

SILVERMEX RESOURCES INC.

(formerly Genco Resources Ltd.)
Consolidated Financial Statements
December 31, 2010 and 2009

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Independent Auditor's Report

To the Shareholders of Silvermex Resources Inc.

We have audited the accompanying consolidated financial statements of Silvermex Resources Inc, which comprise the consolidated balance sheet as at December 31, 2010, and the consolidated statements of loss and comprehensive loss, shareholders' equity, and cash flows for the year then ended, and notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Silvermex Resources Inc. as at December 31, 2010 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Other Matter

The consolidated balance sheet as at December 31, 2009 and consolidated statements of loss and comprehensive loss, shareholder's equity, and cash flows for the year then ended were audited by another auditor who issued an unmodified opinion on March 24, 2010.

(Signed) Deloitte & Touche LLP

Chartered Accountants
March 31, 2011
Vancouver, Canada

SILVERMEX RESOURCES INC.

(formerly Genco Resources Ltd.)

Consolidated Balance Sheets

(Expressed in Canadian dollars)

	December 31 2010 \$	December 31 2009 \$
Assets		
Current assets		
Cash and cash equivalents	17,414,536	625,171
Short-term investments	7,400,203	-
Accounts receivable, net (Note 8)	2,288,506	357,021
Related party receivable (Note 18)	93,000	-
Note receivable, net (Note 7)	2,000,000	2,566,201
Inventory (Note 9)	708,423	231,207
Prepaid expenses and deposits	252,261	137,244
	<u>30,156,929</u>	<u>3,916,844</u>
Mineral property interests (Note 10)	28,423,086	48,493
Property, plant, and equipment, net (Note 11)	<u>35,726,379</u>	<u>33,089,661</u>
	<u><u>94,306,394</u></u>	<u><u>37,054,998</u></u>
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	2,937,783	2,602,117
Deferred gain on sale of Chief Consolidated Mining Company (Note 7)	1,293,265	1,418,501
Current portion of long term debt (Note 12)	487,147	516,937
	<u>4,718,195</u>	<u>4,537,555</u>
Long term debt (Note 12)	917,494	516,936
Asset retirement obligation (Note 13)	1,492,940	105,740
Future income tax (Note 15)	<u>10,955,286</u>	<u>5,943,309</u>
	<u>18,083,915</u>	<u>11,103,540</u>
Shareholders' equity		
Share capital (Note 14)	132,172,307	52,273,254
Contributed surplus	23,689,175	11,849,261
Deficit	<u>(79,639,003)</u>	<u>(38,171,057)</u>
	<u>76,222,479</u>	<u>25,951,458</u>
	<u><u>94,306,394</u></u>	<u><u>37,054,998</u></u>

Nature of operations (Note 1), contingencies and commitments (Note 21) and subsequent events (Note 22)

On behalf of the board of directors:

" Joseph Ovsenek "

Director

" Duane Nelson "

Director

See accompanying notes to the consolidated financial statements.

SILVERMEX RESOURCES INC.

(formerly Genco Resources Ltd.)

Consolidated Statements of Loss and Comprehensive Loss (Expressed in Canadian dollars, except for share amounts)

	Year Ended December 31 2010 \$	Year Ended December 31 2009 \$
Sales	3,950,957	381,648
Cost of sales	<u>3,112,500</u>	<u>42,643</u>
Gross margin	<u>838,457</u>	<u>339,005</u>
Operating expenses (recoveries)		
Administration	4,601,945	2,143,252
Mine overhead	905,503	2,461,089
Expense recoveries	-	(629,619)
Stock-based compensation (Note 14a)	1,053,029	196,703
Impairment of goodwill (Note 4)	<u>37,468,666</u>	<u>-</u>
	<u>44,029,143</u>	<u>4,171,425</u>
Operating loss	<u>(43,190,686)</u>	<u>(3,832,420)</u>
Other income (expense)		
Accretion on long term debt (Note 12)	(45,835)	(97,160)
Gain on sale of Chief Consolidated Mining Company (Note 7)	1,559,753	1,619,520
Loss on settlement of litigation	-	(360,000)
Allowance for value added tax receivable, net (Note 21d)	(525,708)	(2,662,525)
Impairment of property, plant and equipment (Note 11)	-	(5,391,848)
Interest and other income	<u>215,057</u>	<u>201,370</u>
	<u>1,203,267</u>	<u>(6,690,643)</u>
Net loss before tax	<u>(41,987,419)</u>	<u>(10,523,063)</u>
Income tax expense (recovery) (Note 15)		
Current	56,394	-
Future	<u>(575,867)</u>	<u>4,786,126</u>
	<u>(519,473)</u>	<u>4,786,126</u>
Net loss and comprehensive loss	<u>(41,467,946)</u>	<u>(15,309,189)</u>
Loss per share		
Basic and fully diluted	<u>\$ (0.37)</u>	<u>\$ (0.26)</u>
Weighted average number of common shares outstanding	<u>111,513,837</u>	<u>58,619,224</u>

See accompanying notes to the consolidated financial statements.

SILVERMEX RESOURCES INC.

(formerly Genco Resources Ltd.)

Consolidated Statements of Cash Flows

(Expressed in Canadian dollars)

	Year Ended December 31 2010 \$	Year Ended December 31 2009 \$
Cash used in operating activities		
Net loss	(41,467,946)	(15,309,189)
Adjustments for non-cash items:		
Accretion on long term debt (Note 12)	45,835	97,160
Amortization and accretion	1,050,052	601,822
Foreign exchange loss	100,034	-
Non-cash bonuses and fair value loss on bonuses	217,626	79,162
Gain on sale of Chief Consolidated Mining Company (Note 7)	(1,559,035)	(1,619,520)
Loss on settlement of litigation	-	360,000
Future income tax (Note 15)	(575,867)	4,786,126
Allowance for value added tax receivable, net (Note 21d)	525,708	2,662,525
Impairment of property, plant and equipment (Note 11)	-	5,391,848
Impairment of goodwill (Note 4)	37,468,666	-
Expense recoveries	-	(629,619)
Stock-based compensation (Note 14a)	1,053,029	196,703
	<u>(3,141,898)</u>	<u>(3,382,982)</u>
Changes in non-cash working capital (Note 16)	<u>(3,101,971)</u>	<u>(3,848,672)</u>
	<u>(6,243,869)</u>	<u>(7,231,654)</u>
Cash used for (provided by) investing activities		
Expenditures on deferred exploration and development of mineral properties	(140,320)	-
Cash acquired on acquisition of Silver One (Note 4)	4,048,180	-
Purchase of short term investments	(7,400,203)	-
Collections on note receivable (Note 7)	2,000,000	-
Purchase of property, plant, and equipment	(224,434)	(763,387)
Proceeds from sale of property, plant, and equipment	-	1,834,645
	<u>(1,716,777)</u>	<u>1,071,258</u>
Cash provided by financing activities		
Long term debt principal repayments	-	(292,366)
Shares issued for cash, net of issuance costs	24,832,082	6,837,844
	<u>24,832,082</u>	<u>6,545,478</u>
Increase (decrease) in cash during the period	16,871,436	385,082
Effect of changes in foreign exchange rates	(82,071)	(212,913)
Cash and cash equivalents, beginning	625,171	453,002
Cash and cash equivalents, ending	<u>17,414,536</u>	<u>625,171</u>

Supplementary cash flow information (Note 17)

See accompanying notes to the consolidated financial statements.

SILVERMEX RESOURCES INC.

(formerly Genco Resources Ltd.)

Consolidated Statements of Shareholders' Equity

(Expressed in Canadian dollars, except for share amounts)

	Number of Common Shares	Share Capital \$	Contributed Surplus \$	Deficit \$	Total \$
Balance, December 31, 2008	46,335,720	45,326,828	8,984,176	(22,861,868)	31,449,136
Private placements (Note 14ii)	30,736,775	4,121,487	2,756,629	-	6,878,116
Shares issued to settle debt and liabilities (Note 14iii)	6,223,494	2,284,142	-	-	2,284,142
Exercise of warrants	1,422,300	540,797	(88,247)	-	452,550
Stock-based compensation	-	-	196,703	-	196,703
Net loss for the year	-	-	-	(15,309,189)	(15,309,189)
Balance, December 31, 2009	84,718,289	52,273,254	11,849,261	(38,171,057)	25,951,458
Private placements (Note 14iv)	38,780,648	12,433,353	5,581,835	-	18,015,188
Acquisition of Silver One (Note 14i)	89,315,406	57,982,663	7,064,130	-	65,046,793
Shares issued to settle debt and liabilities (Note 14v)	2,969,050	734,711	-	-	734,711
Exercise of stock options	540,000	286,383	(96,383)	-	190,000
Exercise of warrants	14,979,864	8,461,943	(1,762,697)	-	6,699,246
Stock-based compensation	-	-	1,053,029	-	1,053,029
Net loss for the year	-	-	-	(41,467,946)	(41,467,946)
Balance, December 31, 2010	231,303,257	132,172,307	23,689,175	(79,639,003)	76,222,479

See accompanying notes to the consolidated financial statements.

SILVERMEX RESOURCES INC.

(formerly Genco Resources Ltd.)

Notes to the Consolidated Financial Statements

December 31, 2010 and 2009

(Expressed in Canadian dollars)

1. Nature of Operations

Silvermex Resources Inc. (formerly Genco Resources Ltd. and referred to as “the Company” or “Silvermex”) was incorporated under the laws of the Province of British Columbia on February 28, 1980 as Senlac Oil & Gas Ltd. The Company changed its name to Rule Resources Ltd. on June 13, 1980, to Globe Resources Inc. on March 9, 1990, to Genco Resources Ltd. (“Genco”) on March 30, 1998 and to Silvermex Resources Inc. on November 16, 2010.

The Company is a growth-oriented silver and gold producer focused on building a portfolio of high quality, low-cost North American precious metal assets and developing its core asset, La Guitarra, a producing silver and gold property located in the Temascaltepec mining district of central Mexico.

The Company acquired La Guitarra Compania Minera S.A. de C.V. (“La Guitarra”), an operating silver and gold mining company incorporated under the laws of Mexico in 2003 (Note 12).

On September 20, 2010, the Company announced that it had entered into a plan of arrangement with Silvermex Resources Ltd., a TSX Venture company, to acquire 100% of the outstanding shares of Silvermex Resource Ltd. In an all-share transaction. The acquisition was completed on November 16, 2010, and the former Silvermex Resources Ltd. was renamed Silver One Mining Corporation (“Silver One”) (Note 4).

