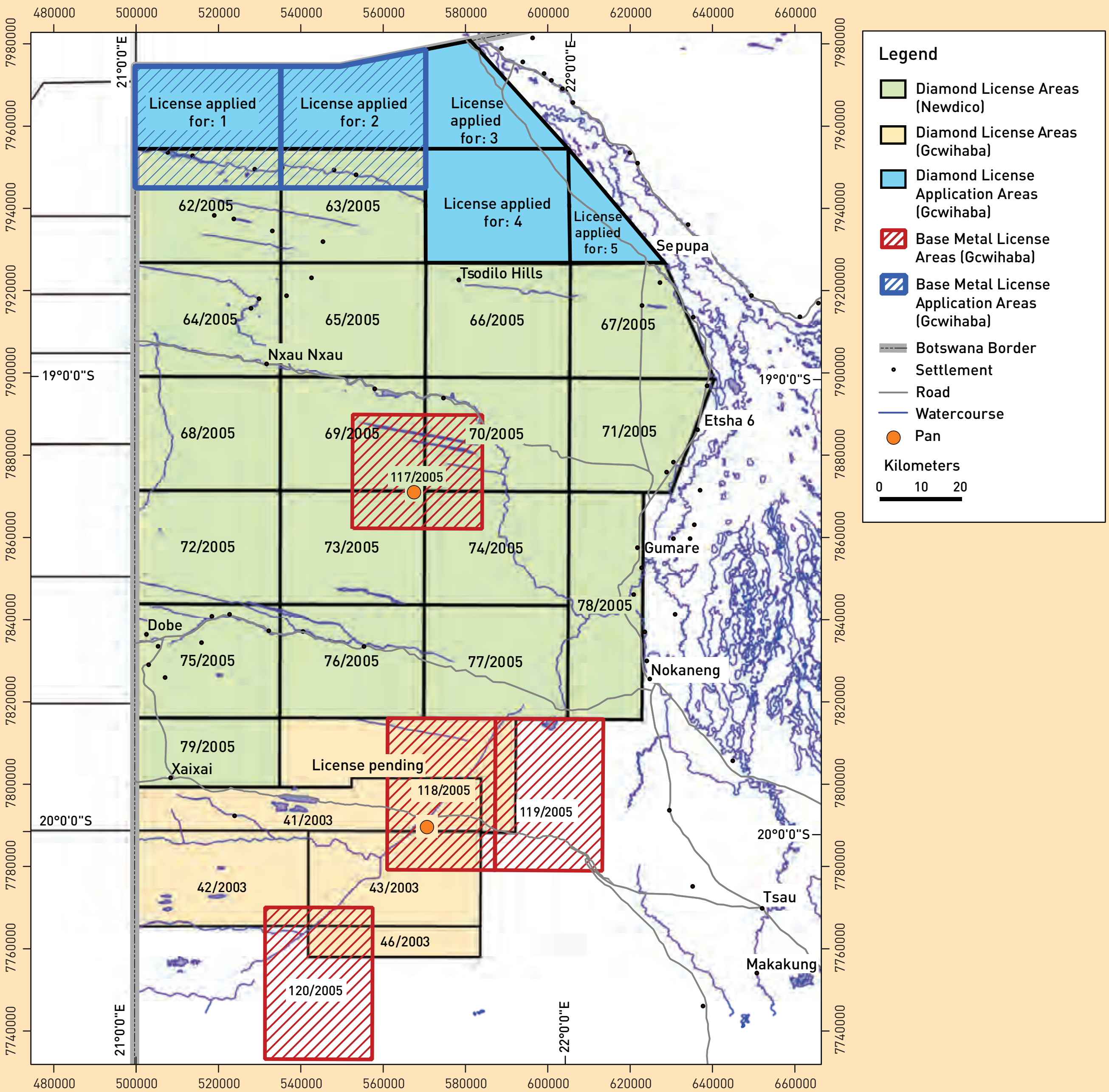
ANNUAL REPORT 2006

tsodilo resources limited

Contents

Newdico and Gcwihaba Prospecting Diamond Licenses - as of March 7, 2007



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President's Message

A very busy and exciting year lies ahead as we make progress in the exploration for an economic kimberlite below the Kalahari cover on this sector of the Congo craton and expand our precious and base metals exploration.

Drilling in the Kalahari

Fellow Shareholders,

2006 was a year of significant advances for Tsodilo Resources Limited ("Tsodilo" or the "Company"). We transitioned from an exploration company which by necessity was reliant on others to perform their work into an efficient and fully equipped exploration company second to none in capabilities and experience. As a result of the decision to purchase a drill rig and supporting equipment as well as geophysical instruments, we now have the ability to select a target; perform a detail ground magnetic survey; and drill test it all in a matter of weeks as opposed to the months or years which it previously took. Since the on-site commissioning of the Atlas Copco CT14 drill rig, we have drilled approximately 5 kilometers in total depth and collected a similar amount of drill core for analysis. Operating our own drill rig has given us the ability and flexibility to advance our exploration at a far greater rate and at a fraction of the per meter drilling costs of what it was previously.

In addition to our exploration program, which is designed to locate an economic kimberlite diamond deposit, the Company will also look to take advantage of opportunities which present themselves in base and precious metals exploration. As precious and base metals are enjoying a tremendous increase in demand and appreciation, it is appropriate that we consider these resources as targets for exploration and development.

During the past year, the Company funded exploration activity by raising funds in the capital markets through the successful issuance of stock by way of private placements. This process will continue in the coming year. Our current share base consists of 13,577,354 issued and outstanding (17,820,448 on a fully diluted basis) common shares. Tsodilo has no debt, a 90% interest in our Botswana Newdico project and a 100% interest in our Botswana Gcwihaba projects. The Company is well positioned to meet the challenges in the upcoming year.

A very busy and exciting year lies ahead as we make progress in the exploration for an economic kimberlite below the Kalahari cover on this sector of the Congo craton and expand our precious and base metals exploration. Please follow our progress carefully and remain informed by regular visits to our website, www.TsodiloResources.com.

James M. Bruchs

President and Chief Executive Officer

March 22, 2007

Management's Discussion and Analysis

This management's discussion and analysis ("MD&A") should be read in conjunction with the Consolidated Annual Financial Statements for the year ended December 31, 2006 and comments on the factors that affected the Company's performance during the periods covered by the Consolidated Annual Financial Statements as well as the Company's financial condition and future prospects. The Company's functional and reporting currency is United States dollars and all amounts stated are in United States dollar unless otherwise noted. The Company changed its financial year end from March 31 to December 31 effective December 31, 2005 and was made to align with the reporting schedule of comparable public companies. The period December 31, 2005 was the transitional period and has a nine month reporting period. This management's discussion and analysis has been prepared as at March 22, 2007.

OVERVIEW

Tsodilo Resources Limited ("Tsodilo" or the "Company") was organized under the laws of the Province of Ontario in 1996 and continued under the laws of the Yukon in 2002. The shares of the Company are listed and posted for trading on the TSX Venture Exchange under the symbol: TSD. Tsodilo is an international diamond exploration company with the majority interest in a kimberlite exploration project in northwest Botswana. The Company has not yet determined whether these properties contain reserves that can be economically mined. As an exploration stage company, the recoverability of amounts shown for exploration expenditures is dependent upon the discovery of reserves that can be economically mined, the securing and maintenance of the interests in the properties, the ability of the Company to obtain the necessary financing to complete the development, and future production or proceeds from the disposition thereof. The Company is also actively reviewing additional opportunities within southern Africa.

