

## **SPROTT RESOURCE CORP.**

### **Management's Discussion and Analysis For the Nine Months Ended September 30, 2008**

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#### **Introduction**

Sprott Resource Corp. ("SRC" or the "Company") is a Canadian based company. The primary purpose of the Company is to invest in natural resources, through direct acquisitions, joint ventures and equity investments. The Company is listed on the Toronto Stock Exchange ("TSX") under the symbol "SCP".

The following information, prepared as of November 12, 2008, should be read in conjunction with the Company's unaudited interim consolidated financial statements for the nine months ended September 30, 2008, as well as the audited consolidated financial statements for the year ended December 31, 2007 and the related management's discussion and analysis (the "Annual MD&A") contained in the 2007 Annual Report. All amounts are expressed in Canadian dollars unless otherwise indicated and prepared in accordance with Canadian generally accepted accounting principles.

#### **Forward-Looking Statements**

Forward-looking statements look into the future and provide an opinion as to the effect of certain events and trends on the business. Forward-looking statements may include words such as "plans", "intends", "anticipates", "should", "estimates", "expects", "believes", "indicates", "suggests" and similar expressions.

This MD&A and in particular the "Outlook" section, contains forward-looking statements. These forward-looking statements are based on current expectations and various estimates, factors and assumptions and involve known and unknown risks, uncertainties and other factors.

It is important to note that:

- Unless otherwise indicated, forward-looking statements in this MD&A describe the Company's expectations as of November 12, 2008.
- Readers are cautioned not to place undue reliance on these statements as the Company's actual results, performance or achievements may differ materially from any future results, performance or achievements expressed or implied by such forward-looking statements if known or unknown risks, uncertainties or other factors affect the Company's business, or if the Company's estimates or assumptions prove inaccurate. Therefore, the Company cannot provide any assurance that forward-looking statements will materialize.
- Subject to applicable laws, the Company assumes no obligation to update or revise any forward-looking statement, whether as a result of new information, future events or any other reason.

The material assumptions that were applied in making the forward looking statements in this MD&A include: expectations as to the Company's future strategy and business plan; and execution of the Company's existing plans, which may change due to changes in the views of the Company or if new information arises which makes it prudent to change such plans.

For a description of material factors that could cause the Company's actual results to differ materially from the forward-looking statements in this MD&A, please see "Risks and Uncertainties" and "Critical Accounting Estimates".

### **Third Quarter Highlights**

Third quarter 2008 net income was \$67,154,702 (\$0.76 per basic share) versus a net loss of \$468,332 (\$0.02 per basic share) in the third quarter 2007.

Cash and cash equivalents and short term investments increased to \$155,569,013 as at September 30, 2008 from \$59,541,557 as at June 30, 2008 and \$66,308,166 as at September 30, 2007.

Net assets increased to \$370,837,562 as at September 30, 2008 from \$139,063,686 as at June 30, 2008 and \$77,560,325 as at September 30, 2007.

A total of 2,808,500 common shares purchased and cancelled under the normal course issuer bid during the third quarter 2008, with an additional 5,124,200 common shares purchased for cancellation after the end of the third quarter 2008.

### **Third Quarter Review**

#### *PBS Coals Corporation*

On September 24, 2008, the Company completed its sale of 17,050,000 shares of PBS Coals Limited ("PBS") to holders of subscription receipts of PBS Coals Corporation and an affiliate, which were issued on July 31, 2008. The Company received net proceeds of \$97,507,445 after commissions from the completion of the sale. Following the completion of the sale, pursuant to agreements with other PBS shareholders and the underwriter of the secondary offering, the Company received additional proceeds of \$2,336,334 in respect of the sale. Concurrent with this PBS sold some shares to third parties resulting in a dilution gain for the Company of \$7,801,465. The Company recognized a taxable capital gain on the sale of \$31,498,057.

On August 22, 2008, the Company signed a lock-up agreement with 7027940 Canada Limited, an affiliate of OAO Severstal (the "Offeror") pursuant to which it agreed to tender its remaining 27,144,938 PBS shares into a takeover bid (the "Offer") by the Offeror for all the issued and outstanding shares of PBS. The Offer was made at \$8.30 per PBS share.