2. Significant Accounting Policies

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and reflect the policies below.

a) Basis of Presentation

These consolidated financial statements include the accounts of the parent company and its wholly owned subsidiaries La Guitarra, Servicios para la Industria Minera, S.A. de C.V., Silver One, Minera Terra Plata, S.A. de C.V., Minera La Rastra, S.A. de C.V. and Rule Nevada Inc. All significant inter-company accounts and transactions have been eliminated.

b) Cash and cash equivalents

Cash and cash equivalents consists of deposits in the bank and highly liquid investments with an original maturity of 90 days or less. At December 31, 2010 and 2009, the Company has no cash equivalents.

c) Short-term Investments

Short-term investments consist of highly liquid deposits with maturities of less than 365 days and locked in interest rates. The deposits are backed by institutions of high credit worthiness.

d) Stock-Based Compensation

All stock-based awards made to employees and non-employees are measured and recognized using a fair value based method. For employees, the fair value of the options is measured at the date of the grant. For non-employees, the fair value of the options is measured on the earlier of the date at which the counterparty performance is complete or the date the performance commitment is reached or the date at which the equity instruments are granted if they are fully vested and non-forfeitable.

SILVERMEX RESOURCES INC.

(formerly Genco Resources Ltd.)

Notes to the Consolidated Financial Statements

December 31, 2010 and 2009

(Expressed in Canadian dollars)

2. Significant Accounting Policies (continued)

e) Inventory

Inventory is valued at the lower of cost and net realizable value. Cost of parts and supplies are determined on an average cost basis. Mineral concentrate inventory includes all direct costs of extracting the ore, direct labour, and all indirect pro-rated costs associated with operating La Guitarra mine. When circumstances that previously caused inventories to be written down below cost no longer exist, the amount of the write-down is to be reversed.

f) Property, Plant, and Equipment

Property, plant, and equipment are recorded at cost less accumulated amortization. Amortization is provided for using the following methods and annual rates on a straight-line basis:

Automotive equipment	4 years
Buildings	20 years
Computer equipment	3.3 years
Furniture and fixtures	10 years
Software	1 year
Leasehold improvements	5 years
Mine equipment	8 years
Mine infrastructure	Unit of production basis

Significant costs related to property acquisitions including undeveloped mineral interests are capitalized until the viability of the mineral interest is determined. The costs are capitalized until such time that it has been determined that a mineral deposit is commercially recoverable and a decision has been made to prepare a mining plan (which occurs upon completion of a positive economic analysis of the mineral deposit). Major development expenditures incurred to expose the ore, increase production or extend the life of an existing mine are capitalized. Mine infrastructure is amortized using the unit-of-production method based on the estimated total recoverable ounces contained in proven and probable reserves at the related mine when operating levels intended by management have been reached. Capitalized costs are written down to their estimated recoverable amount if the properties are determined to be uneconomic or are placed for sale.

Interest and finance costs relating to the construction of plant and equipment are capitalized prior to the commencement of commercial production of a new mine. Depletion of the mine properties is charged on a unit of production basis over the estimated useful life of the mine.

Evaluations of the carrying values of each operation and development property are undertaken in each reporting period to determine if estimated undiscounted future net cash flows are less than the carrying value. Estimated undiscounted future net cash flows are calculated using estimated production sales prices and operating costs, capital costs and reclamation and closure costs. If it is determined that the future net cash flows from an operation or development property are less than the carrying value a write down is recorded with a charge to operations.

g) Impairment of Long-lived Assets

The Company reviews the recoverability of its long-lived assets annually and when events and circumstances indicate an impairment event may have occurred. The Company assesses the recoverability of its long-lived assets by determining whether their carrying value can be recovered over their remaining lives through undiscounted future cash flows. In the event that future recoverability is not supported, an impairment loss is measured and recorded based on the extent that the estimated future cash flows on a discounted cash flows are less than the carrying value.

SILVERMEX RESOURCES INC.

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Notes to the Consolidated Financial Statements

December 31, 2010 and 2009

(Expressed in Canadian dollars)

2. Significant Accounting Policies (continued)

h) Goodwill

Business combinations are accounted for under the acquisition method of accounting whereby acquired assets and liabilities are recorded at fair value as of the date of acquisition. The excess of the purchase price over the fair value of the net assets acquired is recorded as goodwill and allocated to the applicable reporting unit. Goodwill is not amortized, it is tested annually for impairment or more frequently if current events or changes in circumstances indicate that the carrying value of the goodwill of a reporting unit may exceed its fair value. A two-step impairment test is used to identify potential impairment in goodwill and to measure the amount of goodwill impairment, if any. In the first step, the fair value of a reporting unit is compared with its carrying value, including goodwill. When the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is considered not to be impaired and the second step of the impairment test is not undertaken. When the carrying amount of a reporting unit exceeds its fair value, the fair value of the reporting unit's goodwill (determined on the same basis as the value of goodwill is determined in a business combination) is compared with its carrying amount to measure the amount of the impairment loss, if any. When the carrying amount of reporting unit goodwill exceeds the fair value of the goodwill, an impairment loss is recognized in an amount equal to the excess.

i) Foreign Currency Translation

The functional currency of the Company and each of its subsidiaries is the Canadian dollar. Management has determined that all of the Company's subsidiaries were integrated operations to December 31, 2010.

For the Company's foreign subsidiaries the Company has used the temporal method of foreign currency translation. Under the temporal method, foreign currency monetary assets and liabilities are translated into the functional currency at the exchange rates prevailing at the balance sheet date. Non-monetary assets and liabilities denominated in foreign currencies are translated using the rate of exchange at the transaction date. Foreign currency transactions are translated at the functional currency's rate prevailing on the transaction dates. Foreign exchange gains and losses on translation of the foreign operations are included in the determination of earnings. Foreign currency gains and losses have been included in cost of sales and mine overhead costs on the statement of loss and comprehensive loss for the years ended December 31, 2010 and 2009.

j) Loss Per Share

Basic loss per share are computed using the weighted average number of common shares outstanding during the period. Diluted loss per share amounts are calculated giving effect to the potential dilution that would occur if securities or other contracts to issue common shares were exercised or converted to common shares using the treasury stock method. The treasury stock method assumes that proceeds received from the exercise of stock options and warrants are used to redeem common shares at the prevailing market value.

k) Measurement Uncertainty

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as at the date of the balance sheets as well as the reported amounts of revenues, expenses, and cash flows during the periods presented. Such estimates relate primarily to unsettled transactions and events as of the date of the financial statements. Actual results could differ materially from estimated amounts.

SILVERMEX RESOURCES INC.

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Notes to the Consolidated Financial Statements

December 31, 2010 and 2009

(Expressed in Canadian dollars)

2. Significant Accounting Policies (continued)

Amounts recorded for amortization are based on life of mine estimates and the estimated lives and valuation of property, plant and equipment. Stock-based compensation is based upon expected volatility and option life estimates. Asset retirement obligations are based on estimates of abandonment costs, timing of abandonment, inflation and interest rates. The provision for income taxes is based on judgements in applying income tax law and estimates on the timing, likelihood and reversal of temporary differences between the accounting and tax basis of assets and liabilities. Valuation of the Company's mineral property interests are based upon cash flow and commodity price estimates for recognition and impairment analysis. Valuation of the Company's note and taxes receivable are based on assumptions regarding collectability. Estimated outcomes of litigation against the Company are based on discussions with the lawyers of the Company. These estimates are subject to measurement uncertainty and changes in these estimates could materially impact the financial statements of future periods.

l) Revenue Recognition

Revenue from the sale of mineral concentrate is recognized in the accounts when title and risk passes to the buyer, collection is reasonably assured and the price is reasonably determinable. Revenue from the sale of mineral concentrate may be subject to adjustment upon final settlement of metal prices, weights and assays. Adjustments to revenue for metal prices are recorded monthly and other adjustments are recorded on final settlement.

m) Exploration, Development Expenditures and Acquisition of Mineral Properties

Significant mineral property acquisition costs and exploration and development expenditures are capitalized. For the acquisition of mineral properties (whether through asset acquisition or business combination), the fair value is determined by estimating the value of the property's reserves, resources and exploration potential. Capitalized costs are written down to their estimated recoverable amount if the properties are determined to be uneconomic, abandoned, or are placed for sale.

Although the Company has taken steps to verify title to mineral properties in which it has an interest, according to usual industry standards for the stage of exploration on such properties, these procedures do not guarantee the Company's title. Such properties may be subject to prior agreements or transfers and title may be affected by undetected defects.

n) Business combination

A business combination is defined as an acquisition of assets and liabilities that constitute a business. A business is an integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing a return to the Company and its shareholders in the form of dividends, lower costs or other economic benefits. A business consists of inputs, including non-current assets, and processes, including operational processes, that when applied to those inputs, have the ability to create outputs that provide a return to the Company and its shareholders. A business also includes those assets and liabilities that do not necessarily have all the inputs and processes required to produce outputs, but can be integrated with the inputs and processes of the Company to create outputs. When acquiring a set of activities or assets in the exploration and development stage, which may not have outputs, the Company considers other factors to determine whether the set of activities or assets is a business. Those factors include, but are not limited to, whether the set of activities or assets:

- 1) has begun planned principal activities;
- 2) has employees, intellectual property and other inputs and processes that could be applied to those inputs;
- 3) is pursuing a plan to produce outputs; and
- 4) will be able to obtain access to customers that will purchase the outputs.

SILVERMEX RESOURCES INC.

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Notes to the Consolidated Financial Statements

December 31, 2010 and 2009

(Expressed in Canadian dollars)

2. Significant Accounting Policies (continued)

Not all of the above factors need to be present for a particular integrated set of activities or assets in the exploration and development stage to qualify as a business.

Business combinations are accounted for using the acquisition method whereby identifiable assets acquired and liabilities assumed, including contingent liabilities, are recorded at 100% of their acquisition-date fair values. The acquisition date is the date the Company obtains control over the acquiree, which is generally the date that consideration is transferred and the Company acquires the assets and assumes the liabilities of the acquiree. The consideration transferred in a business combination is measured at fair value, which is calculated as the sum of the acquisition-date fair values of the assets transferred by the Company, the liabilities, including contingent consideration incurred and payable by the Company to former owners of the acquiree and the equity interests issued by the Company. The measurement date for equity interests issued by the Company is the acquisition date. Acquisition-related costs, other than costs to issue debt or equity securities, of the acquirer, including investment banking fees, legal fees, accounting fees, valuation fees, and other professional or consulting fees are expensed as incurred. The costs to issue equity securities of the Company as consideration for the acquisition are reduced from share capital as share issue costs.