Corporate

At a special meeting of the holders of common shares of the Company held on April 9, 2002 shareholders approved a restructuring of the Company that incorporated the sale of substantially all of the Company's assets. The assets were transferred in settlement of debt due and owing to Trans Hex Group Limited ("Trans Hex Group"), the principal shareholder and creditor of the Company prior to restructuring, of $612,783. The Company retained an interest in all future dividends that may be paid by either Northbank Diamonds Limited, Hoanib Diamonds (Proprietary) Limited or Trans Hex (Zimbabwe) Limited. In addition, the Company was released from the long-term loans due to Trans Hex Group by the subsidiaries being sold, of $3,341,690, and Trans Hex Group agreed to return the 10,688,137 common shares in the capital of the Company, representing 73.22% of the issued and outstanding shares of the Company at that time, to treasury for cancellation. The special meeting of shareholders also approved the discontinuance of the Company from the Province of Ontario and its continuance under the Business Corporations Act (Yukon), the change of name of the Company from Trans Hex International Ltd. to Tsodilo Resources Limited, the election of new directors and the repeal of the existing stock option plan of the Company and adoption of a new stock option plan. Following the restructuring of the Company, as approved by shareholders in April 2002, Tsodilo has no long-term debt.

Outstanding Share Data

As of March 22, 2007, 13,577,354 common shares of the Company were outstanding. Of the options to purchase common shares issued to eligible persons under the stock option plan of the Company, 1,480,000 options remain outstanding of which 873,375 are exercisable at exercise prices ranging from Canadian $0.15 - $1.85. If all options were vested and exercised, 1,480,000 common shares of the Company would be issued.

As of March 22, 2007, 2,763,094 warrants are outstanding. The warrants were issued by way of the private placements utilized by the Company for financing purposes. Each warrant entitles the holder thereof to purchase one common share of the Company at purchase prices ranging from Canadian $0.70 - $2.35 for a period of two years from the date of issuance. If converted, 2,763,094 common shares of the Company would be issued.

Principal Shareholders of the Company

The largest shareholder of the Company is its President and Chief Executive Officer, James M. Bruchs, who currently owns, controls or directs 2,545,983 or 18.75% of the issued and outstanding common shares as of March 22, 2007. The Firebird Global Master Fund, Ltd. controls 1,875,630 or 13.81% of the issued and outstanding shares as of March 22, 2007 and John R. Redmond, a Director of the Company, currently owns, controls or directs 1,764,359 or 12.99% of the issued and outstanding shares as of March 22, 2007.

Subsidiaries

The Company has a 90% operating interest in its Botswana subsidiary, Newdico (Proprietary) Limited ("Newdico"), which holds prospecting licenses and applications covering approximately 16,800 square kilometers in northwest Botswana on which there is encouragement for the existence of undiscovered kimberlites in at least three separate areas of the property.

The Company's minority partner (10%) in this project, Trans Hex Group, is an established South African diamond mining company. Some, or all, of the current licenses held by Newdico may be subject to the granting of a 2% free carried interest in any mine or mines that may result thereon.

The Company has a 100% interest in its wholly owned Botswana subsidiary, Gcwihaba Resources (Proprietary) Limited ("Gcwihaba"), which has diamond prospecting licenses covering approximately 6,800 square kilometers and base and precious metal licenses covering 3,780 square kilometers.

Exploration Activities

NEWDICO (Pty) Limited ("Newdico")

Summary of work completed in 2006 and to date

- Ground magnetic geophysical surveys over ten priority targets and two paleo drainage channels were completed in the Nxau Nxau area.
- A Geographical Information System was completed with all available geological, geophysical and geochemical data captured onto the system. The data is being used to prioritize target areas for further exploration.
- Access tracks and site clearing totaling 40 kilometers was completed.
- Twenty-five diamond core drill holes were completed to investigate 13 priority targets in the Nxau Nxau kimberlite field. Various half core samples have been collected from those drill holes that intersected kimberlite or kimberlite crater sediments for petrographic description and for analysis of kimberlite indicator minerals.
- Ground magnetic geophysical surveys over 6 priority targets were completed in the northern Ngamiland region.
- In the Guma area, 17 diamond core drill holes over 10 targets have been completed since drilling commenced in late January 2007. Drilling is currently ongoing and expected to continue into the 2nd quarter. Upon completion of the drilling in the Guma area, various half core samples will be collected from select drill holes for petrographic description and for analysis of kimberlite indicator minerals.

Planned Exploration Program for 2007

The program is based on our strategy of using a combination of indicator mineral sampling, magnetic and gravity data to generate individual targets for drill evaluation and our regional strategy of evaluating possible transport corridors giving rise to the alluvial secondary kimberlite indicator minerals ("KIM") and diamond deposits at Tsumkwe and Omatako. Our program for 2007 will include the following:

- Drill evaluation of 10 high-priority targets in the Nxau Nxau kimberlite field.
- Drill evaluation of 4 previously discovered diamondiferous kimberlites in the Nxau Nxau field for petrography and KIM chemistry analysis. Geophysical surveys will be performed prior to drilling.
- The Company will commence a drill program to collect 100 tons of kimberlite for macro diamond analysis on kimberlite A15 if the KIM chemistry of A15 (5) is favorable. A decision is expected in the 2nd quarter of 2007.

The favorable chemistry and diamond preservation potential of the kimberlites in our license blocks together with the known secondary alluvial diamond discoveries down slope across the border in Namibia establish the greater Nxau Nxau field as highly prospective with the possibility of several economic kimberlites present within our ground. To date, at least 18% of the kimberlites discovered and tested for diamond in the Nxau Nxau field are known to be diamondiferous.

GCWIHABA Resources (Pty) Limited ("Gcwihaba")

Diamond Licenses

Summary of work completed in 2006 and to date

- Ground magnetic geophysical surveys over five targets were completed.
- Access tracks and site clearing totaling 19 kilometers was completed.

- During the year our Geographical Information System was completed with all available geological, geophysical and geochemical data for these licenses captured onto the system. The data is being used to prioritize target areas for further exploration.
- Three diamond core drill holes were completed to investigate 3 priority targets in the Gcwihaba. The drill holes did not intersect kimberlite and given the depth of the drill holes (150 – 175 meters) no further work on these targets is recommended even though the magnetic anomaly signatures have not been explained.

Planned Exploration Program for 2007

- Drill evaluation of eight priority targets in the Gcwihaba area is scheduled for the 4th quarter.

Base and Precious Metals Licenses

Summary of work completed in 2006 and to date

- Four base and precious metal licenses were granted to the Company on October 1, 2005, and encompass an area of some 3,780 square kilometers. These licenses were issued for an initial period of three years, renewable for 2 two-year periods.
- The license areas were selected based on the results of a 1999 government geochemical soil sampling program, released and partially reported on in November 2001.
- Three diamond core drill holes were completed on the JEB intrusion (fka 2021A7) to a depth of between 206 – 225 meters. The JEB target is located in the Company's southern most license block and lies south of the Gumare fault. Various half core samples were submitted for multi-element analysis. The results of this multi-element analysis were subject to further study to determine Ni sulfide potential. The metal tenor of the sulfides in the JEB rocks have 1.75% Ni. However, it appears that based on all the data that these rocks crystallized from magma too differentiated to have potential for significant sulfide ores as most of the Ni will have been extracted from the magma by earlier crystallizing olivine and pyroxene.