Subsequent to the end of the quarter, on October 24, 2008, the Company, along with other principal shareholders of PBS, signed a supplemental agreement (the "Supplemental Agreement") with PBS, PBS Coals Corporation, the Offeror and Mining Holding Company LLC ("Mining Holdings" and collectively with the Offeror, the "Purchaser") pursuant to which the Purchaser (i) waived any and all breaches of each and every representation, warranty and/or covenant in the support and purchase agreement between PBS Coals Corporation, PBS, Mining Holdings, the Offeror, Mincorp Acquisition Corp. ("Mincorp") and certain shareholders of Mincorp (the "Support and Purchase Agreement"); (ii) agreed that all mutual conditions and conditions in favour of the Purchaser in the Support and Purchase Agreement had been satisfied or waived; (iii) agreed to take up all PBS shares deposited and not withdrawn under the Offer no later than November 3, 2008, (iv) agreed to pay for all PBS shares taken up in the Offer no later than November 3, 2008 (or November 5, 2008 if the Purchaser received regulatory approval); and (v) agreed to acquire all the outstanding shares of Mincorp immediately following acquisition of the PBS shares. In exchange for the foregoing, the shareholders party to the Supplemental Agreement agreed to a discount of \$381,960,000 under the Offer. The Company's portion of this discount is \$84,478,886 under the Offer. As a result, on November 6, 2008, the Company received net proceeds of \$140,824,099 on its sale of 27,144,938 PBS shares or \$5.1878 per PBS share, rather than \$225,302,985 or \$8.30 per PBS share under the terms of the Offer.

The Supplemental Agreement arose after the Purchaser had advised PBS, PBS Coals Corporation, Mincorp and certain shareholders of Mincorp that, in the Purchaser's view, certain of the representations and warranties contained in the Support and Purchase Agreement were untrue and incorrect in a material respect which, in the Purchaser's view, was likely to have a Material Adverse Effect (as defined in the Support and Purchase Agreement) on PBS Coals Corporation. The Company did not, nor does it, acknowledge or accept that there was any breach by PBS Coals Corporation of the terms of the Support and Purchase Agreement. However, the Company was of the view that there was a significant risk that the Purchaser would not take up and pay for the PBS shares deposited under the Offer without the Company and other principal shareholders agreeing to enter into the Supplemental Agreement. As a result, following negotiations between the Company (and other principal shareholders) and the Purchaser, in order to ensure that the Purchaser would take up and pay for the PBS shares deposited under the Offer, and in an effort to avoid litigation with the Purchaser, the Company entered into the Supplemental Agreement. A copy of the Supplemental Agreement can be obtained from SEDAR ([www.sedar.com](http://www.sedar.com)).

#### *Mantaro Phosphate Project*

On August 18, 2008, a wholly-owned subsidiary of the Company ("Holdco"), which indirectly owns the mineral licences relating to the Mantaro Phosphate Project, completed its amalgamation with Stonegate Minerals Ltd. The amalgamated company is called Stonegate Agricom Ltd. The principals of Stonegate Minerals Ltd. will manage Stonegate Agricom Ltd. and will work on advancing the Mantaro Phosphate Project.

The Company owns 60,000,000 (78.95 percent) of Stonegate Agricom Ltd. Stonegate Agricom Ltd. has 13,999,976 share purchase warrants outstanding exercisable at \$0.75 per common share, none of which the company owns. As at September 30, 2008, Stonegate Agricom had working capital of \$5,712,236.

The Company signed a voting agreement with Stonegate Agricom Ltd. pursuant to which it agreed to vote all of its voting shares in favour of each nominee to the board of directors proposed by Stonegate Agricom Ltd.'s management for a period of three (3) years from the completion of an initial public offering of Stonegate Agricom Ltd., subject to certain conditions including that the board of directors include one representative of the Company. Accordingly, for accounting purposes Stonegate Agricom Ltd. is treated as an equity investment.