It generally requires time to obtain the information necessary to identify and measure the following as of the acquisition date:

- 1) the identifiable assets acquired, and liabilities assumed
- 2) the consideration transferred for the acquiree;

If the initial accounting for a business combination is incomplete by the end of the reporting period in which the combination occurs, the Company reports in its financial statements preliminary amounts for the items for which the accounting is incomplete. During the measurement period, the Company will retrospectively adjust the preliminary estimated amounts recognized at the acquisition date to reflect new information obtained about facts and circumstances that existed as of the acquisition date and, if known, would have affected the measurement of the amounts recognized as of that date. During the measurement period, the Company will also recognize additional assets or liabilities if new information is obtained about facts and circumstances that existed as of the acquisition date and, if known, would have resulted in the recognition of those assets and liabilities as of that date. The measurement period ends as soon as the Company receives the information it was seeking about facts and circumstances that existed as of the acquisition date or learns that more information is not obtainable and shall not exceed one year from the acquisition date.

o) Income Taxes

The provision for income taxes is based on the liability method. Future taxes arise from the recognition of the tax consequences of temporary differences by applying enacted or substantively enacted tax rates applicable to future years to differences between the financial statement carrying amounts and the tax bases of certain assets and liabilities. The effect on future income tax assets and liabilities of a change in tax rates is recognized in the consolidated statement of operations in the period in which the change is substantively enacted. The Company records a valuation allowance against any portion of those future income tax assets that it believes will, more likely than not, fail to be realized.

SILVERMEX RESOURCES INC.

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Notes to the Consolidated Financial Statements

December 31, 2010 and 2009

(Expressed in Canadian dollars)

2. Significant Accounting Policies (continued)

p) Financial Instruments

The Company adopted the provisions of CICA Section 3855, Financial Instruments – Recognition and Measurement, Section 3862, Financial Instruments – Disclosure and Section 3863, Financial Instruments – Presentation which address the classification, recognition, measurement and disclosures of both qualitative and quantitative information that enables users of financial statements to evaluate the nature and extent of risks from financial instruments to which the Company is exposed.

The Sections require financial assets and financial liabilities, including derivatives, be recognized on the balance sheet when the Company becomes a party to contractual provisions of the financial instrument or derivative contract. All financial instruments are measured at fair value on initial recognition except for certain related party transactions. Measurement in subsequent periods depends on whether the financial instrument has been classified as held-for-trading, available-for-sale, held to maturity, loans and receivables or other liabilities.

Held-for-trading financial assets and liabilities are subsequently measured at fair value with gains, losses and transaction costs recognized in the Company's net earnings for the period. Financial assets held-to maturity, loans and receivables and financial liabilities, other than those held-for-trading, are subsequently measured at amortized cost using the effective interest method of amortization. Available-for-sale financial assets are subsequently measured at fair value with unrealized gains and losses, including changes in foreign exchange rates, are recognized in other comprehensive income. Capital transaction costs are added to the carrying amount of the financial instrument.

The Company has designated each of its significant categories of financial instruments as follows:

Cash and cash equivalents	Held-for-trading
Short-term investments	Available for sale
Accounts receivable	Loans and receivables
Note receivable	Loans and receivables
Accounts payable and accrued liabilities	Other financial liabilities
Long term debt	Other financial liabilities

Amended CICA Section 3862 establishes a fair value hierarchy that reflects the significance of inputs used in making fair value measurements as follows:

Level 1 - quoted prices in active markets for identical assets or liabilities;

Level 2 - inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. from derived prices); and

Level 3 - inputs for the asset or liability that are not based upon observable market data.

The items which are carried at fair value are cash and cash equivalents and short-term investments.

SILVERMEX RESOURCES INC.

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Notes to the Consolidated Financial Statements

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(Expressed in Canadian dollars)

2. Significant Accounting Policies (continued)

Categories of Financial Assets and Liabilities

At December 31, 2010, the following table sets forth the levels in the fair value hierarchy into which the Company's financial assets and liabilities are measured and recognized in the balance sheet. Assets are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

	December 31, 2010		December 31, 2009	
	Carrying Amount \$	Fair Value \$	Carrying Amount \$	Fair Value \$
Cash and cash equivalents	17,414,536	17,414,536	625,171	625,171
Short-term Investments	7,400,203	7,400,203	—	—
Accounts Receivable	2,288,506	2,288,506	357,021	357,021
Notes Receivable	2,000,000	2,000,000	2,566,201	2,566,201
Accounts Payable	1,521,574	1,521,574	1,729,492	1,729,492

The Company has determined the estimated fair values of its financial instruments based upon appropriate valuation methodologies. The fair values of the cash and cash equivalents, accounts receivable, and accounts payable approximate their carrying values due to their short term nature and high level of liquidity. The fair value of the short-term investments, note receivable, and long-term debt have been valued at the present value of future cash flows discounted at market rates for similar instruments.

q) Comprehensive Loss

Other comprehensive loss represents the change in net equity for the period that arises from unrealized gains and losses on available-for-sale financial instruments. Amounts included in other comprehensive income are shown net of tax. Cumulative changes in other comprehensive income are included in accumulated other comprehensive income which is presented as a new category in shareholders' equity, if applicable. The Company did not have any transactions during the years ended December 31, 2010 or 2009 that gave rise to other comprehensive loss, and therefore has no balance of accumulated other comprehensive loss.

3. Adoption of New Accounting Policies and Pronouncements

- a) The CICA issued Handbook Sections 1582 – Business Combinations, 1601 – Consolidated Financial Statements, and 1602 – Non-Controlling Interests. Section 1582 replaces Section 1581 – Business Combinations and establishes standards for the accounting for business combinations that is equivalent to the business combination accounting standard under International Financial Reporting Standards (“IFRS”). Sections 1601 and 1602 replace Section 1600 – Consolidated Financial Statements. Section 1601 provides revised guidance on the preparation of consolidated financial statements and Section 1602 addresses accounting for non-controlling interests in consolidated financial statements subsequent to a business combination. These standards are effective January 1, 2011. The Company has early adopted these policies and as a result of adopting this standard the Company expensed \$847,709 in transaction costs which previously would have been capitalized. If the Company had applied Section 1581 to the business combination the common shares issued would have been valued at the time of the date of the business combination announcement and not at the closing date. This difference in the valuation dates of the common shares would have resulted in a different value attributed to the purchase price. If the Company would have applied Section 1581 the value of the purchase price would have been reduced.

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3. Adoption of New Accounting Policies and Pronouncements (continued)

- b) Canadian public companies will be required to prepare their financial statements in accordance with International Financial Reporting Standards (“IFRS”), as issued by the International Accounting Standards Board, for financial years beginning on or after January 1, 2011. Effective January 1, 2011, the Company will adopt IFRS as the basis for preparing its financial statements.

The Company will issue its first IFRS annual consolidated financial statements for the fiscal year ending December 31, 2011, with restatement of comparative balance sheets as at December 31, 2010 and January 1, 2010 and statement of earnings for the year ended December 31, 2010. During the year ending December 31, 2011, the Company will issue interim consolidated IFRS financial statements prepared in accordance with IAS 34 – Interim Financial Reporting for the periods ending March 31, 2011, June 30, 2011 and September 30, 2011, with restatement of comparative balance sheets as at December 31, 2010 and January 1, 2010 and statements of earnings for the comparative periods presented.

4. Acquisition of Silvermex Resources Ltd. and Change of Name

As described in Note 1, the Company closed the acquisition of Silver One on November 16, 2010.

The transaction has been accounted for as a business combination under the acquisition method, with former Genco Resources Ltd. as the acquirer of Silver One. The Company has included the results of Silver One in its consolidated financial statements commencing on November 16, 2010. As described in Note 3(a), the Company has adopted Section 1582 of the CICA Handbook regarding business combinations and as such has applied Section 1582 to the purchase consideration and preliminary purchase price allocations below.

Immediately prior to the completion of the plan of arrangement, the common shares of the Company were split on a ratio of 1 to 1.1 (Note 14). Accordingly, the outstanding share options and warrants were also split on a ratio of 1 to 1.1 and the exercise price of the options and warrants decreased by a ratio of 0.90909. The other terms of the options and warrants were not modified.

Total purchase consideration is as follows:

	\$
Common shares issued	58,055,014
Other share capital items:	
Employee and consultant share options	1,844,727
Warrants	4,116,095
Agents’ common share units	453,308
Aurcana debt assumed to be settled in shares (Note 12)	650,000
Total consideration	65,119,144

Management has determined the date of acquisition to be November 16, 2010 and therefore valued the share consideration at the Company’s closing share price on the acquisition date.

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4. Acquisition of Silvermex Resources Ltd. and Change of Name (continued)

The consideration was comprised of 89,315,406 common shares valued at \$0.65 per share on the acquisition date, issued to the former Silver One shareholders in exchange for their existing Silver One shares, share capital items of the former Silver One assumed was comprised of 7,000,000 employee and consultant share options, 15,795,655 common share warrants and 1,003,244 agents' common share units. Each unit is exercisable at \$0.45 into one common share and one common share purchase warrant which are exercisable at \$0.65. The fair values of the options and warrants were measured on the date of acquisition using the Black-Scholes option pricing model (Note 14).

The allocation of the purchase price has not been finalized as at the date these consolidated financial statements were issued as management is in the process of determining the fair values of identifiable assets acquired and liabilities assumed, measuring the associated future income tax assets and liabilities, and determining the value of goodwill.

The preliminary purchase price allocation below includes management's initial estimates of the fair value of the assets and liabilities acquired, and is therefore subject to change:

Total consideration	\$ 65,119,144
Net assets acquired:	
Cash	4,048,180
Other current assets	456,320
Property, plant and equipment	2,067,031
Mineral properties	28,384,635
Goodwill	37,468,666
Current liabilities	(651,497)
Long-term debt	(924,088)
Asset retirement obligations	(142,259)
Future income taxes	(5,587,844)
	<u>65,119,144</u>

The purchase price of an acquired business is allocated to the underlying tangible and intangible assets acquired and liabilities assumed based upon their respective estimated fair values, with the excess recorded as goodwill. Such estimated fair value assessments require judgment.

The preliminary goodwill on the transaction has arisen primarily due to the change in fair value of the share consideration issued to the former shareholders' of Silver One. During the time period between the date of the announcement of the transaction and the acquisition date, the Company's share price increased significantly, causing an increase in the value of the overall purchase consideration. The Company attributes a portion of the goodwill to the potential of the land and mineral rights acquired to provide reserves and resources over and above the value attributed to the mineral property. Silver One has been classified as a separate reporting unit and operating segment. The Company tested the impairment of goodwill at December 31, 2010 and determined that it could not support the carrying value of the preliminary goodwill and as result recorded an impairment of the goodwill of \$37,468,666.

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4. Acquisition of Silvermex Resources Ltd. and Change of Name (continued)

The Company has included in the consolidated statement of loss and comprehensive loss, a loss of \$183,026 from the date of acquisition to December 31, 2010 from Silver One. Transaction costs of \$847,709 were incurred and were expensed in the period incurred.

Proforma Information (Unaudited)

The net loss for the consolidated Company would have been \$2,422,717 as though the business combination for Silver One had occurred on January 1, 2010. Revenue would not have changed as Silver One had no revenues during 2010.