Planned Exploration Program for 2007

- There are several zones of co-incident base metal anomalies that require follow-up sampling as a first step in the evaluation process. A Chalcophyle Index has been prepared and is currently being reviewed by the Company's consultants in preparation to assist in the prioritization of these zones for further drill testing.
- Exploratory drilling of suspected base metal deposits to determine their nature, composition and size will take place in the 3rd quarter.

LIQUIDITY AND CAPITAL RESOURCES

As at December 31, 2006, the Company had net working capital of $213,702 (2005: $296,541), which included cash and equivalents $201,177 (2005: $289,810). These funds are managed in-house in accordance with specific investment criteria approved by the board of directors, the primary objective being the preservation of capital to assure funding for exploration activities. The Company does not hedge its activities or otherwise use derivatives. At year end the Company did not have any material contractual obligations. The Company is required to spend a minimum on prospecting over the period of its licenses (Newdico: $1.7 million, Gcwihaba: $0.34 million). To date, the Company has exceeded this requirement in the Newdico project.

Financial Instruments

The carrying amounts reflected in the consolidated balance sheets for cash and equivalents, accounts receivable and accounts payable and accrued liabilities approximate their fair values due to the short maturities of these instruments. Due to the nature of the Company's operations, there is no significant credit or interest rate risk.

Operating Activities

Cash outflow used in operating activities decreased from $340,924 in fiscal December 31, 2005 to $284,395 for the year ended December 31, 2006. This decrease is due to the result in gains in foreign exchange.

SELECTED ANNUAL AND QUARTERLY FINANCIAL INFORMATION

ANNUAL INFORMATION

(in US dollars)	Fiscal Year Dec. 31 2006	Nine Months Ended Dec. 31 2005	Fiscal Year Mar. 31 2005
Total Revenues	–	–	–
Loss before non-controlling interest	541,132	470,811	620,822
Basic and diluted loss per share - cents	$0.04	$0.04	$0.07
Non-controlling interest	–	–	–
Net Loss for the Year	541,132	470,811	620,822
Basic and diluted loss per share - cents	$0.04	$0.04	$0.07
Total Assets	3,472,693	2,032,426	2,087,421
Total long term liabilities	245,491	280,642	237,008
Cash dividends declared	–	–	–

QUARTERLY INFORMATION

(in US dollars)

	Quarter 1	Quarter 2	Quarter 3	Quarter 4
Fiscal Year 2005 (ended March 31, 2005)				
Total Revenues	–	–	–	–
Loss for the period	75,106	185,742	113,981	245,993
Basic and diluted loss per share - cents	$0.01	$0.02	$0.01	$0.03
Total assets	1,422,230	1,408,529	1,842,605	2,087,421
Total long term liabilities	213,549	237,245	237,245	237,008
Fiscal Period 2005* (ended December 31, 2005)				
Total Revenues	–	–	–	
Loss for the period	83,068	190,070	197,673	
Basic and diluted loss per share - cents	$0.01	$0.02	$0.02	
Total assets	2,171,006	2,166,670	2,032,426	
Total long term liabilities	294,236	294,236	280,642	

* Transitional period for year end change to December 31

	Quarter 1	Quarter 2	Quarter 3	Quarter 4
Fiscal Year 2006 (ended December 31, 2006)				
Total Revenues	–	–	–	–
Loss for the period	156,252	234,194	89,720	60,966
Basic and diluted loss per share - cents	$0.01	$0.02	$0.01	$0.00
Total assets	2,689,555	2,891,225	3,278,118	3,472,693
Total long term liabilities	289,490	235,769	219,441	245,491

Investing Activities

Cash flow applied in investing activities increased to $1,508,994 for the year ended December 31, 2006 (2005: $281,249). $693,394 or 93.1% of the exploration expenditures were spent on the Newdico properties and $51,108 or 6.9% of the expenditures were on the Gcwihaba properties. Total expenditures of $744,502 on exploration properties for the period ended December 31, 2006 were attributable to the Newdico and Gcwihaba projects in northwest Botswana and included the 10% share funded by the Trans Hex Group for the Newdico project. During the year the Company acquired a Mobile drill rig and support vehicles at a total cost of $752,625. There were no material disposals of capital assets or investments during the year.

In November 2006, the board of directors of Newdico approved an exploration program and budget for the period January 1, to December 31, 2007 that calls for expenditures totaling approximately Pula 10.6 million (approximately $1.7 million as of March 22, 2007). Trans Hex Group is presently responsible for funding 10% of the expenses of this company. The approved exploration program includes provision for additional drilling, soil sampling, airborne and ground magnetics and ground gravity surveying, geophysical interpretation.

The required third year diamond exploration program expenditures, including license fees, for Gcwihaba amount to approximately Pula 0.42 million (approximately $0.07 million as of March 22, 2007). Gcwihaba's expenditures will exceed this required amount. The required expenditure in the first year of the base metal exploration program amounts to approximately Pula 0.20 million (approximately $0.03 million as of March 22, 2007). Gcwihaba expects to meet or exceed this requirement.

Financing Activities

Following the restructuring of Tsodilo in April 2002 and the cancellation of the shares formerly held by Trans Hex, the source of financing for the Company's activities changed from debt (related party) finance to equity, through the issue of units by way of non-brokered private placements. Each unit has consisted of one common share of the Company and one or one-half a warrant of the Company, with each full such warrant entitling the holder to purchase one common share of the Company for a purchase price equal to the unit price for a period of two years from the date of issuance. During the year ended December 31, 2006 the Company received proceeds in the amount of $1,739,907 from the issuance of common shares upon the exercise of warrants during the fiscal period.

Subsequent to the fiscal period end, the Company issued, through non-brokered private placement 141,516 units at a price of $0.68 (C$0.80) per unit for gross proceeds of $95,853. Each unit consists of one common share of the Company and one warrant of the Company, each warrant entitling the holder to purchase one common share of the Company at a price of C$0.80 for a period of two years. The common shares, warrants and warrant shares are subject to a hold period of 12 months, as agreed to by the parties, expiring on February 15, 2008.

Tsodilo expects to raise the amounts required to fund its 90% share of the Newdico project, the Gcwihaba projects and corporate general and administration expenses, by way of negotiated non-brokered private placements.

RESULTS OF OPERATIONS

On a consolidated basis Tsodilo recorded a net loss of $541,132 in the fiscal year ended December 31, 2006 ($0.04 cents per common share) compared to a net loss of $470,811 in the nine month fiscal period ended December 31, 2005 ($0.04 cents per common share). The Company experienced increases in travel, investor relations and office and admin expenses reflecting increased activity in general corporate activity partially offset by reductions in consulting and legal and audit as a result of less reliance on outside consultants and professional services. The increase in stock option expense reflects the timing of option grants and the change in year end from March 31 to December 31 in 2005, resulting in options issued in one period would have been reported in the next fiscal if the year end had not been changed.

