and once policies are established they will not, as a matter of policy, be revised unless IFRS changes.

Accounting standards effective in the current period but not yet adopted

IFRS 9, *Financial Instruments: Classification and Measurement*, issued in December 2009, effective for annual periods beginning on or after January 1, 2015, with early adoption permitted, introduces new requirements for the classification and measurement of financial instruments. Management anticipates that this standard will be adopted in the Company's financial statements for the year beginning July 1, 2015 and has not yet considered the potential impact of its adoption.

IFRS 10, 11, 12 and 13 were all issued in May 2011 and are effective for annual periods beginning January 1, 2013, with early adoption allowed. The Company has not yet considered the potential impact, if any, of the adoption of these standards.

IFRS 10, *Consolidated Financial Statements,* replaces the consolidation guidance in IAS 27, *Consolidated and Separate Financial Statements,* and SIC-12, *Consolidation — Special Purpose Entities*, by introducing a single consolidation model for all entities based on control, irrespective of the nature of the investee.

IFRS 11, *Joint Arrangements,* introduces new accounting requirements for joint arrangements, replacing IAS 31, *Interests in Joint Ventures*. It eliminates the option of accounting for jointly controlled entities by proportionate consolidation.

IFRS 12, *Disclosure of Interests in Other Entities,* requires enhanced disclosures about both consolidated entities and unconsolidated entities in which an entity has involvement.

IFRS 13, *Fair Value Measurement,* replaces the guidance on fair value measurement in existing IFRS accounting literature with a single standard. It defines and provides guidance on determining fair value and requires disclosures about fair value measurements, but does not change the requirements regarding which items are measured or disclosed at fair value.

Changes in Accounting Policy - continued

Accounting standards effective in the current period but not yet adopted - continued

IAS 28, *Investments in Associates and Joint Ventures*, amended in 2011, effective for annual periods beginning on or after January 1, 2013, with early adoption permitted, prescribes the accounting for investments in associates and establishes the requirements for the application of the equity method when accounting for investments in associates and joint ventures. Management anticipates that this amendment will be adopted in the Company's financial statements for the year beginning July 1, 2013 and has not yet considered the potential impact, if any, of its adoption.

Financial Assets

The Company's financial instruments are comprised of the following:

Financial assets:	*Classification*
Cash and cash equivalents	Held for trading
Accounts receivable	Loans and receivables
Lease deposit	Loans and receivables
Financial liabilities:	*Classification*
Customer deposits and deferred revenue	Other financial liabilities
Accounts payable and accrued liabilities	Other financial liabilities
Dividends payable	Other financial liabilities
Preferred shares	Other financial liabilities
Long-term debt	Other financial liabilities

Held for trading:
Financial assets are designated as held for trading if they were acquired principally for the purpose of selling in the short term. Held for trading assets are recognized and carried at their fair value.

Loans and receivables:
Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are initially recognized at fair value plus any directly attributable transaction costs. Subsequent to initial recognition loans and receivables are measured at amortized cost using the effective interest method, less any impairment losses.

Other financial liabilities:
Other financial liabilities are recognized initially at fair value net of any directly attributable transaction costs. Subsequent to initial recognition these financial liabilities are measured at amortized cost using the effective interest method. The effective interest method is a method of calculating the amortized cost of a financial liability and of allocating interest and any transaction costs over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability or (where appropriate) to the net carrying amount on initial recognition. Other financial liabilities are de-recognized when the obligations are discharged, cancelled or expired. Impairment of non-financial assets

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

Evidence of impairment could include:

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

The carrying amount of financial assets is reduced by any impairment loss directly for all financial assets with the exception of accounts receivable, where the carrying amount is reduced through the use of an allowance account. When accounts receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognized in income for the period.

Financial Assets - continued

Impairment of financial assets - continued:
If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through income for the period to the extent that the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognized.

Financial instruments recorded at fair value:
Financial instruments recorded at fair value on the condensed interim consolidated statement of financial position are classified using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

- Level 1 valuation based on quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 valuation techniques based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices);
- Level 3 valuation techniques using inputs for the asset or liability that are not based on observable market data (unobservable inputs).

As of December 31, 2012 and June 30, 2012 cash and cash equivalents are measured at fair value and as such are classified within Level 1 of the fair value hierarchy.