5. Financial Instruments

The Company's financial instruments consist of cash, short-term investments, accounts receivable, note receivable, accounts payable, and long term debt.

It is management's opinion that the Company's exposure to significant currency, credit, liquidity, or price risks as follows:

a) Currency Risk

The Company is exposed to the financial risk related to the fluctuation of foreign exchange rates. The Company operates in Mexico, its revenues are generated in United States ("US") dollars and its cost of sales are incurred in Mexican pesos. A significant change in the currency exchange rates between the Canadian dollar relative to the US dollar and the Mexican peso would have an effect on the Company's results from operations, financial position or cash flows. The Company has not hedged its exposure to currency fluctuations.

As at December 31, 2010, the Company is exposed to currency risk through the following assets and liabilities denominated in US dollars and Mexican pesos:

	<u>US Dollars</u>	<u>Mexican Pesos</u>
Cash	1,742,064	940,282
Accounts receivable	1,766,421	2,938,397
Accounts payable and accrued liabilities	(223,638)	(13,220,652)
Long term debt	(1,404,640)	—
Future income taxes	—	(145,752,284)
Asset retirement obligations	(142,256)	(16,721,294)
Net foreign currency exposure	<u>1,737,951</u>	<u>(171,815,551)</u>

Based on the above net exposures as at December 31, 2010, and assuming that all other variables remain constant, a 10% depreciation or appreciation of the Canadian dollar against the US dollar would result in a decrease/increase of \$173,447 in the Company's net earnings. Likewise, a 10% depreciation or appreciation of the Canadian dollar against the Mexican peso would result in a decrease/increase of \$1,400,141 in the Company's net earnings.

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5. Financial Instruments (continued)

b) Credit Risk

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

Financial instruments that potentially subject the Company to a concentration of credit risk consist of cash, accounts and the note receivable. The Company deposits cash with financial institutions it believes to be creditworthy. Cash balances at these financial institutions may exceed the federally guaranteed amount.

The Company's accounts receivable are primarily derived from input tax credits receivable and trade receivables for sales of mineral concentrate. The Company maintains an allowance for doubtful accounts receivable in those cases for which the expected collectability of accounts receivable is in question (Note 21).

Note receivable due from Andover Ventures Inc. relates to the sale of shares from Chief Consolidated Mining Company (Note 7). As the collectability of the note was uncertain in 2009, the Company has recorded a valuation allowance in 2009 against the note with the fair value determined to be the value of the underlying security. For 2010, the amount of the remaining note receivable is less than the fair value of the pledged Chief shares therefore the note receivable is recorded at its face value.

c) Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company manages liquidity by maintaining adequate cash balances and by raising equity or debt financing. The Company has no assurance that such financing will be available on favourable terms. The Company believes it is subject to liquidity risk through its working capital. In general, the Company attempts to avoid exposure to liquidity risk by obtaining corporate financing through the issuance of common shares.

d) Price Risk

The Company is subject to price risk from fluctuations in the market price of silver and gold, which in turn is affected by numerous factors including central bank policies, producer hedging activities, the value of the US dollar relative to other major currencies, global demand and supply and global political and economic conditions. The carrying value of the Company's mine infrastructure and exploration costs could be adversely affected by any reductions in the long term prices of silver and gold.

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6. Management of Capital

The Company's objectives of capital management are intended to safeguard the Company's normal operating requirements on an ongoing basis and the continued development and exploration of its mineral properties. The capital of the Company consists of the items included in the consolidated shareholders' equity and long term debt.

These consolidated financial statements have been prepared assuming the Company will continue as a going concern. Although the Company has completed private placements, it will still need to target sources of additional financing through alliances with financial, exploration and mining entities, or other business and financial transactions to assure continuation of the Company's exploration and development programs. There can be no assurance that the Company will be able to continue to raise funds, in which case the Company may be unable to meet its obligations. The net realizable value of the Company's assets may be materially less than the amounts recorded in these financial statements should the Company be unable to secure sufficient additional financing in the future and therefore be in a position to realize its assets and discharge its liabilities in the normal course of business.

In order to facilitate the management of its capital requirements, the Company prepares expenditure budgets that are updated as necessary depending on various factors, including successful capital deployment and general industry conditions. In order to maintain or adjust its capital structure the Company may issue new shares or debt. The Company is not subject to any externally imposed capital requirements.

7. Sale of Shares of Chief Consolidated Mining Company

During 2008, the Company reached an agreement with Andover Ventures Inc. ("Andover") to sell the Company's 64.7% interest in Chief Consolidated Mining Company ("Chief"), for cash consideration of US\$4,878,002, and 1,500,000 Andover shares with Andover pledging the entire amount of the Chief shares as collateral. This sale was not completed by Andover under the agreed terms and during 2008, the Company initiated legal action against Andover relating to Andover's failure to fulfill its obligations under the purchase agreement.

During the first quarter of 2009, a settlement (the "2009 Settlement") was reached with Andover and new terms for the sale of Chief were agreed. As part of the 2009 Settlement, the parties agreed to terminate all previous agreements and Andover agreed to purchase the Chief shares for a promissory note (the "Note") of \$5,000,000 plus amounts previously paid to the Company in 2008 totalling \$2,000,000 in cash and \$857,500 in Andover shares. The Note was due to be repaid in September 2009 bore quarterly interest at a specified rate of US prime plus 2%, subject to a minimum rate of 4% per year. The Company received the Chief shares as collateral for the Note.

Based on the book value of the Chief shares in 2009, a gain of \$5,431,820 resulted. The gain was deferred and was to be recognized as proceeds were received. During the year ended December 31, 2009 the Company recognized a gain of \$1,579,520 in the statement of loss and comprehensive loss relating to the cash proceeds and Andover shares received prior to the 2009 Settlement. During the fourth quarter of 2009, the Company evaluated the recoverability of the promissory note and concluded that it was impaired and recognized an allowance for impairment of the receivable totalling \$2,433,799 which reduced the carrying value of the Note and also reduced the amount of the deferred gain on the disposal of the Chief shares. The amount of the impairment was equal to the value of the pledged Chief shares. The remaining gain on the sale of \$1,418,501 was deferred. To date the Company has received a total of \$416,437 in interest from Andover.

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7. Sale of Shares of Chief Consolidated Mining Company (continued)

During 2010, the Company and Andover agreed to amend the 2009 Settlement and entered into a new agreement (the "2010 Agreement"). Under the terms of the 2010 Agreement, the Company agreed to new terms of repayment which included \$2,000,000 during 2010 and a remaining \$2,000,000 to be paid in September 2011. The Company continued to have a pledge over the shares of Chief as collateral. As a result of the collections made in 2010, and the continued access to the collateral, a portion of the impairment recorded in 2009 was reversed and the Note was recorded for the remaining proceeds to be received of \$2,000,000 as of December 31, 2010.

During the year ended December 31, 2010, the Company recognized a gain of \$1,559,053 due to the payments received from Andover during 2010. The remaining gain of \$1,293,265 remains deferred and will be recognized when the remaining amount is collected in 2011.

8. Accounts Receivable, Net

The breakdown of the Company's accounts receivable are as follows:

	December 31 2010 \$	December 31 2009 \$
Trade receivable (Note 20)	1,766,942	293,794
Value Added Taxes Receivable (Note 21d)	2,886,792	2,670,107
Other	453,460	323,208
	<u>5,107,194</u>	<u>3,287,109</u>
Valuation allowance (Note 21d)	<u>(2,818,688)</u>	<u>(2,930,088)</u>
	<u>2,288,506</u>	<u>357,021</u>

9. Inventory

	December 31 2010 \$	December 31 2009 \$
Mineral concentrate	334,242	—
Parts and supplies	374,181	231,207
	<u>708,423</u>	<u>231,207</u>

10. Mineral Property Interests

	December 31 2010 \$	December 31 2009 \$
San Marcial Property	7,266,628	—
Peñasco Quemado Property	8,553,711	—
La Frazada Property	7,640,421	—
Rosario Property	4,923,877	—
Other properties	38,449	48,493
	<u>28,423,086</u>	<u>48,493</u>

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10. Mineral Property Interests (continued)

San Marcial Property, Sinaloa, Mexico

In October 2007, Silver One executed a term sheet and on March 19, 2009, finalized the formal agreement with Silver Standard to earn a 100% interest in the San Marcial Project. Under the current agreement, an option payment of 1,000,000 common shares of the Company was required in February 2011. This payment has not been made to date as the agreement is in the process of being renegotiated due to the acquisition of Silver One by Silvermex. In addition to the share payment, the Company has an option to pay \$6,000,000 in either cash or shares at the election of Silver Standard, by February 1, 2012, and a 1% net smelter royalty ("NSR") capped at \$13,750,000 less the \$6,000,000 payment and the value of the 1,000,000 shares to be issued to Silver Standard in February 2011. The Company is obligated to pay Silver Standard US\$100,000 per month if commercial production commences on the property while the property is still under option from Silver Standard. These payments will be credited against the purchase price. There is also a 3% NSR on the property, and the Company is also obligated to pay US\$100,000 to International American Resources Inc. as a production payment.

Peñasco Quemado Property, Tubutama Sonora, Mexico

Silver One holds a 100% interest in the Peñasco Quemado Project and has entered into a Funding Agreement with Silver Standard Resources Inc. ("Silver Standard"). The agreement allows for a joint venture agreement to be formed upon notification by the Company that it has prepared a resource estimate that meets or exceeds an aggregate of 30 million ounces of silver in the measured, indicated and inferred mineral resource categories. Upon such notification, Silver Standard may elect to enter into the joint venture by expending the greater of double the expenditures incurred to that date by the Company or US\$1,000,000. Upon the formation of the joint venture, Silver Standard would acquire a 51% interest and would be the operator of the project. Silver Standard may increase its interest to 70% by paying all costs required to complete a feasibility study.

The Funding Agreement contains a right of first refusal to Silver Standard for the Company's interest in the project. The Funding Agreement also contains a dilution provision which provides that in the event either party's interest is diluted below 10%, it shall relinquish its participating interest to the other party in return for a 1% NSR.

La Frazada Property, Nayarit, Mexico

Silver One acquired 100% of the La Frazada Property through staking.

Rosario Property, Sinaloa, Mexico

On November 30, 2009, Silver One acquired all of outstanding shares of La Rastra S.A. de C.V. ("La Rastra") from Aurcana Corporation ("Aurcana"). La Rastra holds the rights to, amongst others, the Rosario, San Juan and Plomosas concessions which are cumulatively referred to as the Rosario Project.

