Gammon Gold Inc.

Amended Management's Discussion and Analysis

For the year ended December 31, 2008

This amended and restated Management's Discussion and Analysis ("MD&A"), dated August 12, 2009, relates to the financial condition and results of operations of Gammon Gold Inc. ("the Company") together with its wholly owned subsidiaries, and should be read in conjunction with the Company's amended and restated consolidated financial statements for the year ended December 31, 2008, and notes thereto. Details of the restatement are provided in note 2 to the December 31, 2008 restated consolidated financial statements. The amended and restated consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). All results are presented in United States dollars, unless otherwise stated. Statements are subject to the risks and uncertainties identified in the Forward-Looking Statements portion of this document. The first, second, third and fourth quarters of the Company's fiscal year are referred to as "Q1", "Q2", "Q3" and "Q4", respectively.

AMENDMENT AND RESTATEMENT MADE AUGUST 12, 2009

During the preparation of the June 30, 2009 interim financial statements, the Company determined that certain items in the December 31, 2008 consolidated financial statements had been incorrectly translated into the Company's functional currency, the United States dollar. In the Company's Mexican operations, inventory is initially recorded in Mexican pesos. When translating these balances to the US dollar, the Company used the current exchange rate instead of the rate in effect when the costs were incurred. The impact of this adjustment was to change the inventory balances and production costs in each period. For the year ended December 31, 2008, the effect of the above was to increase inventories by $9.3 million, increase production costs by $0.6 million, reduce amortization and depletion by $0.3 million, and increase foreign exchange gains by $9.6 million. Net earnings increased by $9.3 million and basic and diluted net earnings per share increased from $0.25 and $0.25 to $0.34 and $0.33 per share respectively. There was no income tax effect as a result of this adjustment. There was no material impact of these changes on the opening deficit or accumulated other comprehensive income or on amounts reported prior to 2008.

In addition, the Company determined that upon initial adoption of Section 3031, *Inventories*, on January 1, 2008, a reversal should have been recorded for previously recognized net realizable value adjustments. Section 3031, *Inventories*, requires that when the net realizable value of inventory increases, previously recorded adjustments to reduce inventory to its net realizable value are reversed. On implementation of this section on January 1, 2008 the Company did not identify that there were previous net realizable value adjustments that were required to be reversed. The effect of this restatement is to increase inventories by $1.6 million at January 1, 2008, with a $1.1 million decrease to deficit and a $0.5 million increase to future income tax liabilities.

As a result, the Company incorrectly presented the consolidated balance sheet as at December 31, 2008, and the consolidated statements of operations and comprehensive income / (loss), cash flows and shareholders' equity for the year ended December 31, 2008, and is correcting such presentation in the amended and restated consolidated financial statements. Further information on these adjustments and a reconciliation of amounts previously reported is contained in note 2 of the Company's amended and restated consolidated financial statements for the year ended December 31, 2008.

For the convenience of the reader, this 2008 MD&A sets forth the amended MD&A in its entirety. The Company has not modified or updated the disclosure presented in this MD&A, except as required to reflect the effects of the restatement discussed above. Accordingly, this 2008 MD&A does not reflect events occurring after the original filing, or modify or update those disclosures affected by subsequent events. The Company has not amended and does not intend to amend any of its previously filed Quarterly Reports for the quarterly periods ended March 31, 2008, June 30, 2008, September 30, 2008 and March 31, 2009. Accordingly, this 2008 MD&A should be read in conjunction with the Company's filings subsequent to the original filing.

The Company's Chief Executive Officer and Chief Financial Officer have reissued the certifications required by National Instrument 52-109 and Section 302 of the Sarbanes Oxley Act.

OVERVIEW OF THE BUSINESS

Gammon Gold Inc. is a publicly traded gold and silver producer engaged in the mining, development, exploration and acquisition of resource properties. The Company owns and operates two producing mines in Mexico, the Ocampo mine in Chihuahua State, and the El Cubo mine in Guanajuato State, and also owns the Guadalupe y Calvo advanced exploration property in Chihuahua State, Mexico. The Company's common shares are listed on the Toronto Stock Exchange (TSX: GAM) and the New York Stock Exchange (NYSE: GRS). Further details on Gammon Gold Inc. can be found in the Company's associated documents, including its Annual Information Form, at www.sedar.com or on the Company's website at www.gammongold.com.

In 2008, the global economy was turbulent, experiencing all-time highs and all-time lows. Like many corporations worldwide, the Company experienced challenges in the second half of 2008 as a result of the significant economic downturn and financial uncertainty that followed the decrease in bank liquidity and resulting credit crisis. With the expectation of a continuing downturn in 2009, the Company could continue to face challenges, such as volatility in commodity prices which directly impacts the Company's revenues and cash flows, higher costs and reduced availability of funding, and currency devaluations. In response to these conditions, the Company has undertaken a number of initiatives to contain costs, and prioritize and delay capital expenditures.

Despite the significant economic downturn experienced in the second half of 2008, the price of gold remained relatively strong throughout most of the year, with an average closing price of $871 per ounce, a 25% increase over the average closing price in 2007. In 2008, the Company sold 24% more gold ounces and realized an average selling price of $864 per ounce, a 24% increase over 2007's realized average selling price of $699 per ounce. Although the price of gold declined significantly in second half of the year, in late December it began to rebound, closing the year at $870. Subsequent to year end, the gold price has further increased, trading well in excess of $900 per ounce, as investors seek refuge in gold in the face of economic uncertainty.

Silver traded in the range of $8.88 to $20.92 per ounce during 2008, an almost unprecedented $12.04 per ounce annual range. The closing price of $14.99 represented a 12% increase over the prior year. However, during the last half of the year silver prices declined significantly and underperformed the gold price. The price of silver has improved moderately in 2009, as investors have also begun to seek refuge in silver in the face of economic uncertainty.

As a result of the significant decline in the price of silver, the gold-to-silver ratio increased from 53:1 during the first six months of the year to 79:1 in the fourth quarter, reducing the silver contribution to the Company's gold equivalent ounces produced by approximately 13,000 ounces. Therefore, as a result of the volatility in the gold equivalent ratio during 2008, when making annual and quarterly comparisons, the reader should focus on actual gold and silver production and sales.

OUTLOOK

The Company is providing the following guidance for fiscal 2009 (assuming a gold-to-silver ratio of 78:1):

- Gold production of 185,000 – 205,000 ounces;
- Silver production of 8,170,000 – 8,945,000 ounces;
- Gold equivalent production of 290,000 – 320,000 ounces; and
- Total cash costs per gold equivalent ounce of $410 – 445(1).

(1) *The Company has included a non-GAAP performance measure, total cash cost per gold equivalent ounce, throughout this document. For further information, see the Non-GAAP Measures section on page 19.*

In an effort to preserve working capital in the current environment of commodity price volatility, the Company has temporarily deferred work at the Guadalupe y Calvo advanced exploration development project. As part of the scoping study for this project that was scheduled for completion in Q1 2009, the Company completed 126 holes for 38,399 metres in 2008, bringing the project total drilling to 183 holes for 52,075 metres. Further drilling and engineering work required to complete the scoping study has been temporarily postponed. The Company will re-evaluate this decision once the backlog of core logging and assays is eliminated and the metallurgical column testwork has been completed in Q2 2009.

2008 HIGHLIGHTS

The Company's turn-around strategy implemented in December 2007 resulted in a year of unprecedented success, including:

- Net earnings and net earnings per share of $40.0 million and $0.34 respectively, versus a net loss and net loss per share of $101.3 million and $0.90 respectively, in 2007, representing an improvement of 139% year over year.
- Total production of 154,428 gold ounces and 5,778,874 silver ounces, or 251,510 gold equivalent ounces, at a cash cost per gold equivalent ounce of $528. In 2007, the Company produced 121,387 gold ounces, 5,035,704 silver ounces, or 218,734 gold equivalent ounces, at a cash cost per gold equivalent ounce of $670, an improvement of 27% and 15% on gold and silver production respectively and 21% on cash cost per gold equivalent ounce.
- Revenue from mining operations increased 39.7% to $212.5 million compared to $152.1 million in 2007, reflecting increased production and an average gold selling price of $864 per ounce and silver selling price of $14.66 per ounce, versus average selling prices of $699 and $13.42 per ounce of gold and silver respectively, in 2007.
- Cash flow from operations increased by $90.1 million, or 264%, to a positive $55.9 million, compared to a negative $34.2 million in 2007.

- Net free cash flow(2) of negative $10.9 million was an improvement year over year of $92.4 million, or 89%, compared to negative net free cash flow of $103.3 million in 2007. In the first quarter of 2009, the Company has generated positive net free cash flow and has accumulated a cash balance of $19.6 million at March 20, 2009.
- During the second half of 2008, the Company completed Phase I of the Ocampo mill expansion (averaging 2,321 TPD during the first month of commissioning in December 2008), which increases the mill capacity to 2,400 to 2,600 tonnes per day (TPD). Phase II construction of the mill expansion commenced in October 2008, and has expanded the mill capacity by an additional 10-15% in Q1 2009.
- In Q3, the Company launched an 18-month, $26 to $29 million exploration program.
- On October 14, 2008 the Company began trading on the New York Stock Exchange under the trading symbol "GRS".
- The Company ended the year with a balance outstanding on its credit facility at essentially the same level as at the end of January 2008, when the turn-around strategy started to take root and the new executive team was in place.
- On November 28, 2008, the Company's credit facility was restructured and extended. The existing $60 million revolving credit facility was converted to a $30 million non-revolving term facility that will be repaid in scheduled installments over a 19 month period, and a $20 million revolving term credit facility that expires on November 27, 2009.
- During the year, a settlement agreement was reached related to a $12.4 million claim brought against the Company by Midas Fund Inc. Midas agreed to dismiss the claim in exchange for a $200,000 cash payment by the Company. The settlement did not constitute an admission of liability by the Company or the other defendants.
- During the year, the $13 million claim brought against an inactive subsidiary of the Company, initiated by Mr. Rafael Villagomez, a former 50% owner of the shares of El Cubo, was dismissed by the courts of the State of Guanajuato, Mexico.

(2) *The Company has included a non-GAAP performance measure, net free cash flow, throughout this document. For further information, see the Non-GAAP Measures section on page 19.*

GROWTH STRATEGY

Gammon Gold Inc. is committed to responsibly operating and organically growing a precious metals company while balancing the needs of its stakeholders. The Company's growth strategy is to increase its production profile organically, reduce cash costs and increase its reserve base through a number of initiatives as follows:

- Expansion opportunities at the Ocampo Open Pit mine, Ocampo Underground mine and El Cubo Underground mine;
- Additional engineering studies at Ocampo indicate the potential for additional expansion opportunities beyond the 2009 capital expansion program;
- The recently expanded exploration program which was announced in Q2 is designed to increase resources, convert resources in 2009 and increase the Company's production profile; and
- Actively pursuing selective acquisitions in North America.

These growth initiatives are expected to be supported by the significant improvement in the Company's cash flow performance that, together with the Company's existing financing facility and working capital position, should be more than sufficient to fully fund the 2009 capital expansion programs. As previously noted, the Company has temporarily deferred work at the Guadalupe y Calvo advanced exploration development project to maximize company-wide cash flow generation, due to the current economic and metal price environment.

SUMMARIZED ANNUAL FINANCIAL AND OPERATING RESULTS

(in thousands, except ounces, per share amounts, average realized prices and total cash costs)

	YEAR ENDED		
	DECEMBER 31, 2008 (as restated)	DECEMBER 31, 2007	DECEMBER 31, 2006
Gold ounces sold	150,646	121,107	67,477
Silver ounces sold	5,606,539	5,027,983	1,888,324
Gold equivalent ounces sold(1)	245,028	218,200	105,181
Gold equivalency rate	59	52	50
Gold ounces produced	154,428	121,387	67,477
Silver ounces produced	5,778,874	5,035,704	1,888,324
Gold equivalent ounces produced(1)	251,510	218,734	105,181
Revenue from mining operations	$212,522	$152,059	$64,236
Production costs, excluding amortization and depletion	$127,651	$144,623	$37,944
Net earnings / (loss)	$39,994	($101,314)	($25,308)
Net earnings / (loss) per share	$0.34	($0.90)	($0.29)
Net earnings / (loss) per share, diluted(2)	$0.33	($0.90)	($0.29)
Cash flows from / (used in) operations	$55,933	($34,192)	($20,026)
Net free cash flow(3)	($10,908)	($103,334)	($123,349)
Total assets	$795,178	$753,952	$716,321
Total long-term financial liabilities	$12,668	$1,334	$63,608
Total cash costs per gold equivalent ounce(3)	$528	$670	$366
Total cash costs per gold ounce(3)	$313	$649	$195
Average realized gold price per ounce	$863.58	$698.91	$606.99
Average realized silver price per ounce	$14.66	$13.42	$12.18
Cash dividends declared	$Nil	$Nil	$Nil

(1) *Gold equivalent ounces include silver ounces produced and sold converted to a gold equivalent based on the ratio of the actual realized sales prices of the commodities.*
(2) *Net loss per share on a diluted basis is the same as net loss per share on an undiluted basis in 2007 and 2006, as all factors were anti-dilutive.*
(3) *See the Non-GAAP Measures section on page 19.*

REVIEW OF ANNUAL FINANCIAL RESULTS

For Gammon Gold, 2008 was a year focused on the execution of the Company's turn-around strategy that was launched late in the fourth quarter of 2007. This strategy included several cost reduction and productivity improvement initiatives aimed at increasing the production and reducing total cash costs per gold equivalent ounce at both mine sites. In addition, the Company continued to make strategic capital investments to expand production capacities at the Ocampo mine.

During 2008, the Company sold 150,646 gold ounces, 5,606,539 silver ounces, or 245,028 gold equivalent ounces, representing a 12.3% increase over sales of 218,200 gold equivalent ounces in 2007. Total revenues during the year were $212.5 million, representing an increase of $60.4 million over revenues of $152.1 million in the prior year. This increase in revenue resulted from the 24% higher sales of gold ounces and 12% higher sales of silver ounces during the year, combined with the 24% stronger gold prices realized in 2008.

Consolidated net earnings of $40.0 million in 2008 represented a $141.3 million improvement, or 139%, over the consolidated net loss of $101.3 million in 2007. This improvement was due to the increased sales and production of gold and silver ounces mentioned previously, reduced operating costs, and improved realized metal prices. In addition, the Company benefited from a $27.9 million change in non-cash foreign exchange gains year-over-year resulting from the weakening of the Mexican peso and Canadian dollar against the US dollar during the year. 2008 earnings also improved when compared to the prior year because 2007 included future income tax expense of $43 million related to the Mexican Single Rate Tax which was substantively enacted on September 28, 2007. For further details on this item, see the discussion of Income Tax Expense / (Recovery) on page 14.

The 2008 consolidated cash cost per gold equivalent ounce result of $528 represents a 21% improvement over the total cash costs per gold equivalent ounce of $670 in 2007. This year-over-year improvement was achieved through improved productivity at the Ocampo mine, cost management initiatives implemented at both mine sites, and the favourable impact of the weakening of the Mexican peso. Annual cash costs per gold equivalent ounce were negatively impacted by the unfavorable increase in the gold equivalency rate in the second half of the year. If the gold equivalency rate had remained at 2007 levels, consolidated cash costs would have been $512 per gold equivalent ounce for 2008, a 24% improvement over the 2007 result.

The Company reported cash flow from operations of $55.9 million, an increase of $90.1 million or 264%, over the prior year. This significant increase in cash flow resulted from improved metal prices, increased production and sales, and higher working capital inflows.

SUMMARY OF QUARTERLY FINANCIAL AND OPERATING RESULTS

(in thousands, except ounces, per share amounts, average realized prices and total cash costs)

	Q4 2008 (as restated)	Q3 2008 (as restated)	Q2 2008 (as restated)	Q1 2008 (as restated)	Q4 2007	Q3 2007	Q2 2007	Q1 2007
Gold ounces sold	41,004	33,914	44,273	31,455	28,665	25,104	31,006	36,332
Silver ounces sold	1,534,318	1,338,864	1,484,763	1,248,594	1,183,729	1,068,809	1,306,267	1,469,178
Gold equivalent ounces sold(1)	60,662	56,573	72,694	55,099	49,969	44,863	57,063	66,305
Gold equivalency rate(2)	79	59	52	53	56	54	51	49
Gold ounces produced	43,768	34,096	43,465	33,099	27,571	26,444	32,246	35,126
Silver ounces produced	1,649,893	1,372,123	1,445,887	1,310,971	1,140,797	1,115,233	1,357,708	1,421,966
Gold equivalent ounces produced(1)	64,889	57,521	71,154	57,946	48,184	47,091	59,312	64,147
Revenue from mining operations	$48,262	$48,342	$64,550	$51,368	$39,700	$30,444	$38,415	$43,500
Production costs, excluding amortization and depletion, as previously reported	$22,804	$41,220	$36,303	$26,697	$33,511	$33,957	$39,714	$37,440
Restated adjustments	$1,717	$1,220	($305)	($2,005)	-	-	-	-
As restated	$24,521	$42,440	$35,998	$24,692	$33,511	$33,957	$39,714	$37,440
Net earnings / (loss)	$21,757	($6,529)	$6,522	$8,489	($20,729)	($44,835)	($25,488)	($10,262)
Restated adjustments	$9,798	$3,076	($1,674)	($1,445)	-	-	-	-
As restated	$31,555	($3,453)	$4,848	$7,044	($20,729)	($44,835)	($25,488)	($10,262)
Net earnings / (loss) per share, basic	$0.18	($0.05)	$0.06	$0.07	($0.19)	($0.38)	($0.23)	($0.10)
Restated adjustments	$0.08	$0.03	($0.02)	($0.01)	-	-	-	-
As restated	$0.26	($0.02)	$0.04	$0.06	($0.19)	($0.38)	($0.23)	($0.10)
Net earnings / (loss) per share, diluted(3)	$0.18	($0.05)	$0.05	$0.07	($0.19)	($0.38)	($0.23)	($0.10)
Restated adjustments	$0.08	$0.03	($0.01)	($0.01)	-	-	-	-
As restated	$0.26	($0.02)	$0.04	$0.06	($0.19)	($0.38)	($0.23)	($0.10)
Cash from / (used in) operations	$9,965	$7,071	$24,342	$14,555	$2,704	($10,475)	($17,064)	($9,260)
Net free cash flow(4)	($6,446)	($10,353)	$5,297	$1,592	($10,767)	($36,648)	($35,494)	($20,425)
Total cash costs, per gold equivalent ounce(4)	$384	$735	$505	$491	$676	$764	$702	$575
Restated adjustments	$29	$22	($4)	($36)	-	-	-	-
As restated	$413	$757	$501	$455	$676	$764	$702	$575
Total cash costs, per gold ounce(4)	$192	$655	$245	$158	$589	$832	$743	$656
Restated adjustments	$42	$36	($7)	($63)	-	-	-	-
As restated	$234	$691	$238	$95	$589	$832	$743	$656
Average realized gold price(5)	$796	$855	$897	$928	$795	$679	$677	$656
Average realized silver price(5)	$10.05	$14.46	$17.08	$17.69	$14.32	$12.54	$13.34	$13.40
Cash dividends declared	$Nil	$Nil	$Nil	$Nil	$Nil	$Nil	$Nil	$Nil

(1) *Gold equivalent ounces include silver ounces produced and sold converted to a gold equivalent based on the ratio of the actual realized sales prices of the commodities.*
(2) *Silver ounce equal to one gold ounce.*
(3) *Net loss per share on a diluted basis is the same as net loss per share on an undiluted basis in Q1 through Q4 2007 and Q3 2008 as all factors were anti-dilutive.*
(4) *See the Non-GAAP Measures section on page 19.*
(5) *Average realized prices are on a per ounce basis.*

REVIEW OF FOURTH QUARTER FINANCIAL RESULTS

During the fourth quarter of 2008, the Company sold 41,004 gold ounces, 1,534,318 silver ounces, or 60,662 gold equivalent ounces, which represents an increase of 21.4% over sales of gold equivalent ounces in the same period of the prior year. Fourth quarter revenues increased to $48.3 million compared to Q4 2007 revenues of $39.7 million. This $8.6 million increase in revenue was entirely due to increased production and sales of gold and silver ounces, as realized metal prices did not improve quarter over quarter in light of the economic downturn that occurred in the second half of the year. Fourth quarter revenues decreased by $0.1 million compared to Q3 2008 revenues as a result of a decrease in metal prices, offset by increased production during the quarter.