On August 29, 2008, the Company filed a National Instrument 43-101 compliant technical report in respect of the Mantaro Phosphate Project (the "43-101 Report"). A copy of the report can be obtained from SEDAR ([www.sedar.com](http://www.sedar.com)).

At this stage, work in respect of the Mantaro Phosphate Project is focused on engaging in consultations with local residents at and near the location of the mineral claims with a view to obtaining the necessary community agreements required to further explore the property. The work recommended to advance the project is outlined in the 43-101 Report.

#### *Normal Course Issuer Bid*

On August 26, 2008, the Company announced a normal course issuer bid (the "NCIB") to repurchase up to 8 million of its common shares. This figure is slightly less than 10 percent of the public float as at August 22, 2008 (80,690,324). The total issued and outstanding as at August 22, 2008 was 89,777,224.

The NCIB may not extend beyond August 28, 2009, which is one year after August 29, 2008, the date on which purchases were first permissible under the NCIB. All purchases by the Company under the NCIB have been and will be made under the facilities of the TSX; the purchase and payment for the common shares has been and will be made by the Company in accordance with the requirements of the TSX; the price that the Company will pay for common shares acquired by it has been and will be the market price of the common shares at the time of acquisition; and all purchases

have been and will be made by means of open market transactions during the period the NCIB is outstanding.

Pursuant to TSX policies, daily purchases made by the Company may not exceed 156,994 common shares, which is 25% of the six-month average daily trading volume of common shares on the TSX as at August 22, 2008.

The Company initiated the NCIB because it believed that its common shares had been trading in a price range that did not adequately reflect their value in relation to the Company's assets and future prospects. The Company believes that the repurchase for cancellation of its common shares through the NCIB, at appropriate times, can enhance shareholder value and constitutes an attractive investment and an appropriate use of financial resources.

To the knowledge of the Company, no director or officer, no person acting jointly or in concert with SRC and no person holding more than 10 percent or more of the common shares intended to sell common shares during the course of the NCIB at the time the NCIB was announced.

To date, the Company has purchased for cancellation 7,932,700 common shares. The average price paid for each common share purchased under the NCIB to date is \$2.454 per common share. The Company has nearly completed its total allowable purchase of 8 million shares under the NCIB. The Company intends to complete the remaining purchases within the next few days.

#### *Waseca Energy Inc.*

Subsequent to the end of quarter, the Company purchased 45,289,000 common shares of Waseca Energy Inc. ("Waseca") for \$27,173,400 (\$0.60 per common share), as part of a larger private placement of 52,199,589 common shares completed by Waseca. The Company owns 79.72 percent of the outstanding common shares of Waseca.

Waseca is a private oil and gas company whose primary focus will be heavy oil production from the Lloydminster area on the boarder of central Alberta and Saskatchewan. Waseca currently owns four (4) prospective petroleum and natural gas leases and intends to begin drilling in the fourth quarter of 2008 on such leases.

## **Results of Operations**

### *Nine month results*

During the nine months ended September 30, 2008, the Company reported net earnings of \$73,837,737 (\$1.13 per basic share) compared to net earnings of \$707,580 (\$0.05 per basic share) reported in the same period of 2007.

The 2008 earnings include \$77,747,940 from the gain on the sale of investments, \$11,580,825 resulting from the gain on dilution from investments, and \$11,163,543 resulting from the equity pick-up of PBS Coals Corporation.

General and administrative expenses increased from \$1,307,775 to \$22,329,510. The increase is due mainly to incurring management fees of \$2,236,999 (2007 - \$112,700) and management incentive fees of \$18,212,927 (2007 - \$nil) under the terms of the management services agreement (the "MSA") with Sprott Consulting Limited Partnership ("SCLP").

Significant expense items also include: professional fees for accounting, legal and tax services of \$551,434 (2007 - \$317,592); consulting fees of \$189,747 (2007 - \$126,378); wages and benefits decreased to \$133,123 (2007 - \$152,714); and office and miscellaneous expenses of \$599,886 (2007 - \$154,796).

An income tax expense of \$4,994,448 (2007 - \$nil) was incurred mainly to the gain on the sale of investments recognized during the period. A future income tax liability of \$31,498,057 was allocated to the net unrealized gains on available for sale investments.