As of the date of the acquisition of Silver One, the remaining obligations under the purchase agreement included the delivery of 1,000,000 shares to be issued upon the earlier of October 9, 2011 or the commencement of production; US\$500,000 (\$499,000) to Aurcana upon the earlier of April 9, 2012 or six months after the commencement of commercial production; a further US\$500,000 (\$499,000) by October 9, 2012. The obligation to deliver shares of the Company has been recorded within equity at a fair value of \$650,000 and formed part of the purchase price to acquire Silver One.

Additional contingent consideration of US\$500,000 (\$499,000) to Aurcana or 500,000 shares at the option of Aurcana within 18 months following the commencement of commercial production; US\$500,000 to Aurcana or 500,000 shares at the option of Aurcana within 24 months following the commencement of commercial production; and, US\$500,000 to Aurcana within 30 months following commencement of commercial production or 500,000 shares at the option of Aurcana. The Company estimated the fair value of the contingent consideration to be negligible.

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11. Property, Plant, and Equipment (continued)

The Company recorded amortization of \$1,040,648, of which \$194,263 was included in mine overhead, \$722,258 was included in cost of sales and \$124,127 was included in administration expenses on the statement of loss and comprehensive loss for the year ended December 31, 2010. The Company recorded amortization of \$473,710, of which \$194,584 was included in mine overhead, \$210,723 was included in cost of sales and \$68,403 was included in administration expenses on the statement of loss and comprehensive loss for the year ended December 31, 2009.

During the year ended December 31, 2009 the Company sold a ball mill for US\$1,500,000 (\$1,792,546) with a carrying value of \$1,676,565, for a gain of \$115,981.

During 2009, the Company recorded an asset impairment of \$5,391,848 on its mine infrastructure costs at its La Guitarra mine. After completing a review of the discounted value of future cash flows it was determined that the carrying value of its mine infrastructure costs at its La Guitarra mine was not likely to be fully recoverable. Previous reviews of the discounted value of future cash flows assumed the Company would enter a development period and complete a mine expansion. However, due to delays the Company has removed this assumption from its discounted value of future cash flows model and has only used anticipated cash flows from existing operations. The difference between the carrying value of the Company's mine infrastructure costs and its revised discounted future cash flow model was recognized as an impairment.

During 2010, the Company conducted an asset impairment of test on its mine infrastructure costs at its La Guitarra mine. After completing a review of the value of future cash flows it was determined that the carrying value of its mine infrastructure costs at its La Guitarra mine are fully recoverable. As the estimated undiscounted cash flows exceeded the carrying value, there was no impairment recognized.

La Guitarra Property, Temascaltepec, Mexico

The Company owns and leases concessions which are primarily located in the Municipality of Temascaltepec, in Mexico State. The Company directly holds title to 38 of the mineral concessions and 5 concessions are leased from a third party, Mario Héctor Gottfried Joy.

The concession owned by Mario Héctor Gottfried Joy are not currently in production. Royalty payments of 1.5% of the amount received in final payment for the silver and gold produced is payable when the properties are in production. If the price of silver is more than US\$15 per ounce, the royalty increases to 2%. An additional, one-time payment to Mr. Gottfried Joy of US \$200,000 is payable when the production has totalled 30,000 equivalent ounces of gold.

Acquisition costs relating to the La Guitarra properties have been capitalized and grouped with exploration costs.

12. Long Term Debt

Pursuant to the acquisition of La Guitarra, the Company agreed to pay US\$4,000,000 of the purchase price as a promissory note to Goldcorp Inc. ("Goldcorp"). The debt bears no interest, is unsecured, and is repayable by instalments of US\$500,000 on each of the first through eighth anniversaries of the closing date. The final instalment is due in August 2011 is US\$500,000 (\$499,000) and is recorded as a current liability.

The debt has been discounted for financial reporting purposes to its fair value on its original acquisition date. The rate used to discount the debt to its fair value was 5% which was based on the cost of borrowing of similar companies for the same purpose. The Company recognized an accretion of interest of \$38,104 during the year ended December 31, 2010 (December 31, 2009 – \$97,160).

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12. Long Term Debt (continued)

As part of the acquisition of Silver One on November 16, 2010 (Note 4), the Company assumed a debt of Silver One relating to the 2009 acquisition of 100% of the outstanding shares of La Rastra S.A. de C.V. ("La Rastra") from Aurcana Corporation ("Aurcana"). The remaining obligations under the agreement include the requirement to deliver 1,000,000 common shares on a specified date (See Note 10) and remaining debt payments of US\$500,000 (\$499,000) to Aurcana upon the earlier of April 9, 2012 or six months after the commencement of commercial production; a further US\$500,000 (\$499,000) by October 9, 2012.

The debt payments to Aurcana have been discounted for financial reporting purposes to its fair value. The rate used to discount the debt to its fair value was 5.89%, which was based on the cost of borrowing of similar companies for the same purpose. The Company recognized an accretion of interest of \$7,731 during the year ended December 31, 2010 (December 31, 2009 – \$Nil).

The balance of the long-term debt at December 31, 2010 is as follows:

	December 31 2010 \$	December 31 2009 \$
Due to Goldcorp	487,147	1,033,873
Due to Aurcana - debt payable	917,494	—
	<u>1,404,641</u>	<u>1,033,873</u>
Less: current portion of debt	(487,147)	(516,937)
	<u>917,494</u>	<u>516,936</u>

Required Debt Payments

	\$
2011	499,000
2012	998,000
	<u>1,497,000</u>

The difference between the fair value of the payments and their face values was due to the discounting of the debt at the time of acquisition.

13. Asset Retirement Obligation

	December 31 2010 \$	December 31 2009 \$
Balance, beginning	105,740	225,327
Accretion expense for the period	9,404	24,052
Asset retirement obligations assumed in Silver One acquisition	142,259	—
Change in estimate	1,235,537	(143,639)
Balance, ending	<u>1,492,940</u>	<u>105,740</u>

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13. Asset Retirement Obligation (continued)

The Company's estimates of the costs of reclaiming its properties are based on current legal and regulatory requirements. At December 31, 2010, the Company's undiscounted future asset retirement obligation estimate was \$4,159,567 (December 31, 2009 – \$1,321,856). The provision is the discounted value of the estimated future reclamation and property closure costs based on the Company's individual property closure plans. The Company anticipates settling these obligations within the next 16 years. The present value of the provision has been calculated using a weighted average credit adjusted risk-free discount rate of 8.09% and an inflation factor of 3.0%.

14. Share Capital

The Company has an unlimited number of common shares authorized without par value.

- i) On November 16, 2010, the Company completed the plan of arrangement for the acquisition of Silver One (Note 4) in an all-share transaction. In consideration for 100% of the outstanding shares of Silver One, Silvermex issued 89,315,406 shares and assumed 7,000,000 employee and consultant stock options, 15,795,653 warrants and 1,003,244 agents' common share units of Silver One and share obligations to Aurcana. The fair value of the 7,000,000 employee and consultant share options assumed was determined using the Black-Scholes pricing model using the following assumptions: a weighted average exercise price of \$0.35, a weighted average risk free rate of 1.43%, weighted average volatility of 95%, a weighted average expected life of 1.6 year and with no dividends being paid. With these assumptions, the fair value was determined to be \$2,932,700 with \$1,844,732 for the vested options at the date of acquisition which was recognized as part of the consideration paid and \$1,087,973 for the unvested options which is recognized as stock-based compensation expense over the remaining vesting period.

The fair value attributable to the 460,000 common share warrants was \$152,583. The fair value was determined using the Black-Scholes pricing model using the following assumptions: an exercise price of \$0.45, a risk free rate of 1.67%, volatility of 92%, an expected life of 1.2 year and with no dividends being paid.

The fair value attributable to the 15,335,655 common share warrants was \$3,963,512. The fair value was determined using the Black-Scholes pricing model using the following assumptions: an exercise price of \$0.65, a risk free rate of 1.67%, volatility of 92%, an expected life of 1.2 years and with no dividends being paid.

The fair value attributable to the 1,003,244 agents' common share options portion of the units was \$332,779. The fair value was determined using the Black-Scholes pricing model using the following assumptions: exercise price of \$0.45, a risk free rate of 1.67%, volatility of 92%, an expected life of 1.2 years and with no dividends being paid.

The fair value attributable to the 1,003,244 agents' common share warrants portion of the units was \$120,529. The fair value was determined using the Black-Scholes pricing model using the following assumptions: exercise price of \$0.65, a risk free rate of 1.67%, volatility of 92%, an expected life of 1.2 years and with no dividends being paid.

In conjunction with the plan of arrangement, immediately prior to the completion of the plan of arrangement, the common shares were split on a ratio of 1 to 1.1. The outstanding share options and warrants were split on a ratio of 1 to 1.1 and the exercise price of the options and warrants decreased on a ratio of 1.1 to 1. The other terms of the options and warrants were not modified. All amounts of shares, warrants and options and their exercise prices have been adjusted in this note disclosure to reflect the stock split.

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14. Share Capital (continued)

- ii) During May 2009, the Company completed a 22,879,635 unit private placement at a price of \$0.22 per unit for gross proceeds of \$4,991,920. Each unit consisted of 1.0 common share and 1.0 warrant to purchase one common share for \$0.32 for a period of three years. The agent was paid a fee of \$239,034 and issued 684,732 broker's warrants. Each broker warrant is exercisable to purchase 1.0 share at \$0.32 for a period of three years.

The fair value of the common share purchase warrants was determined using the Black-Scholes pricing model using the following assumptions: a risk free rate of 1.41%, volatility of 131%, an expected life of 1.5 years and with no dividends being paid. The fair value attributable to the common shares and warrants was \$3,325,760 and \$1,666,160 respectively. The fair value attributed to the broker's warrants was \$74,675.

During October 2009, the Company completed a 7,857,140 unit private placement at a price of \$0.32 per unit for gross proceeds of \$2,499,999. Each unit consisted of 1.0 common share and 1.0 warrant to purchase one common share for \$0.41 for a period of two years. The agent and was paid a fee of \$150,000 and issued 471,428 broker's warrants. Each broker warrant is exercisable to purchase 1.0 share at \$0.41 for a period of two years.

The fair value of the common share purchase warrants was determined using the Black-Scholes pricing model using the following assumptions: a risk free rate of 0.52%, volatility of 156%, an expected life of 1 year and with no dividends being paid. The fair value attributable to the common shares and warrants was \$1,594,871 and \$905,128 respectively. The fair value attributed to the broker's warrants was \$110,667.