Forward-looking Information

This Management's Discussion & Analysis (MD&A) contains forward-looking statements that involve known and unknown risks, uncertainties and other factors which may cause actual results, performance or achievements of the Company, or the industry in which it operates, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. When used in this document, the words "may", "should", "would", "could", "will", "intend", "plan", "anticipate", "believe", "estimate", "expect" the negative thereof, other variations thereon, or comparable terminology are intended to identify forward-looking statements. Such forward-looking statements reflect the current expectations of the management of the Company with respect to future events based on currently available information and are subject to such risks and uncertainties. Many factors could cause our actual results to differ materially from the statements made, including those factors summarized below under the heading "Risk Factors" and discussed in filings made by us with the Canadian securities regulatory authorities.

Should one or more of these risks and uncertainties, such as actual results of current exploration programs, the general risks associated with the mining industry, the price of gold and other metals, currency and interest rate fluctuations, increased competition and general economic and market factors, occur or should assumptions underlying the forward looking statements prove incorrect, actual results may vary materially from those described herein as intended, planned, anticipated, or expected. The forward-looking statements contained in this MD&A speak only as of the date hereof. The Company does not undertake or assume any obligation to release publicly any revisions to these forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events, except as required by law. Stakeholders are cautioned not to put undue reliance on such forward-looking statements.

Risk Factors

Events seemingly unrelated to us, or to our industry, may adversely affect our finances or operations in ways that are hard to predict or defend against. For example, credit contraction in financial markets may hamper our ability to access credit when needed or rapid changes in foreign exchange rates may adversely affect our financial results. Finally, a reduction in credit, combined with reduced economic activity, may adversely affect businesses and industries that constitute a significant portion of our customer base. As a result, these customers may need to reduce purchases from us, or we may experience greater difficulty in collecting amounts due from them. Any of these events, or others caused by uncertainty in world financial markets, may have a material adverse effect on our business, operating results, and financial condition.

Risk Factors - continued

In addition to the foregoing, the Company is exposed in varying degrees to a variety of financial instrument related risks. The Company's primary risk management objective is to protect earnings and cash flow and, ultimately, shareholder value. Risk management strategies, as discussed below, are designed and implemented to ensure that the Company's risks and the related exposure are consistent with its business objectives and risk tolerance. There have been no changes to the risks to which the Company is exposed or to the corresponding risk management strategies during the current period.

Credit risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Company's primary exposure to credit risk is in its accounts receivable. In an effort to mitigate this risk, management actively manages and monitors its receivables and obtains pre-payments where warranted. Bad debt experience has not been significant and it has been determined that no allowance is required as all amounts outstanding are considered collectible.

Liquidity risk

Liquidity risk arises through the excess of financial obligations over available financial assets due at any point in time. The Company has reported a working capital deficiency of $206,648 (June 2012 - $176,687). This includes financial liabilities (a specific long-term debt instrument plus preferred shares and dividends payable) with an aggregate carrying amount of $781,656 (June 2012 - $781,656) which are past due and for which the timing of future cash flows are undetermined. The Company manages its liquidity risk through the management of its capital (note 11) which incorporates the continuous monitoring of actual and projected cash flows to ensure that it has sufficient liquidity to meet its operating commitments without incurring unacceptable losses or risking damage to the Company's reputation.

Market risks

The Company is exposed to interest rate risk and currency risk. The interest rate risk arises from two long-term debt instruments for which interest rates are fixed annually based upon prevailing market rates. Currency risk relates to accounts receivable and accounts payable denominated in US dollars and the potential for future cash flows to fluctuate because of changes in foreign exchange rates. Credit risk is minimized through the reduction of debt when cash flow permits. Currency risk is closely monitored but not actively managed. During the period the Company incurred a loss on foreign exchange in the amount of $7,905 (Sept 2011 – $5,443).

Sensitivity to market risks

If interest rates are 1% higher on the next subsequent interest adjustment date the monthly payments required on long-term debt over the next twelve months will increase by $273 representing additional interest expense.

At December 31, 2012 the Company had US$214,010 (2011 –US$7,885) included in accounts receivable. A 5% increase in the value of the Canadian dollar relative to the US dollar would result in a reduction of $10,860 in future cash inflow.

At December 31, 2012 the Company had US$105,654 (2011 – US$161,810) included in accounts payable. A 5% decrease in the value of the Canadian dollar relative to the US dollar would result in an increase of $5,361 in future cash outflow.

The existence of both accounts receivable and accounts payable denominated in US$ do not serve as a hedge with respect to currency risk.

Based upon observations of recent market trends management believes that each of these outcomes is possible but most likely exceed the Company's immediate market risk exposures.