Expenses were offset by \$896,545 (2007 - \$545,713) in interest income earned on the Company's surplus cash balance.

### *Three month results*

During the three months ended September 30, 2008, the Company reported net earnings of \$67,154,702 (\$0.76 per basic share) compared to a loss of \$468,332 (\$0.02 per basic share) incurred in the third quarter of 2007. The earnings include \$74,574,666 (2007 - \$nil) from the gain on the sale of investments, \$11,212,948 (2007 - \$nil) resulting from the gain on dilution from investments, and \$6,083,158 (2007 - \$nil) resulting from the equity pick-up of PBS Coals Corporation.

General and administrative expenses increased from \$647,318 to \$20,009,863, with the increase being attributable primarily to the management fees of \$1,258,676 (2007 - \$112,700) and management incentive fees of \$17,429,777 (2007 - \$nil), respectively, both payable to SCLP.

Significant expense items also include professional fees for accounting, legal and tax services, which were \$320,114 (2007 - \$90,694). The increase in professional fees is attributable to greater transactional activity. Consulting fees of \$124,275 (2007 - \$41,146), and office and miscellaneous, which were \$489,274 (2007 - \$55,006).

An income tax expense of \$4,994,448 (2007 - \$nil) was incurred mainly to the gain on the sale of investments recognized during the period.

Expenses were offset by \$454,160 (2007 - \$396,880) in interest income earned on the Company's surplus cash balance.

### *PBS Coals Corporation Investment*

Up to September 24, 2008, PBS was an equity investee of the Company. Up to that date, the Company's investment in PBS was accounted for using the equity method. As at September 24, 2008, (the date of the first sale of PBS shares), the summarized assets, liabilities and results of operations of PBS are as follows:

	<i>(thousands of U.S.dollars)</i>
Total current assets	117,210
Total non-current assets	<u>581,157</u>
Total assets	<u>698,367</u>
Total current liabilities	45,188
Total non-current liabilities	358,990
Non-controlling interest	<u>19,827</u>
	424,005
Share capital	236,926
Retained earnings	<u>37,436</u>
Total liabilities and equity	<u>698,367</u>

Revenue	223,760
Expenses	(192,374)
Non-controlling interest	<u>(2,006)</u>
Net earnings for equity accounting purposes	<u>29,380</u>

On September 24, 2008, the Company's interest in PBS was reduced to below 20% and, as a result, the Company no longer accounts for its investment in PBS using the equity method. As of September 24, 2008, the Company's holdings in PBS are classified as available-for-sale.

### Summary of Quarterly Results (unaudited)

	September 30, 2008	June 30, 2008	March 31, 2008	Dec. 31, 2007	Sept. 30, 2007	June 30, 2007	March 31, 2007	Dec. 31, 2006
Total Revenues	\$nil	\$nil	\$nil	\$nil	\$nil	\$nil	\$nil	\$nil
Deferred exploration expenditures	\$197,549	\$13,269,052	\$356,712	\$147,141	\$200,553	\$241,342	\$251,822	\$231,353
Net earnings (loss)	\$67,154,702	\$6,959,243	(\$276,208)	\$1,302,769	(\$468,332)	(\$626,764)	\$1,802,676	\$292,800
Net earnings (loss) per share basic	\$0.76	\$0.13	(\$0.01)	\$0.03	(\$0.02)	(\$0.07)	\$0.19	\$0.03

The net earnings for the quarter ended September 30, 2008 included a gain on the sale of investments of \$74,574,666, resulting predominately from the sale of PBS shares, and \$11,212,948 resulting from the dilution gains. The net earnings for the quarter ended June 30, 2008 included a \$3,173,274 gain from the sale of investments and \$4,988,385 equity earnings of PBS. The net earnings for the quarter ended December 31, 2007 included a foreign exchange gain of \$1,510,550 resulting in part from the strengthening of the U.S. dollar over the period immediately prior to the closing of the Company's investment in PBS. The net earnings for the quarter ended March 31, 2007 included a \$2,101,743 dilution gain on the Company's investment in South American Silver Corporation. The net earnings for the quarter ended December 31, 2006 included a \$1,057,012 gain on the disposal of certain investments, and was offset by a write down of the carrying value of the Company's mineral properties amounting to \$411,669.

