

SAN MARCO RESOURCES INC.

Interim Financial Statements
For the Third Quarter ended
August 31, 2009
Management Discussion and Analysis

General

The purpose of this Management Discussion and Analysis (“MD&A”) is to explain management’s point of view on San Marco Resources Inc.’s (the “Company”) past performance and future outlook. This report also provides information to improve the reader’s understanding of the interim financial statements and related notes, and should therefore be read in conjunction with the interim financial statements of the Company and notes thereto for the nine months ended August 31, 2009. Additional information on the Company is available on SEDAR. The date of this MD&A is October 23, 2009.

Management

At the Annual General Meeting held on July 15, 2009 and subsequent appointments by the Board of Directors the Board now consists of the following new directors: Robert Willis P. Eng. CEO, Graham Thody CA Chairman of the Audit Committee, William Myckatin P. Eng., and R. Stuart (Tookie) Angus LLB. Christopher Dyakowski P. Geo, the previous CEO remains as a director of the Company. Leslie Fowler CA remains as CFO and Michael Mallard is Secretary and Vice President of corporate communications.

Nature of Business

The Company was incorporated on September 27, 2005 under the Company Act of British Columbia and commenced business on November 29, 2005. The Company is a natural resource company engaged in the acquisition and exploration of mining properties. The Company’s current holdings are the Alwin claims in the Kamloops Mining Division, British Columbia where the Company has acquired a 100% undivided interest.

In addition to the Alwin Property the Company has engaged qualified consultants to investigate possible precious metal properties in North America, Central America and South America. The costs of this work will be written off as incurred unless an agreement has been entered into to acquire a property.

Results of Operations

The Company’s net loss for the nine months ended August 31, 2009 was \$272,316 compared to the net loss of \$121,929 for the nine months ended August 31, 2008. The net loss for the three months ended August 31, 2009 was \$156,623 compared to the net loss of \$75,357 for the three months ended August 31, 2008. This loss resulted in a net loss of \$0.03 per share for the nine months ended August 31, 2009 compared to a net loss of \$0.02 per share for the nine months ended August 31, 2008.

The general and administration expenses for the nine months ended August 31, 2009 were \$275,175 compared to \$171,636 for the nine months ended August 31, 2008. The August 2008 expenses are primarily related to the Company obtaining its listing on the TSX Venture Exchange in December 2007 and the provision of a Stock Based Compensation Expense which results from the fair value of the stock options granted. The Stock Based Compensation Expense was expensed in the amount of \$84,604 in the period ended August 31, 2009.

The higher administrative expenses in the third quarter result from the new management establishing a permanent office, incurring higher professional fees and instituting a property investigation program. The first and second quarters of 2009 administrative expenses are primarily the result of recording the Compensation Expense related to the granting of additional stock options in the latter part of the year ended November 30, 2008. All expenses directly related to the development of the mineral property have been Capitalized as Deferred Exploration Costs.

The Company's has had preliminary exploration carried out on its projects but they have not been developed to a revenue producing stage.

In the quarter ended February 29, 2008 the Company recorded \$43,125 as a future income tax recovery. This amount is the offset to the charge to share capital representing the tax related to the renunciation of cumulative eligible exploration costs transferred to the subscribers of the flow through shares.

Summary of Quarterly Results

	3rd Quarter	2nd Quarter	1st Quarter	4th Quarter	3rd Quarter	2nd Quarter	1st Quarter	4th Quarter
	<u>2009</u>	<u>2009</u>	<u>2009</u>	<u>2008</u>	2008	<u>2008</u>	<u>2008</u>	<u>2007</u>
Three Months Ended	Aug 31, 2009	May 31 2009	Feb 28, 2009	Nov 30, 2008	Aug 31, 2008	May 31 2008	Feb 29, 2008	Nov 30, 2007
Total Revenue	nil	nil	nil	nil	nil	nil	nil	nil
Net Loss	(156,623)	(59,448)	(56,245)	(24,595)	(75,357)	(13,266)	(33,306)	(31,869)
Loss per share	(0.02)	(0.01)	(0.01)	(0.00)	(0.01)	(0.00)	(0.01)	(0.01)
Basic & Diluted	(0.02)	(0.01)	(0.01)	(0.00)	(0.01)	(0.00)	(0.01)	(0.01)
Total Assets	2,158,169	631,697	668,414	683,312	697,862	717,542	747,163	202,204

Exploration Activities

The Company did not incur any exploration costs during the nine month period ended August 31, 2009 as the planned property program was completed and reported on prior to November 30, 2008.