Consolidated net earnings were $31.6 million in the fourth quarter of 2008, representing a $52.3 million or 253% improvement over the Company's consolidated net loss of $20.7 million in the fourth quarter of 2007, and a $35.1 million or 1002% improvement over the consolidated net loss in Q3 2008. This increase in earnings is due to increased production and the continuing positive effects of the Company's turn-around strategy that are being realized in 2008. During the quarter, the Mexican peso to US dollar exchange rate averaged 13.1, as compared to the previous nine months where it averaged 10.5. Approximately 60% of the Company's expenditures are denominated in Mexican pesos, and therefore these Mexican denominated costs decrease significantly when presented in US dollar terms at current exchange rates. Also contributing to the improvement quarter over quarter is the $24.4 million reduction in tax expense and the $17.1 million increase in foreign exchange gains in 2008 versus 2007.

Total cash costs per gold equivalent ounce for the fourth quarter decreased 39% to $413, compared to $676 per gold equivalent ounce in the same period in 2007, and 45% compared to $757 per gold equivalent ounce in Q3 2008. The fourth quarter of 2008 represented the Company's best ever quarterly cash cost performance since declaring commercial production at Ocampo in January 2007, despite the adverse gold-to-silver ratio of 79:1 experienced in the quarter. This reduction in cash costs per gold equivalent ounce is as a result of improved production at both the Ocampo and El Cubo mills, targeted production cost reductions achieved through the Company's turn-around strategy, and the positive effects of the devaluation of the Mexican peso. Also, in the third quarter, the Company recorded mark-to-market valuation adjustments for inventories of $90 per gold equivalent ounce. The mark-to-market adjustments primarily represented non-cash valuation adjustments to previously inventoried costs for low grade ore-in-process, when quarter-end gold and silver prices indicated that the balance sheet carrying value was not fully recoverable. In the fourth quarter, as a result of strengthening commodity prices, the Company recorded a reversal of a portion of these net valuation adjustments for inventory still on hand at year end, of $34 per gold equivalent ounce.

The Company reported cash flow from operations during the fourth quarter of $10.0 million, an increase of $7.3 million, or 270%, over the prior year and $2.9 million or 41% over Q3 2008. This improvement in operating cash flow resulted from the increased metal production and sales achieved in the fourth quarter.

RESULTS OF OPERATIONS

(in thousands, except ounces and total cash costs)

	OCAMPO		EL CUBO		CORPORATE	
	2008 (as restated)	2007	2008 (as restated)	2007	2008	2007
Gold ounces produced	115,656	87,647	38,772	33,740	-	-
Silver ounces produced	3,995,725	3,453,389	1,783,149	1,582,315	-	-
Gold equivalent ounces produced[(1)]	182,399	154,424	69,111	64,310	-	-
Gold ounces sold	112,682	87,367	37,964	33,740	-	-
Silver ounces sold	3,867,178	3,445,668	1,739,361	1,582,315	-	-
Gold equivalent ounces sold[(1)]	177,404	153,890	67,624	64,310	-	-
Revenue from mining operations	$154,313	$107,833	$58,209	$44,226	-	-
Production costs	$86,026	$102,658	$41,625	$37,645	-	-
Refining costs	$1,156	$1,046	$506	$464	-	-
Net earnings / (loss) before other items	$31,881	($33,454)	$19	($9,296)	($19,016)	($18,872)
Total cash costs per gold equivalent ounce[(2)]	$491	$702	$623	$593	-	-
Total cash costs per gold ounce[(2)]	$269	$703	$441	$511	-	-

(1) *Gold equivalent ounces include silver ounces produced and sold converted to a gold equivalent based on the ratio of the actual realized sales prices of the commodities.*
(2) *See the Non-GAAP Measures section on page 19.*

OPERATIONAL REVIEW – OCAMPO MINE

As a result of the 2008 turn-around strategy, a number of improvement initiatives were implemented at the Company's Ocampo mine. The following table summarizes some of the key production and cost initiatives being managed:

AREAS FOR IMPROVEMENT	MEASURES TO BE TAKEN THROUGHOUT 2008	UPDATE ON PROGRESS
Equipment Availability (Fixed & Mobile)	- Operator training to be provided by equipment supplier to strengthen operating and maintenance practices - Seasoned fixed and mobile maintenance managers to be appointed - Maintain sufficient spares inventory to minimize downtime	- Trainers have been hired to train all employees on proper operating procedures. - Additional maintenance managers were hired. - Expanded spares inventory level is being maintained to minimize downtime. Much of these spares are being held as consignment, thereby keeping costs to a minimum.
Insufficient Underground Development	- New underground equipment by mid-2008 to allow accelerated development - Achieve an annualized target of 50 development metres per day - Increase underground production by the end of 2008	- All equipment (including scissor lifts, and an additional truck and additional scoop tram) arrived and was commissioned by June 2008. - Averaged 39 development metres per day for 2008, and 38 metres per day in the second half of 2008. - Recruited a full time development trainer. - Recruitment of three expatriate senior supervisors to focus on organizational effectiveness and improved mining methods.
Underground Mining Method Selection	- Continue development of longhole mining stopes to maximize productivity and minimize dilution - Training on longhole mining methods and utilization of proper equipment - Establish quality assurance / quality control team dedicated to dilution management	- Progress is being made with respect to longhole mining. For 2009, 75% of the stoping tonnage is expected to come from longhole mining. - A dedicated trainer has been hired to continuously improve longhole mining methods. - A third longhole drill was transferred from El Cubo to support the expansion program. - A dedicated quality control department is focused on continuously reducing dilution.
Processing Facility Availability	- Appointment of seasoned processing manager - Maintain proper inventory of spares - Appointment of seasoned maintenance manager	- Expanded spares inventory level is being maintained to minimize downtime. - Seasoned Managers were appointed. - Processing plant averaged 2,117 TPD in Q4, and 2,171 TPD in December, the first full month of commissioning the Phase I expansion. - With access to grid power for 30% of the site's needs, mill availability averaged 93% throughout the last three quarters. - Q4 heap leach processing rate of 8,060 TPD was consistent with design capacity.
Cost Management Issues	- Ongoing improvements to reporting systems and cost control measures - Continued implementation of optimal mining methods - Optimization of consumable and reagents usage - Continue focus on optimizing workforce	- Continued improvement of IT systems in an effort to identify areas to reduce costs. - Current projects include increasing capacity and reducing consumables at the mill and implementing paste fill in the underground. - Cyanide destruction management initiatives are gaining traction. Cyanide-associated cost reductions are anticipated once the Phase 1 expansion achieves steady state levels. - Progressed tying into the main power grid that will give the operations access to full grid power, and which costs +50% less per kWh than the current on-site generation. The site expects to be fully on grid power in Q2 2009. - Implemented use of split benches and backhoe mining to minimize the dilution of high grade mill material in the open pit. - Reduced operating strip ratio during the latter part of 2008. The operating strip ratio reduced from 6.78:1 in the first quarter of 2008 to 4.15:1 in Q4. - Parked excess open pit equipment thereby reducing the operating and maintenance cost for that equipment. - Continue to monitor headcount levels, and actively recruiting for several key management positions.

AREAS FOR IMPROVEMENT	MEASURES TO BE TAKEN THROUGHOUT 2008	UPDATE ON PROGRESS
Labour Relations – Compensation Challenges	- Production bonus schedule to be implemented - Enhance communications with workforce - Proactive labour relations program implemented - Continual improvement to safety and mine services - Appoint more experienced mine management team	- Production bonus program was fully implemented in Q1. - Regular pre-shift meetings are held with workers to encourage safe working methods. - 12 experienced managers were appointed by the end of Q4. - A long-term incentive retention plan was implemented for key personnel during Q2.

OCAMPO UNDERGROUND MINE

	QUARTER ENDED		YEAR ENDED	
	DECEMBER 31, 2008	DECEMBER 31, 2007	DECEMBER 31, 2008	DECEMBER 31, 2007
Tonnes of ore mined	72,566	81,210	313,575	412,493
Tonnes of ore mined per day	789	883	857	1,130
Average grade of gold(1)	3.48	3.09	3.26	3.48
Average grade of silver(1)	173	172	173	193
Average grade of gold equivalent(1)	5.68	6.20	6.23	7.22
Metres developed	3,269	2,989	14,527	12,766

(1) *Grams per tonne.*

The Company mined 72,566 tonnes of underground ore in the fourth quarter of 2008, for a total of 313,575 tonnes annually, or 857 TPD. In the fourth quarter, underground production was negatively impacted by the development required to change to longhole mining which caused stoping delays, and a lack of qualified personnel in key areas of the underground.

Due to the success of the open pit re-phasing, additional high grade open pit ore can be sequenced and directed to the mill facility which allows the Company to dedicate more time to training in the underground. With the appointment of expatriate trainers, the Company will focus on providing additional training in mining methods that are not typically utilized in Mexico and supervision such that the underground workforce will embrace this more efficient and effective team approach to mining. In addition, production engineers have been assigned to interface between operations and planning personnel, to improve the coordination of underground teams.

The Company continues to focus on the necessary underground development to have more ore tonnes available for stoping, which will provide increased flexibility in sequencing mining areas and ultimately, increased mining productivity and efficiency. The in-process underground exploration diamond drilling program is expected to increase the Company's reserves and confidence in the mining blocks being developed. The Company continues to develop the Santa Eduviges decline, located under the Plaza de Gallos portion of the Ocampo Open Pit mine, as lateral drilling drifts are being developed to allow delineation drilling for planning a possible second underground mine and an additional source of high grade ore feed to the mill.

OCAMPO OPEN PIT MINE

	QUARTER ENDED		YEAR ENDED	
	DECEMBER 31, 2008	DECEMBER 31, 2007	DECEMBER 31, 2008	DECEMBER 31, 2007
Total tonnes mined	7,050,090	6,682,603	27,883,370	24,651,769
Total tonnes mined per day	76,631	72,637	76,184	67,539
Tonnes of ore mined	987,540	654,605	3,534,014	4,082,339
Operating stripping ratio	4.15:1	9.21:1	6.89:1	5.04:1
Average grade of gold(1)	1.09	0.75	0.96	0.60
Average grade of silver(1)	47	34	38	21
Average grade of gold equivalent(1)	1.68	1.35	1.58	1.01
Tonnes of marginal material wasted in Q4	127,654	-	127,654	-
Average grade of gold(1)	0.22	-	0.22	-
Average grade of silver(1)	6	-	6	-
Average grade of gold equivalent(1)	0.29	-	0.29	-
Total tonnes ore mined and marginal material wasted	1,115,194	654,605	3,661,668	4,082,339
Average grade of gold(1)	0.99	0.75	0.93	0.60
Average grade of silver(1)	42	34	37	21
Average grade of gold equivalent(1)	1.52	1.35	1.54	1.01

(1) *Grams per tonne.*

The Company mined 27,883,370 tonnes from the open pit in 2008, a 13% improvement over the tonnes mined in 2007. The enhanced maintenance program that occurred in the second quarter of 2008 improved equipment availability, thereby allowing the Company to mine 987,540 tonnes of ore in Q4, representing a 51% increase over the fourth quarter of 2007. The Company continued to send high grade open pit ore to the mill to take advantage of the increased throughput capacity, better economics and recoveries of the mill circuit, thereby improving recovered metal content. During the fourth quarter, due to volatile metal prices, the Company elected to stockpile the lower grade open pit ore, for processing at a later date. Also during Q4, 127,654 tonnes of 0.2 to 0.5 gold equivalent grams per tonne were sent for waste due to metal price volatility. Had management not done this, ore mined would have been 1,115,194 tonnes at 0.99 gold grams per tonne and 42 silver grams per tonne, in-line with 2007 year end reserve grades.

The Company continued its planned pre-stripping program during the year, with accelerated stripping activities at the Conico pit. Stripping activities at the Picacho pit were deferred in the latter half of the second quarter, as an independent third-party study verified that the Company could now reduce the accelerated stripping rate and still maintain the required rates of ore mining. The revised open pit phasing has resulted in a reduction in the operating stripping ratio from 6.78:1 in Q1 2008 to 4.15:1 in Q4 2008, and is expected to further decline in future quarters to be closer to the life of mine rate within the range of 2-3:1 as per the current reserve model.

OCAMPO MILL CIRCUIT

	QUARTER ENDED		YEAR ENDED	
	DECEMBER 31, 2008	DECEMBER 31, 2007	DECEMBER 31, 2008	DECEMBER 31, 2007
Tonnes from the underground	78,455	96,881	310,680	362,057
Tonnes from the open pit	116,275	37,151	350,139	104,070
Total tonnes of ore processed	194,730	134,032	660,819	466,127
Total tonnes of ore processed per day	2,117	1,457	1,806	1,277
Average grade of gold processed(1)	3.44	2.57	3.25	2.93
Average grade of silver processed(1)	154	137	149	163
Gold equivalent grade processed(1)	5.42	5.04	5.72	6.06
Gold ounces produced	20,385	10,301	65,679	43,591
Silver ounces produced	822,632	475,111	2,658,151	2,153,849
Gold equivalent ounces produced	30,906	18,906	109,961	85,239

(1) *Grams per tonne.*

The Ocampo Mill Circuit processed 660,819 tonnes during the year at an average rate of 1,806 TPD, which was an increase of 41% over 2007. In addition, total tonnes processed during the fourth quarter were 194,730 at an average of 2,117 TPD, representing the best quarter in the history of the operation. The commissioning of the 2,400 – 2,600 TPD expansion in November largely contributed to this increase, and will allow these rates of production to further improve in 2009.

Mill availability improved during 2008, and averaged 91% for the year as a result of the improved maintenance program and more reliable power supply. The Company remains on schedule and on budget in having access to an additional 20 megawatts of grid power in the first half of 2009. This 20 megawatt power supply will eliminate the Company's reliance on diesel generators, thereby providing a far more reliable source of power at a significantly reduced cost. To date, the Company has installed all electrical equipment and has substantially completed the required substation, and two transformers have been installed. In addition, cyanide destruction management initiatives are gaining traction with a number of cost reductions anticipated to be realized once the Phase 1 expansion achieves steady state levels.

Grades decreased to 5.72 gold equivalent grams per tonne in 2008 from 6.06 in the same period in 2007. This decline is virtually all due to the depreciation in the silver price which caused the unfavourable gold equivalency rate discussed previously. At the end of the year, ore stockpiles ahead of the mill were 15,482 tonnes, minimizing the possibility of future production interruption due to feed variability from the underground or the open pit. The focus going forward will remain on maintaining more than sufficient stockpiles ahead of both processing facilities to ensure ongoing production during any period of downtime.

In October, a decision was made to install a third mill at the Ocampo processing plant, and as a result, the Marcey mill, which was on care and maintenance at El Cubo's Chirimetera plant, was moved to Ocampo in early October. This is the second phase of the three-phase processing plant expansion program that was completed in Q1 2009, and will increase throughput capacity to 2,800 – 3,000 TPD. The detailed engineering on final processing capacity will be completed in early 2009.

OCAMPO CRUSHING & HEAP LEACH CIRCUIT

	QUARTER ENDED		YEAR ENDED	
	DECEMBER 31, 2008	DECEMBER 31, 2007	DECEMBER 31, 2008	DECEMBER 31, 2007
Open pit ore placed on the heap leach pad	741,560	616,121	3,080,771	2,563,660
Underground mine tonnes placed on heap leach pad	-	1,411	-	95,019
Total tonnes of ore processed	741,560	617,532	3,080,771	2,658,679
Total tonnes of ore processed per day	8,060	6,712	8,417	7,284
Average grade of gold processed(1)	0.91	0.63	0.76	0.62
Average grade of silver processed(1)	41	27	30	26
Gold equivalent grade processed(1)	1.43	1.43	1.25	1.57
Gold ounces produced	13,492	9,252	49,977	44,056
Silver ounces produced	353,796	270,949	1,337,575	1,299,540
Gold equivalent ounces produced	18,016	14,164	72,438	69,185

(1) *Grams per tonne.*

During 2008, the Company placed 3,080,771 tonnes on the heap leach pad, which averaged 8,417 TPD and represents a 5% increase over the name-plate capacity of 8,000 TPD. Construction of the heap leach pad expansion was completed during the second quarter, increasing its capacity from 5 million to 12 million tonnes. The crushing plant availability continued to improve in the second half of the year as a result of the improved maintenance program and more reliable power supply.

During the fourth quarter, a decision was made to defer a $10-$12 million heap leach pad expansion from 2009 to 2010. To accomplish this, management made the decision to stockpile low grade ores (below 0.7 gold equivalent grams per tonne) until the latter part of 2010 and to operate at a stacking rate of 5,000 to 7,000 tonnes per day. The result is that stacked headgrades for gold and silver will be substantially increased over historical levels, thereby allowing management to maintain metal production, while conserving pad capacity.

As of the end of the year, the Company has 43,515 tonnes of ore, grading 0.98 gold equivalent grams per tonne, stockpiled ahead of the heap leach to minimize the impact of any open pit production issues due to unfavourable weather conditions and periods of equipment downtime. Due to metal price volatility, management made a decision in the third quarter to defer low grade ore for processing at a later date. As a result, at December 31st, the Company had also stockpiled 216,192 tonnes with a grade of 0.63 grams per gold equivalent tonne.

OCAMPO CASH COSTS

The Company saw a reduced cash cost per gold equivalent ounce result at Ocampo in 2008, as cash costs of $491 per gold equivalent ounce were achieved, compared to the 2007 cash cost result of $702. This favorable change was driven by productivity improvements, such as higher daily mill tonnage and increased equipment availability, and strong open pit production. In addition, the weakened Mexican peso in the fourth quarter resulted in lower costs when translated to US dollars.

The improved cash cost result was partially offset by the unfavorable change in the gold equivalency rate. If the gold equivalency rate had remained at 2007 levels, cash costs per gold equivalent ounce at Ocampo would have been $466 or $25 per gold equivalent ounce lower. Also, in the second and third quarters, the Company recorded mark-to-market valuation and other adjustments for inventories of $34 per gold equivalent ounce. The mark-to-market adjustments primarily represented non-cash valuation adjustments to previously inventoried costs for low grade ore-in-process, when quarter-end gold and silver prices indicated that the balance sheet carrying value was not fully recoverable. In the fourth quarter, as a result of strengthening commodity prices, the Company recorded a reversal of a portion of these net valuation adjustments for inventory still on hand at year end, of $12 per gold equivalent ounce.

OCAMPO EXPLORATION

In early 2008 the Company committed to a minimum $7.5 million exploration program at Ocampo during 2008 – 2009, to be funded from operating cash flow. The Ocampo Mining district is at a key cross-road in its history. With the open pit mines now operating smoothly, and the underground mine under continuous improvement, the Company can now begin to expand exploration efforts beyond the known core of the district. The past year's exploration efforts were designed to complete definition drilling on the known deposits, and to complete some step-out drilling as well, but future exploration will be designed to test new target ideas beyond the known deposits. To date, less than 20% of the land position has seen any systematic exploration. With the known resources occupying just a small part of the land position, with the known ore systems open to the NE and SE, with known ore deposits the west (Moris) and northeast (Pinos Altos) of the Company's land position, there is ample encouragement to invest in a more thorough exploration program on the unexplored portion of the property.