### Liquidity and Capital Resources

The Company's aggregate operating, investing and financing activities during the nine month period resulted in a net cash inflow of \$72,968,258. As at September 30, 2008, the Company had cash and cash equivalents and short term investments of \$155.6 million (December 31, 2007 - \$34.1 million), and working capital of \$131.1 million (December 31, 2007 - \$33.6 million). Cash equivalents and short term investments comprise Government of Canada treasury bills.

In addition, the Company held a portfolio of investments with a fair value of \$258,172,446. These investments include \$241,082,438 in publicly traded securities and \$17,090,008 of equities in private companies. Private company securities are less liquid than public company securities. If the Company were required to liquidate its private company securities, it may not receive proceeds equal to the fair value of such securities. However, the Company is well capitalized and does not anticipate the need to sell such securities in order to raise liquidity.

## **Capital Expenditures**

### *Purchases of Securities*

During the quarter, the Company purchased \$39,005,199 (2007 - \$1,000,000) of securities, of which \$23,165,199 (2007 - \$nil) were public securities and \$15,840,000 (2007 - \$1,000,000) were private securities. Of the public securities, \$9,670,200 was purchases of exchange traded funds that track the performance of gold and silver bullion. The Company intends to replace such securities in the fourth quarter with gold and silver bullion. Management believes that gold and silver bullion will strengthen over time as government deficits increase in size and low-yielding government debt becomes relatively unattractive.

### *Deferred Exploration Costs*

Deferred exploration costs incurred by the Company in the nine months ended September 30, 2008 were \$585,543 (2007 - \$1,995,694). The costs relate to the Appleton Linear Project.

## **Financing Activities**

During the third quarter, the Company received \$43,275,294 from the exercise of 17,313,454 share purchase warrants. On May 13, 2008, the Company announced a warrant incentive program (the "Warrant Incentive Program") to encourage the early exercise of 39,920,000 outstanding warrants that expire September 5, 2009 (the "Old Warrants"), which were issued as part of the financing completed in September 2007. The Warrant Incentive Program expired on July 7, 2008. The Old Warrants are exercisable at \$2.50 per share. Warrant holders who elected to exercise their Old Warrants as part of the Warrant Incentive Program received a bonus one-half of one new common share purchase warrant (a "New Warrant"), which is exercisable for one common share of the Company at a price of \$4.25 until December 31, 2010, subject to the Company's ability to accelerate the expiry of the New Warrants if the trading price of the Company's common shares is equal to or greater than \$6.00 for twenty (20) consecutive trading days. There were 30,000 share purchase warrants and 7,500 options exercised during the comparative quarter for proceeds of \$71,125.

During the nine months period ended September 30, 2008, the Company received \$91,971,354 from the exercise of share purchase warrants and \$669,700 from the exercise of stock options. As at September 30, 2008, 33,188,568 of the Old Warrants were exercised under the Warrant Incentive Program for total proceeds of \$82,971,420 and consequently 16,594,284 New Warrants were issued. During the nine months period ended September 30, 2007 last year the Company received \$2,140,963 from the exercise share purchase warrants and stock options.

## **Off-Balance Sheet Arrangements**

The Company has not entered into any material off-balance sheet arrangements such as guarantee contracts, contingent interests in assets transferred to unconsolidated entities, derivative financial obligations, or with respect to any obligations under a variable interest equity arrangement.

## **Transactions with Related Parties**

### *MSA with SCLP*

The Company is party to the MSA with SCLP, an entity with directors and management in common. The MSA has an initial term of three years to September 2010. Pursuant to the terms of the MSA, SCLP through its predecessor was appointed by the Company to manage, or engage others to manage, the undertaking and affairs of the Company. In consideration for providing these services, the Company has agreed to pay SCLP an annual services fee equal to 2% of the net asset value (as defined in the MSA) of the Company calculated and payable at the end of each calendar quarter based on the average month-end net asset value of the Company and an annual incentive

fee (the "Incentive Fee") equal to 20% of: (a) the pre-tax profits of the Company for the year minus (b) the average month-end net asset value of the Company for the year multiplied by the percentage return of the Canadian 30-Year Generic Bond Index.