Exploration expenditure on all projects amounted to $744,502 during the year ended December 31, 2006 compared to $282,977 for the period ended December 31, 2005. Exploration expenditure incurred on the Newdico project for the year ended December 31, 2006 was $693,394 compared to $239,505 for the period ended December 31, 2005. The principal components of the Newdico exploration program were: (a) additional soil sampling and the completion of the processing and analysis of the soil samples; (b) commissioning of further ground magnetic and gravity survey of selected aeromagnetic anomalies; (c) analyzing detailed proprietary aeromagnetic maps covering the target areas;

and (d) commencement of a reverse circulation drilling program on selected targets. Exploration expenditure incurred on the Gcwihaba project for the year ended December 31, 2006 was $51,108 compared to $43,472 for the period ended December 31, 2005. The principal component of the Gcwihaba exploration program was commencement of a reverse circulation drilling program on selected targets

PERSONNEL

At December 31, 2006 the Company and its subsidiaries employed eighteen (18) individuals as compared to six at December 31, 2005, including senior officers, administrative and operations personnel including those on short-term contract bases.

FOURTH QUARTER – 2006

The fourth quarter was a normal operating period for a quarter and year end. Having acquired drilling equipment during the year, the Company was able to continue its drilling program to the end of the year. Operating expenses were at normal levels for the last quarter of the year.

RISKS AND UNCERTAINTIES

Tsodilo's primary objective is the discovery of an economic kimberlite diamond deposit capable of rapid advancement to feasibility stage and ultimate development as a producing property. The discovery of a kimberlite is only the first step in the exploration process. Subsequent evaluation begins with caustic fusion diamond analysis of the kimberlite and, if results warrant, continues through progressively larger mini-bulk and bulk samples in order to make an increasingly accurate determination of the content and quality of the diamonds. Early stages of kimberlite evaluation provide an initial qualitative assessment rather than an accurate indication of either the grade of the ore body or the value per carat of the diamonds. Collection of larger bulk samples and formal appraisal of a commercial-size parcel of diamonds are necessary to make an accurate determination of these parameters. At any stage in the process, the results may indicate that the deposit lacks the required economic value.

Capital Requirements

In the absence of cash flow from operations, Tsodilo relies on capital markets to fund its operations. The ongoing exploration and eventual successful development of a diamond mine would require significant additional financing. There can be no assurance that adequate funding will be available, or available under terms favorable to the Company, for these purposes when ultimately required. The exploration and development of mineral deposits involve significant financial risks over an extended period of time. Even a combination of careful evaluation, experience and knowledge may not eliminate these risks. While discovery of a diamond deposit may result in substantial rewards, few exploration properties ultimately become producing mines.

Off-Balance Sheet Arrangements

The Company has not entered into any off-balance sheet financing arrangements.

Exploration Risks

The Company's operations are subject to all the hazards and risks normally incident to the exploration, development and mining of diamond deposits, any of which could result in damage to life or property, environmental damage and possible legal liability for any or all damage. Whether a diamond deposit will ultimately be commercially viable depends on a number of factors, including the particular attributes of the deposit such as the deposit's size; the quality and quantity of the diamonds; its proximity to existing infrastructure; financing costs and the prevailing prices for diamonds. Also of key importance are government regulations, including those relating to prices, taxes, royalties, land tenure, land use, the importing and exporting of diamonds and production plant and equipment, and environmental protection. The effects of these factors cannot be accurately predicted, but any combination of them may impede the development of a deposit or render it uneconomic.

At this time, the major portion of the Company's exploration activity is carried out in partnership with another party. Doing so allows the Company to maximize its exposure to promising exploration opportunities, to manage the risks inherent in diamond exploration, and to optimize its use of financial and management resources.

Currency Risks

The Company's financing has generally been received in United States dollars while significant portions of its operating expenses has been and will be incurred in Botswana Pula. On May 29, 2005, the Botswana Minister of Finance and Development Planning announced a 12% devaluation of the pula against a basket of currencies, as well as a change in the system of exchange-rate adjustments to a crawling peg rather than the discrete steps previously used, in order to improve Botswana's competitiveness. This action has stabilized the current pula / dollar rates similar to those in 2002.

Key Personnel

The Company is dependent upon on a relatively small number of key employees, the loss of any of whom could have an adverse effect on the Company. The Company currently does not have key personal insurance on these individuals.

ACCOUNTING STANDARDS

Tsodilo follows Canadian generally accepted accounting principles. The Company has adopted the policy of deferring property specific acquisition and exploration costs. Deferred costs relating to properties that are relinquished, or where continued exploration is deemed inappropriate, are written off in the year such assessment is made. If Tsodilo adopted a policy of expensing all exploration costs, the Company's asset base, shareholders' equity, and loss from operations would be materially different.

Changes in Accounting Policies including Initial Adoption

There were no changes in accounting policies for the fiscal year ended December 31, 2006. The following accounting policies impact 2007.

Effective January 1, 2007, the Company will be required to adopt the Canadian Institute of Chartered Accountants ("CICA") Handbook Section 1506. This Section establishes criteria for changing accounting policies, together with treatment and disclosure of changes in accounting policies and estimates and correction of errors. The Company is assessing the impact of the adoption of Section 1506 on the consolidated financial statements of the Company.

Effective January 1, 2007, the Company will be required to adopt the Canadian Institute of Chartered Accountants ("CICA") Handbook Section 1530. This Section establishes standards for reporting and display of comprehensive income. It does not address issues of recognition or measurement for comprehensive income and its components. The Company is assessing the impact of the adoption of Section 1506 on the consolidated financial statements of the Company.

Effective January 1, 2007, the Company will be required to adopt CICA Handbook Section 3051 which replaces Section 3050. This Section establishes standards for accounting for investments subject to significant influence and for measuring and disclosing certain other non-financial instrument investments. The adoption of Section 3051 is not expected to have a material impact on the consolidated financial statements of the Company.

Effective January 1, 2007 the Company will be required to adopt CICA Handbook Section 3251 which replaces Section 3250. This Section establishes standards for the presentation of equity and changes in equity during the reporting period. The adoption of Section 3251 is not expected to have a material impact on the consolidated financial statements of the Company.

Effective January 1, 2007, the Company will be required to adopt the changes to CICA Handbook Section 3855 and to adopt Section 3861 which replaces Section 3250. Section 3855 establishes standards for recognizing and measuring financial assets, financial liabilities and non-financial derivatives. Section 3861 establishes standards for presentation of financial instruments and non-financial derivatives, and identifies the information that should be disclosed about them. The Company is assessing the impact of the adoption of Sections 3855 and 3861 on the consolidated financial statements of the Company.

Effective January 1, 2007, the Company will be required to adopt the changes to CICA Handbook Section 3865. This Section establishes standards for when and how hedge accounting may be applied. The adoption of Section 3865 is not expected to have a material impact on the consolidated financial statements of the Company.

Over the next five years the CICA will adopt its new strategic plan for the direction of accounting standards in Canada which was ratified in January 2006. As part of that plan, accounting standards in Canada for public companies will converge with International Financial Report Standards (IFRS) over the next five years. The Company continues to monitor and assess the impact of the planned convergence of Canadian GAAP with IFRS.