- iii) During the year ended December 31, 2009, the Company issued 1,921,750 common shares in connection with its La Guitarra property payment at a fair value of \$0.28 per share for a total of \$545,078 and issued 2,649,320 common shares with a fair value of \$0.37 per share for a total of \$987,473 to a vendor to settle balances owing. The Company also issued 1,365,640 common shares for a total of \$758,107 to directors and officers for bonuses earned in 2008.
- iv) During February and March 2010, the Company completed the private placement of 14,587,100 units at a price of \$0.33 per unit for gross proceeds of \$4,773,960. Of the total number of units issued, 10,021,781 units consisted of 1.0 common share and a one-half transferable warrant and 4,565,319 units consisted of 1.0 common shares and a one-quarter transferable warrant to purchase a further share for \$0.41 for a period of two years. The agent was paid a fee of \$381,917 and issued 440,000 broker's warrants. Each whole broker warrant is exercisable to purchase 1.0 share at \$0.41 for a period of two years. Other share issuance costs for the private placement were \$125,747.

The fair value of the common share purchase warrants was determined using the Black-Scholes pricing model using the following assumptions: a risk free rate of 0.59%, volatility of 117%, an expected life of 1 year and with no dividends being paid. The fair value attributable to the common shares and warrants was \$4,096,040 and \$677,920 respectively. The fair value attributed to the broker's warrants was \$49,514.

During December 2010, the Company completed the private placement of 24,193,548 units at a price of \$0.62 per unit for gross proceeds of \$15,000,000. Of the 24,193,548 units, 23,166,499 units were a brokered private placement for gross proceeds of \$14,363,230 and 1,027,049 units were a non-brokered private placement for gross proceeds of \$636,770. Each unit consisted of one common share and half of one warrant. Each whole warrant entitles the holder to purchase a further share for \$0.90 for a period of three years. The agents were paid a fee of \$1,005,426, representing 7% of the gross proceeds raised in the brokered portion of the private placement and were issued 1,621,655 broker's warrants equal to 7% of the number of units sold in the brokered portion of the private placement. The Company paid \$35,650 representing 7% of the gross proceeds raised in the non-brokered private placement and issued 57,893 warrants equal to 7% of the units issued in the non-brokered portion of the private placement. All of the agents' warrants are exercisable to purchase one share at \$0.71 for a period of two years.

SILVERMEX RESOURCES INC.

(formerly Genco Resources Ltd.)

Notes to the Consolidated Financial Statements

December 31, 2010 and 2009

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14. Share Capital (continued)

The fair value of the 12,096,774 common share purchase warrants was determined using the Black-Scholes pricing model using the following assumptions: a risk free rate of 1.57%, volatility of 117%, an expected life of three year and with no dividends being paid. The fair value attributable to the common shares and warrants was \$11,115,005 and \$3,884,995 respectively. The fair value attributed to the 1,621,655 broker warrants and the 57,893 non-broker warrants was determined using the Black-Scholes pricing model using the following assumptions: a risk free rate of 1.38%, volatility of 111%, an expected life of two year and with no dividends being paid. The fair value attributable to the broker warrants and to the non-broker warrants was \$935,990 and \$33,405 respectively.

- v) During September 2010, the Company issued 760,697 common shares for a total of \$217,626 to a former director and officer for bonuses earned and issued 2,208,353 common shares for a total of \$517,138 to Goldcorp Inc. in satisfaction of a US\$500,000 instalment payment on the promissory note related to the acquisition of La Guitarra (Note 12).

a) Options

The Company has established a share purchase option plan whereby the Company's directors may from time to time grant options to employees and non-employees. The maximum term of any option may be ten years, but generally options are granted for five years or less. The fair value of options granted during the year ended December 31, 2010 was determined using an option pricing model assuming no dividends are to be paid, a weighted average volatility of the Company's share price of 97.8%, an annual weighted average risk free interest rate of 1.78% and vesting over various periods from immediately to five years. As of December 31, 2010 the weighted remaining contractual life of the options outstanding was 3.63 years (December 31, 2009 – 3.44 years) and 9,633,329 stock options were exercisable (December 31, 2009 – 2,660,332). During the year ended December 31, 2010, the Company recognized stock-based compensation expense in the amount of \$1,053,029 (December 31, 2009 – \$196,703).

A summary of the Company's options at December 31, 2010 are as follows:

	Number of Options	Weighted Average Exercise Price Per Share \$
Balance, December 31, 2008	3,797,694	2.36
Granted	1,430,000	0.51
Forfeited	(1,644,354)	2.83
Expired	(110,000)	0.95
Balance, December 31, 2009	3,473,340	1.42
Granted *	10,373,700	0.34
Exercised	(540,000)	0.35
Forfeited	(497,200)	1.20
Expired	(181,500)	0.74
Balance, December 31, 2010	12,628,340	0.60

* Includes 7,000,000 employee and consultant stock options that were assumed in the business acquisition of Silver One (Note 4).

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Notes to the Consolidated Financial Statements

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(Expressed in Canadian dollars)

14. Share Capital (continued)

A summary of the Company's options by range of exercise price at December 31, 2010 are as follows:

<u>Expiry Date</u>	<u>Exercise Price</u>	<u>Outstanding</u>	<u>Vested</u>
January 26, 2011	\$1.82	299,840	299,840
June 5, 2011	\$1.86	13,200	13,200
July 31, 2011	\$0.30	300,000	300,000
November 28, 2011	\$2.05	166,100	166,100
February 27, 2012	\$2.77	156,750	156,750
February 8, 2013	\$3.64	393,250	363,689
August 28, 2013	\$1.30	704,000	704,000
February 9, 2014	\$0.26	1,200,000	1,200,000
August 31, 2014	\$0.40	770,000	770,000
October 19, 2014	\$0.76	220,000	220,000
December 14, 2014	\$0.34	1,350,000	1,350,000
February 9, 2015	\$0.36	313,500	156,750
March 2, 2015	\$0.36	506,000	418,000
May 12, 2015	\$0.41	2,650,000	1,325,000
June 21, 2015	\$0.32	1,400,000	650,000
June 30, 2015	\$0.41	55,000	—
July 31, 2015	\$0.41	55,000	—
August 11, 2015	\$0.27	1,855,700	1,540,000
August 31, 2015	\$0.41	55,000	—
October 5, 2015	\$0.41	55,000	—
October 31, 2015	\$0.45	55,000	—
November 15, 2015	\$0.63	55,000	—
Balance, December 31, 2010		12,628,340	9,633,329

The weighted average remaining contractual life of the exercisable options is 3.63 years (December 31, 2009 – 3.44 years).

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14. Share Capital (continued)

b) Warrants

A summary of the Company's warrants at December 31, 2010 as follows:

	Number of Warrants	Weighted Average Exercise Price Per Share \$
Balance, December 31, 2008	4,106,666	4.77
Issued	31,892,936	0.35
Exercised	(1,422,300)	0.32
Expired	(4,106,666)	4.77
Balance, December 31, 2009	30,470,636	0.35
Issued*	36,164,200	0.69
Exercised	(14,979,928)	0.40
Balance, December 31, 2010	51,654,908	0.57

* Includes warrants issued in the business acquisition (Note 4)

The weighted average contractual life of the outstanding warrants is 2.36 years.

Expiry Date	Exercise Price	Outstanding
September 30, 2011	\$0.41	1,181,714
May 8, 2012	\$0.32	12,769,900
May 15, 2012	\$0.32	2,291,670
May 27, 2012	\$0.32	3,391,667
February 12, 2012	\$0.41	2,669,230
February 24, 2012	\$0.41	550,000
February 12, 2012	\$0.65	14,550,655
February 12, 2012	\$0.45	460,000
March 5, 2012	\$0.41	13,750
December 16, 2013	\$0.90	12,096,774
December 16, 2012	\$0.71	1,679,548
Balance, December 31, 2010		51,654,908

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December 31, 2010 and 2009

(Expressed in Canadian dollars)

14. Share Capital (continued)

c) Agents' Common Share Units

A summary of the Company's agents' common share units at December 31, 2010 as follows:

	Number of Agents' Common Share Units	Weighted Average Exercise Price Per Share \$
Balance, December 31, 2009	—	—
Issued	1,003,244	0.45
Exercised	—	—
Balance, December 31, 2010	<u>1,003,244</u>	0.45

The 1,003,244 agents' common share units expire on February 12, 2012. Each unit is exercisable at \$0.45 in to one common share and one common share warrant. Each full warrant is exercisable at \$0.65 into a common share until February 12, 2012.

SILVERMEX RESOURCES INC.

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Notes to the Consolidated Financial Statements

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(Expressed in Canadian dollars)

15. Income Taxes

The following table reconciles the expected income tax payable (recovery) at the Canadian federal and provincial statutory income tax rates to the amounts recognized in the consolidated statements of operations for the years ended December 31, 2010 and 2009.

	Year Ended December 31 2010 \$	Year Ended December 31 2009 \$
Net income (loss) before tax	(41,987,419)	(10,523,063)
Income tax rate	28.50 %	25.00 %
Expected income tax recovery at combined Federal and Provincial rates	(11,966,414)	(2,630,766)
Increase (decrease) due to:		
Impact of higher statutory rates in foreign subsidiaries	7,973	287,758
Effect of reduced tax rate	131,182	824,438
Non-deductible stock-based compensation expense	300,113	49,176
Non-taxable portion of capital gains	(222,265)	—
Non-deductible goodwill	10,678,569	—
Non-deductible accretion on long term debt	13,062	24,290
Effect of benefitting previously unrecognized tax losses	(623,095)	—
Other non-deductible expenses and permanent differences	499,095	185,700
Effect of tax rate change on deferred tax balances	(421,711)	—
Impact of difference in functional and tax currencies	(41,705)	—
Adjustment to valuation allowance	1,125,723	6,045,530
Income tax recovery	(519,473)	4,786,126
	December 31 2010 \$	December 31 2009 \$
The provision for income taxes consists of:		
Current income taxes	56,394	—
Future income taxes	(575,867)	4,786,126
	(519,473)	4,786,126

The potential benefit arising from operating losses has been recognized as a future tax asset. To the extent that these benefits may not be realized, a valuation allowance is provided.

The following tables reflect future income tax assets and liabilities as at December 31, 2010 and 2009:

	December 31 2010 \$	December 31 2009 \$
Future income tax liabilities:		
Book value of mineral properties in excess of tax value	(10,613,990)	(6,056,792)
Book value of property, plant and equipment in excess of tax value	(481,482)	—
Other tax assets	140,186	113,483
	(10,955,286)	(5,943,309)

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Notes to the Consolidated Financial Statements

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(Expressed in Canadian dollars)

15. Income Taxes (continued)

	December 31 2010 \$	December 31 2009 \$
Future income tax assets:		
Non-capital loss carry forwards	12,775,399	8,823,140
Unamortized share issuance costs	830,855	283,857
Tax value of investments in excess of book value	327,196	963,075
Tax value of other assets in excess of book value	2,686,439	3,867,062
Valuation allowance	<u>(16,619,889)</u>	<u>(13,937,134)</u>
	<u>—</u>	<u>—</u>

The Company has non-capital loss carry forwards expiring in the following years by country:

	Canada \$	Mexico \$	Total \$
2013	—	692,179	692,179
2014	894,865	2,241,118	3,135,983
2015	1,664,483	26,620	1,691,103
2016	—	1,334,931	1,334,931
2017	—	8,425,843	8,425,843
2018	—	7,039,186	7,039,186
2019	—	3,386,244	3,386,244
2020	—	424,882	424,882
2026	1,575,219	—	1,575,219
2027	5,086,223	—	5,086,223
2028	3,518,878	—	3,518,878
2029	1,886,794	—	1,886,794
2030	8,631,048	—	8,631,048
	<u>23,257,510</u>	<u>23,571,003</u>	<u>46,828,513</u>

16. Changes in Non-Cash Working Capital

	Year Ended December 31 2010 \$	Year Ended December 31 2009 \$
Accounts receivable	(2,196,158)	(270,269)
Inventory	(477,216)	122,082
Prepaid expenses and deposits	(56,535)	220,893
Accounts payable and accrued liabilities	<u>(372,062)</u>	<u>(3,921,378)</u>
	<u>(3,101,971)</u>	<u>(3,848,672)</u>

SILVERMEX RESOURCES INC.