During the three months ended September 30, 2008, management fees of \$1,258,676 (September 30, 2007 - \$112,700) were incurred, which are payable to SCLP under the MSA. The amount accrued for management incentive fees to the three months is \$17,429,777 (September 30, 2007 - \$nil). During the nine months ended September 30, 2008, management fees of \$2,236,999 (September 30, 2007 - \$112,700) were incurred, which are payable to SCLP under the MSA. The amount for management incentive fees to the nine months is \$18,212,927 (September 30, 2007 - \$nil).

#### *Other Transactions with Related Parties*

Related party transactions not disclosed elsewhere in these consolidated financial statements are as follows:

During the three months ended September 30, 2008:

- Aggregate legal fees of \$nil (September 30, 2007 - \$312,428) were charged by a legal firm in which a former director was a partner.
- Consulting fees of \$30,208 (September 30, 2007 - \$40,023) were charged by officers or former officers of the Company. Of this amount \$30,208 was charged to loss (September 30, 2007- \$20,155), \$nil was included in deferred costs (September 30, 2007 - \$19,868).

During the nine months ended September 30, 2008:

- Aggregate legal fees of \$nil (September 30, 2007 - \$474,051) were charged by a legal firm in which a former director was a partner.
- Consulting fees of \$42,332 (September 30, 2007 - \$131,283) were charged by officers or former officers of the Company. Of this amount \$42,332 was charged to loss (September 30, 2007- \$82,475), \$nil was included in deferred costs (September 30, 2007 - \$48,808).
- Included in accounts payable and accrued liabilities as at September 30, 2008 was \$19,503,853 (December 31, 2007 - \$417,606) payable to directors and officers of the Company, including \$19,471,603 (December 31, 2007 - \$392,406) payable to SCLP. These amounts are non-interest bearing and have no specific terms of repayment.

Transactions with related parties are recorded at the exchange amount, being the price agreed between the parties.

#### **Critical Accounting Estimates**

The accounting estimates considered to be significant to the Company include the valuation of investments, the carrying value of mining claims and deferred exploration, the computation of stock-based compensation expense, and the valuation of warrants.

The Company's investments in available-for-sale securities having quoted market values and which are publicly traded or can be converted into publicly traded securities are recorded on the basis of period-end market bid quotations.

The Company's investments in available for sale securities which are not publicly traded or cannot be converted into publicly traded securities are recorded at cost and are adjusted downwards by the Company if circumstances, such as a subsequent known transaction, warrant a revaluation of the holding to reflect its fair market value. During the quarter ended September 30, 2008 a 50% impairment on a privately held uranium investment was incurred to reflect declining market conditions in uranium equities and a decline in the price of uranium, the underlying commodity.

Management reviews the carrying values of its mining claims on a quarterly basis to determine whether an impairment should be recognized. In addition, capitalized costs related to abandoned properties are written off in the period of abandonment. Capitalized costs in respect of the Company's mining claims amounted to \$585,543 as at September 30, 2008. These costs may not be recoverable and there is a risk that these costs may be written down in future quarters.

The Company uses the fair-value method of accounting for share purchase warrants and stock-based compensation related to incentive stock options and share purchase warrants granted, modified or settled. Under this method, compensation cost attributable to all share purchase warrants and incentive stock options granted are measured at fair value at the grant date and for incentive stock options are expensed over the vesting period with a corresponding increase to contributed surplus. In determining the fair value, the Company makes estimates of the expected volatility of the stock as well as an estimated discount rate. Changes to these estimates could result in the fair value of the share purchase warrants and stock-based compensation being less than or greater than the amount recorded. During the first nine months of 2008, the Company recorded stock-based compensation expense of \$nil (2007 - \$nil).