DISCLOSURE CONTROLS

The Company's Chief Executive Officer and Chief Financial Officer are responsible for establishing and maintaining the Company's disclosure controls and procedures. The Chief Executive Officer and the Chief Financial Officer, after evaluating the effectiveness of the Company's disclosure controls and procedures as at December 31, 2006, have concluded that the Company's disclosure controls and procedures were adequate and effective to ensure that material information relating to the Company would have been known to them.

RELATED PARTY TRANSACTIONS

During the year ended December 31, 2006, the Company borrowed $100,000 on an interim basis from a person who is an officer and director of the Company. The loan had no interest rate, no maturity date, and no terms of repayment. The loan was repaid during the year. The Company did not enter into transactions with related parties during the year ended December 31, 2005.

OUTLOOK

Diamond exploration remains a high-risk undertaking requiring patience and persistence. Despite difficult capital markets in the junior resource sector, the Company remains committed to international diamond exploration through carefully managed programs.

ADDITIONAL INFORMATION

Additional information relating to Tsodilo Resources Limited is available on its website www.TsodiloResources.com or through SEDAR at www.sedar.com.

FORWARD-LOOKING STATEMENTS

The Annual Report, including this MD&A, contains certain forward-looking statements related to, among other things, expected future events and the financial and operating results of the Company. Forward-looking statements are subject to inherent risks and uncertainties including, but not limited to, market and general economic conditions, changes in regulatory environments affecting the Company's business and the availability and terms of financing. Other risks are outlined in the Uncertainties and Risk Factors section of this MD&A. Consequently, actual results and events may differ materially from those included in, contemplated or implied by such forward looking statements for a variety of reasons. Readers are therefore cautioned not to place undue reliance on any forward-looking statement. The Company disclaims any intention and assumes no obligation to update any forward-looking statement even if such information becomes available as a result of future events or for any other reason.

L. Kirk Boyd

Chief Financial Officer

March 22, 2007

Financial Reporting Responsibility of Management

The annual report and consolidated financial statements have been prepared by management. The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and include amounts that are based on informed judgments and best estimates. The financial information presented in this annual report is consistent with the consolidated financial statements. Management acknowledges responsibility for the fairness, integrity and objectivity of all information contained in the annual report including the consolidated financial statements. Management is also responsible for the maintenance of financial and operating systems, which include effective controls to provide reasonable assurance that assets are properly protected and that relevant and reliable financial information is produced. Our independent auditors have the responsibility of auditing the consolidated financial statements and expressing an opinion on them.

The Board of Directors, through its Audit Committee, is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control. The Audit Committee is composed of three directors, all of whom qualify as unrelated directors and are independent of management and free from any interest or business relationship which could, or could be perceived to, materially interfere with their ability to act in the best interests of the Company. This committee meets periodically with management and the external auditors to review accounting, auditing, internal control and financial reporting matters. The Audit Committee reviews the annual financial statements before they are presented to the Board of Directors for approval and considers the independence of the auditors.

The financial statements for the period ended December 31, 2006 have been audited by KPMG Inc., the external auditors, in accordance with Canadian generally accepted auditing standards on behalf of the shareholders. Their report follows hereafter.

James M. Bruchs
President and Chief Executive Officer
March 22, 2007

L. Kirk Boyd
Chief Financial Officer
March 22, 2007

Auditors' Report to the Shareholders of Tsodilo Resources Limited

We have audited the consolidated balance sheets of Tsodilo Resources Limited as at December 31, 2006 and the consolidated statements of operations, deficit and cash flows for each of the years in the two-year period ended December 31, 2006. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2006 and the results of its operations and its cash flows for each of the years in the two-year period ended December 31, 2006 in accordance with Canadian generally accepted accounting principles.

KPMG Inc.

Registered accountants and auditors

Bloemfontein, South Africa

March 22, 2007

Tsodilo Resources Limited

Consolidated Balance Sheets

As at December 31, 2006 and 2005

(in United States dollars – note 2)

	2006	2005
ASSETS		
Current		
Cash and equivalents	**201,177**	289,810
Amounts receivable and prepaid expenses	**53,055**	28,055
	254,232	317,865
Exploration Properties *(note 3)*	**2,424,118**	1,679,616
Property, Plant and Equipment *(note 4)*	**794,343**	34,945
	3,472,693	2,032,426
LIABILITIES		
Current		
Accounts payable and accrued liabilities	**40,530**	21,324
NON-CONTROLLING INTEREST *(note 3)*	**245,491**	280,642
SHAREHOLDERS' EQUITY		
Share Capital *(note 5)*	**27,024,564**	26,218,172
Warrants *(note 5)*	**1,018,683**	140,112
Contributed Surplus *(note 5)*	**6,336,204**	6,023,823
Cumulative Translation	**(837,425)**	(837,425)
Deficit	**(30,355,354)**	(29,814,222)
	3,186,672	1,730,460
	3,472,693	2,032,426

Going Concern *(note 1)*

Subsequent events *(note 5)*

Commitments *(note 11)*

APPROVED ON BEHALF OF THE BOARD OF DIRECTORS

James M. Bruchs
Director

Patrick C. McGinley
Director

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

Tsodilo Resources Limited

Consolidated Statements of Operations

For the years ended December 31, 2006 and 2005
(in United States dollars – note 2)

	2006	2005
EXPENSES		
Consulting fees	-	17,939
Corporate remuneration	**124,254**	99,844
Corporate travel and subsistence	**36,089**	5,029
Investor relations	**74,437**	35,374
Legal and audit	**37,392**	56,799
Office and administration	**67,305**	40,836
Amortization	**5,092**	1,688
Foreign exchange (gain)/loss	**(60,876)**	50,546
Stock-based compensation *(note 5)*	**257,439**	162,756
	541,132	470,811
Loss before non-controlling interest	**(541,132)**	(470,811)
Non-controlling interest	-	–
Loss for the period	**(541,132)**	(470,811)
Basic and diluted loss per share - cents *(note 7)*	**($0.04)**	($0.04)

Consolidated Statements of Deficit

For the years ended December 31
(in United States dollars – note 2)

	2006	2005
Deficit – Beginning of period	**(29,814,222)**	(29,343,411)
Loss for the year	**(541,132)**	(470,811)
Deficit - End of year	**(30,355,354)**	(29,814,222)

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

Tsodilo Resources Limited

Consolidated Statements of Cash Flows

For the years ended December 31, 2006 and 2005
(in United States dollars – note 2)

	2006	2005
CASH PROVIDED BY (USED IN):		
OPERATING ACTIVITIES		
Loss for the year	**(541,132)**	(470,811)
Adjustments for non-cash items:		
Amortization	**5,092**	1,688
Stock-based compensation *(note 5)*	**257,439**	162,756
	(278,601)	(306,367)
Net change in non-cash working capital balances	**(5,794)**	34,557
	(284,395)	(340,924)
INVESTING ACTIVITIES		
Exploration properties	**(617,723)**	(273,924)
Additions to Property, Plant and Equipment	**(891,271)**	(7,325)
	(1,508,994)	(281,249)
FINANCING ACTIVITIES		
Issue of common shares	**1,739,905**	230,544
Contribution from non-controlling interest	**(35,151)**	43,634
	1,704,756	274,178
Change in cash and equivalents - For the period	**(88,633)**	(347,995)
Cash and equivalents - Beginning of period	**289,810**	637,805
Cash and equivalents - End of period	**201,177**	289,810

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

Tsodilo Resources Limited
Notes to the Consolidated Financial Statements

For the years ended December 31, 2006 and 2005

1. NATURE OF OPERATIONS AND GOING CONCERN

Tsodilo Resources Limited ("Tsodilo" or the "Company") is an international diamond exploration company engaged in the process of exploring its mineral properties in northwest Botswana. The Company has not yet determined whether these properties contain reserves that can be economically mined. As an exploration stage company, the recoverability of amounts shown for exploration expenditures is dependent upon the discovery of reserves that can be economically mined, the securing and maintenance of the interests in the properties, the ability of the Company to obtain the necessary financing to complete the development, and future production or proceeds from the disposition thereof. The Company is also actively reviewing additional opportunities within Africa.