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Notes to the Consolidated Financial Statements

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17. Supplementary Cash Flow Information

	Year Ended December 31 2010 \$	Year Ended December 31 2009 \$
Interest paid	—	7,231
Income taxes paid	—	—
Non-cash items:		
Shares issued to acquire mineral property interest	519,967	546,000
Shares issued for payment of debt	217,572	399,348

As consideration for the acquisition of Silver One in 2010, the Company issued 89,315,406 shares, assumed 7,000,000 employee and consultant stock options, 15,795,653 warrants and 1,003,244 agents' common share units and assumed debt to Aurcana of Silver One for a total value of \$65,119,144 (Note 4).

18. Related Party Transactions

During the year ended December 31, 2010 the Company completed a private placement (Note 14) at a price of \$0.33 per unit of which a director subscribed for 5,665,319 common shares and 550,000 warrants.

During the year, the Company provided a loan to a director of the Company for \$93,000, bearing interest at 5.0% per annum, due on demand, with the principal and interest due on or before March 10, 2011 (subsequently repaid in 2011).

The above transactions were in the normal course of operations, occurring on terms and conditions that are similar to those of transactions with unrelated parties and, therefore, are measured at the exchange amount.

19. Segmented Information

The Company has two reportable operating segments, being the La Guitarra operating and future development operations and the Silver One exploration operations. All revenues and cost of sales relate to the sale of mineral concentrate in Mexico. As the Silver One segment was created on November 16, 2010, the level of activities in the segment are not significant.

The Company's assets by geographic location are as follows:

	December 31 2010 \$	December 31 2009 \$
Canada	26,822,243	3,239,865
Mexico	67,484,151	33,815,133
	<u>94,306,394</u>	<u>37,054,998</u>

20. Economic Dependence

All sales of mineral concentrate are to Compania Minera Pena de Bernal, S.A. de C.V. Included in accounts receivable as at December 31, 2010 is \$1,766,942 (December 31, 2009 - \$293,795) owing from Compania Minera Pena de Bernal.

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Notes to the Consolidated Financial Statements

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(Expressed in Canadian dollars)

21. Contingencies and Commitments

a) Tax Reassessment

During the year ended December 31, 2010 the Company received a tax reassessment from the Mexican tax authorities in the amount of approximately \$3,100,000. The reassessment is attributable to (a) Value Added Tax ("VAT") refunds collected by the Company that the Servicio de Administracion Tributaria ("SAT") argues that the Company was not entitled to, and (b) SAT argues that certain inter-company loans should have been treated as income. The Company's has contested the claim and its claim has been admitted to the Tax Court. Although the Company believes the reassessment is without merit and that it will ultimately be successful in having it reversed, the Company has posted a bond subsequent to December 31, 2010, for MXN\$38,891,963 (\$3,136,701) with SAT for the full amount of the tax reassessment. The Company has not recorded the impact of this assessment. The bond will be classified as restricted cash in the subsequent year.

b) Payment Dispute

A payment related lawsuit was filed during the year ended December 31, 2010, against the Company's Mexican subsidiary relating to work completed under contract. Subsequent to the year end, the Supreme Court of Guanajuato ruled that the Company's damages are limited to approximately of US\$81,000 (\$80,500) plus interest at a rate of 5% calculated monthly. The Company has recorded a liability of US\$81,000 but believes that the interest portion of the claim (approximately US\$120,000) is without merit.

c) Employee Lawsuit

During the year ended December 31, 2010 the Company received a notice informing them that a former employee had sued La Guitarra subsidiary claiming unpaid salary and expense reimbursements. The amount of the potential liability cannot be determined at the current date but based on the information available, the Company has recorded a liability in the amount of \$220,096 (MXN\$2,700,000).

d) Value Added Tax Receivable (Note 8)

The Company has certain VAT receivables in Mexico amounting to \$2,558,384 (December 31, 2009 – \$2,662,525). During 2008, the Company received an assessment from the SAT advising that most of the refund was rejected. The Company has appealed the decision and has received judgements in its favour. However, due to the uncertainty of the timing and the collectability, the Company recorded an allowance for the full amount of the receivable as of December 31, 2010 with an increase to the allowance. During 2010, the Company recorded a net increase to the allowance of \$525,708 (December 31, 2009 - \$2,662,525).

e) Additional commitments for mineral property option and acquisition agreements, see Note 10 and Note 11.

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December 31, 2010 and 2009

(Expressed in Canadian dollars)

22. Subsequent Events

The following list of material events that occurred after December 31, 2010:

- a) Subsequent to December 31, 2010, 158,250 options were exercised for proceeds of \$70,500.
- b) Subsequent to December 31, 2010, the Company granted 2,820,000 stock options to directors, officers and employees with an exercise price of \$0.74 and five year lives. 100,000 stock options were granted to an employee with an exercise price of \$0.90 and five year lives.
- c) Subsequent to December 31, 2010, the Company issued 1,960,336 shares on the exercise of warrants for gross proceeds of \$1,137,178. Of the total amount, \$555,645 was received during the year ended December 31, 2010.
- d) Subsequent to December 31, 2010, the Company issued 360,000 shares on the exercise of agents' common share units. The gross proceeds of \$162,000 were received during the year ended December 31, 2010.
- e) Subsequent to December 31, 2010, the Company signed a three year lease agreement with minimum monthly lease payments of \$13,730, for a Vancouver head office.
- f) See Note 21(a) for \$3,136,701 bond posted subsequent to December 31, 2010.

Management's Discussion and Analysis

For the Year Ended December 31, 2010

Silvermex Resources Inc.

(formerly Genco Resources Ltd.)

TSX: SLX



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Dated: March 30, 2011

Introduction

For the purpose of this Management's Discussion and Analysis ("MD&A"), the terms "the Company" and "Silvermex", refer to Silvermex Resources Inc. and its subsidiaries. The information provided in this MD&A is supplemented by disclosure contained within the Company's audited consolidated financial statements for the year ended December 31, 2010, and Silvermex's Annual Information Form for the year ended December 31, 2010, both of which are available on SEDAR at www.sedar.com.

All information contained in this MD&A was prepared in accordance with Canadian Generally Accepted Accounting Principles ("GAAP"). All dollar amounts are expressed in Canadian dollars unless specifically stated otherwise.

Cautionary Note Regarding Forward Looking Statements

Silvermex's MD&A contains certain forward-looking statements that involve risks and uncertainties such as statements of the Company's plans, objectives, strategies, expectations, and intentions. The words "may", "would", "could", "will", "intend", "plan", "believe", "estimate", "expect" and similar expressions, as they relate to the Company, or its management, are intended to identify such forward-looking statements. Forward-looking statements in this MD&A include, but are not limited to, statements relating to the actual results of exploration activities, the timing and amount of estimated future production, delineating and developing additional reserves and resources, completion of development or construction activities, capital expenditures, environmental initiatives, requirements for additional capital, future prices of precious and base metals, currency fluctuations and the timing and possible outcomes of pending litigation. Many factors could cause the Company's actual results, performance or achievements to be materially different from any future results, performance or achievements that may be expressed or implied by such forward-looking statements, including those factors discussed below and in filings made with the Canadian Securities Regulatory Authorities. Should one or more of these risk factors or uncertainties materialize, or should assumptions underlying the forward-looking statements prove incorrect, actual results may vary materially from those described herein as intended, planned, anticipated, believed, estimated or expected. Silvermex does not intend, and does not assume any obligation, to update these forward-looking statements.

Risks and uncertainties may include, but are not limited to, changes in general economic conditions, currency fluctuation, changes in the legal, social or political conditions, fluctuations in metals prices, changing costs of services and materials, difficulty in obtaining required equipment supplies and services in a timely manner, changes in reserve and resource estimates, changes in labour laws, access to capital, and other risks and uncertainties unique to the Company or common to public companies, mining companies and companies doing business in multiple political jurisdictions. Also refer to "Risk Factors" in the Company's Annual Information Form for the year ended December 31, 2010.

Qualified Person

Pursuant to National Instrument 43-101, Robert Fraser, M.Sc. P.Geo is the Qualified Person responsible for the technical disclosure in this MD&A.

Overview

Silvermex is a growth-oriented silver and gold producer focused on building a portfolio of high quality, low-cost North American precious metal assets and developing its core asset, La Guitarra, a producing silver and gold property located in the Temascaltepec mining district of central Mexico . The Company has mining operations in Mexico and owns exploration properties in Canada, Mexico and the United States.

The Company's core assets in the Temascaltepec Mining District of Mexico, aside from the producing La Guitarra silver-gold mine and mining concessions, include over 39,000 hectares in one of Mexico's oldest and most prolific silver districts. La Guitarra mine currently consists of two underground operation centres, La Guitarra and San Rafael, and a flotation mill with a proven capacity of 320 tonnes per day.

In January 2010, Silvermex released results of an updated resource and reserve audit for its La Guitarra Mine and Temascaltepec Mining District. The reserve and resource calculations are based on assay data obtained from diamond drilling and sampling both on surface and from underground, and ore body modelling.

On September 20, 2010 Genco Resources Ltd. ("Genco") announced that it had entered into an agreement with Silvermex Resources Ltd to acquire 100% of the shares in an all-share transaction. The transaction was carried out by way of a plan of arrangement and was approved by the shareholders of both companies and The Supreme Court of British Columbia, Prior to the completion of the transaction, Genco subdivided all of its common shares on a 1.1 for 1 basis. All of these shares were exchanged on a 1 for 1 basis. The transaction closed on November 16, 2010. Simultaneously with closing, Genco Resources Ltd. changed its name to Silvermex Resources Inc., and Silvermex Resources Ltd. changed its name to Silver One Mining Corporation ("Silver One"). A new board of directors and management of Silvermex were also appointed.