The determination of the Company's income and other tax liabilities involves the interpretation of complex laws and regulations and the exercise of judgment. The Company's provision for income taxes represents management's interpretation of such laws and regulations and its estimate at the time of the current and future income tax implications of transactions and events affecting the Company. However, all tax filings are subject to potential audit and reassessment. As such, the actual tax expense or liability can differ from the amount estimated and recorded or the amount originally estimated and recorded may be subsequently adjusted, and the difference can be material. An adjustment to the Company's provision for income taxes could have a material impact on the Company's financial position.

## **Recent accounting pronouncement**

### *Future accounting and reporting changes*

The CICA issued the new Handbook Section 3064, "Goodwill and Intangible Assets", which will replace Section 3062, "Goodwill and Other Intangible Assets". The new standard establishes revised standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. The new standard also provides guidance for the treatment of preproduction and start-up costs and requires that these costs be expensed as incurred. The new standard applies to annual and interim financial statements relating to fiscal years beginning on or after October 1, 2008. Management is currently assessing the impact of these new accounting standards on its consolidated financial statements.

### *International Financial Reporting Standards ("IFRS")*

In 2006, the Canadian Accounting Standards Board ("AcSB") published a new strategic plan that will significantly affect financial reporting requirements for Canadian companies. The AcSB strategic plan outlines the convergence of Canadian GAAP with IFRS over an expected five year transitional period. In February 2008 the AcSB announced that 2011 is the changeover date for publicly-listed companies to use IFRS, replacing Canada's own GAAP. The date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. The transition date of January 1, 2011 will require the restatement for comparative purposes of amounts reported by the Company for the year ended December 31, 2010. While the Company has begun

assessing the adoption of IFRS for 2011, the financial reporting impact of the transition to IFRS cannot be reasonably estimated at this time.

### **Changes in Accounting Policies including Initial Adoption**

During the quarter, the Company adopted a short-term investment accounting policy. Short-term investments are liquid Canadian dollar denominated investments in Government of Canada treasury bills with terms to maturity of greater than 90 days but not more than one year. Short-term investments are classified as held-for-trading and recorded at fair value with realized and unrealized gains and losses reported in the statement of operations.

On January 1, 2008, the Company adopted the following new accounting standards issued by the Canadian Institute of Chartered Accountants (“CICA”); Section 1535 “Capital Disclosures”, Section 3862 “Financial Instruments – Disclosures” and Section 3863 “Financial Instruments – Presentation”. These new requirements of Sections 1535, 3862 and 3863 are for disclosure purposes only and have not impacted the financial results of the Company.

#### *Capital disclosures – section 1535*

Section 1535 specifies the disclosure of (i) an entity’s objectives, policies, and processes for managing capital; (ii) quantitative data about what the entity regards as capital; (iii) whether the entity has complied with any capital requirements; and (iv) if it has not complied, the consequences of such non-compliance.

#### *Financial instruments – sections 3862 and 3863*

The new Sections 3862 and 3863 replace Section 3861, “Financial Instruments – Disclosure and Presentation”, revising and enhancing its disclosure requirements, and carrying forward unchanged its presentation requirements. The new sections place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how a company manages those risks.

### **Financial Instruments**

#### Fair value of financial instruments

The Company’s financial instruments consist of cash and cash equivalents, short term investments, note receivable, promissory notes receivable, investments and accounts payable and accrued liabilities. Cash equivalents and short term investments consist of highly liquid investments held in the form of Government of Canada treasury bills, the investment terms of which are less than 90 days at the time of acquisition, and are all held in Canadian dollars. The Company has no asset backed commercial paper. Portfolio investments in securities of publicly-traded companies are reported at fair value. The fair values of the other instruments approximate their book value due to their short-term nature.

#### Currency risk

The Company is exposed to the financial risk related to the fluctuation of foreign exchange rates. The Company operates in Canada, the United States and Peru and a portion of its expenses are incurred in U.S. dollars. The Company does not hedge its exposure to fluctuations in the exchange rate. Future changes in exchange rates could have a material effect on the Company’s business, financial condition and results of operations.