During the year, the Company spent $2.9 million on Ocampo drilling. This work included the following:

- A substantial surface drill program to better define the limits of mineralization in the Plaza de Gallos ("PDG") open pits. This drilling consisted of 108 holes of reverse circulation drilling for a total of 15,516 metres, and 31 holes of diamond drilling for a total of 5,231 metres. The total of reverse circulation and diamond drilling in the PDG open pits in 2008 was 139 holes for a total of 20,747 metres. This work was used to refine the Company's Resource and Reserve estimates, as well as long-range mine planning, for the PDG open pits. The Company plans a further 12,000 metres of definition drilling in the open pits in 2009.
- In addition to the surface definition drilling on the open pits, the Company drilled 85 holes for a total of 13,574 metres in the Northeast Area using two underground diamond drills. This drilling was mostly directed to the San Fernando Vein, the San Amado Vein, the Aventurero Vein, and the Balvanera Vein. Results from the San Fernando and San Amado Veins were positive. Strongly mineralized vein was discovered on the San Amado that is still open to the NE. The Company plans a further 10,500 metres of underground diamond drilling in the Northeast Area in 2009 to test the downward extension of known vein ore shoots to the 1,380 metres elevation.
- Fieldwork in 2008 discovered a 450 metre outcropping NE extension of the San Amado Vein on surface that extends past any known workings or past drilling. This obvious surface target is covered to the NE by post-mineral rocks, but the termination of veining to the NE is unknown due to this post-mineral cover. For 2009 the Company plans a step-wise program to test the San Amado NE extension first with 2,000 metre of surface drilling, and if results are positive, with a substantial drift on the 1,611 level to test the vein further at depth.

HOLE	TARGET	INTERVAL	TRUE WIDTH(1)	GOLD (G/T)	SILVER (G/T)	GOLD EQUIVALENT (G/T)(50:1)
OU-426	SAN AMADO	5.00	3.50	30.57	2,126	73.09
OU-428	SAN AMADO	3.65	2.45	82.40	681	96.02

(1) True widths are subject to some interpretation.

Note: This exploration information has been reviewed by Qualified Person, Mr. Ramon Luna. All sample analyses were performed by Chemex Laboratories, based in Vancouver, British Columbia using standard fire assay procedures.

- During 2008 the Company completed 27,493 metres of underground workings, of which 5,564 metres were new drifts along mineralized structures. This work will be compiled along with the 2008 underground drilling to build a new ore model and resource – reserve model in Q3 2009.
- Exploration at Ocampo to date has focused on the PDG and Northeast Area veins. For 2009 the Company is planning a new surface brownfields exploration program at Ocampo on the existing large land position. Much of this land position has not been explored far beyond the presently-recognized resources in the past, and the new program will consist of basic geology and geochemistry to define drill targets for the following year.

OPERATIONAL REVIEW – EL CUBO MINE

As with Ocampo, in 2008 the Company has implemented a number of production and cost initiatives at the El Cubo mine as part of the Company-wide turn-around strategy.

AREAS FOR IMPROVEMENT	MEASURES TO BE TAKEN THROUGHOUT 2008	UPDATE ON PROGRESS
High Labour Costs	- Optimization of workforce to reduce total site manning of both employees and contractors	- As mills have been placed on care and maintenance and underground ore haulage level ramps up, the workforce (contractor and union) level has reduced by 29% from 1,296 in January to 920 by the end of December. No work stoppage occurred, however lower productivities resulted from the disruptive re-organization. - A further 5-10% reduction will take place through attrition in 2009.
Processing Facilities	- Advancing key capital projects by early 2008 to drive production throughput and plant availability - Integration of the El Cubo mine workings with the Las Torres shaft and mill infrastructure - All underground ore hauled via train at the 600 level to the Las Torres shaft and plant	- Majority of capital projects (including the installation of a gravity circuit) were completed. - Continued focus on determining ways to improve production throughput and plant availability. - 60% to 80% of the underground production is now being transferred via the underground workings directly to the Torres shaft and mill infrastructure. Ramp-up to full production is anticipated by year end 2009.
Equipment Availability	- Additional mobile equipment for the underground - Improved preventative maintenance practices implemented	- Key new underground equipment arrived in July and early August, and has been fully commissioned.
Lack of Underground Development	- Focus on extending existing underground exploration development into areas of known structures which have been neglected historically due to a lack of capital and priority - Annualized target of 75 development metres per day	- Continued focus on underground exploration and development to build on the number of available longhole stopes. - Averaged 64 development metres per day in Q4 2008.
Underground Mining Method Selection	- Improved overall mining methods - Establish quality assurance / quality control team dedicated to dilution management	- Continued to introduce longhole mining methods. - Longhole mining training program completed in Q2 2008. - A dedicated quality assurance team is now on site that is focused on reducing dilution.

EL CUBO UNDERGROUND AND MILLING OPERATIONS

	QUARTER ENDED		YEAR ENDED	
	DECEMBER 31, 2008	DECEMBER 31, 2007	DECEMBER 31, 2008	DECEMBER 31, 2007
Tonnes of ore mined	158,974	160,278	648,373	689,753
Tonnes of ore mined per day	1,728	1,742	1,771	1,890
Total tonnes of ore processed	160,719	160,278	658,105	689,753
Total tonnes of ore processed per day	1,746	1,742	1,798	1,890
Average grade of gold processed(1)	2.11	1.74	1.98	1.77
Average grade of silver processed(1)	103	88	94	83
Gold equivalent grade processed(1)	3.41	3.33	3.59	3.38
Gold ounces produced	9,891	8,017	38,772	33,740
Silver ounces produced	473,466	394,738	1,783,148	1,582,316
Gold equivalent ounces produced	15,966	15,112	69,111	64,038

(1) *Grams per tonne*

The Company mined 648,373 tonnes of ore at the El Cubo mine in 2008, a 6% decrease compared to 2007. This mining performance reduction was primarily due to the test cessation of Rezagas (old stope backfill material) mining during the third quarter of 2008 in an effort to focus on increasing in-situ ores mining rates, and the disruption associated with the downsizing and restructuring of the workforce. In the fourth quarter, management recommenced Rezagas mining, but at reduced levels due to the unfavourable gold-to-silver ratio and depressed silver prices, and continued to focus on in-situ mining, which is expected to result in further cost savings. Despite the reduction of the workforce by 29% throughout the year, mining of in-situ ores improved by 55% from January to December.

During the second quarter, the Company installed a gravity circuit at the Las Torres mill which has improved the facility's overall metallurgical recovery of higher grade ores. With all primary processing activities now consolidated at the Las Torres mill, management placed the grinding circuit at the Tajo mill on care and maintenance. Until the necessary permits to allow for cyanidation at Las Torres are received, the concentrate is being leached at the Tajo mill. Once permits are obtained, the Tajo mill will be fully placed on care and maintenance, and all processing will take place at the Las Torres mill.

EL CUBO CASH COSTS

The Company saw an increase in the cash costs per gold equivalent ounce result at El Cubo in 2008, as cash costs of $623 per gold equivalent ounce were achieved, compared to the 2007 cash cost result of $593. Cash costs per gold equivalent ounce increased due to the workforce restructuring costs of $0.6 million or $9 per gold equivalent ounce, and the reduction in rezagas mining in the year by 49%. In addition, the unfavorable increase in the gold equivalency rate caused higher cash costs per gold equivalent ounce. If the gold equivalency rate had remained at 2007 levels, cash costs per gold equivalent ounce at El Cubo would have been $590, in line with 2007 cash costs per gold equivalent ounce. Offsetting this increase in cash costs per gold equivalent ounce at El Cubo was the favorable impact of the devaluation of the Mexican peso in the fourth quarter of 2008.

The Company expects 2009 cash costs per gold equivalent ounce to further decrease due to resuming the mining of low cost rezagas material, and realizing the benefits of the reduced workforce.

EL CUBO EXPLORATION

An underground diamond drill program using Company drill equipment was initiated in June on some of the more prospective veins. Drilling expenditures in 2008 totalled $0.4 million. A total 5,262 metres were drilled to test down dip projections of several veins. The principal targets were:

- Villalpando Vein from Levels 4 and 14 - with 2,913 metres of drilling
- 176 Vein and 178 Vein from Level 0 - with 1,110 metres
- Villalpando del Alto and Guadalupe Veins from Level 13 - with 812 metres

Some additional ore was added to the Villalpando structure on Level 4 and 14 and indications of down-dip continuity for the 176 and 178 Veins were obtained from the drilling. This is a significant result as no veining in this part of the mine (Area I) has as yet been explored or developed. Further exploration in 2009 will target down dip structures particularly where they occur in the favourable La Bufa rhyolite and Peregrina intrusive.

In addition, exploration drifting was completed on several veins, including La Loca – Level 12 (98 metres), La Loca – Level 6 (115 metres), and Villalpando – Level 5 (118 metres). Within Peñoles concessions the exploration drifting occurred principally on San Alberto – Level 600 (74 metres) and Fatima – Level 600 (49 metres).

Surface diamond drilling was suspended for the year in 2008, while surface geologic mapping and sampling could be advanced. During the year the Company decided to dedicate greater efforts to develop a property-wide renewed exploration program for the district. This work will extend into the first half of 2009 and will entail a careful compilation of the district's geology and geochemistry, include new geologic mapping with the intent to develop a prioritized series of exploration targets for new ore systems, as well as extensions to known vein systems.

GUADALUPE Y CALVO EXPLORATION PROJECT

Exploration at the Guadalupe y Calvo Project in 2008 focused on detailed drilling, with as much a five drill rigs running at a time. During the year, the Company drilled an additional 126 diamond drill holes for a total of 38,399 metres. Along with previous drilling done by the Company, the total drilling in the project is now 183 diamond drill holes for a total of 52,075 metres. This year's drilling was designed to fill in the previous drilling on 25 x 40 metre centres to define a measured and indicated resource on the project. The results of this drilling are being integrated into an updated geologic and ore model for the deposit. Drilling expenditures in 2008 totalled $4.6 million.

Preliminary metallurgical tests were also performed on the mineralization discovered to date. These tests showed that six samples of vein and typical-grade wallrock stockworks averaged 84% gold and 89% silver recoveries using bottle roll cyanide tests on -150 micron mineralization.

In addition to testing the potential open pit mineralization, the 2008 drilling tested potential underground mineralization in the Rosario Vein. Results were generally positive. This drilling extended bonanza grade mineralization to an elevation of 1,955 metre, well below the 2,200 metre elevation that was known previously. Two of the deepest intercepts were holes GC-67 with a 2.0 metre long intercept grading 9.16 gold grams per tonne and 686 silver grams per tonne at 1,955 metre elevation, and GC-68 with a 4.0 metre long intercept grading 5.11 gold grams per tonne and 470 silver grams per tonne at 1,955 metre elevation. These are just two out of a total of sixty-four drill intercepts on the property that had grades in excess of 3.0 gold equivalent grams per tonne (using gold equivalent ratio of 80:1) over minimum drill lengths of 1.4 metres, and of fifteen drill intercepts that had grades in excess of 10.0 gold equivalent grams per tonne (using gold equivalent ratio of 80:1). The drilling shows that the vein mineralization is open at depth.

For 2009, the Company is planning to complete the geologic and resource model, a preliminary scoping study, as well as complete a district-wide reconnaissance exploration program on the large land package presently around the known deposit. This work will include an extensive geochemical – geological program to determine if there are other worthy drill targets on the large land package.

Note: The scientific and technical information related to the Guadalupe y Calvo Project is based on the technical report on this project dated November 25, 2002 and was prepared by Qualified Person, Clancy J. Wendt, and Mark G. Stevens, C.P.G., Pincock, Allen & Holt in accordance with National Instrument 43-101. The full text of this report is available under the Company's profile at www.sedar.com.

CONSOLIDATED EXPENSES

(in thousands)

	YEAR ENDED		
	DECEMBER 31, 2008 (AS RESTATED)	DECEMBER 31, 2007	DECEMBER 31, 2006
General and administrative	$29,945	$24,156	$28,247
Amortization and depletion	$40,380	$43,392	$18,757

General and administrative costs include expenses related to the overall management of the business which are not part of direct mine operating costs. These costs are generally incurred at the corporate offices located in Canada and Mexico. General and administrative costs increased by $5.8 million when compared to 2007 primarily due to higher performance-based compensation costs, and increased professional fees and administrative costs year-over-year. General and administrative costs include stock-based compensation and share-based bonuses payable, both non-cash expenses that totaled $9.7 million in 2008 (2007 - $4.0 million). During the 2008 compensation review, it was determined that senior executive officers would not receive increases in 2009 base salaries, in an effort to conserve funds of the Company. In addition, the Board of Director's Compensation Committee proposed that 2008 annual incentive bonuses be awarded to executive officers in the form of share-based compensation, plus additional tax benefits. The shares awarded are valued at the volume weighted average trading price of the Company's shares for the five days prior to the award, and vest over an eighteen-month period. Subject to shareholder and stock exchange approvals, the executives will receive the number of shares equivalent to the bonus value, using the grant date price. In the event that approval is not obtained, the executives are entitled to receive an amount in cash, equal to the product of the number of shares that would have been issued and the trading price of the Company's shares on the date paid. As at December 31, 2008, the Company has recorded $5.6 million in compensation expense related to these share-based bonuses.

Amortization and depletion, which primarily relates to mining activities, decreased by 7% to $40.4 million for the year, compared to $43.4 million for 2007. This change is primarily attributable to the Company's change in the estimated useful lives of its mines, partially offset by increases in units of production and amortization of capital additions. During the second quarter of 2008 the Company reviewed the appropriateness of its current estimated useful lives of the mines, which was based on proven and probable reserves, and determined that based on the characteristics of the current reserves and resources at Ocampo and El Cubo, the estimated useful life is more accurately reflected by proven and probable reserves and the portion of mineralization currently in resources that is expected to be classified as reserves. This change in estimate was applied prospectively effective April 1, 2008 and had the impact of reducing amortization and depletion by approximately $4.6 million.

CONSOLIDATED OTHER INCOME / (EXPENSE)

(in thousands)

	YEAR ENDED		
	DECEMBER 31, 2008 (AS RESTATED)	DECEMBER 31, 2007	DECEMBER 31, 2006
Interest on long-term debt	($1,936)	($3,897)	($5,272)
Foreign exchange gain / (loss)	$18,942	($8,933)	($1,497)
Interest and other income	$410	$772	$785

Interest on long-term debt decreased by $2.0 million to $1.9 million in 2008 from $3.9 million in 2007 as a result of the reduction in the average balance outstanding on the Company's credit facility year-over-year. For the first four months of 2007, the balance outstanding on the facility was $120 million. In late April 2007, the Company used a significant portion of the proceeds from a $200 million CAD equity offering to repay the $120 million credit facility.

Foreign exchange gains increased by $27.8 million, from a loss of $8.9 million in 2007 to a gain of $18.9 million in 2008, as a result of the translation of net monetary liabilities in the Company's Canadian and Mexican operations to US dollars. The weakened Mexican peso and Canadian dollar in the second half of 2008 caused foreign exchange gains, primarily as a result of the Company's future income tax liabilities which are denominated in these currencies and that are translated into US dollars at each balance sheet date. The Company will continue to experience non-cash foreign currency gains or losses as a result of fluctuations between the US and Canadian dollars and the Mexican peso.

The Company earned interest on short-term investments and other income of $0.4 million during 2008, compared to $0.8 million in 2007.

CONSOLIDATED INCOME TAX EXPENSE / (RECOVERY)

During the year ended December 31, 2008, the Company incurred current tax expense of $1.0 million and a future income tax recovery of $10.7 million, versus current tax expense of $Nil and future tax expense of $27.6 million in 2007. The future income tax recovery in the current year is primarily a result of a continued assessment of the impact of the Mexican Single Rate Tax on the Company's ability to utilize the future income tax assets recognized in the Mexican subsidiaries. In Q3 2007, the Company recorded a significant future income tax adjustment resulting from the Single Rate Tax that was substantively enacted on September 28, 2007. Under this new tax regime, the Company's Mexican subsidiaries now pay a 17.5% tax (with lower transitional rates for 2008 and 2009) on the Company's revenues less certain deductions, all determined on a cash basis. The Company pays the Single Rate Tax to the extent that it exceeds its income tax otherwise determined pursuant to the pre-existing income tax system in each taxation year. During the year ended December 31, 2008, the Company was subject to the Single Rate Tax.

FINANCIAL CONDITION

(in thousands)

	AS AT DECEMBER 31, 2008 (AS RESTATED)	AS AT DECEMBER 31, 2007	
Current assets	$79,469	$69,525	Current assets increased in 2008 primarily due to increased inventory on hand at the end of the year resulting from higher production volumes, a decrease in commodity tax receivables due to improved collection, offset by an increase in trade receivables.
Long-term assets	715,709	684,427	Long-term assets increased in 2008 as a result of capital acquisitions partially offset by amortization and depletion, and due to a long-term consultancy agreement signed in Q2 2008.
Total assets	795,178	753,952	
Total current liabilities	61,318	50,352	Current liabilities increased in 2008 primarily as a result of increased payables and accruals resulting from accelerated maintenance and development and associated payment terms, partially offset by a lower current portion of long-term debt outstanding.
Total long-term liabilities	95,250	116,950	Long-term liabilities decreased in 2008 due to a decrease in future tax liabilities partially offset by an increase in long-term obligations resulting from the 8 year consultancy agreement signed in Q2 2008.
Total liabilities	156,568	167,302	
Shareholders' equity	$638,610	$586,650	Shareholders' equity increased in 2008 as a result of positive earnings year-to-date, and exercises of stock options which increased the capital stock balance.

LIQUIDITY AND CAPITAL RESOURCES

The Company's balance of cash and cash equivalents as at December 31, 2008 was $3.3 million, consistent with the balance as at the end of 2007 of $3.7 million. Factors that can impact on the Company's liquidity are monitored regularly and include the market prices of gold and silver, production levels, operating cash costs, capital costs and exploration expenditures and currencies.

CASH FLOW

(in thousands)

	YEAR ENDED		
	DECEMBER 31, 2008	DECEMBER 31, 2007	DECEMBER 31, 2006
Cash flow from / (used in) operating activities	$55,933	($34,192)	($20,026)
Cash flow used in investing activities	(66,376)	(73,487)	(87,782)
Cash flow from financing activities	9,992	107,314	106,132
Decrease in cash and cash equivalents	(451)	(365)	(1,676)
Cash and cash equivalents, beginning of year	3,709	4,074	5,750
Cash and cash equivalents, end of year	$3,258	$3,709	$4,074

Operating activities contributed $55.9 million during 2008 compared to 2007, when operating activities used cash flows of $34.2 million. This improvement of $90.1 million, or 264%, resulted from increased cash flows from earnings due to stronger metal prices, increased metal production, realized cost efficiency initiatives and positive changes in non-cash working capital balances.

Investing activities for the year ended December 31, 2008 used cash of $66.4 million as a result of expenditures on mining interests and property, plant and equipment, which compared to $73.5 million in 2007. Current year expenditures were largely for the purposes of the capital expansion program, the benefits of which will be seen in 2009. As of December 31, 2008 the Company had committed to purchase $2.9 million in property, plant and equipment that will be financed by operating cash flow, and will be delivered throughout the first half of 2009.

Financing activities for 2008 contributed cash of $10.0 million compared to 2007, when financing activities contributed $107.3 million. The significant cash flow from financing activities in 2007 resulted from the $200 million CAD equity offering which took place in the second quarter of that year. A large portion of the proceeds from this offering were used to pay down the Company's $120 million credit facility. Cash flows from financing activities have also decreased in 2008 compared to 2007 due to reduced proceeds from the exercise of stock options.

CREDIT FACILITY

During the majority of 2008, the Company had access to a $60 million revolving credit facility with a lending syndicate comprised of the Bank of Nova Scotia and the Bank of Montreal, expiring on December 31, 2008. On November 28, 2008, the terms of the Company's credit facility were revised and extended. Under the terms of the revised agreement, the Company has access to a $50 million credit facility comprised of a $30 million non-revolving term credit facility and a $20 million revolving term credit facility. The non-revolving facility is repayable in five installments and matures on June 28, 2010, while the revolving facility matures on November 27, 2009 and may be renewed at the sole discretion of the lenders. At the end of 2008, the Company had a balance of $30 million outstanding on the non-revolving facility, and had withdrawn $7.13 million against the revolving facility, for a total of $37.13 million outstanding. In addition, the Company has issued a $1 million letter of credit against the revolving facility, leaving a total of $11.87 million available for future funding.