The Alwin Property, Kamloops Mining Division, British Columbia

By an Agreement dated December 7, 2005 as amended on March 14, 2007, the Company acquired a 100% undivided interest (subject to a 2% Net Smelter Return) in the Alwin Property situated near Logan Lake, British Columbia for a total consideration of \$50,000 and issuing 125,000 shares all of which has been completed.. The Alwin Property covers four mineral claims (totalling 575.136 hectares). Of these claims, two claims overstate three crown granted

claims whose under surface rights are included in a mining lease which is included in the mineral interests optioned by the Company. The Company has an option to purchase ¾ of the Net Smelter Return Royalty for \$1.5 million within five years from the date the Property is put into commercial production.

DEFERRED EXPLORATION COSTS ON ALWIN PROPERTY

	<u>August 31, 2009</u>	<u>Nov. 30, 2008</u>
Drilling sampling, prospecting and line cutting	\$ 251,359	\$ 251,359
Travel, supplies and field expenses	75,476	75,476
Project management fees	41,170	41,170
Geological surveys, consulting and reports	<u>96,900</u>	<u>96,900</u>
	464,905	464,905
LESS: BC MINING AND EXPLORATION TAX CREDIT	<u>(29,541)</u>	<u>(29,541)</u>
DEFERRED EXPLORATION END OF PERIOD	<u>\$ 435,364</u>	<u>\$ 435,364</u>

Exploration Program

The previously announced drill and associated exploration program has been completed and assay results have been published. The program consisted of seven diamond drill holes aggregating 1224.9 meters. Five holes were drilled in the vicinity of the former mine workings and three holes tested coincident alteration and IP chargeability anomalies extending away from the workings.. The host rock in all of the drill core is quartz monzonite of the Bethsaida phases of the Late Triassic-age GuichonCreek batholith. Five hundred and seventy eight samples were submitted to Acme Labs Ltd. The analytical results were published in a press release dated September 8, 2008.

Property Analysis

The Alwin property has historically been recognized as a small high grade copper resource confined to a main structural control. Recent drilling has removed this stigma, indicating the presence of porphyry style mineralization associated with the main structure (holes 08-01 and 08-02) and in two new areas of the property (holes 08-05 and 08-06).

Mineralization and alteration observed in holes 08-05 and 08-06 are believed similar in nature to mineralization and alteration of the Valley Copper deposit and are both located within two to three km of the mine. This in fact, may be a westerly extension of this very valuable deposit.

Liquidity and Capital Resources

The Company has no known mineral resources and is not in commercial production on any of its properties and accordingly, the Company does not generate cash from operations. The Company finances development and exploration activities by raising capital from equity markets from time to time. During the three months ended August 31, 2009 the Company issued 6,460,500 shares for \$1,622,625 new equity.

As at August 31, 2009 compared to November 30, 2008 the Company's liquidity and capital resources are as follows:

	August 31, 2009 \$	November 30, 2008 \$
Cash and receivables	1,612,530	166,698
Prepaid expenses	6,939	-
Payables and accrued liabilities	52,275	12,332

The Company's operations consist of acquisition, maintenance and exploration of mining properties. The Company's financial success will be dependent in the extent to which it can discover new mineral deposits.

Contractual commitments

The Company does not have any long term contractual commitments.

Off balance sheet arrangements

The Company has no off balance sheet arrangements.

Related party transactions

During the period ended August 31, 2009 the Company paid \$22,500 in management and administration fees to a company controlled by the former CEO, \$10,000 to the current CEO, and \$9,416 in legal fees to a firm in which former director W. Schmidt is a partner. .

These transactions are in the normal course of operations and are measured at the exchange amounts established and agreed to by the related parties.

Risks and uncertainties

The principal business of the Company is the exploration and development of mineral properties. Given the nature of the mining business, the limited extent of the Company's assets and the present stage of exploration, the following risks factors, among others, should be considered.

The Company is in the process of exploring its mineral properties and has not yet determined whether the properties contain economically recoverable reserves and, therefore, does not generate any revenues from production. The recovery of expenditures on mineral properties and the related deferred exploration expenditures are dependent on the existence of economically recoverable mineralization, the ability of the Company to obtain financing necessary to complete the exploration and development of the mineral properties, and upon future profitable production, or alternatively, on the sufficiency of proceeds from disposition. Mineral exploration is highly speculative in nature, involves many risks and frequently is non-productive. There is no assurance that the exploration efforts will be successful.

Since the Company does not generate any revenues from production, it may not have sufficient financial resources to undertake by itself all of its planned mineral acquisition and exploration

activities. Operations will continue to be financed primarily through the sale of securities, such as common shares. The Company will need to continue its reliance on sale of such securities for future financing, which may result in dilution to existing shareholders. In addition, the amount of additional funds required may not be available under favourable terms, if at all, and will depend largely on the market conditions.