Certain of the Company’s financial instruments are exposed to fluctuations in the U.S. dollar. A hypothetical change of 10% to the foreign exchange rate between the U.S. dollar and the

Canadian dollar applied to the average level of U.S. denominated cash and cash equivalents during the quarter would result in a decrease of \$35,325 to the Company's earnings for the nine month period ended September 30, 2008.

#### Credit risk

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its commercial obligations.

The Company's cash is held primarily through large Canadian financial institutions. Short-term investments consist of Government of Canada treasury bills, which have an original maturity of 90 days or less from the date of purchase and are readily convertible into a known amount of cash.

#### Market risk

Market risk is the risk that changes in market prices, such as interest rates and equity prices, will affect the Company's operations or the value of its financial instruments. The Company will generate a portion of its revenue from the proceeds of disposition from its equity investments in natural resource companies. The values of such investments are subject to general market risks and all the risks specific to natural resource companies. If the value of these investments declines, as a result of company specific issues or market conditions generally, the Company will not be able to generate income and may suffer capital losses.

The Company manages its cash according to its operational needs and to optimize revenues from interest.

#### Liquidity risk

The Company manages liquidity risk by maintaining sufficient cash and cash equivalents balances to enable settlement of transactions on the due date.

The Company invests in securities of private companies. In some cases, the Company may be restricted by contract or by applicable securities laws from selling such securities for a period of time. The inability to sell such securities may impair the Company's ability to exit such investments when the Company considers it appropriate.

#### Interest rate risk

The Company is exposed to minimal interest rate risk on its short term investments with terms of maturity within one year.

## Outstanding Share Data

Authorized Capital:

Common shares, no par value, unlimited shares

Issued and outstanding:

83,690,924 common shares as at November 12, 2008.

Outstanding options, warrants, and convertible securities as at November 12, 2008:

Type of Security	Number	Exercise Price	Expiry date
Share purchase warrants	3,855,430	\$2.50	September 5, 2009
Share purchase warrants	16,594,284	\$4.25	December 31, 2010 (1)
Stock options	90,000	\$1.30	August 6, 2009
Stock options	100,000	\$1.75	June 9, 2010
Stock options	75,000	\$3.32	August 26, 2013

(1) The expiry date of these warrants may be accelerated by the Company if the Company's share price closes at or above \$6.00 per share for twenty (20) consecutive trading days.

## Risks and Uncertainties

Investments in commodities and companies, which explore for and/or produce commodities, are substantial. The Company will attempt to mitigate such risk by maintaining a diversified portfolio of assets. Management will also attempt to balance such risk through joint ventures and option agreements with other companies. Beyond such risk, management is faced with a number of other risk factors as detailed in the Annual MD&A.

## Internal Control over Financial Reporting

As at the date of this report, management is not aware of any change in the Company's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## Outlook

The price of commodities and the share prices of companies involved in the exploration and production of commodities experienced large declines during the third quarter and subsequent to the third quarter. The ongoing credit crisis, evidently deteriorating economic fundamentals and forced sales resulting from redemptions of mutual funds and hedge funds, among other reasons, may result in additional price deterioration. Due to this uncertainty, and the increased risk relating to the credit and equity markets, the Company has been and will continue to be cautious in making additional investments. Cash is extremely valuable in the current economic environment.

The Company believes that there will be attractive investment opportunities resulting from the recent price declines and inability of exploration companies and producing companies to secure credit or equity financing. As a result of the timely disposition of its PBS shares for substantial proceeds, the Company is uniquely positioned to take advantage of these circumstances.

Stonegate Agricom Ltd. and Waseca, will work on developing the Mantaro Phosphate Project and on exploring existing oil and gas leases and acquiring additional oil and gas leases for exploration and development, respectively. Both are well capitalized to meet their near term goals and do not need to raise additional funds at this time.

Both companies have strong management teams. The Company intends to work closely with each company to explore possible business opportunities in each company's respective area.

**Other Information**

Additional information related to the Company is available for viewing on SEDAR at [www.sedar.com](http://www.sedar.com) and at the Company's website at [www.sprottresource.com](http://www.sprottresource.com).