As at December 31, 2006, the Company reported an accumulated deficit of $30,355,354 (2005: $29,814,222) and cash outflows from operations $284,395 (2005: $340,924) for the period then ended. The cash position of the Company is insufficient to finance continued exploration. The continuity of the Company's operations is dependent on Tsodilo raising future financing for working capital, the continued exploration and development of its properties, and for acquisition and development costs of new project opportunities. There can be no assurance that adequate financing will be available, or available under terms favorable to the Company. These financial statements have been prepared on a going concern basis that assumes the continuity of operations and realization of assets and settlement of liabilities in the normal course of business. Should it be determined that the Company is no longer a going concern, adjustments, which could be significant, would be required to the carrying value of assets.

Tsodilo expects to raise amounts to fund continued exploration by way of negotiated non-brokered private placements (refer note 5).

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of consolidation and preparation of the consolidated financial statements

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and include the accounts of the Company and its direct and indirect subsidiaries. All inter-company transactions and balances have been eliminated.

Group Companies: December 31, 2006 and 2005

	2006	2005
Tsodilo Resources Bermuda Limited	**100%**	100%
Gcwihaba Resources (Proprietary) Ltd (Botswana) ("Gcwihaba")	**100%**	100%
Newdico (Proprietary) Limited (Botswana) ("Newdico")	**90%** *(note 3)*	81% *(note 3)*

Earnings per share

Basic Earnings-Per-Share (EPS) is computed as net income (loss) applicable to common stockholders' divided by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur from common shares issued through stock options, warrants and other convertible securities when the effect would be dilutive.

Use of estimates

The preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements. The most significant estimates are related to the recoverability of exploration expenditures, fixed assets and contingencies. Actual results could differ from those estimates.

Exploration properties

All costs relating to the acquisition, exploration and development of non-producing mining properties are capitalized as incurred. The amounts capitalized represent costs to be charged to operations in the future and do not necessarily reflect the present or future values of the particular properties.

If a property proceeds to development, these costs become part of preproduction and development costs of the mine and will be amortized over the expected life of the mine. If a property is abandoned, sold or continued exploration is not deemed appropriate in the foreseeable future or when other events and circumstances indicate that the carrying amount may not be recovered, the related costs and expenditures are written down to the net recoverable amount at the time the determination is made. Proceeds from the sale of exploration properties are credited to the costs of the relevant property.

Exploration costs that do not relate to specific non-producing mining properties are expensed as incurred.

Property, Plant and Equipment

Property, plant and equipment are amortized principally on a straight-line basis over their estimated useful lives of three to ten years. Property, plant and equipment awaiting installation on site are not amortized until they are commissioned. Property, plant and equipment are reviewed for impairment and if deemed impaired, an impairment loss is measured and recorded based on the net recoverable value of the asset.

Foreign currency translation

The Company's functional and reporting currency is the US dollar. The Company's subsidiaries are accounted for as integrated foreign operations. Transactions of the Company and its subsidiaries originating in foreign currencies are translated at the rates in effect at the time of the transaction. Monetary items are denominated in foreign currencies which are translated to US dollar at exchange rates in effect at the balance sheet dates and non-monetary items are translated at rates of exchange in effect when the assets were acquired or obligations incurred. Revenue and expense items are translated at the average rate prevailing during the year except for depreciation, depletion, amortization and write-downs, which are translated at the same exchange rates as the assets to which they relate. Foreign exchange gains and losses are included in the statement of operations.

Cash and Equivalents

Cash and equivalents are comprised of cash, term deposits and money market instruments with investment grade credit ratings and market maturity dates remaining of 90 days or less from the date of acquisition.

Income Taxes

The Company uses the asset and liability method of accounting for income taxes. Assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. A valuation allowance is recorded against any future income to an asset if it is more than likely than not that the asset will not be realized. Future income tax assets and liabilities are measured using tax rates in effect for the period in which those temporary differences are expected to be recovered or settled. The effect on future income tax assets and liabilities of a change in tax rates or laws is recognized as part of the provision for income taxes in the period the changes are considered substantively enacted.

Stock-Based Compensation Plans

Tsodilo has a Stock Option Plan (refer to note 5). Under the Stock Option Plan, the Company may grant options to directors, officers and employees for up to 1,789,750 shares of common stock. The exercise price is determined by the Chairman of the Compensation Committee and the President and CEO in consultation with the board of directors, but is not less than the market price of the Company's stock on the date of the grant. An option's maximum term is 5 years. The Company uses the fair value method of accounting for stock options. Under the fair value method stock-based payments are measured at the fair value of the equity investments and are amortized over the vesting period. Consideration paid on exercise of stock options is credited to common share capital.

3. EXPLORATION PROPERTIES

These may be summarized as follows:

	Newdico Botswana	**Gcwihaba Botswana**	**Total**
	$	$	$
Balance at March 31, 2005	1,260,547	136,092	1,396,639
Apr. to Dec. 2005 expenditures	239,505	43,472	282,977
Balance at December 31, 2005	**1,500,052**	**179,564**	**1,679,616**
Jan. to Dec. 2006 expenditures	693,394	51,108	744,502
Balance at December 31, 2006	**2,193,446**	**230,672**	**2,424,118**

A summary of the significant agreements entered into by the Company is as follows:

Newdico (Proprietary) Limited - Botswana

Newdico holds prospecting licenses in the Ngamiland District of northwest Botswana. The Company acquired the various licenses in 1999, 2001 and 2003. In 2005, the Company was reissued its prospecting licenses for an initial term of three years, and are renewable for 2 two year periods upon application and have a final expiry of 2012. The terms of the licenses also require Newdico to spend a minimum of Botswana Pula 8.6 million (approximately $1.4 million) on prospecting over this period, inclusive of the renewals.

Originally, Newdico was held 75% by Tsodilo and 25% by Trans Hex Group Limited ("THG"), with Tsodilo being the operator. THG has funded or been attributed to its proportionate share of expenditure and these amounts have been reflected as non-controlling interest of $245,491 (2005: $280,642) in the financial statements. During the year ended December 31, 2006, THG decided not to fund its proportional share of expenditures on cash calls and therefore as of January 1, 2007, the Company's interest in Newdico had effectively increased from 75% to 90% (2005: 81%) in accordance with the exploration agreement between the two parties.

Trans Hex Group has also advanced funds amounting to $205,591 (2005: $205,591) to Newdico, relating to exploration properties which have been written off in earlier years. This liability has not been recorded in these financial statements as it is repayable only from Trans Hex Group's share of any future earnings of Newdico after repayment of loans relating to the Newdico Project.