LIQUIDITY OUTLOOK

The global credit and financial markets are currently experiencing an unprecedented downturn that is negatively impacting nearly all businesses, including gold and silver mining operations. Some of the key effects that are directly impacting the Company are the higher costs and availability of funding, currency devaluations, and volatility in global equity, commodity, foreign exchange and precious metals markets. Material increases or decreases in the Company's liquidity and capital resources will be substantially determined by the success or failure of the Company's operations, exploration, development and construction programs, its ability to obtain equity or other sources of financing, and the price of gold and silver. The Company has reviewed its cash generating potential, and cash utilization and working capital requirements in light of the current economic circumstances, the results of which are discussed below.

Improving the Company's liquidity position was a key focus in 2008 and remains a key focus going forward. Liquidity risk is the risk that the Company will encounter difficulties in meeting obligations associated with its financial liabilities and other contractual obligations. The Company's strategy for managing liquidity is based on achieving positive cash flows from operations to internally fund operating and capital requirements. Due to the current economic environment and fluctuating commodity prices, the Company is highly focused on preserving cash and identifying sources of cash inflows. In an effort to preserve cash, the Company has reduced capital expenditures and operating costs where appropriate.

The Company monitors and manages liquidity risk by preparing regular periodic cash flow forecasts, seeking flexibility in financing arrangements, and expects to build a cash reserve in 2009. During 2008 and continuing into 2009, management undertook various initiatives to manage operating and liquidity risks, taking into account the current economic conditions, including:

- Implementation of cost reduction initiatives, including employee and contractor reductions at the El Cubo mine, renegotiation of key supplier contracts, and more rigorous cost management through improved approval processes;
- Actively managing the Company's working capital by ensuring sufficient cash is available to support management objectives, while continuing to meet obligations;
- Deferring a number of capital programs at the Ocampo mine to 2010, and deferring drilling at Guadalupe y Calvo and the El Cubo mine until the global economic market has stabilized; and
- Renegotiating the Company's credit facility as discussed above.

Net free cash flow for 2008 was a negative $10.9 million in a year in which the Company continued significant investment in mineral properties and property, plant and equipment. The Company is forecasting positive net free cash flow for 2009, to be achieved through positive operating cash flows. The extent of cash flows generated from operations will vary depending on the prices of gold and silver, fluctuations in the Mexican peso, and total production. In addition to cash flows from operations, as at March 20, 2009, the Company has a balance of $19.6 million in cash and cash equivalents and $11.87 million available of the $20 million revolving credit facility discussed above.

In accordance with the terms of the revised credit facility agreement, the Company is required to make $22.5 million in principal repayments on its non-revolving facility in 2009. This facility also includes a clause whereby the Company is required to make additional prepayments on the overall credit facility balance equal to 75% of its excess cash flow in the six months ending June 30, 2009, and each fiscal quarter thereafter. Excess cash flow has been defined as cash flow from operations determined in accordance with Canadian generally accepted accounting principles, less scheduled interest and principal payments, cash taxes, capital and exploration expenditures, and general and administrative expenditures. In addition, the overall credit facility is subject to certain monthly and quarterly financial and operating covenants.

The Company has total commitments relating to future capital expenditures of $3.8 million as at March 20, 2009.

The Company always attempts to target the best sources of funding to supplement operating cash flows and finance the Company's development, while optimizing the Company's capital structure through the appropriate mix of capital. The operational turn-around that is underway at Ocampo, combined with the solid contributions from El Cubo, are expected to continue strengthening the Company's balance sheet and liquidity position. In today's metal price environment, the Company anticipates that funding from existing cash reserves, operating cash flows and the in-place credit facility should be sufficient to fund the Company's anticipated working capital requirements, growth plans and debt repayments in 2009.

CONTRACTUAL OBLIGATIONS

A summary of the Company's contractual obligations at December 31, 2008 is summarized as follows:

(in thousands)

	Total	Less than 1 year	1 – 3 years	3 – 4 years	4 – 5 years	Greater than 5 years
Payables and accruals	$ 30,457	$ 30,457	$ -	$ -	$ -	$ -
Long-term debt	37,130	29,630	7,500	-	-	-
Interest on long-term debt	631	631	-	-	-	-
Capital leases	2,028	1,511	517	-	-	-
Long-term obligation	6,000	400	1,600	800	800	2,400
Future purchase commitments	2,859	2,859	-	-	-	-
Total	$ 79,105	$ 65,488	$ 9,617	$ 800	$ 800	$ 2,400

OUTSTANDING SHARE DATA

The Company's share capital was comprised of the following as at December 31, 2008:

	DECEMBER 31, 2008	DECEMBER 31, 2007
Authorized:		
Unlimited number of common shares		
Unlimited number of non-cumulative, dividends to be determined by the Board of Directors not to exceed 12%, non-participating, non-voting, Class "A" preferred shares, redeemable at paid-in value		
Unlimited number of non-cumulative, dividends to be determined by the Board of Directors not to exceed 13%, non-participating, non-voting, Class "B" preferred shares, redeemable at paid-in value		
Issued:		
Common shares	120,040,768	117,432,363

At March 25, 2009, the Company had common shares outstanding of 122,549,168.

OFF-BALANCE SHEET ARRANGEMENTS

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

TRANSACTIONS WITH RELATED PARTIES

The Company paid or has payable the following amounts to directors for services other than in their capacity as directors, and companies controlled by or related to directors:

(in thousands)

		YEAR ENDED	
	DECEMBER 31, 2008	DECEMBER 31, 2007	DECEMBER 31, 2006
Production costs – labour(1)	$33,762	$31,147	$19,509
Mining interests – labour(1)	$1,167	$2,437	$3,717
Production costs – mine consumables(2)	$14,655	$2,033	$3,041
Capital assets(3)	$94	$25	$916

(1) The Company pays a third party company owned by the brother of Mr. Fred George, a director of the Company, for the provision of workers in Mexico at cost plus 10%. Gammon is committed to a fair and transparent procurement process for all goods and services and accordingly, in late 2007, a competitive bid process was conducted. Four organizations submitted bids after which the same related party was selected as the most competitively priced and best resourced organization to provide the requested services.

(2) The Company pays two third party companies owned by the father of Mr. Canek Rangel, a director of the Company, for the provision of lubricant and fuel. The Company is confident these costs are at fair market value as the prices of these consumables are regulated in Mexico.

(3) The Company paid Mr. Canek Rangel or a third party company owned by the father of Mr. Rangel, a director of the Company, for the provision and construction of production and support facilities, and mineral properties. The Company believes these costs were at fair market value.

No director, senior officer, principal holder of securities or any associate or affiliate thereof of the Company has any interest, directly or indirectly, in material transactions with the Company or any of its direct or indirect wholly-owned subsidiaries, other than the above-noted transactions, which were in the normal course of operations.

The Company has a Stock Option Plan for directors, officers, employees and consultants of the Company and its subsidiaries. The purpose of the plan is to encourage ownership of the Company's common shares by the persons who are primarily responsible for the management and profitable growth of the Company's business, to provide additional incentive for superior performance, and to attract and retain valued personnel. For the purposes of the plan, a consultant is defined as an individual that is engaged by the Company, under a written contract, to provide services on an ongoing basis and spends a significant amount of time on the Company's business and affairs. The definition of consultant also includes an individual whose services are engaged through a personal holding company.

NON-GAAP MEASURES

TOTAL CASH COST PER OUNCE CALCULATION

Total cash costs per ounce is a non-GAAP performance measure that Management uses to better assess the Company's performance for the current period and its expected performance in the future. The Company believes that, in addition to conventional measures prepared in accordance with GAAP, certain investors use this measure to evaluate the Company's performance and cash generating capabilities. Total cash costs per ounce does not have any standardized meaning prescribed by GAAP, and should not be considered in isolation of or as a substitute for performance measures prepared in accordance with GAAP. This measure is not necessarily indicative of operating profit or cash flow from operations as determined under GAAP. Other companies may calculate these measures differently. Total cash costs per ounce is calculated by dividing all of the costs absorbed into inventory, excluding amortization and depletion, by applicable ounces sold.

The following provides a reconciliation of total cash costs per ounce to the financial statements:

(in thousands, except ounces, cash costs and silver prices)

	Quarter Ended				Year Ended			
	December 31, 2008 (restated)		December 31, 2007		December 31, 2008 (restated)		December 31, 2007	
Production costs per financial statements	$	24,521	$	33,511	$	127,651	$	144,623
Refining costs per financial statements		508		326		1,662		1,510
Total cash costs	$	25,029	$	33,837	$	129,313	$	146,133
Divided by gold equivalent ounces sold(1)		60,662		49,969		245,028		218,200
Total cash cost per gold equivalent ounce	$	413	$	676	$	528	$	670
Total cash costs (per above)	$	25,029	$	33,837	$	129,313	$	146,133
Less: Silver revenue (see below)		(15,420)		(16,951)		(82,192)		(67,476)
	$	9,609	$	16,886	$	47,121	$	78,657
Divided by gold ounces sold		41,004		28,665		150,646		121,107
Total cash cost per gold ounce(2)	$	234	$	589	$	313	$	649
Average realized silver price	$	10.05	$	14.32	$	14.66	$	13.42
Multiplied by silver ounces sold		1,534,318		1,183,729		5,606,539		5,027,983
Silver revenue	$	15,420	$	16,951	$	82,192	$	67,476

(1) *Gold equivalent ounces include silver ounces produced and sold converted to a gold equivalent based on the ratio of the actual realized sales prices of the commodities.*
(2) *The calculation of total cash cost per gold ounce includes the by-product silver sales revenue.*

NET FREE CASH FLOW

Net free cash flow represents an indication of the Company's continuing capacity to generate discretionary cash flow from operations, comprising cash flows from operating activities net of total capital expenditures. It does not necessarily represent the cash flow in the period available for Management to use at its discretion, which may be affected by other sources and non-discretionary uses of cash. Net free cash flow is intended to provide additional information, does not have any standardized meaning prescribed by GAAP and should not be considered in isolation or as a substitute for measures of performance prepared in accordance with GAAP. Other companies may calculate this measure differently. The following is a reconciliation of net free cash flow to the financial statements:

(in thousands)

	Quarter Ended				Year Ended			
	December 31, 2008		December 31, 2007		December 31, 2008		December 31, 2007	
Cash flows from / (used in) operating activities	$	9,965	$	2,704	$	55,933	$	(34,192)
Less: Capital expenditures		(16,411)		(13,471)		(66,841)		(69,142)
Net free cash flow	$	(6,446)	$	(10,767)	$	(10,908)	$	(103,334)

RISKS AND UNCERTAINTIES

The Company's business contains significant risk due to the nature of mining, exploration, and development activities. Certain risk factors listed below are related to the mining industry in general, while others are specific to Gammon. Included in the risk factors below are details on how management seeks to mitigate these risks wherever possible. For additional discussion of these and other risk factors, please refer to the Company's Annual Information Form which is available on the Company's website at www.gammongold.com or on SEDAR at www.sedar.com.

NATURE OF MINERAL EXPLORATION AND MINING

Because mines have limited lives based on proven and probable mineral reserves, the Company will be required to continually replace and expand its mineral reserves as its mines produce gold. The Company's ability to maintain or increase its annual production of gold and silver in the future will be dependent in significant part on its ability to identify and acquire additional commercially viable mineral properties, bring new mines into production, and to expand mineral reserves at existing mines.

Mineral resource exploration and development is a highly speculative business, characterized by a number of significant risks including, among other things, unprofitable efforts resulting not only from the failure to discover mineral deposits but also from finding mineral deposits that, though present, are insufficient in quantity and quality to return a profit from production. There can be no assurance that the Company will successfully acquire additional mineral rights. While the discovery of additional ore-bearing structures may result in substantial rewards, few properties which are explored are ultimately developed into producing mines. Major expenses may be required to establish reserves by drilling and to construct mining and processing facilities at a particular site. It is impossible to ensure that the current exploration and development programs of the Company will result in profitable commercial mining operations. The profitability of the Company's operations will be, in part, directly related to the cost and success of its exploration and development programs which may be affected by a number of factors.

Mining is inherently dangerous and subject to conditions or events beyond the Company's control, which could have a material adverse effect on the Company's business. Mining involves various types of risks and hazards, including, but not limited to, environmental hazards; industrial accidents; metallurgical and other processing problems; unusual or unexpected rock formations; structural cave-ins or slides; seismic activity; flooding; fires; periodic interruptions due to inclement or hazardous weather conditions; variations in grade, deposit size, density and other geological problems; mechanical equipment performance problems; unavailability of materials and equipment; labour force disruptions; unanticipated or significant changes in the costs of supplies; and unanticipated transportation costs. Where considered practical to do so, the Company maintains insurance against risks in the operation of its business in amounts which it believes to be reasonable. Such insurance, however, contains exclusions and limitations on coverage. The Company may suffer a material adverse effect on its business if it incurs losses related to any significant events that are not covered by its insurance policies.

RESERVE ESTIMATES

Mineral resource and reserve figures are based upon estimates made by Company personnel and independent geologists. These estimates are imprecise and depend upon geological interpretation and statistical inferences drawn from drilling and sampling analysis, which may prove to be unreliable. There can be no assurance that these estimates will be accurate; that reserves, resources or other mineralization figures will be accurate; or that this mineralization could be mined or processed profitably. Mineralization estimates for the Company's properties may require adjustments or downward revisions based upon further exploration or development work or actual production experience. In addition, the grade of ore ultimately mined, if any, may differ from that indicated by drilling results. There can be no assurance that minerals recovered in small scale tests will be duplicated in large scale tests under on-site conditions or in-production scale. The reserve and resource estimates have been determined and valued based on assumed future prices, cut-off grades and operating costs that may prove to be inaccurate. Extended declines in market prices for gold and silver may render portions of the Company's mineralization uneconomic and result in reduced reported mineralization. Any material reductions in estimates of mineralization, or of the Company's ability to extract this mineralization, could have a material adverse effect on the Company's results of operations or financial condition.

EFFECTIVE INTERNAL CONTROL OVER FINANCIAL REPORTING

The Company is required to maintain effective internal control over financial reporting under the Sarbanes-Oxley Act of 2002 and related regulations. Any material weakness in internal control over financial reporting that needs to be addressed, disclosure of management's assessment of our internal control over financial reporting, or disclosure of the public accounting firm's report on internal control over financial reporting that reports a material weakness in internal control over financial reporting may reduce the price of the Company's common shares. In connection with the audit of the consolidated financial statements for the year ended December 31, 2008, the Company and its independent registered public accounting firm identified a deficiency in internal control over financial reporting that was a "material weakness" as defined by standards established by the Public Company Accounting Oversight Board. The deficiency resulted in the correction of the translation of certain foreign currency balances into United States dollars and the reversal of previously recorded net realizable value adjustments on inventory balances. The Company has restated its consolidated financial statements for the year ended December 31, 2008 to correct the accounting treatment for these items. However, there can be no assurance that the Company's remediation of internal control over financial reporting relating to the identified material weakness will re-establish the effectiveness of internal control over financial reporting or that the Company will not be subject to material weaknesses in the future.

RESTATEMENT OF CONSOLIDATED FINANCIAL STATEMENTS

The Company restated its consolidated financial statements and other financial information for the year ended December 31, 2008 with respect to the foreign currency translation of certain balances into United States dollars and the reversal of previously recorded net realizable value adjustments on inventory balances. The restatement of prior financial statements may expose the Company to risks associated with litigation, regulatory proceedings and government enforcement actions, including the risk that the SEC may disagree with the manner in which the Company has accounted for and reported the financial impact.

FOREIGN OPERATIONS

All of the Company's property interests are located in Mexico, and are subject to Mexican federal and state laws and regulations. As a result, the Company's mining investments are subject to the risks normally associated with the conduct of business in foreign countries. The Company believes the present attitude of the governments of Mexico and of the States of Chihuahua and Guanajuato (where the Company's projects are located) to foreign investment and mining to be favourable; however, any variation from the current regulatory, economic and political climate could have an adverse effect on the affairs of the Company.

The risks of conducting business in a foreign country may include, among others, labour disputes, invalidation of governmental orders and permits, corruption, uncertain political and economic environments, sovereign risk, war (including in neighbouring states), civil disturbances and terrorist actions, arbitrary changes in laws or policies of particular countries, the failure of foreign parties to honour contractual relations, corruption, foreign taxation, delays in obtaining or the inability to obtain necessary governmental permits, opposition to mining from environmental or other non-governmental organizations, limitations on foreign ownership, limitations on the repatriation of earnings, limitations on gold exports, instability due to economic under-development, inadequate infrastructure and increased financing costs. In addition, the enforcement by the Company of its legal rights to exploit its properties may not be recognized by the government of Mexico or by its court system. These risks may limit or disrupt the Company's operations, restrict the movement of funds or result in the deprivation of contractual rights or the taking of property by nationalization or expropriation without fair compensation.

ENVIRONMENTAL LAWS AND REGULATIONS

The Company's exploration and production activities in Mexico are subject to regulation by governmental agencies under various environmental laws. These laws address emissions into the air, discharges into water, management of waste, management of hazardous substances, protection of natural resources, antiquities and endangered species and reclamation of lands disturbed by mining operations. Environmental legislation in many countries is evolving and the trend has been towards stricter standards and enforcement, increased fines and penalties for non-compliance, more stringent environmental assessments of proposed projects and increasing responsibility for companies and their officers, directors and employees. Compliance with environmental laws and regulations may require significant capital outlays on behalf of the Company and may cause material changes or delays in the Company's intended activities. There can be no assurance that future changes in environmental regulations will not adversely affect the Company's business.

PROPERTY RIGHTS, PERMITS AND LICENSING

The Company's current and anticipated future operations, including further exploration, development activities and expansion or commencement of production on the Company's properties, require certain permits and licenses from various levels of governmental authorities. The Company may also be required to obtain certain property rights to access, or use, certain of its properties in order to proceed to development. There can be no assurance that all licenses, permits or property rights required for the expansion and construction of mining facilities and the conduct of mining operations will be obtainable on reasonable terms or in a timely manner, or at all, that such terms may not be adversely changed, that required extension will be granted, or that the issuance of such licenses, permits or property rights will not be challenged by third parties. Delays in obtaining or a failure to obtain such licenses, permits or property rights or extension thereto; challenges to the issuance of such licenses, permits or property rights, whether successful or unsuccessful; changes to the terms of such licenses, permits or property rights; or a failure to comply with the terms of any such licenses, permits or property rights obtained; could have a material adverse impact on the Company.

UNCERTAINTY OF TITLE

The Company cannot guarantee that title to its properties will not be challenged. Title insurance is generally not available for mineral properties and the Company's ability to ensure that it has obtained secure claim to individual mineral properties or mining concessions may be severely constrained. The Company's mineral properties may be subject to prior unregistered agreements, transfers or claims, and title may be affected by, among other things, undetected defects. A successful challenge to the precise area and location of these claims could result in the Company being unable to operate on its properties as permitted or being unable to enforce its rights with respect to its properties.

COMMODITY PRICE RISK

The profitability of the Company's gold mining operations will be significantly affected by changes in the market prices for gold and silver. Gold and silver prices fluctuate on a daily basis and are affected by numerous factors beyond the Company's control. The supply and demand for gold and silver, the level of interest rates, the rate of inflation, investment decisions by large holders of gold and silver, including governmental reserves, and stability of exchange rates can all cause significant fluctuations in gold and silver prices. Such external economic factors are in turn influenced by changes in international investment patterns and monetary systems, and political developments. The price of gold and silver has fluctuated widely and future serious price declines could cause continued commercial production to be impractical. Depending on the price of gold and silver, cash flow from mining operations may not be sufficient to cover costs of production and capital expenditures. If, as a result of a decline in gold and silver prices, revenues from metal sales were to fall below operating costs, production may be discontinued.

The Company presently does not employ any hedging instruments to manage its commodity price risk.

INTEREST RATE RISK

The Company is exposed to interest rate risk on its variable rate debt. At December 31, 2008, the Company had $37.13 million of variable rate debt which carries an interest rate of LIBOR plus 3.50% for LIBOR loans, prime rate plus 2.50% or one-month BA Schedule I rate plus 3.5% for Prime Rate Loans, or Alternate Base Rate Canada plus 2.5% or one-month LIBOR plus 3.5% for Base Rate Canada Loans. The Company has not entered into any agreements to hedge against unfavourable changes in interest rates, but may actively manage its exposure to interest rate risk in the future.