Change in accounting policy

Effective on December 1, 2007, the Company adopted the Canadian Institute of Chartered Accounts (“CICA”) Handbook Section 3862, “Financial Instruments – Disclosure” and Section 3863, “Financial Instruments – Presentation”. These sections carry forward the former presentation requirements and increase the emphasis on recognition and management of the risks associated with recognized and unrecognized financial instruments. The adoption of these sections had no impact on the financial position or net earnings for the period ended August 31, 2008.

Effective on December 1, 2007, the Company adopted the CICA Handbook Section 1535 “Capital Disclosures”, which requires disclosure of information about an entity’s capital and its objectives, policies and process for managing capital.

Effective on December 1, 2007 the Company adopted CICA Handbook Section 1400, “General Standards of Financial Statement Presentation”. These sections provide revised guidance on management’s responsibility to assess and disclose the Company’s ability to continue as a concern. The adoption of this section had no significant impact on the Company’s financial statements.

Effective December 1, 2007 the Company has adopted the “CICA” Handbook section 1530. Comprehensive loss reflects net loss and other comprehensive income (loss) for the year. Other comprehensive income (loss) includes changes in unrealized foreign currency translation amounts arising from self-sustaining foreign operations, unrealized gains and losses on available-for-sale assets and changes in the fair value of derivatives designated as cash flow hedges to the extent they are effective. The adoption of this section had no impact of the statement of operations for period ended August 31, 2008.

International Financial Reporting Standards (“IFRS”)

In 2006, the Canadian Accounting Standards Board (“AcSB”) published a new strategic plan that will significantly affect financial reporting standards for Canadian companies. The AcSB strategic plan outlines the convergence of Canadian generally accepted accounting principals (“Canadian GAAP”) with IFRS over an expected five-year transitional period. In February 2008, the AcSB announced that 2011 is the changeover date for publicly accountable companies to use IFRS, replacing Canadian GAAP. This 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 could require the restatement for comparative purposes of amounts reported by the Company for the year ended November 30, 2010. The Company is currently assessing the financial reporting impact of the transition to IFRS.

Critical Accounting Estimates

The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of expenses during the reporting period. Significant areas requiring the use of management estimates relate to the determination of stock based compensation, impairment of mineral properties, deferred exploration costs and Provincial tax credit. Actual results could differ from those reported. By their nature, these estimates are subject to measurement uncertainty and impact on the financial statements of future periods could be material. The financial statements have, in management's opinion, been properly prepared within the significant policies summarized in this note.

Stock-Based Compensation

The Company follows the recommendation of CICA handbook Section 3870 "Stock-based Compensation and Other Stock-based Payments". Under this section the compensation expense for stock options grants to employees and non-employees is recorded at the fair value of the stock options issued at the grant date, which is determined using the Black-Scholes Option Pricing Model.

Compensation expense for stock options granted to non-employees is recognized as the options are earned and the services are provided. Compensation expense for stock options granted to employees is amortized over the vesting period. Consideration paid by employees and non-employees on the exercise of stock options is recorded as share capital.

Financial Instruments

Effective November 1, 2006, the Company adopted CICA Section 3855, *Financial Instruments – Recognition and Measurement*. The section establishes standards for determining when a financial asset, financial liability or non-financial derivative is to be recognized on the balance sheet and whether it will be measured using a cost-based or fair value method. The adoption of this new accounting policy had no significant effect on these financial statements.

Disclosure of outstanding share data

As at October 14, 2009 the Company had 14,142,329 common shares issued and outstanding. As of August 31, 2009 the Company has issued 221,346 incentive stock options exercisable at \$0.25 per share and 280,000 at \$0.40 to directors, officers and employees. On October 5, 2009 the Company granted 1,250,000 additional stock options to its directors, officer, employees and consultants. These options are exercisable for a period of 3 years at \$0.51 per share. This increases the total number of options to 1,751,346 as at October 14, 2009.

There are one-half non-transferable common share purchase warrants outstanding convertible into 3,205,000 common shares. Each whole warrant can be exercisable to purchase a share during the two year period ending August 19, 2011 at a price of \$0.45 in the first year and \$0.65 in the second year.

The warrants provide that if the closing price of the Company's shares equals or exceeds \$0.90 per share for 20 consecutive trading days after December 19, 2009, the Company may give, within five trading days thereof, notice to the warrant holders that the warrants must be exercised within 30 days (including non-trading days) of such notice or the warrants will terminate.

The shares and any shares issued on exercise of the warrants are subject to restrictions on transfer until December 20, 2009.