Some, or all, of the current licenses held by Newdico may be subject to the granting of a 2% free carried interest in any diamond mine or mines that may result thereon.

Gcwihaba Resources (Proprietary) Limited – Botswana

Gcwihaba, a wholly owned subsidiary of the Company, holds prospecting licenses in the southern Ngamiland project area.

Diamond Exploration

The terms of the licenses grant Gcwihaba the right to prospect for a total of three years to 2006, and were renewed for 2 two year period with a final expiry of 2010. The terms require Gcwihaba to spend a minimum of Botswana Pula 1.05 million (approximately $0.17 million) on prospecting over the initial period of the licenses exclusive of the current renewals.

Base and Precious Metal Exploration

The terms of the licenses grant Gcwihaba the right to prospect for a total of three years to 2008, and are renewable for 2 two year periods upon application and have a final expiry of 2012. The terms require Gcwihaba to spend a minimum of Botswana Pula 0.72 million (approximately $0.12 million) on prospecting over this period, exclusive of their current renewals.

4. PROPERTY, PLANT AND EQUIPMENT

December 31, 2005	Cost	Accumulated amortization	Book value
Vehicles	**40,473**	**21,555**	**18,918**
Furniture and Equipment	**32,595**	**16,568**	**16,027**
	73,068	**38,123**	**34,945**

December 31, 2006			
Vehicles	**887,855**	**132,387**	**755,468**
Furniture and Equipment	**76,484**	**37,609**	**38,875**
	964,339	**169,996**	**794,343**

An amount of $126,781 of the accumulated depreciation has been capitalized under exploration properties.

5. SHARE CAPITAL

Common Shares

Authorized

The authorized capital stock of the Company comprises an unlimited number of common shares.

Issued and outstanding

Details of the issued and outstanding common shares are as follows:

	Shares (number)	Amount $
Issued and outstanding at March 31, 2005	10,481,626	25,909,032
On exercise of warrants (including $78,596 reallocated from warrants) (b)	563,419	309,140
Issued and outstanding at December 31, 2005	**11,045,045**	**26,218,172**
On private placement for cash (i)	468,776	499,990
On private placement for cash (ii)	319,108	248,828
On private placement for cash (iii)	649,984	405,441
On private placement for cash (iv)	161,586	100,000
On private placement for cash (v)	791,339	485,648
Ascribed to warrants issued (b)	-	(933,515)
Issued and outstanding at December 31, 2006	13,435,838	27,024,564

(i) Private Placement

In January 2006, the Company issued, through a non-brokered private placement, 468,776 units of the Company at a price of $1.07 (C$1.25) per unit for gross proceeds to the Company of $499,990. Each unit consists of one common share of the Company and one warrant of the Company, each warrant entitling the holder to purchase one common share of the Company at a price of $0.87 (C$1.00) for a period of two years. The common shares, warrants and warrant shares are subject to a hold period of 12 months as agreed to by the parties, expiring on January 27, 2007.

(ii) Private Placement

In February 2006, the Company issued, through a non-brokered private placement, 319,108 units of the Company at a price of $0.78 (C$0.90) per unit for gross proceeds to the Company of $248,828. Each unit consists of one common share of the Company and one warrant of the Company, each warrant entitling the holder to purchase one common share of the Company at a price of $0.87 (C$1.00) for a period of two years. The common shares, warrants and warrant shares are subject to a statutory hold period under securities laws of 4 months, expiring on June 21, 2006.

(iii) Private Placement

In May 2006, the Company issued, through a non-brokered private placement 649,984 units of the Company at a price of $0.63 (C$0.70) per unit for gross proceeds to the Company of $405,441. Each unit consists of one common share of the Company and one warrant of the Company, each such warrant entitling the holder to purchase one common share of the Company at a price of $0.62 (C$0.70) for a period of two years. The common shares, warrants and warrant shares are subject to a negotiated hold period of 12 months, expiring on May 9, 2007.

(iv) Private Placement

In July 2006, the Company issued, through a non-brokered private placement 161,586 units of the Company at a price of $0.62 (C$0.70) per unit for gross proceeds to the Company of $100,000. Each unit consists of one common share of the Company and one warrant of the Company, each such warrant entitling the holder to purchase one common share of the Company at a price of $0.62 (C$0.70) for a period of two years. The common shares, warrants and warrant shares are subject to a negotiated hold period of 12 months, expiring on July 28, 2007.

(v) Private Placement

In September 2006, the Company issued, through a non-brokered private placement 791,339 units of the Company at a price of $0.63 (C$0.70) per unit for gross proceeds to the Company of $485,648. Each unit consists of one common share of the Company and one warrant of the Company, each such warrant entitling the holder to purchase one common share of the Company at a price of $0.63 (C$0.70) for a period of two years. The Company has negotiated finder's fees of $13,875, payable in accordance with the policies of the TSX Venture Exchange with respect to 500,000 units of the placement. The common shares, warrants and warrant shares are subject to a statutory hold period under securities laws of 4 months, expiring on January 27, 2007.

(vi) Private Placement

In February 2007, the Company issued, through a non-brokered private placement 141,516 units of the Company at a price of \$0.68 (C\$0.80) per unit for gross proceeds to the Company of \$95,853. Each unit consists of one common share of the Company and one warrant of the Company, each such warrant entitling the holder to purchase one common share of the Company at a price of \$0.68 (C\$0.80) for a period of two years. The common shares, warrants and warrant shares are subject to a negotiated hold period of 12 months, expiring on February 13, 2008.

(b) Warrants

As at December 31, 2006, the following warrants were outstanding:

		Number of Warrants			Value		
Expiry	**Exercise Price**	**Opening**	**Issued/ (Exercised) (Expired)**	**Closing**	**Opening (dollars)**	**Issued/ (Exercised) (Expired)**	**Closing (dollars)**
June 1, 2006	C\$0.75	65,024	(65,024)	-	14,164	(14,164)	-
October 14, 2006	C\$1.12	56,969	(56,969)	-	20,156	(20,156)	-
November 8, 2006	C\$2.35	26,668	(26,668)	-	20,622	(20,622)	-
March 4, 2007	C\$1.15	230,785	-	230,785	85,170	-	85,170
January 27, 2008	C\$1.00	-	468,776	468,776	-	146,788	146,788
February 21, 2008	C\$1.00	-	319,108	319,108	-	109,988	109,988
May 4, 2008	C\$0.70	-	649,984	649,984	-	167,886	167,886
July 19, 2008	C\$0.70	-	161,586	161,586	-	49,643	49,643
September 21, 2008	C\$0.70	-	791,339	791,339	-	459,208	459,208
		379,446	2,242,132	2,621,578	140,112	878,571	1,018,683

During the year 2,390,853 warrants issued and a value of \$933,813 was attributed as at December 31, 2006 (2005: none issued). During the year ended December 31, 2006 warrants were valued using the Black-Scholes model, using key assumptions of volatility ranging from 69-89%, a risk-free interest rate of 4.5%, a term equivalent to the life of the warrant, and reinvestment of all dividends in the Company.