FOREIGN CURRENCY EXCHANGE RATE RISK

All metal sales revenues for the Company are denominated in US dollars. The Company is primarily exposed to currency fluctuations relative to the US dollar on expenditures that are denominated in Canadian dollars and Mexican pesos, such as payments for labour, operating supplies and property, plant and equipment. These potential currency fluctuations could have a significant impact on production costs and thereby, the profitability of the Company. The Company is also exposed to the impact of currency fluctuations on its monetary assets and liabilities. The Company does not actively manage this foreign currency exposure.

CREDIT RISK

Credit risk relates to accounts receivable and other contracts, and arises from the possibility that any counterparty to an instrument fails to perform. The Company only transacts with highly-rated counterparties and a limit on contingent exposure has been established for each counterparty based on the counterparty's credit rating.

CHANGES IN ACCOUNTING POLICIES

(i) Section 3031, Inventories

Effective January 1, 2008, the Company prospectively implemented Section 3031, *Inventories*, which replaces Section 3030 of the same title. This new standard provides guidance on the determination of cost and requires inventories to be measured at the lower of cost and net realizable value, with more specific guidance on the costs to include in the cost of inventory. Costs such as storage costs and administrative overhead that do not contribute to bringing inventories to their present location and condition are specifically excluded from the cost of inventories and expensed in the period incurred. In addition, the new Section requires that previous write-downs of inventories be reversed when there is a subsequent increase in the net realizable value of the inventories. The recommendations also clarified that major spare parts are to be included in property, plant and equipment. As a result of adopting these recommendations, the Company reclassified $2.7 million of supplies inventories to property, plant, and equipment related to major spare parts on January 1, 2008, and recorded $4.9 in net realizable value write-down reversals throughout the year. Otherwise, this new standard did not have a significant impact on the Company's financial results.

(ii) Section 3862, Financial Instruments – Disclosures and Section 3863, Financial Instruments – Presentation

Effective January 1, 2008, the Company adopted Section 3862, *Financial Instruments – Disclosures*, and Section 3863, *Financial Instruments – Presentation*. These sections replace existing Section 3861, *Financial Instruments – Disclosure and Presentation*. The presentation standards are carried forward unchanged. The disclosure standards introduce new disclosures to improve the information about financial instruments. This standard requires the disclosure of qualitative and quantitative information about the exposure to risks arising from financial instruments including a sensitivity analysis to market risk. The adoption of these standards did not have any effect on the financial position or performance of the Company.

(iii) Section 1535, Capital Disclosures

Effective January 1, 2008, the Company adopted Section 1535, *Capital Disclosures*. This section establishes standards for disclosing information that enables users of financial statements to evaluate the entity's objectives, policies and processes for managing capital. The adoption of this standard did not have any effect on the financial position or performance of the Company.

RECENT CANADIAN ACCOUNTING PRONOUNCEMENTS

The following is an overview of a recent accounting pronouncement that the Company will be required to adopt in future years:

(i) Section 3064, Goodwill and Intangible Assets

In January 2008, the CICA issued Section 3064, *Goodwill and Intangible Assets*, which replaces existing Section 3062, *Goodwill and Other Intangible Assets*. This new section establishes standards for the recognition of internally developed intangible assets. The standards for the recognition and impairment testing of goodwill are carried forward unchanged. This section is applicable to the Company commencing January 1, 2009. The Company does not expect that this section will have a significant impact on the Company's financial statements.

(ii) EIC-173, Credit Risk and the Fair Value of Financial Assets and Financial Liabilities

In January 2009, the Emerging Issues Committee of the CICA issued EIC-173, *Credit Risk and the Fair Value of Financial Assets and Financial Liabilities*. This abstract requires that credit risk be taken into account in determining the fair value of financial instruments and financial liabilities, including derivative instruments. The Company does not expect that this abstract will have a significant impact on the Company's financial statements.

(iii) Section 1582, Business Combinations, Section 1601, Consolidated Financial Statements and Section 1602, Non-controlling Interests

In January 2009, the CICA issued Section 1582, *Business Combinations*, Section 1601, *Consolidated Financial Statements*, and Section 1602, *Non-controlling interests* which replace Section 1581, *Business Combinations* and Section 1600, *Consolidated Financial Statements*. Section 1582 establishes standards for the accounting for business combinations that is equivalent to the business combination accounting standard under International Financial Reporting Standards ("IFRS"). Section 1582 is applicable for business combinations with acquisition dates on or after January 1, 2011. Early adoption of this section is permitted. Section 1601 together with Section 1602 establishes standards for the preparation of consolidated financial statements. Section 1601 is applicable for the Company's interim and annual consolidated financial statements for fiscal years beginning on or after January 1, 2011. Early adoption of this section is permitted. If the Company chooses to early adopt any one of these sections, the other two sections must also be adopted at the same time.

(iv) International Financial Reporting Standards

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 of 2008, the AcSB announced that 2011 is the changeover date for publicly accountable enterprises to use IFRS. 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.

The Company has developed a three phase changeover plan to adopt IFRS by 2011 as follows:

- Phase 1 – Scope and Plan: This first phase involves the development of an initial project plan and structure, the identification of differences between IFRS and existing Canadian GAAP, and an assessment of their applicability and the expected impact on the Company.
- Phase 2 – Design and Build: The second phase includes the detailed review, documentation and selection accounting policy choices relating to each IFRS standard. This phase will also include assessing the impact of the conversion on business activities, including the effect on information technology and data systems, income tax, internal controls over financial reporting, and disclosure controls. In this

phase, accounting policies will be finalized, first-time adoption exemptions and exceptions will be considered, and draft financial statements and note disclosures will be prepared.

- Phase 3 – Implement and Review: The final phase involves the actual implementation of IFRS standards. This phase will involve the finalization of IFRS conversion impacts, approval and implementation of accounting policies, implementation and testing of new processes, systems and controls, and the execution of detailed training where required.

As at December 31, 2008, the first phase of the Company's IFRS project was completed. An IFRS implementation team has been created, and third party advisors have been engaged to assist in this project. The Company determined that the most significant impact of the IFRS conversion will be the implementation of International Accounting Standard 16 – *Property, Plant and Equipment* (IAS 16). This standard requires the componentization of the Company's fixed assets where the useful lives of components are different than the overall asset. In addition, the International Accounting Standards Board currently has an Extractive Activities project underway to develop accounting standards for extractive activities. It is expected that a discussion paper will be released in early 2009, and that final standards will not be issued until after the Company implements IFRS in 2011. Therefore, the Company's accounting policies specific to mining and related activities may be impacted once final IFRS standards are released on this topic, subsequent to IFRS adoption. At this time, the impact on the Company's financial position and results of operation is not reasonably determinable or estimable for any of the IFRS conversion impacts identified.

The Company is in the second phase of the project, and is currently evaluating the specific impacts of IFRS, and developing recommendations and accounting policies. The preliminary timeline is to complete the second phase of the project during 2009 and the third phase during the first half of 2010.

SUBSEQUENT EVENTS

(i) Proposed transaction

On March 12, 2009, the Company announced that it entered into a letter agreement ("letter of intent") with Capital Gold Corporation ("Capital Gold") relating to a proposed acquisition of all of the outstanding shares of Capital Gold by the Company in exchange for the issuance of 0.1028 Gammon Gold shares for each Capital Gold common share outstanding, for a total issuance of approximately 20 million common shares. The all-share transaction is subject to satisfactory completion of due diligence and the negotiation of definitive documentation, receipt of Capital Gold shareholder approval, regulatory approvals and the satisfaction of certain other conditions.

The letter of intent provides that the parties plan to complete their respective technical, operating and financial due diligence and negotiate the terms of a definitive agreement by March 31, 2009. Capital Gold has agreed to a non-solicitation period expiring on March 31, 2009, subject to fiduciary outs, and both parties have agreed to the payment of a break fee to the other party in the amount of $4 million, payable only under certain circumstances.

Capital Gold is a gold production and exploration company and operates the El Chanate gold property in Sonora, Mexico.

On March 31, 2009, discussions regarding the proposed acquisition of Capital Gold were terminated. No break fee will be exchanged.

(ii) Other

Subsequent to year-end, certain employees, consultants, officers and directors of the Company exercised 2,508,400 stock options for total proceeds of $11.5 million. As a result, capital stock increased by $22.4 million and contributed surplus decreased by $10.9 million.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of the Company's consolidated financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. The following is a list of the accounting policies that the Company believes are critical, due to the degree of uncertainty regarding the estimates or assumptions involved and the magnitude of the asset, liability, revenue or expense being reported:

(i) Ore inventories

Finished goods, work-in-process, heap leach ore and stockpile ore are valued at the lower of the average cost or net realizable value (NRV). NRV is the difference between the estimated future realizable gold price based on prevailing and long-term prices, less estimated costs to complete production into a saleable form. The assumptions used in the valuation of work-in-process inventories include estimates of gold contained in the ore stacked on leach pads, assumptions of the amount of gold stacked that is expected to be recovered from the leach pads, the amount of gold in mill circuits and in stockpiles, and an assumption of the gold price expected to be realized when the gold is recovered. Write-downs of ore in stockpiles, ore on leach pads, in-process and finished metal inventories resulting from NRV impairments are reported as a component of current period costs. The primary factors that influence the need to record write-downs include prevailing and long-term gold prices and prevailing costs for production inputs such as labour, fuel and energy, materials and supplies, as well as realized ore grades and actual production levels. When the circumstances that previously caused inventories to be written down below cost no longer exist or when there is clear evidence of an increase in net realizable value because of changed economic circumstances, the amount of the write-down or a portion thereof is reversed so that the new carrying amount is the lower of the cost and the revised net realizable value. The reversal is limited to the amount of the original write-down for inventory still on hand.

Ore on leach pads is ore that is placed on pads where it is saturated with a chemical solution that dissolves the gold contained in the ore. Costs are attributed to the leach pads based on current mining costs, including applicable depletion and amortization relating to mining operations, incurred up to the point of placing the ore on the pad. Costs are removed from the leach pad based on the average cost per recoverable ounce of gold on the leach pad as the gold is recovered. Estimates of recoverable gold on the leach pads are calculated from the quantities of ore placed on the pads, the grade of ore placed on the leach pads and an estimated percentage of recovery. Timing and ultimate recovery of gold contained on leach pads can vary significantly from the estimates. The quantities of recoverable gold placed on the leach pads are reconciled to the quantities of gold actually recovered (metallurgical balancing), by comparing the grades of ore placed on the leach pads to actual ounces recovered. The nature of the leaching process inherently limits the ability to precisely monitor inventory levels. As a result, the metallurgical balancing process is constantly monitored and the engineering estimates are refined based on actual results over time. The ultimate recovery of gold from a pad will not be known until the leaching process is completed.

The allocation of costs to ore in stockpiles, ore on leach pads and in-process inventories and the determination of NRV involve the use of estimates. There is a high degree of judgment in estimating future costs, future production levels, proven and probable mineral reserve estimates, gold and silver prices, and the ultimate estimated recovery for ore on leach pads. There can be no assurance that actual results will not differ significantly from estimates used in the determination of the carrying value of inventories.

(ii) Mineral reserves and resources used to measure depletion and amortization

The Company records depletion and amortization expense based on the estimated useful economic lives of long-lived assets. Property, plant and equipment are amortized on a straight-line basis over their estimated useful lives. Mining interests are amortized using the units of production method over proven and probable reserves of the mine and the portion of mineralization expected to be classified as reserves. Changes in reserve and resources estimates are generally calculated at the end of each year and cause amortization expense to increase or decrease prospectively. The estimation of quantities of reserves and resources is complex, requiring significant subjective assumptions that arise from the evaluation of geological, geophysical, engineering and economic data for a given ore body. This data could change over time as a result of numerous factors, including new information gained from development activities, evolving production history and a reassessment of the viability of production under different economic conditions. Changes in data and/or assumptions could cause reserve and resources estimates to substantially change from period to period. Actual production could differ from expected based on reserves and resources, and an adverse change in gold prices could make a reserve or resource uneconomic to mine. Variations could also occur in actual ore grades and gold and silver recovery rates from estimates. A key trend that could reasonably impact reserves and resources estimates is rising market mineral prices, because the mineral price assumption is closely related to the trailing three-year average market price. As this assumption rises, this could result in an upward revision to reserves and resources estimates as material not previously classified as a reserve or resource becomes economic at higher gold prices.

Effective April 1, 2008, the Company changed its estimate of the useful lives of its mines to be based on proven and probable reserves of the mine and the portion of mineralization expected to be classified as reserves. Previously, the Company estimated the useful life based on proven and probable reserves to be mined. During the second quarter, the Company reviewed the appropriateness of its current estimate, and determined that based on the characteristics of the current reserves and resources at Ocampo and El Cubo, the estimated useful life is more accurately reflected by proven and probable reserves and the portion of mineralization expected to be classified as reserves. Consistent with Section 1506, *Accounting Changes*, the change in estimate was applied prospectively. The impact of this change on the Company's financial results for the nine months ended December 31, 2008 was to reduce amortization and depletion by approximately $4.6 million, and to reduce inventories by approximately $0.4 million.

(iii) Goodwill and long-lived assets

Goodwill is not amortized and is assessed for impairment at the reporting unit level on at least an annual basis. Any potential goodwill impairment is identified by comparing the fair value of a reporting unit to its carrying value. If the fair value of the reporting unit exceeds its carrying value, goodwill is considered not to be impaired. If the carrying value of the reporting unit exceeds its fair value, a potential goodwill impairment has been identified and must be quantified by comparing the estimated fair value of the reporting unit's goodwill to its carrying value. Any goodwill impairment will result in a reduction in the carrying value of goodwill on the consolidated balance sheet and in the recognition of a non-cash impairment charge in operating income.

The Company periodically assesses the recoverability of long-lived assets when there are indications of potential impairment. In performing these analyses, the Company considers such factors as current results, trends and future prospects, current market value and other economic factors. A substantial change in estimated undiscounted future cash flows for these assets could materially change their estimated fair values, possibly resulting in additional impairment.

(iv) Post-employment and post-retirement benefits

Certain estimates and assumptions are used in actuarially determining the Company's defined pension and employee future benefit obligations. Significant assumptions used to calculate the pension and employee future benefit obligations are the discount rate and long-term compensation rate. These assumptions depend on various underlying factors such as economic conditions, investment performance, employee demographics and mortality rates. These assumptions may change in the future and may result in material changes in the pension and employee benefit plans expense.

(v) Future income taxes and valuation allowances

The Company is periodically required to estimate the tax basis of assets and liabilities. Where applicable tax laws and regulations are either unclear or subject to varying interpretations, it is possible that changes in these estimates could occur that materially affect the amounts of future income tax assets and liabilities recorded in the financial statements. Changes in future tax assets and liabilities generally have a direct impact on earnings in the period of changes.

Each period, the Company evaluates the likelihood of whether some portion or all of each future tax asset will not be realized. This evaluation is based on historic and future expected levels of taxable income, the pattern and timing of reversals of taxable temporary timing differences that give rise to future tax liabilities, and tax planning initiatives. Levels of future taxable income are affected by, among other things, market gold prices, production costs, quantities of proven and probable gold reserves, interest rates and foreign currency exchange rates. If it is determined that it is more likely than not (a likelihood of more than 50%) that all or some portion of a future tax asset will not be realized, a valuation allowance is recorded. Changes in valuation allowances are recorded as a component of income tax expense or recovery for each period.

(vi) Asset retirement obligations

Asset retirement obligations ("AROs") arise from the acquisition, development, construction and normal operation of mining property, plant and equipment, due to government controls and regulations that protect the environment and public safety on the closure and reclamation of mining properties. The Company records the fair value of an ARO in the financial statements when it is incurred, and capitalizes this amount as an increase in the carrying amount of the related asset. The fair values of AROs are measured by discounting the expected cash flows using a discount factor that reflects the credit-adjusted risk-free rate of interest. The Company prepares estimates of the timing and amounts of expected cash flows when an ARO is incurred, which are updated to reflect changes in facts and circumstances. In the future, changes in regulations, laws or enforcement could adversely affect operations; and any instances of non-compliance with laws or regulations that result in fines or injunctions or delays in projects, or any unforeseen environmental contamination at, or related to, the mining properties could result in significant costs.

The principal factors that can cause expected cash flows to change are: the construction of new processing facilities; changes in the quantities of material in reserves and a corresponding change in the life of mine plan; changing ore characteristics that ultimately impact the environment; changes in water quality that impact the extent of water treatment required; and changes in laws and regulations governing the protection of the environment. In general, as the end of the mine life nears, the reliability of expected cash flows increases, but earlier in the mine life, the estimation of an ARO is inherently more subjective. Significant judgments and estimates are made when estimating the fair value of AROs. Expected cash flows relating to AROs could occur over periods up to 20 years and the assessment of the extent of environmental remediation work is highly subjective. Considering all of these factors that go into the determination of an ARO, the fair value of AROs can materially change over time.

FINANCIAL INSTRUMENTS

The Company can manage its exposure to fluctuations in commodity prices, interest rates and foreign exchange rates by entering into derivative financial instrument contracts. Gammon's exposure with respect to commodity prices, interest rates and foreign exchange is described under the section entitled Risks and Uncertainties. As at December 31, 2008, Gammon had not entered into any derivative contracts for the purpose of hedging exposure to commodity prices, interest rates and foreign exchange rates.

CONTROLS AND PROCEDURES

(i) Evaluation of Disclosure Controls and Procedures (as restated)

The Company maintains disclosure controls and procedures designed to ensure that information required to be disclosed in annual filings, interim filings or other reports filed or submitted under provincial and territorial securities legislation or reports filed or submitted under the U.S. Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the applicable time periods, and that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosures. As of December 31, 2008 an evaluation was carried out, under the supervision of and with the participation of management, including the Chief Executive Officer and the Chief Financial Officer, of the effectiveness of disclosure controls and procedures as defined in Rule 13a-15(e) under the U.S. Securities Exchange Act of 1934 and in National Instrument 52-109 under the Canadian Securities Administrators Rules and Policies. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as at December 31, 2008.

In connection with the restatement of the December 31, 2008 financial statements, management, with the participation of the Chief Executive Officer and the Chief Financial Officer, has re-evaluated the effectiveness of disclosure controls and procedures. Based on the reassessment, the Chief Executive Officer and Chief Financial Officer have concluded that as of December 31, 2008, the Company's disclosure controls and procedures were not effective because of the material weakness in internal controls over financial reporting described below.

(ii) Management's Report on Internal Control Over Financial Reporting (as restated)

Management, including the Chief Executive Officer and Chief Financial Officer, is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rule 13a-15(e) under the U.S. Securities Exchange Act of 1934 and in National Instrument 52-109 under the Canadian Securities Administrators Rules and Policies. Management is furthermore responsible for the evaluation of the effectiveness of internal control over financial reporting for the year ended December 31, 2008. The Company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian generally accepted accounting principles and reconciled to US GAAP. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements.

As of December 31, 2008, management evaluated the effectiveness of the Company's internal control over financial reporting. In making this evaluation, management used the criteria set forth in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on Gammon's management assessment, management concluded that the Company's design and operating effectiveness of internal control over financial reporting was effective as at December 31, 2008. No material weaknesses were identified by management during this evaluation.

Based upon its assessment, management concluded that, as of December 31, 2008, the Company's internal control over financial reporting was effective. However, during the preparation of the June 30, 2009 interim financial statements the Company determined that a restatement of its previously issued financial statements was necessary. As a result of the financial statement restatement, the Company reassessed its internal control over financial reporting and determined that a material weakness existed at December 31, 2008.

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the Company's annual or interim financial statements will not be prevented or detected on a timely basis. The material weakness in internal control over financial reporting as of December 31, 2008 existed as management did not maintain effective monitoring controls and procedures over the foreign currency translation of selected accounts or the recognition of net realizable value adjustments on inventory balances. Specifically, management did not maintain effective monitoring controls and procedures to provide reasonable assurance that inventory balances were translated in accordance with GAAP, or that previously recognized net realizable value adjustments were reversed as required upon initial adoption of Section 3031, *Inventories*. This control deficiency resulted in the restatement of the consolidated financial statements for the year ended December 31, 2008.