(c) Contributed Surplus

As at March 31, 2005	5,846,718
Relating to expiry of warrants	14,349
Relating to issue of stock options	162,756
As at December 31, 2005	6,023,823
Relating to the expiry of warrants	54,942
Relating to issue of stock options	257,439
As at December 31, 2006	6,336,204

(d) Stock Option Plan

Outstanding stock options granted to directors, officers and employees at December 31, 2006 and December 31, 2005 were as follows:

Expiry	Price	Outstanding March 31, 2005	Granted/ (Cancelled/ Exercised)	Outstanding December 31, 2005	Granted	(Cancelled)		Outstanding December 31, 2006
June 24, 2007	C$0.15	150,000	(50,000)	100,000			(i)	**100,000**
September 18, 2007	C$0.23	150,000	(50,000)	100,000			(i)	**100,000**
December 31, 2007	C$0.41	50,000	-	50,000			(ii)	**50,000**
July 8, 2008	C$0.50	150,000	(50,000)	100,000			(ii)	**100,000**
January 1, 2009	C$0.75	60,000	-	60,000		(10,000)	(ii)	**50,000**
August 31, 2009	C$0.75	260,000	-	260,000		(10,000)	(ii)	**250,000**
January 3, 2010	C$1.85	85,000	(50,000)	35,000		(25,000)	(ii)	**10,000**
August 19, 2010	C$1.25	-	280,000	280,000		(20,000)	(ii)	**260,000**
January 3, 2011	C$1.25	-	-	-	85,000	(25,000)	(ii)	**60,000**
April 27, 2011	C$0.70	-	-	-	300,000		(ii)	**300,000**
August 18, 2011	C$0.70	-	-	-	65,000		(ii)	**65,000**
November 1, 2011	C$1.00	-	-	-	50,000		(ii)	**50,000**
		905,000	80,000	985,000	500,000	(90,000)		**1,395,000**
Options exercisable at end of year		696,250		680,000				**873,375**
Weighted average exercise price								
- issued		C$0.55		C$0.67				**C$0.76**
- outstanding		C$0.60		C$0.83				**C$0.80**
- exercisable		C$0.46		C$0.65				**C$0.79**

All options have a term of five years.

(i) These common share purchase options vest as to one-half immediately and one-half on the six-month anniversary of the date granted.

(ii) These common share purchase options vest as to one-quarter immediately and one-quarter on each of the six-month, 12-month and 18-month anniversaries of the date granted.

(iii) The Company recognized an expense of $257,439 (2005: $162,756) relating to the fair value of options granted or vesting during the year. The fair value of options granted was calculated using the Black-Scholes model, using key assumptions of volatility of 88%, a risk-free interest rate of 4%, a term equivalent to the life of the option, and reinvestment of all dividends in the Company. The Company will recognize expense of C$124,043 relating to options granted before December 31, 2006 but not yet vested.

On January 2, 2007, the Company issued 85,000 options under its Stock Option Plan to persons who were officers and employees of the Company.

6. INCOME TAXES

The recovery of income taxes varies from the amounts that would be computed by applying the Canadian federal and provincial statutory rate of approximately 36.12% (Dec. 2005 – 36.12%) to income before taxes as follows:

	December 31 2006	December 31 2005
Net loss for the period	(541,132)	(470,811)
Income tax (recovery) provision at Canadian statutory income tax rates	(195,457)	(170,057)
Current year losses not recognized	106,030	111,263
Permanent differences	89,427	58,794
Provision for (recovery of) income taxes	-	-

The following summarizes the principal temporary differences and related future tax effect:

	Dec 31 2006	Dec 31 2005
Property, Plant and Equipment	14,000	12,000
Exploration & Development - Canada	93,000	92,000
Exploration & Development - Botswana	(890,617)	(606,000)
Losses carried forward - Canada	1,389,000	1,585,000
Losses carried forward - Botswana	941,562	642,000
Other	42,000	42,000
Subtotal – future income tax asset	1,588,944	1,767,000
Valuation allowance	(1,588,944)	(1,767,000)
Net future income tax asset recorded	-	-

At December 31, 2006, the Company has Canadian net operating losses carried forward that expire as follows:

Loss	**Year of Expiry**	
740,000	2007	(1)
818,000	2008	(1)
697,000	2009	(1)
315,000	2010	(1)
369,000	2011	(1)
492,000	2012	*(1)
185,000	2012	*(2)
214,000	2013	(2)

* 2005 was a transitional year for year end change from March 31 to December 31. (1) expires March 31 and (2) expires December 31.

Total assessable losses relating to the activity in Botswana as at December 31, 2006 was $3,337,768 (December 31, 2005: $1,778,000) of which $2,606,760 (December 31, 2005: $1,680,000) have no expiry date.

7. LOSS PER SHARE

Loss per share is computed on the basis of the loss of $541,132 for the year ended December 31, 2006 (2005: $470,811) and the weighted average number of common or equivalent shares outstanding during period, December 31, 2006: 12,473,977 (2005: 10,811,496). The effect of stock options and warrants in computing diluted per share amounts for December 31, 2006 and December 31, 2005 is anti-dilutive.

8. RELATED PARTY TRANSACTIONS

During the year ended December 31, 2006, the Company borrowed $100,000 on an interim basis from a person who is an officer and director of the Company. The loan had no interest rate, no maturity date, and no terms of repayment. The loan was repaid during the year. The Company did not enter into transactions with related parties during the year ended December 31, 2005.

9. SEGMENTED INFORMATION

Substantially all working capital balances of the Company are situated at the head office in Canada and in Botswana. Materially all of the Company's property plant and equipment is presently located in Canada ($2,720) and Botswana ($791,623). The geographic distribution of the property acquisition costs and exploration expenditures is outlined in note 3.

10. FINANCIAL INSTRUMENTS

The carrying amounts reflected in the consolidated balance sheets for cash and equivalents, accounts receivable and accounts payable and accrued liabilities approximate their fair values due to the short maturities of these instruments.

11. COMMITMENTS

All operating leases that are for a period of no longer than one year are prepaid.

Minimum lease payments for leased storage space are as follows:

2008	27,216
2009	27,216

The lease commitment is for storage space in Botswana at an annual rental of BWP 158,888 per year for 2008 and 2009 converted at an exchange rate as of the date of the report to US dollar.

The Company holds prospecting licenses which require the Company to spend a specified minimum amount on prospecting over the period of the terms as outlined in note 3.

Corporate Information

DIRECTORS

James M. Bruchs
Gaborone, Botswana
Appointed as director in 2002

Patrick C. McGinley
Washington, D.C.
Appointed as director in 2002

R. Stuart Angus
Vancouver, British Columbia
Appointed as director in 2004

John R. Redmond
Potomac, Maryland
Appointed as director in 2005

OFFICERS

James M. Bruchs, B.Sc., J.D.
President and
Chief Executive Officer
Appointed in 2002

L. Kirk Boyd, B.Com.
Chief Financial Officer
Appointed in 2005

Gail McGinley
Corporate Secretary
Appointed in 2005

CORPORATE HEAD OFFICE

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AUDITORS

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LEGAL COUNSEL

Fasken Martineau DuMoulin LLP
Toronto, Ontario

REGISTRAR AND TRANSFER AGENT

Computershare Trust
Company of Canada
Toronto, Ontario

STOCK EXCHANGE LISTING

TSX Venture Exchange
Trading Symbol: TSD

Design: Macrae Design