As a result of the aforementioned material weakness as of December 31, 2008, management has revised its previously reported assessment of the effectiveness of internal control over financial reporting and have concluded that, as of December 31, 2008, the Company's internal control over financial reporting was not effective.

KPMG LLP, an independent registered public accounting firm has audited the effectiveness of the Company's internal control over financial reporting as at December 31, 2008.

(iii) Remediation of Material Weakness in Internal Control over Financial Reporting

Management has engaged in, and continues to engage in, efforts to address the material weakness in internal control over financial reporting identified above, by performing a thorough review of the Company's translation of foreign currency balances in accordance with GAAP and by reviewing previously recorded net realizable value adjustments to ensure all appropriate reversals are recorded. Management will also amend period close procedures to include procedures to monitor foreign currency translation and inventory net realizable value adjustments.

(iv) Change in Internal Control over Financial Reporting

There were no changes in the Company's internal control over financial reporting that occurred during the three months ended December 31, 2008 that materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

CAUTIONARY NOTE TO U.S. INVESTORS

Cautionary Note to U.S. Investors concerning estimates of Measured and Indicated Resources: We advise U.S. investors that while such terms are recognized and permitted under Canadian regulations, the U.S. Securities and Exchange Commission does not recognize them. The term "resources" does not equate to the term "reserves", and U.S. investors are cautioned not to assume that any part or all of the mineral deposits in these categories will ever be converted into reserves.

Cautionary Note to U.S. Investors concerning estimates of Inferred Resources: We advise U.S. investors that while such term is recognized and permitted under Canadian regulations, the U.S. Securities and Exchange Commission does not recognize it. "Inferred resources" have a great amount of uncertainty as to their existence, and great uncertainty as to their economic and legal feasibility. It cannot be assumed that all or any part of an inferred mineral resource will ever be upgraded to a higher category. Under Canadian rules estimates of inferred mineral resources may not form the basis of feasibility or other economic studies. U.S. investors are cautioned not to assume that any part or all of an inferred resource exists, or is economically or legally mineable.

The consolidated financial statements of the Company have been prepared by management in accordance with Canadian generally accepted accounting principles ("GAAP") (see Note 2: *Summary of Significant Accounting Policies* to the financial statements), which differ in certain material respects from accounting principles generally accepted in the United States of America ("U.S. GAAP"). Differences between GAAP and U.S. GAAP that are applicable to the Company are described in the Company's 40-F form filed with the U.S. Securities and Exchange Commission, which is available at www.edgar.com. The Company's reporting currency is in United States dollars unless otherwise noted.

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

Certain information regarding the Company contained herein may constitute forward-looking statements within the meaning of applicable securities laws. Forward-looking statements are subject to a variety of risks and uncertainties which could cause actual events or results to differ from those reflected in the forward-looking statements. Should one or more of these risks and uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those described in forward looking statements. Specific reference is made to "Risk Factors" in the Company's Annual Information Form and 40F Report. Forward-looking statements may include estimates, plans, expectations, opinions, forecasts, projections, guidance or other statements that are not statements of fact including, without limitation, statements regarding potential mineralization and reserves, including the impact of any future exploration on reserve estimates; expectations regarding the timing and extent of production at the Company's projects; estimates regarding the future costs related to exploration at the Company's projects; the nature and availability of additional funding sources; and future plans and objectives of the Company. In some cases, you can identify forward-looking statements by the use of words such as may, will, should, could, expect, plan, intend, anticipate, believe, estimate, predict, potential or continue or the negative or other variations of these words, or other comparable words or phrases. Although the Company believes that the expectations reflected in such forward-looking statements are reasonable, it can give no assurance that such expectations will prove to have been correct. Important factors that could cause actual results to differ materially from the Company's expectations include, among others, risks related to international operations, including political turmoil and limited local infrastructure to support large scale mining operations; the actual results of current exploration activities; conclusions of economic evaluations and changes in project parameters as plans continue to be refined; and fluctuations in future prices of gold and silver. These factors are set out in the Company's Annual Information Form. The Company's forward-looking statements are expressly qualified in their entirety by this cautionary statement.

Gammon Gold Inc.

Restated Consolidated Financial Statements (Note 2)

December 31, 2008 and 2007

(in United States Dollars, unless otherwise stated)

Gammon Gold Inc.

Consolidated Balance Sheets

(in thousands of United States Dollars)

At December 31	2008 (as restated, Note 2)	2007
ASSETS		
Current		
Cash and cash equivalents	$ 3,258	$ 3,709
Receivables		
Commodity taxes	8,762	10,240
Trade / other	4,932	1,740
Inventories (Note 6)	60,128	51,586
Prepaids and deposits	2,389	2,250
	79,469	69,525
Deposits on property, plant and equipment	4,930	5,395
Other long-term assets (Note 3 (q))	4,653	192
Long-term ore stockpiles (Note 6)	2,201	-
Mining interests and property, plant and equipment (Note 7)	597,126	572,041
Goodwill	106,799	106,799
	$ 795,178	$ 753,952
LIABILITIES		
Current		
Payables and accruals	$ 30,457	$ 17,279
Current portion of long-term debt and capital leases and other long-term obligations (Notes 8 and 9)	30,861	33,073
	61,318	50,352
Long-term debt and capital leases (Note 8)	7,991	1,334
Other long-term obligations (Note 9)	4,677	-
Asset retirement obligations (Note 10)	3,622	2,991
Employee future benefits (Note 11)	1,659	3,746
Future income taxes (Note 12)	77,301	108,879
	156,568	167,302
SHAREHOLDERS' EQUITY (Note 13)		
Capital stock	719,426	699,512
Contributed surplus	33,288	42,373
Deficit	(120,538)	(161,669)
Accumulated other comprehensive income	6,434	6,434
	638,610	586,650
	$ 795,178	$ 753,952

Nature of operations and going concern assumption (Note 1)
Commitments and contingencies (Note 14)
Subsequent events (Note 22)

Signed on behalf of the Board: *"Signed"* *Fred George, Director* *"Signed"* *George Elliott, Director*

Gammon Gold Inc.

Consolidated Statements of Operations and Comprehensive Income / (Loss)

(in thousands of United States Dollars except per share data)

For the years ended December 31	2008 (as restated, Note 2)	2007
Revenue from mining operations	$ 212,522	$ 152,059
Expenses		
Production costs, excluding amortization and depletion	127,651	144,623
Refining costs	1,662	1,510
General and administrative	29,945	24,156
Amortization and depletion	40,380	43,392
	199,638	213,681
Earnings / (loss) before other items	12,884	(61,622)
Interest on long-term debt	(1,936)	(3,897)
Foreign exchange gain / (loss)	18,942	(8,933)
Interest and other income	410	772
	17,416	(12,058)
Earnings / (loss) before income taxes	30,300	(73,680)
Future income tax (recovery) / expense (Note 12)	(10,738)	27,634
Current tax expense	1,044	-
	(9,694)	27,634
Net earnings / (loss) and comprehensive income / (loss)	$ 39,994	$ (101,314)
Earnings / (loss) per share (Note 15)		
Basic	$ 0.34	$ (0.90)
Diluted	$ 0.33	$ (0.90)
Weighted average shares outstanding (Note 15)		
Basic	119,110,568	113,176,605
Diluted	120,812,872	113,176,605

See accompanying notes to the consolidated financial statements.

Gammon Gold Inc.

Consolidated Statements of Cash Flows

(in thousands of United States Dollars)

For the years ended December 31	2008 (as restated, Note 2)	2007
OPERATING ACTIVITIES		
Net earnings / (loss)	$ 39,994	$ (101,314)
Items not affecting cash (Note 16)	8,790	85,646
Change in non-cash operating working capital (Note 16)	7,149	(18,524)
	55,933	(34,192)
INVESTING ACTIVITIES		
Decrease / (increase) in deposits on property, plant and equipment	465	(4,345)
Expenditures on mining interests and property, plant & equipment	(66,841)	(69,142)
	(66,376)	(73,487)
FINANCING ACTIVITIES		
Repayment of capital lease obligation	(2,551)	(2,500)
Proceeds from long-term debt	13,880	36,973
Repayment of long-term debt	(8,109)	(130,624)
Net proceeds from issuance of capital stock	-	170,026
Proceeds from exercise of stock options	6,772	33,439
	9,992	107,314
Net decrease in cash and cash equivalents	(451)	(365)
Cash and cash equivalents, beginning of year	3,709	4,074
Cash and cash equivalents, end of year	$ 3,258	$ 3,709

Cash and cash equivalents is comprised of the following:

	2008	2007
Cash	$ 3,258	$ 3,601
Restricted cash	-	108
	$ 3,258	$ 3,709

See accompanying notes to the consolidated financial statements.

Gammon Gold Inc.

Consolidated Statements of Shareholders' Equity

(in thousands of United States Dollars)

For the years ended December 31	2008 (as restated, Note 2)	2007
Capital stock		
Balance, beginning of year	$ 699,512	$ 463,333
For cash pursuant to exercise of stock options	6,772	33,439
Fair value of share-based compensation	13,142	32,714
Public offering	-	178,120
Share issuance costs	-	(8,094)
Balance, end of year	$ 719,426	$ 699,512
Contributed surplus		
Balance, beginning of year	$ 42,373	$ 71,747
Fair value of share-based compensation	(13,142)	(32,714)
Forfeitures of stock options	(429)	(1,848)
Stock option expense	4,486	5,188
Balance, end of year	$ 33,288	$ 42,373
Deficit		
Balance, beginning of year	$ (161,669)	$ (60,355)
Application of new inventory standard (Note 2)	1,137	-
Net earnings / (loss)	39,994	(101,314)
Balance, end of year	(120,538)	(161,669)
Accumulated other comprehensive income	6,434	6,434
Total deficit and accumulated other comprehensive income	$ (114,104)	$ (155,235)
Total shareholders' equity	$ 638,610	$ 586,650

See accompanying notes to the consolidated financial statements.

1. Nature of operations and going concern assumption

Gammon Gold Inc. (the "Company") is a publicly traded company engaged in the mining, development, exploration and acquisition of resource properties. The Company's common shares are listed on the Toronto Stock Exchange (TSX: GAM) and the New York Stock Exchange (NYSE: GRS).

These financial statements have been prepared on the basis of accounting principles applicable to a going concern, which assume that the Company will continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities in the normal course of operations. The future of the Company is dependent on its ability to raise capital, its ability to generate sufficient cash flow from the Ocampo and El Cubo properties to make required debt repayments and fund capital expenditures, fluctuations in foreign currency exchange rates, and the market price of gold and silver. During the year, the Company has generated positive earnings and cash flows from operations and renegotiated its credit facility. The Company has forecasted continuing positive earnings and cash flows in future years, thereby making the going concern assumption appropriate. If the going concern assumption were not appropriate for these financial statements then adjustments would be necessary to the carrying values of assets and liabilities, the reported revenues and expenses, and the balance sheet classifications used.

2. Restatement of consolidated financial statements

During the preparation of the June 30, 2009 interim consolidated financial statements, the Company determined that certain items in the December 31, 2008 consolidated financial statements had been incorrectly translated into the Company's functional currency, the United States dollar, and that upon initial adoption of Section 3031, *Inventories*, on January 1, 2008, a reversal should have been recorded for previously recognized net realizable value adjustments.

Foreign currency translation:

In the Company's Mexican operations, inventory is initially recorded in Mexican pesos. When translating these balances to the US dollar, the Company used the current exchange rate instead of the rate in effect when the costs were incurred. The impact of this adjustment was to change the inventory balances and production costs in each period. There was no income tax effect as a result of this adjustment. There was no material impact of these changes on the opening deficit or accumulated other comprehensive income or on amounts reported prior to 2008.

Net realizable value adjustments:

Section 3031, *Inventories*, requires that when the net realizable value of inventory increases, previously recorded adjustments to reduce inventory to its net realizable value are reversed. On implementation of this section on January 1, 2008 the Company did not identify that there were previous net realizable value adjustments that were required to be reversed. The effect of this restatement is to increase inventories by $1.6 million at January 1, 2008, with a $1.1 million decrease to deficit and $0.5 million increase to future income tax liabilities.

Other impacted amounts presented throughout these restated consolidated financial statements and accompanying notes have been amended as appropriate.

(in thousands of United States Dollars unless otherwise noted)

The following table outlines the impact of the adjustment by financial statement line item in the Company's consolidated balance sheet, consolidated statement of operations, and consolidated statement of cash flow as at and for the period ended December 31, 2008. Only those line items impacted by the restatement have been disclosed.

	Previously reported	Foreign currency adjustments	Net realizable value adjustments	As restated
Consolidated balance sheet at December 31, 2008:				
Inventories	$ 49,318	$ 9,231	$ 1,579	$ 60,128
Long term ore stockpiles	2,119	82	-	2,201
Deficit	(131,430)	9,313	1,579	(120,538)
Consolidated Statement of Operations:				
Production costs, excluding amortization and depletion	$ 127,024	$ 627	$ -	$ 127,651
Amortization, depletion and accretion	40,715	(335)	-	40,380
Foreign exchange gain	9,337	9,605	-	18,942
Future income tax recovery	(10,296)		(442)	(10,738)
Net earnings	30,239	9,313	442	39,994
Consolidated Statement of Cash Flows:				
Net earnings	$ 30,239	$ 9,313	$ 442	$ 39,994
Amortization, depletion and accretion	40,704	(335)	-	40,369
Unrealized foreign exchange gain	(13,582)	(10,165)	-	(23,747)
Future income tax recovery	(10,296)	-	(442)	(10,738)
Change in inventories	(9,416)	1,187	-	(8,229)
Total operating cash flow	55,933	-	-	55,933

3. Summary of significant accounting policies

(a) Basis of presentation

The consolidated financial statements have been prepared by the Company in accordance with Canadian generally accepted accounting principles, using the following significant accounting policies. These financial statements are prepared in United States dollars, unless otherwise indicated.

(b) Consolidation

These consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, Gammon Lake Resources (NS) Incorporated, Gammon Lake de Mexico S.A. de C.V., Gammon Lake Resources (USA) Inc., Gammon Lake Holdings Inc., Mexgold Resources Inc., Compania Minera El Cubo S.A. de C.V., and Metales Interamericanos S.A de C.V. All significant intercompany balances and transactions have been eliminated on consolidation.

(c) Foreign currency translation

The functional currency of the Company's operations is the United States dollar ("US dollar"). Non-US dollar balances are translated into US dollars as follows: monetary assets and liabilities are translated to US dollars at the period-end exchange rate; non-monetary assets and liabilities are translated at the rate prevailing at the time of the transaction; and revenue and expense transactions are translated using average exchange rates, except for expenses that relate to non-monetary assets and liabilities, which are translated at the same historical exchange rate as the related asset or liability. Translation gains or losses are recognized in earnings in the period in which they occur.

(d) Use of estimates

The presentation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts for assets and liabilities and disclosure of contingent liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. The significant areas requiring the use of management estimates and assumptions relate to mineral reserves that are the basis for future cash flow estimates utilized in impairment calculations; depletion and amortization calculations; estimates of recoverable gold and other minerals in current and long-term stockpile and leach pad inventories; estimates of fair value for certain reporting units and asset impairment; write-downs of inventory to net realizable value; post-employment, post-retirement and other employee future benefits; valuation allowances for future income tax assets; asset retirement obligations; reserves for contingencies and litigation; and the fair value and accounting treatment of financial instruments. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Accordingly, actual results could differ from those estimates.

(e) Revenue recognition

Revenue from the sale of gold, silver, and doré bars is recognized when persuasive evidence of a sale arrangement exists, the risks and rewards of ownership passes to the purchaser including delivery of the product, the selling price is fixed or determinable, and collectibility is reasonably assured. Sales of the doré bars are recorded at estimated values, and are further adjusted based upon final quality assessment and quotations.

(f) Cash and cash equivalents

The Company considers deposits in banks, certificates of deposits, and short-term investments with original maturities of three months or less from the acquisition date as cash and cash equivalents.

(g) Inventories

Supplies inventory

Supplies inventory consists of mining supplies and consumables used in the operation of the mines, and is valued at the lower of average cost and net realizable value.

Current and long-term ore stockpiles inventory

Stockpiles represent ore that has been mined and is available for further processing. Stockpiles are measured by estimating the number of tonnes added and removed from the stockpile, the number of contained ounces (based on assay data) and the estimated metallurgical recovery rates (based on the expected processing method). Stockpile ore tonnages are verified by periodic surveys. Costs are allocated to stockpiles based on the current mining cost per tonne incurred up to the point of stockpiling the ore, including applicable overhead, depletion and amortization relating to mining operations, and removed at the average cost per tonne. Ore stockpiles inventory is measured at the lower of cost and net realizable value.

Ore in process inventory

The recovery of gold and silver is achieved through a milling and heap leaching process. Costs are added to ore on leach pads and in the mill based on current mining costs, including applicable depletion and amortization relating to mining operations. Costs are removed from ore on leach pads and in the mill as ounces are recovered, based on the average cost per ounce of gold and silver in ore in process inventory. Ore in process inventory is measured at the lower of cost and net realizable value.

Finished goods

Finished goods inventory consists of gold, silver, and doré bars, and is valued at the lower of cost and net realizable value.

For all ore inventories, net realizable value is calculated as the difference between the estimated future metal revenue based on prevailing and long-term metal prices and estimated costs to complete production into a saleable form.

(h) Mineral interests

The carrying value of mineral interests represents the accumulated costs to date related to the acquisition, exploration and development of the Company's producing mineral properties. Production stage mining interests are amortized over the life of the mine using the unit-of-production method based on estimated proven and probable reserves of the mine and the portion of mineralization expected to be classified as reserves, or on a straight-line basis over the term of the lease.

The expected useful lives used in amortization and depletion calculations are determined based on the facts and circumstances associated with the mining interest. Any changes in estimates of useful lives are accounted for prospectively from the date of the change.

Mining costs associated with stripping activities in an open pit mine are capitalized if they represent a betterment to the mineral property in that access is gained to sources of reserves that will be produced in future periods that would otherwise not have been accessible. Capitalized stripping costs are amortized over the life of the deposit benefiting from the stripping using the unit-of-production method based on estimated proven and probable reserves of the mine and the portion of mineralization expected to be classified as reserves.

(i) Property, plant and equipment and amortization

Property, plant and equipment are recorded at cost. Amortization is calculated on the straight-line basis over the estimated useful lives of the assets, as follows:

Equipment under capital lease	*lease term*	Vehicles	*4 years*
Heavy equipment	*5-10 years*	Buildings	*20 years*
Other equipment	*8-9 years*	Office equipment	*3-10 years*
Processing plant	*8-9 years*		

(j) Impairment of long-lived assets

The Company assesses the impairment of long-lived assets, which consist primarily of mining interests and property, plant and equipment, whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. An impairment loss will be recognized if the carrying amount of a long-lived asset is not recoverable. The carrying amount of a long-lived asset is not recoverable if the carrying amount exceeds the sum of the undiscounted cash flows expected to result from its use and eventual disposition. The impairment loss to be recognized is measured as the amount by which the carrying amount of the long-lived asset exceeds its fair value.

Annually, or when events or circumstances indicate that the carrying amount may not be recoverable, the Company reviews the carrying value of its mining interests. The recoverability of the book value of each property is assessed for indicators of impairment such as adverse changes to the estimated recoverable ounces of gold, estimated future commodity prices, and estimated expected future operating costs, capital expenditures and reclamation expenditures. If it is determined that the deferred costs related to a property are not recoverable over its productive life, those costs will be written down to fair value as a charge to operations in the period in which the determination is made. The amounts at which mining interests and the related deferred costs are recorded do not necessarily reflect present or future values.

(k) Goodwill and goodwill impairment

Acquisitions of businesses are accounted for using the purchase method whereby assets and liabilities acquired are recorded at their fair values as of the date of acquisition and any excess of the purchase price over such fair value is recorded as goodwill. Goodwill is identified and allocated to reporting units by preparing estimates of the fair value of each reporting unit and comparing this amount to the fair value of assets and liabilities in the reporting unit.

The Company evaluates, on an annual basis, the carrying amount of goodwill to determine whether current events and circumstances indicate that such carrying amount may no longer be recoverable. To accomplish this, the Company compares the fair value of its reporting units to their carrying amounts. Fair value is calculated as an appropriate multiple of projected future net earnings. If the carrying amount exceeds the fair value, the Company compares the implied fair value of the reporting unit's goodwill to its carrying amount, and any excess of the carrying amount over the fair value is charged to operations. Assumptions underlying fair value estimates are subject to significant risks and uncertainties.

(l) Asset retirement obligations

The Company's mining and exploration activities are subject to various governmental laws and regulations relating to the protection of the environment. These environmental regulations are continually changing, and the Company intends to make future expenditures to comply with such laws and regulations. The Company is required to record a liability and corresponding asset, for the estimated present value of future cash flows associated with site closure and reclamation when the liability is incurred and a reasonable estimate of the fair value can be made. The present value of future cash flows is determined using the credit adjusted risk free rate. These asset retirement costs are amortized over the life of the related assets on a straight-line basis. At the end of each period, the liability is increased to reflect the passage of time and changes in the estimated future cash flows underlying any initial fair value measurements.

(m) Share-based compensation

The Company uses the fair value method of accounting for employee share-based compensation and other share-based payments made in exchange for goods and services. Under this method, the Company recognizes a compensation expense for all awards made to employees and non-employees, based on the fair value of the options on the date of grant, which is determined by using an option pricing model. The fair value of the options is expensed over the vesting period of the options. The Company's stock option plan is described in Note 13.

(n) Income taxes

Income taxes are calculated using the asset and liability method. Under this method, current income taxes are recognized for the estimated income taxes payable for the current period. Future income tax assets and liabilities are determined based on the difference between the financial reporting and tax basis of assets and liabilities and on unclaimed losses carried forward. Future income tax assets and liabilities are measured using the enacted or substantively enacted tax rates that will be in effect when the differences are expected to reverse or when unclaimed losses are expected to be utilized. A valuation allowance is recognized to the extent that the recoverability of future income tax assets is not considered to be more likely than not.

(o) Earnings / (loss) per common share

Earnings / (loss) per common share is calculated based on the weighted average number of common shares outstanding for the period. Diluted earnings / (loss) per common share considers the potential exercise of all outstanding options using the treasury stock method. This method assumes that proceeds received from the exercise of the in-the-money stock options and warrants are used to repurchase shares at the average market price for the year.

(p) Employee future benefits

The Company has defined benefit pension plans that provide benefits to certain of its employees. The cost of the accrued benefit liability for pension benefits earned by employees is actuarially determined using the projected benefit method prorated on service and management's best estimate of salary escalation and retirement ages.

Actuarial gains/losses arise from changes in actuarial assumptions used to determine the accrued benefit liability. The excess of the net actuarial gain / (loss) over 10% of the greater of the accrued benefit liability and the fair value of plan assets is amortized over the average remaining service period of active employees.

(q) Other long-term assets

Included in other long-term assets is the costs of an eight-year consultancy agreement with a third party, whereby the Company will receive assistance with strategic planning, business development, procurement and authorization of land, employer-employee relations, community and government relations, and environmental relations. Amortization of the contract cost is calculated on a straight-line basis over the term of the agreement. See Note 8 for further details on the related obligation. In 2007, other long-term assets related to deferred compensation arising on the Mexgold Resources Inc. acquisition in 2006.

(in thousands of United States Dollars unless otherwise noted)

(r) Financial Instruments

The Company's financial instruments are classified as follows:

Asset / Liability	Classification	Measurement
Cash and cash equivalents	Held-for-trading	Fair value
Restricted cash	Held-for-trading	Fair value
Receivables	Loans and receivables	Amortized cost
Payables and accruals and other long-term obligations	Other financial liabilities	Amortized cost
Long-term debt and capital leases	Other financial liabilities	Amortized cost

Transaction costs other than those related to financial instruments classified as held-for-trading, which are expensed as incurred, are added to the fair value of the financial asset or financial liability on initial recognition and amortized using the effective interest rate method.

Fair values are based on quoted market prices where available from active markets, otherwise fair values are estimated using a variety of valuation techniques and models.

All derivative instruments, including embedded derivatives, are recorded on the balance sheet at fair value unless exempted from derivative treatment as a normal purchase and sale. All changes in fair value are recorded in earnings unless cash flow hedge accounting is used, in which case changes in fair value are recorded in other comprehensive income. There were no embedded derivatives for the years ended December 31, 2008 and 2007.

(s) Hedges

Hedging relationships that meet documentation requirements, and can be proven to be effective both at the inception and over the term of the relationship qualify for hedge accounting. Specifically, in a cash flow hedge, the effective portion of the change in the fair value of hedging derivatives is recorded in other comprehensive income and reclassified to earnings in the period in which the hedged item is realized. Any ineffective portion of the change in fair value of hedging derivatives is recognized in net earnings in the reporting period. Where documentation and effectiveness requirements are not met, the derivatives are classified as held for trading and the change in fair value is recognized in earnings in the reporting period.

Fair value hedges and the related hedged items are recognized on the balance sheet at fair value with any changes in fair value recognized in net income. To the extent the fair value hedge is effective, the changes in fair value of the hedge and the hedged item will offset each other.

The Company did not enter into any hedging relationships in the current year.

(t) Recent accounting pronouncements

The following is an overview of recent accounting pronouncements that the Company will be required to adopt in future years:

(i) Section 3064, Goodwill and Intangible Assets

In January 2008, the CICA issued Section 3064, *Goodwill and Intangible Assets*, which replaces existing Section 3062, *Goodwill and Other Intangible Assets*. This new section establishes standards for the recognition of internally developed intangible assets. The standards for the recognition and impairment testing of goodwill are carried forward unchanged. This section is applicable to the Company commencing January 1, 2009. The Company does not expect that this Section will have a significant impact on the Company's financial statements.

(ii) EIC-173, Credit Risk and the Fair Value of Financial Assets and Financial Liabilities

In January 2009, the Emerging Issues Committee of the CICA issued EIC-173, *Credit Risk and the Fair Value of Financial Assets and Financial Liabilities*. This abstract requires that credit risk be taken into account in determining the fair value of financial instruments and financial liabilities, including derivative instruments. The Company does not expect that this abstract will have a significant impact on the Company's financial statements.

(iii) Section 1582, Business Combinations, Section 1601, Consolidated Financial Statements and Section 1602, Non-controlling Interests

In January 2009, the CICA issued Section 1582, *Business Combinations*, Section 1601, *Consolidated Financial Statements*, and Section 1602, *Non-controlling interests* which replace Section 1581, *Business Combinations* and Section 1600, *Consolidated Financial Statements*. Section 1582 establishes standards for the accounting for business combinations that is equivalent to the business combination accounting standard under International Financial Reporting Standards ("IFRS"). Section 1582 is applicable for business combinations with acquisition dates on or after January 1, 2011. Early adoption of this section is permitted. Section 1601 together with Section 1602 establishes standards for the preparation of consolidated financial statements. Section 1601 is applicable for the Company's interim and annual consolidated financial statements for fiscal years beginning on or after January 1, 2011. Early adoption of this section is permitted. If the Company chooses to early adopt any one of these sections, the other two sections must also be adopted at the same time.

(iv) International Financial Reporting Standards

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 of 2008, the AcSB announced that 2011 is the changeover date for publicly accountable enterprises to use IFRS. 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.

4. Changes in accounting policies

(i) Section 3031, Inventories

Effective January 1, 2008, the Company prospectively implemented Section 3031, *Inventories*, which replaces Section 3030 of the same title. This new standard provides guidance on the determination of cost and requires inventories to be measured at the lower of cost and net realizable value, with more specific guidance on the costs to include in the cost of inventory. Costs such as storage costs and administrative overhead that do not contribute to bringing inventories to their present location and condition are specifically excluded from the cost of inventories and expensed in the period incurred. In addition, the new Section requires that previous write-downs of inventories be reversed when there is a subsequent increase in the net realizable value of the inventories. The recommendations also clarified that major spare parts are to be included in property, plant and equipment. As a result of adopting these recommendations, the Company reclassified $2.7 million of major spare parts from supplies inventories to property, plant, and equipment on January 1, 2008. In addition, the Company recognized reversals of net realizable adjustments in the amount of $4.9 million during the year. Otherwise, this new standard did not have a significant impact on the Company's financial results.

(ii) Section 3862, Financial Instruments – Disclosures and Section 3863, Financial Instruments – Presentation

Effective January 1, 2008, the Company adopted Section 3862, *Financial Instruments – Disclosures*, and Section 3863, *Financial Instruments – Presentation*. These sections replace existing Section 3861, *Financial Instruments – Disclosure and Presentation*. The presentation standards are carried forward unchanged. The disclosure standards introduce new disclosures to improve the information about financial instruments. This standard requires the disclosure of qualitative and quantitative information about the exposure to risks arising from financial instruments, including a sensitivity analysis for market risk. The adoption of these standards did not have any effect on the financial position or performance of the Company. See Note 19 for further information.

(iii) Section 1535, Capital Disclosures

Effective January 1, 2008, the Company adopted Section 1535, *Capital Disclosures*. This section establishes standards for disclosing information that enables users of financial statements to evaluate the entity's objectives, policies and processes for managing capital. The adoption of this standard did not have any effect on the financial position or performance of the Company. See Note 20 for further information.

(in thousands of United States Dollars unless otherwise noted)

5. Change in estimate

Effective April 1, 2008, the Company changed its estimate of the useful lives of its mines to be based on proven and probable reserves of the mine and the portion of mineralization expected to be classified as reserves. Previously, the Company estimated the useful life based on proven and probable reserves to be mined. Consistent with Section 1506, *Accounting Changes*, the change in estimate was applied prospectively. The impact of this change on the Company's financial results for the nine months ended December 31, 2008 was to reduce amortization and depletion by approximately $4.6 million, and to reduce inventories by approximately $0.4 million.

6. Inventories

	December 31 2008 (as restated)	December 31 2007
Supplies	$ 14,073	$ 14,809
Ore stockpiles	3,534	3,338
Ore in process	43,832	31,869
Finished goods	890	1,570
	62,329	51,586
Less: Long-term ore stockpiles	(2,201)	-
	$ 60,128	$ 51,586

During the year, the Company recognized $8,318 of inventory net realizable value adjustments (2007 - $32,972) as an expense. As a result of the increase in expected future commodity prices, the Company recognized net realizable value adjustment reversals during the year, which had the effect of decreasing expenses by $3,278, for an overall net realizable value adjustment expense of $5,040 during 2008.

7. Mining interests and property, plant and equipment

	December 31, 2008			December 31, 2007		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Mining interests:						
Producing properties	$ 334,896	$ 58,277	$ 276,619	$ 306,024	$ 35,877	$ 270,147
Exploration properties	119,400	-	119,400	110,555	-	110,555
	454,296	58,277	396,019	416,579	35,877	380,702
Property, plant and equipment:						
Processing plant	95,183	27,828	67,355	89,277	17,519	71,758
Heavy equipment	70,913	23,075	47,838	64,818	14,618	50,200
Other equipment	41,515	3,287	38,228	40,913	2,358	38,555
Buildings	22,524	4,015	18,509	18,519	3,088	15,431
Office equipment	5,621	2,809	2,812	5,026	1,882	3,144
Vehicles	3,303	2,059	1,244	3,238	1,397	1,841
Equipment under capital lease	9,165	2,754	6,411	9,083	1,631	7,452
Major spare parts	6,439	522	5,917	-	-	-
Construction in progress	12,793	-	12,793	2,958	-	2,958
	267,456	66,349	201,107	233,832	42,493	191,339
Total	$ 721,752	$ 124,626	$ 597,126	$ 650,411	$ 78,370	$ 572,041

(in thousands of United States Dollars unless otherwise noted)

The following table summarizes the movements in capitalized stripping costs:

	December 31 2008	December 31 2007
Balance, beginning of year	$ -	$ -
Stripping costs capitalized	7,352	-
Amortization	-	-
Balance, end of year	$ 7,352	$ -

8. Long-term debt and capital leases

	December 31 2008	December 31 2007
(a) Revolving credit facility	$ 6,855	$ 30,480
(a) Non-revolving term loan	29,582	-
(b) Capital leases for equipment	1,910	3,606
(c) Other long-term debt	105	321
	38,452	34,407
Less: Current portion of long-term debt and capital leases	30,461	33,073
	$ 7,991	$ 1,334

The estimated future minimum debt and lease payments under all facilities are as follows:

2009	$	30,461
2010	$	7,834
2011	$	157

(a) On November 12, 2007, the Company replaced its $20,000 revolving facility with a $60,000 revolving facility, expiring on December 31, 2008. Interest was payable at prime rate plus 0.75% or in the case of US dollar advances, LIBOR + 1.75%.

On November 28, 2008, the terms of the Company's credit facility were revised and extended. Under the terms of the new agreement, the Company will have access to a $50,000 credit facility comprised of a $30,000 non-revolving credit facility and a $20,000 revolving credit facility. The non-revolving facility is repayable in varying amounts and matures on June 30, 2010. In addition to the required repayments, the Company is required, commencing June 30, 2009, to prepay outstanding credit in an amount equal to 75% of the excess of cash flow from operations over expenditures on mining interests and property, plant and equipment, scheduled principal repayments on long-term debt, and taxes paid, for the six months ended June 30, 2009 and for each subsequent fiscal quarter .The revolving facility matures on November 27, 2009 and may be renewed at the sole discretion of the lenders. Interest is payable at LIBOR + 3.5%. As at December 31 2008, the Company had drawn $7,130 under the revolving facility and $30,000 under the non-revolving facility.

The credit facility contains various covenants that include a fixed charge coverage ratio of at least 1.15:1 up to March 31, 2009 and at least 1.25:1 thereafter, a leverage ratio of no more than 3:1, a tangible net worth of at least $394,600 plus 50% of positive net income earned subsequent to September 30, 2008, and certain other operational covenants. The facility is secured by a first-ranking lien on all present and future assets, property and undertaking of the Company.

(b) The Company is obligated under various capital leases for equipment, all of which expire by 2011. All capital lease agreements provide that the Company can purchase the leased equipment at the end of the lease term for a nominal amount. Interest payable on the various leases range from a fixed rate of 7.38% to variable rates between LIBOR + 2.50% and LIBOR + 2.75%.

(c) The Company is obligated under certain other agreements maturing in 2010. These loans are non-interest bearing, with quarterly payments of approximately $15.

(in thousands of United States Dollars unless otherwise noted)

9. Other long-term obligations

During the current fiscal year, the Company entered into an eight-year consultancy agreement with a third party, whereby the Company will receive assistance with strategic planning, business development, procurement and authorization of land, employer-employee relations, community and government relations, and environmental regulations. The obligation is non-interest bearing, and has been recorded at fair value using a discount rate of 7%, with payment terms as follows: an initial payment of $1,000 was made in the second quarter, and an additional payment of $400 was made in the third quarter. An additional payment of $400 will be made in January 2009, and seven annual payments of $800 will be made in January of each subsequent year. As of December 31, 2008, the total balance outstanding is $4,676 (current portion – $400).

10. Asset retirement obligations

The Company's asset retirement obligations consist of reclamation costs for the Ocampo and El Cubo mines. The present value of the obligation is currently estimated at $3,622 (2007 - $2,991), reflecting payments that will commence in 10 – 20 years. Significant reclamation activities include land rehabilitation, demolition of buildings and mine facilities, ongoing care and maintenance and other costs.

The undiscounted value of the reclamation costs liability is $13,298 (2007 - $10,625). The credit adjusted risk-free rate used in estimating the obligation was 8%, and the inflation rate used was 5.4% (2007 – 3.5%). Changes to the reclamation and closure cost obligation balance during the year were as follows:

	December 31 2008	December 31 2007
Asset retirement obligations, beginning of year	$ 2,991	$ -
Foreign exchange adjustment	(620)	-
Obligations incurred	803	2,945
Accretion expense	190	46
Revisions in estimates	258	-
Asset retirement obligations, end of year	$ 3,622	$ 2,991

11. Employee future benefits

The Company has three defined benefit plans that provide employee future benefits, other than pensions, to certain of its employees.

The Company accrues for employee future benefits for contract workers and employees in Mexico paid through an employment services company or by its subsidiaries. These benefits consist of a one-time payment equivalent to 12 days wages for each year of service (at the employee's most recent salary, but not to exceed twice the legal minimum wage), payable to all employees with 15 or more years of service, as well as to certain employees terminated involuntarily prior to the vesting of their seniority premium benefit. Under Mexican Labour Law, the Company also 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.

On September 12, 2008, the Company established a post-retirement benefit plan for a member of senior management. The plan provides for a lump sum retirement payment at age 65, determined as a multiple of the members' aggregate salary in 2006 and 2007.

All plans are unfunded. An actuarial valuation was performed for all plans as at December 31, 2008.

(in thousands of United States Dollars unless otherwise noted)

Information about the Company's benefit plans, in aggregate, is as follows:

	December 31 2008	December 31 2007
Accrued benefit obligation:		
Balance, beginning of year	$ 3,746	$ 3,366
Foreign exchange adjustment	(453)	(37)
Service cost	462	399
Interest cost	227	112
Benefits paid	(213)	-
Early settlements	(1,527)	-
Actuarial loss	22	332
Deficit	2,264	4,172
Unamortized actuarial loss	(605)	(426)
Accrued benefit liability	$ 1,659	$ 3,746

Employee future benefit expense recognized during the year was as follows:

	December 31 2008	December 31 2007
Employee future benefits expense:		
Service cost	$ 462	$ 398
Interest cost	227	112
Actuarial loss	38	249
Past service costs	(260)	-
	467	759
Difference between costs arising in the period and costs recognized in the period in respect of:		
Actuarial gains	72	-
Net expense for the year	$ 539	$ 759
Significant assumptions used:		
Discount rate	8.04%	4.00%
Rate of compensation increase	5.22%	1.50%

12. Income taxes

The following table reconciles the expected income tax (recovery) / payable at the statutory income tax rate to the amounts recognized in the consolidated statements of operations for the years ended December 31, 2008 and 2007.

	December 31 2008 (restated)	December 31 2007
Net earnings / (loss) before income taxes	$ 30,300	$ (73,680)
Income tax rate	35.50%	38.12%
Expected income tax expense / (recovery) based on above rates	10,756	(28,086)
Effect of lower tax rates in foreign jurisdictions	(4,819)	7,458
Non-deductible stock option expense	1,441	1,538
Other	302	(6,727)
Change in Mexican statutory income tax regime	-	43,081
Valuation allowance	(17,374)	10,370
Provision for income taxes	$ (9,694)	$ 27,634

(in thousands of United States Dollars unless otherwise noted)

The following reflects future income tax liabilities at December 31, 2008 and 2007:

	December 31 2008	December 31 2007
Accounting value of mineral properties in excess of tax value	$ 85,340	$ 108,666
Accounting value of inventories in excess of tax value	11,311	10,297
Deductible share issue costs	(1,871)	(3,638)
Future employee benefits	(436)	(769)
Unrealized foreign exchange gains / (losses)	1,938	(4,201)
Other	(2,146)	-
Non-capital losses carried forward	(64,251)	(66,266)
	29,885	44,089
Valuation allowance	47,416	64,790
Future income tax liabilities recognized	$ 77,301	$ 108,879

The Company has tax loss carryforwards expiring in the following years:

	Canada	Mexico	Total
2009	2,433	-	2,433
2010	-	1,146	1,146
2011	-	36	36
2012	-	4,089	4,089
2013	2,755	11,316	14,071
2014	5,416	17,201	22,617
2015	4,622	42,723	47,345
2016	-	41,493	41,493
2017	-	46,114	46,114
2018	-	12,884	12,884
2026	6,781	-	6,781
2027	14,434	-	14,434
2028	10,297	-	10,297
	$ 46,738	$ 177,002	$ 223,740

13. Shareholders' equity

(a) Capital stock

Authorized:
Unlimited number of common shares.

Unlimited number of non-cumulative, dividends to be determined by the Board of Directors not to exceed 12%, non-participating, non-voting, Class "A" preferred shares, redeemable at their paid-in value.

Unlimited number of non-cumulative, dividends to be determined by the Board of Directors not to exceed 13%, non-participating, non-voting, Class "B" preferred shares, redeemable at their paid-in value.

(in thousands of United States Dollars unless otherwise noted)

Issued and outstanding:

	Number of Common Shares	Ascribed Value
Balance, December 31, 2006	102,146,108	$ 463,333
For cash pursuant to exercise of share purchase options	5,286,255	33,439
Fair value of options exercised	-	32,714
Public offering	10,000,000	178,120
Share issuance costs	-	(8,094)
Balance, December 31, 2007	117,432,363	$ 699,512
For cash pursuant to exercise of share purchase options	2,558,405	6,772
Fair value of options exercised	-	12,694
Fair value of shares issued	50,000	448
Balance, December 31, 2008	120,040,768	$ 719,426

(b) Stock options (in Canadian dollars)

The Company has a stock option plan under which options to purchase common shares of the Company may be granted to directors, senior officers, employees and service providers of the Company. The aggregate number of common shares that may be reserved for issuance under the plan is 23,600,000. The maximum number of common shares that may be reserved for issuance to any one person under the plan is 5% of the shares outstanding at the time of grant (on a non-diluted basis), less the aggregate number of shares reserved for issuance to such person under any other option to purchase shares from treasury granted as a compensation or incentive mechanism. Stock options are generally exercisable for a maximum period of five to seven years from the grant date, and have vesting periods as determined by the Company's Board of Directors.

The fair value of the options granted was calculated using the Black-Scholes option-pricing model with the following weighted average assumptions:

	December 31 2008	December 31 2007
Dividend yield	0%	0%
Expected volatility	53.35%	55.32%
Risk free interest rate	3.45%	4.21%
Expected life	6.13 years	5 years
Weighted average grant date fair value	$5.23	$8.56

	December 31, 2008		December 31, 2007	
	Shares	Weighted Average Price	Shares	Weighted Average Price
Outstanding, beginning of year	9,544,920	$ 6.35	14,040,342	$ 4.75
Granted	1,885,000	$ 8.73	1,800,000	$ 16.41
Expired / forfeited	(321,422)	$ (9.45)	(1,009,167)	$ (18.31)
Exercised	(2,558,405)	$ (2.69)	(5,286,255)	$ (7.00)
Outstanding, end of year	8,550,093	$ 7.85	9,544,920	$ 6.35
Options exercisable, end of year	6,514,593	$ 7.56	8,926,656	$ 6.13

(in thousands of United States Dollars unless otherwise noted)

During the year ended December 31, 2008, employees, consultants, officers and directors of the Company exercised 2,558,405 (2007 – 5,286,255) options for total proceeds of $6,893 (2007 - $38,815). Set forth below is a summary of the outstanding options to purchase common shares as at December 31, 2008:

		Options outstanding			Options exercisable	
	Option Price	Number outstanding	Weighted average exercise price	Average life (yrs)	Number exercisable	Weighted average exercise price
$	5.01 - 5.50	2,013,700	$ 5.45	0.35	2,013,700	$ 5.45
$	5.51 - 6.00	573,400	$ 5.68	0.10	573,400	$ 5.68
$	6.01 - 6.50	1,894,500	$ 6.18	1.60	1,579,500	$ 6.12
$	6.51 - 7.00	558,050	$ 6.58	3.49	289,050	$ 6.55
$	7.01 - 7.50	235,000	$ 7.45	0.18	235,000	$ 7.45
$	7.51 - 9.00	195,000	$ 8.09	3.24	53,750	$ 8.00
$	9.01 - 9.50	891,500	$ 9.26	2.63	494,750	$ 9.15
$	9.51 - 10.00	917,000	$ 9.92	6.02	90,000	$ 9.99
$	10.01 - 10.50	89,333	$ 10.49	2.45	60,333	$ 10.49
$	10.51 - 11.00	799,277	$ 10.64	2.95	779,277	$ 10.64
$	11.01 - 18.00	50,000	$ 13.00	3.54	12,500	$ 13.00
$	18.01 - 21.00	333,333	$ 20.35	3.25	333,333	$ 20.35
	Total	8,550,093			6,514,593	

(c) Share-based compensation

In 2008, the Company awarded share-based compensation to certain employees in lieu of a cash bonus. The shares awarded are valued at the volume weighted average trading price of the Company's shares for the five days prior to the award, and vest over an eighteen-month period. Subject to shareholder and stock exchange approvals, the employees will receive the number of shares equivalent to the bonus value, using the grant date price. In the event that approval is not obtained, the employees are entitled to receive an amount in cash, equal to the product of the number of shares that would have been issued and the trading price of the Company's shares on the date paid. Until the necessary approvals are obtained, this liability is remeasured at each reporting period of the Company and the change is recognized in general and administrative expenses. The amount of compensation expense recorded in 2008 with respect to share-based compensation was $5,587.

14. Commitments and contingencies

Option and joint venture agreements

(a) Minera Fuerte Mayo, S.A. de C.V. ("Fuerte Mayo") / Compania Minera Brenda, S.A. de C.V. ("Brenda")

As a result of an agreement dated February 21, 2003 in which the Company acquired the remaining 40% of the title and interest in a group of claims located in the municipality of Ocampo from Brenda, the Company agreed to pay 8% of net profits attributable to the development of the mining claims and their concessions up to a maximum of $2,000. As at December 31, 2007, the Company had paid Brenda $455.

During the year ended December 31, 2008, a contract addendum was signed which eliminated the clause containing the percentage of profits payable up to a maximum of $2,000, and instead the Company agreed to pay Brenda a total of $2,000 for the group of claims. The Company had previously paid $455 and during the current year, the Company paid a further $750, resulting in a balance payable at December 31, 2008 of $795.

(in thousands of United States Dollars unless otherwise noted)

(b) Compania Minera Global, S.A. de C.V. ("Global")

On July 17, 2000, the Company entered into an agreement with Global for consulting services to assist in the negotiations of an agreement with Minerales de Soyopa, S.A. de C.V. ("Soyopa") to secure the right to acquire the then remaining fifty-one percent (51%) interest in the Ocampo property. As part of the consideration for the successful negotiation and execution of the agreement between the Company and Soyopa, the Company agreed that if it should subsequently sell the lands, claims and concessions described in the agreements, the Company shall be required to pay Global $1,000. The lands, claims and concessions have not been sold.

(c) Compania Minera Las Torres, S.A. de C.V. ("Las Torres")

On September 7, 2004, a subsidiary of the Company entered into a mining lease agreement with Las Torres. Pursuant to the agreement, the Company acquired the right to explore, develop and mine the Las Torres Gold-Silver property located in Guanajuato State, Mexico, for a five-year period, subject to renewal for a further five-year period. The annual lease payments total $480 for the first year and $720 for each year thereafter. In addition, the Company is required to pay a 3.5% net smelter return on all gold and silver sales equal to or above $350.00 per gold ounce and $5.50 per silver ounce, with a minimum monthly royalty of $20. The royalty will gradually decrease to a 3.0% net smelter return for sales of gold and silver at or below $300.00 per gold ounce and $5.00 per silver ounce.

On November 28, 2008, the Company entered into an agreement with Las Torres such that the Company will pay $10.00 per ounce for each ounce of ore processed at the Las Torres mill from existing El Cubo claims. In addition, as a result of this amendment the Company issued a letter of credit in the amount of $1,000 to Las Torres.

Pursuant to the original mining lease agreement with Las Torres, minimum annual lease and royalty payment commitments for successive years approximate:

	Lease Payments	Royalty Payments
2009	$ 720	$ 180

Other contingencies

In March 2008, the Company was named as a defendant in a claim filed by Ed J. McKenna. The plaintiff was seeking, among other things, an order certifying the action as a class proceeding and $75 million in special and general damages and $5 million in punitive damages on behalf of the class. In July 2008, the claim was amended to, among other things, assert new claims and increase the damages sought from $80 million to $160 million. Management is of the opinion that the claim is without merit, and that a strong defence exists against the claim. Therefore, no provision for loss has been reflected in the accounts of the Company.

The Company is involved in legal proceedings arising in the ordinary course of its business. In the opinion of management, the ultimate liability with respect to these actions will not materially affect the Company's financial position, results of operations or cash flows.

Other commitments

At December 31, 2008, the Company has purchase commitments in the amount of approximately $2.9 million (2007 - $2.8 million) related to acquisitions of equipment. The equipment is expected to be delivered during the first half of 2009.

15. Earnings / (loss) per share

Basic earnings / (loss) per share is calculated based on the weighted average number of shares outstanding during the year ended December 31, 2008 of 119,110,568 (December 31, 2007 – 113,176,605). Diluted earnings / (loss) per share is based on the assumption that options under the stock option plan have been exercised on the later of the beginning of the year and the date granted. As of December 31, 2008, 3,275,433 stock options (December 31, 2007 – 9,544,920) were excluded from the computation of diluted earnings per share because their effect would have been anti-dilutive.

(in thousands of United States Dollars unless otherwise noted)

16. Supplemental cash flow information

		December 31 2008 (as restated)		December 31 2007
Items not affecting cash:				
Amortization, depletion and accretion	$	40,369	$	43,392
Amortization of transaction costs		55		-
Unrealized foreign exchange (gain) / loss		(23,747)		10,063
Stock option expense, net of forfeitures		4,250		4,035
Employee future benefits		(1,019)		522
Future income tax (recovery) / expense		(10,738)		27,634
Other long-term obligations		(606)		-
Other long-term assets		226		-
	$	8,790	$	85,646
Change in non-cash working capital:				
Receivables	$	(6,155)	$	3,074
Prepaids and deposits		(582)		(1,474)
Inventories		(8,229)		(5,604)
Payables and accruals		22,115		(14,520)
	$	7,149	$	(18,524)
Supplemental information:				
Interest paid	$	2,527	$	4,567
Taxes paid	$	2,882	$	-
Non-cash transactions:				
Acquisition of assets under capital lease	$	860	$	635

17. Related party transactions

The Company had the following related party transactions, which were in the normal course of operations and measured at fair value:

			December 31 2008		December 31 2007
(a)	Production costs – labour	$	33,762	$	31,148
(a)	Mining interests – labour		1,167		2,437
(b)	Production costs – consumables		14,655		2,033
(c)	Capital assets		94		25
		$	49,678	$	35,643

(a) The Company pays a third party company related to a director for the provision of workers in the Mexican operations at cost plus 10%.

(b) The Company pays two third party companies related to a director for the provision of lubricant and fuel, the prices of which are regulated in Mexico.

(c) The Company paid a director, or a third party company related to a director, for the provision and construction of production and support facilities and mineral properties.

As at December 31, 2008, the Company had included $1,922 (2007 - $1,775) in payables and accruals and $1,022 (2007 - $Nil) included in prepaids and deposits, representing amounts owing or paid to these related parties.

(in thousands of United States Dollars unless otherwise noted)

18. Financial instruments

The Company's financial instruments consisted of cash and cash equivalents, restricted cash, receivables, payables and accruals, long-term debt and capital leases. Unless otherwise noted, it is management's opinion that the Company is not exposed to significant interest or credit risks arising from these financial instruments. Some of the Company's receivables and payables are denominated in Mexican Pesos or Canadian dollars. Balances are translated at the period end based on the Company's accounting policy as set out in Note 3(c) to the consolidated financial statements.

The Company estimates that the fair value of its cash and cash equivalents, restricted cash, receivables, payables and accruals, and long-term debt approximate the carrying value of the assets and liabilities due to the relatively short terms to maturity or due to the borrowing terms being comparable to current market terms for similar liabilities.

19. Financial risk management

In the normal course of operations, the Company is exposed to commodity price, interest rate, foreign currency exchange, credit and liquidity risks. The Company has recently developed a risk management process to identify, analyze, and assess these risks, and has formed a Risk Committee to monitor these risks. The Board of Directors has overall responsibility for the oversight of the Company's risk management framework, and receives reports from the Risk Committee.

Commodity price risk

The profitability of the Company's gold mining operations will be significantly affected by changes in the market prices for gold and silver. Gold and silver prices fluctuate on a daily basis and are affected by numerous factors beyond the Company's control. The supply and demand for gold and silver, interest rates, the rate of inflation, investment decisions by large holders of gold and silver, including governmental reserves, and stability of exchange rates can all cause significant fluctuations in gold and silver prices. Such external economic factors are in turn influenced by changes in international investment patterns and monetary systems, and political developments. The Company does not actively hedge this exposure.

Interest rate risk

The Company is exposed to interest rate risk on its variable rate debt. The Company has not entered into any agreements to hedge against unfavourable changes in interest rates. If interest rates had been 50 basis points higher during the year, equity and net earnings would have decreased by $161, arising mainly as a result of higher interest rates on variable borrowings. This analysis assumes that other variables remain constant (a 50 basis point decrease in interest rates would have had the equal but opposite effect).

Foreign currency exchange rate risk

All metal revenues for the Company are denominated in US dollars. The Company is primarily exposed to currency fluctuations relative to the US dollar on expenditures that are denominated in Canadian dollars (CAD) and Mexican Pesos (MXN). These potential currency fluctuations could have a significant impact on production costs and thereby, the profitability of the Company. The Company is also exposed to the impact of currency fluctuations on its monetary assets and liabilities. The Company does not actively manage this exposure.

At December 31, 2008, the Company's exposure to foreign currency exchange risk was as follows:

	CAD	MXN
Cash and cash equivalents	$ 44	19,037
Receivables	190	148,160
Payables and accruals	(8,485)	(114,517)
Long-term debt and capital leases	(112)	(5,718)
Future income tax liabilities	(67,328)	(308,720)
Net balance sheet exposure	$ (75,691)	(261,758)

(in thousands of United States Dollars unless otherwise noted)

A 10% weakening of these currencies against the US dollar at December 31st would have increased / (decreased) equity and net earnings by the amounts shown below. This analysis assumes that other variables, in particular interest rates, remain constant (a 10% strengthening would have had the equal but opposite effect).

	Equity / earnings
Translation of net CAD exposure	$ 5,631
Translation of net MXN exposure	1,744

Credit risk

Credit risk relates to receivables and other contracts, and arises from the possibility that any counterparty to an instrument fails to perform. For cash and cash equivalents and receivables, the Company's credit risk is limited to the carrying amount on the balance sheet. The Company manages credit risk by transacting with highly-rated counterparties and establishing a limit on contingent exposure for each counterparty based on the counterparty's credit rating. Exposure on receivables is limited as the Company sells its products to a small number of organizations, on which the historical level of defaults is minimal.

Liquidity risk

Liquidity risk is the risk that the Company will be unable to meet its financial obligations as they become due. The Company manages this risk through regular monitoring of its cash flow requirements to support ongoing operations and expansionary plans. The Company ensures that there are sufficient committed loan facilities to meet its business requirements, taking into account its anticipated cash flows from operations and its holdings of cash and cash equivalents.

Effective November 28, 2008, the Company's credit facility was restructured and extended. The existing $60 million revolving credit facility was converted to $30 million non-revolving credit facility, of which $30 million was outstanding on December 31, 2008, that will be repaid in scheduled instalments over a 19 month period and a $20 million revolving facility that expires on November 27, 2009 of which $7.13 million was drawn at December 31, 2008.

The following are the contractual maturities of financial liabilities, including interest payments:

	Carrying amount	Contractual cash flows	Less than 6 months	6 - 12 months	1 - 2 years	2 – 5 years	More than 5 years
Payables and accruals	$ 30,457	$ (30,457)	$ (30,457)	$ -	$ -	$ -	$ -
Long-term debt and capital leases	38,452	(39,893)	(9,121)	(22,710)	(7,901)	(161)	-
Other long-term liabilities	4,677	(6,000)	(400)	-	(800)	(2,400)	(2,400)
	$ 73,586	$ (76,350)	$ (39,978)	$ (22,710)	$ (8,701)	$ (2,561)	$ (2,400)

20. Capital management

The primary objective of managing the Company's capital is to ensure that there is sufficient available capital to support the funding requirements of the Company, including capital expenditures, in a way that optimizes the cost of capital and shareholder returns, and ensures that the Company remains in a sound financial position. There were no changes to the Company's overall capital management approach during the current year.

The capital of the Company consists of items included in Shareholder's equity and debt obligations. The Company manages and makes adjustments to the capital structure as opportunities arise in the market place, as and when borrowings mature, or when funding is required. This may take the form of raising equity or debt.

(in thousands of United States Dollars unless otherwise noted)

The Company monitors capital through the gross debt to total equity ratio, and targets a ratio of less than 25%. As at December 31, 2008, the ratio of gross debt to total equity was 6.02% (December 31, 2007 – 5.86%), calculated as follows:

	December 31, 2008 (as restated)	December 31, 2007
Current portion of long-term debt	$ 30,461	$ 33,073
Long-term debt	7,991	1,334
Gross debt	38,452	34,407
Shareholders' equity	$ 638,610	$ 586,650
Gross debt / Shareholders' equity	6.02%	5.86%

21. Segmented information

Information is reported on a mine by mine basis, and therefore the Company's operating segments are represented by the individual mines and the corporate operations. Revenue in both mining segments is derived from the sale of gold and silver.

The following are the operating results by segment:

December 31, 2008 (as restated)	Ocampo	El Cubo	Corporate	Total
Revenue from mining operations	$ 154,313	$ 58,209	$ -	$ 212,522
Production costs	86,026	41,625	-	127,651
Refining costs	1,156	506	-	1,662
General and administrative	8,983	2,092	18,870	29,945
Amortization and depletion	26,267	13,967	146	40,380
	122,432	58,190	19,016	199,638
Earnings / (loss) before other items	$ 31,881	$ 19	$ (19,016)	$ 12,884
Expenditures related to mining interests and property, plant and equipment	$ 50,419	$ 16,237	$ 185	$ 66,841
Total assets	$ 411,510	$ 382,544	$ 1,124	$ 795,178

December 31, 2007	Ocampo	El Cubo	Corporate	Total
Revenue from mining operations	$ 107,833	$ 44,226	$ -	$ 152,059
Production costs	106,977	37,645	-	144,623
Refining costs	1,046	464	-	1,510
General and administrative	4,682	682	18,792	24,156
Amortization and depletion	28,582	14,731	80	43,392
	141,287	53,522	18,872	213,681
Loss before other items	$ (33,454)	$ (9,296)	$ (18,872)	$ (61,622)
Expenditures related to mining interests and property, plant and equipment	$ 53,806	$ 15,255	$ 81	$ 69,142
Total assets	$ 379,285	$ 373,044	$ 1,623	$ 753,952

All goodwill included on the balance sheet relates to the El Cubo operating segment.

22. Subsequent events

(i) Proposed transaction

On March 12, 2009, the Company announced that it entered into a letter agreement ("letter of intent") with Capital Gold Corporation ("Capital Gold") relating to a proposed acquisition of Capital Gold by the Company. The all-share transaction is subject to satisfactory completion of due diligence and the negotiation of definitive documentation, receipt of Capital Gold shareholder approval, regulatory approvals and the satisfaction of certain other conditions. The letter of intent contemplates, among other things, the issuance of 0.1028 Gammon Gold shares for each Capital Gold common share outstanding, for a total issuance of 20,389,591 common shares.

The letter of intent provides that the parties plan to complete their respective technical, operating and financial due diligence and negotiate the terms of a definitive agreement by March 31, 2009. Capital Gold has agreed to a non-solicitation period expiring on March 31, 2009, subject to fiduciary outs, and both parties have agreed to the payment of a break fee to the other party in the amount of $4,000, payable only under certain circumstances.

Capital Gold is a gold production and exploration company and operates the El Chanate gold property in Sonora, Mexico.

On March 31, 2009, discussions regarding the proposed acquisition of Capital Gold were terminated. No break fee will be exchanged.

(ii) Other

Subsequent to year-end, certain employees, consultants, officers and directors of the Company exercised 2,508,400 stock options for total proceeds of $11,508. As a result, capital stock increased by $22,383 and contributed surplus decreased by $10,875.

23. Comparative figures

Certain of the comparative figures for December 31, 2007 have been reclassified to conform with the financial statement presentation adopted for December 31, 2008.