Silver One was previously listed on the TSX Venture Exchange. Its historical information and regulatory filing, including information on the history of its properties may be found on sedar.com under Silver One.

During December 2010, the Company completed a private placement of 24,193,548 units at a price of \$0.62 per unit for gross proceeds of \$15,000,000. Each unit consists of one common share and a one-half warrant to purchase a further share for \$0.90 for a period of three years. The agents of the brokered private placement were paid a fee of \$1,005,426. The Company also paid \$35,650 in fees for the non-brokered private placement. These fees represent 7% of the gross proceeds raised. 1,621,655 broker's warrants equal to 7% of the number of units sold in the brokered portion of the private placement, and 57,893 warrants equal to 7% of the units issued in the non-brokered portion of the private placement were issued. All of the agents' warrants are exercisable to purchase one share at \$0.71 for a period of two years.

Outlook

During April 2010, the La Guitarra Mill recommenced some operations following a 17 month closure, milling ore from existing stockpiles and dumps on a limited basis. Although the ore milled was considered low grade, metal prices at the time combined with low associated mining and milling costs made the processing of this material attractive on a cost recovery basis. In May 2010, La Guitarra received the necessary authorization to purchase explosives and resumed underground mining operations.

Management did not expect to reach profitable levels of production immediately, but anticipated losses would be reduced with the restart of mining operations. Production steadily ramped up from the recommencement of operations in April 2010, to September, 2010, when production rates were more consistent. Although production costs during the restart of operations were higher than costs reported in the past, these increased costs were largely offset by improved metal prices. The Company's focus in the short term is to lower mining costs and to increase metal production. Several options are being explored to increase metal production, but the Company believes any increase in production must be sustainable and not short term in nature.

The Company is undertaking a significant underground drilling and development campaign to identify areas to increase mine output, but the Company believes any increase in this approach requires a renewed focus by mine management and the workforce, and the coordination of several capital projects being undertaken at the same time.

The Company's long term goal remains focused on production expansion of the La Guitarra mill and mine and it continues to evaluate different production and expansion scenarios to better take advantage of the potential of the Temascaltepec district. A primary objective is also to increase mine output to match the mill capacity. This requires a well managed and successful surface exploration and drilling program which will focus on existing targets and the compilation of existing exploration data, as well as a change from the current mining practices, a successful underground drilling/development program, a renewed focus by mine management and the workforce, and the coordination of several capital projects being undertaken at the same time.

Mine Operations

In late October 2008, a group which included former employees of Silvermex's subsidiary, Servicios para la Industria Minera, S.A. de C.V. ("SIMSA"), closed the La Guitarra operations by blocking mine access. The dispute was resolved in November 2009 with metal production resuming in April 2010. The Company had no production during the year ended December 31, 2009. All mineral sales recorded for the year ended December 31, 2009 relate to the sale of mineral concentrate produced prior to December 31, 2008, and were recognized in accordance with the Company's revenue recognition policy.

The following table summarizes metal production at La Guitarra Mine for the respective years:

	2010 ⁽¹⁾	2009 ⁽²⁾
Tonnes ore milled	39,896	Nil
Tonnes ore milled per day ⁽³⁾	157	Nil
Silver equivalent grade (g/t)	189	0
Silver grade (g/t)	131	0
Gold grade (g/t)	1.13	0
Silver recovery (%)	88.87	0
Gold recovery (%)	82.33	0
eAg shipped (ounces) ⁽⁴⁾	177,814	24,583
Silver shipped (ounces) ⁽⁴⁾	125,835	14,565
Gold shipped (ounces) ⁽⁴⁾	1,020	156
eAg sales (ounces)	160,289	21,699
Silver sales (ounces)	112,690	12,644
Gold sales (ounces)	934	141
Average realized silver price (US\$)	26.52	17.67
Average realized gold price (US\$)	1351.54	1,134.72
Gold\$/Silver\$ equivalency factor	50.96	64.22

⁽¹⁾ Production at La Guitarra restarted on April 21, 2010.

⁽²⁾ All sales relate to mineral concentrates produced during 2008 and sold during 2009.

⁽³⁾ Tonnes milled per day in 2010 based on 254 operating days. The mill did not operate in 2009 due to illegal roadblock and mine closure.

⁽⁴⁾ Ounces contained in mineral concentrate shipped during the period. This excludes inventory of 19,543oz of silver concentrate at the Mine site as at December 31, 2010. This inventory was shipped in January 2011 and revenues will be recognized in 2011.

Exploration and Mine Development

La Guitarra Mine Development

The Company's primary objective continues to be to delineate and develop additional reserves and resources in order to operate the mine at its optimal level by the fourth quarter of 2011.

The San Rafael underground workings, directly contiguous to the La Guitarra zone, have recently been de-watered. Following the rehabilitation and development of this zone, this area will provide the primary feed for the mill.

Approximately 3,900 m of underground development totalling \$2.4 million in expenditures are planned for 2011. This includes 600 m of crosscut development for diamond drill platforms. Mining is scheduled to be conducted on multiple levels allowing for a consistent number of workplaces at any one time to meet production targets.

Although potential new production centres have been identified at Mina de Agua, Coloso and Nazareno, at this time Silvermex plans to focus development on existing areas of production at La Guitarra and San Rafael. During the three month period ended December 31, 2010, work at La Guitarra focused on expanding current areas of production and rehabilitation work to restart production on the La Cruz level.

La Guitarra Exploration

Within the Temascaltepec Mining District the Company has adopted a systematic approach to exploration, which involves the identification of potential economic mineralization through underground and surface sampling followed by drill testing priority targets.

The Company has completed over 85,000 metres of core and reverse circulation drilling since August 2006. Initial drilling focused on developing reserves and resources near the existing La Guitarra Mine. The Company has conducted additional drilling in the areas of Mina de Agua, Nazareno and Coloso with significant mineralization identified in each of these areas. Silvermex estimates that less than 5% of the identified vein system has been drill tested to date.

Drilling targets have been identified and some have been advanced significantly. Areas such as Mina de Agua, Coloso and Nuevo Descubrimiento have already been drilled from surface and/or sampled underground with very positive results. Others, like Rincon and Maravillas have seen historic production with very high grades but little or no exploration using modern techniques has been done.

The new resource model, combined with a comprehensive program of surface mapping and sampling will assist in prioritizing our drill targets for 2011. Approximately 7,500m of surface drilling and 7,500m of underground drilling is planned for this year. Management is confident that this exploration program will lead to the development of near-term ore supply and delineate potential new ore bodies and resources.

San Marcial Property

The results of the diamond drill program consisting of 22 holes totalling 3706.5 meters on this property have been previously publicly disclosed by Silver One. Final check assays from a second laboratory have been received and the QA/QC work has not indicated any issues with respect to the assaying by the both the principal and secondary laboratory for the drill program so the results are considered satisfactory and suitable for reserve/ resource work. An updated mineral resources estimate and block model is being prepared in-house and will be completed in the near future.

Upon completion of the resource estimate and block model, the Company will internally evaluate whether it has sufficient resource to prepare a preliminary mine plan and incorporate the data into a scoping study to determine the economic viability of the San Marcial Property.

Rosario Property

The Company is evaluating the strategic synergy provided by the existing infrastructure at the Rosario Property and its proximity to the San Marcial project. The Rosario Property contains a camp, mill site, tailings facility, water rights and electrical contract and infrastructure that could allow the San Marcial project to commence production in a shorter time frame and at a lower capital cost. In addition, the Company is also encouraged by the exploration potential identified by Grupo México and Aurcana Corporation on this project. Channel samples were obtained from the lowest working levels and the results were encouraging. The Company is looking at exploration opportunities to expand the historic resource, reviewing existing production records and evaluating the potential of these properties to go back into production.

Environmental Matters

Silvermex recently commissioned a pilot water treatment facility at La Guitarra to ensure constant water quality control of a stream near the Company's operations. This facility has shown that the technology selected is successful and a plan and budget for an expansion and a further upgrade are scheduled for the first half of 2011. As development continues at La Guitarra, the Company will be initiating a number of environmental initiatives and stringent control procedures. These include: the continuous analysis of water, water treatment, surface remediation, waste management and recycling programs. The Company will continue these initiatives in order to improve the area for the safety and health of our workers and local communities.

Selected Annual Information

The following is a summary of the Company's financial results for the three most recently completed financial years:

	2010	2009	2008
Total revenue	\$3,950,957	\$381,648	\$6,604,496
Gross margin	\$838,457	\$339,005	(\$708,115)
Net loss	(\$41,467,946)	(\$15,309,189)	(\$9,990,220)
Basic and fully diluted loss per share	(\$0.37)	(\$0.26)	(\$0.24)
Total assets	\$94,306,394	\$37,054,998	\$47,021,055
Total long term liabilities	\$13,365,720	\$6,565,985	\$5,341,323
Dividends declared	Nil	Nil	Nil

The fluctuation in revenues from 2008 to 2010 reflect the closure of the La Guitarra Mine toward the end of 2008, limited processing in 2009 of inventory mined in 2008, and the reopening of the Mill and Mine and resumption of operations in 2010. The Company's net loss in 2009 was higher than the net losses incurred in 2008 due to an allowance of \$2,662,525 provided on the Company's Value Added Tax ("VAT") receivable with the Mexican tax authority, recognizing an impairment loss of property, plant and equipment \$5,391,848, and a future income tax expense of \$4,786,126. The net loss in 2010 is higher than that of 2009 principally due to the impairment of the goodwill (\$37,468,666) which arose on the acquisition of Silver One. The preliminary goodwill on the acquisition transaction arose primarily due to the change in the fair value of the share consideration received by the former shareholders of Silver One. During the time period between the date of the announcement of the transaction and the acquisition date, the Company's share price increased significantly, causing an increase in the overall value of the purchase consideration. The Company tested the value of goodwill at December 31, 2010 for impairment and determined that it could not support the carrying value of the preliminary goodwill, and as a result recorded an impairment.

The decrease in total assets from 2008 to 2009 is in part due to an impairment of property, plant and equipment of \$5,391,848, while the increase from 2009 to 2010 is due to the acquisition of Silver One and its net assets (totaling \$65,119,144) less the impairment of goodwill arising on that acquisition of \$37,468,666, and the net proceeds of the \$13,916,847 private placement which closed in December 2010. Total long term liabilities increased from 2009 to 2010 due to the increase in future income taxes relating to the acquisition of Silver One.

The Financial Statements have been prepared in accordance with Canadian generally accepted accounting principles (GAAP) as described in Note 2 to the Financial Statements for the year ended December 31, 2010. Except as noted, all dollar amounts contained in this discussion and analysis and in the Financial Statements are in Canadian dollars.

Results of Operations

Total assets were \$94,306,394 at December 31, 2010, which is an increase from the total of \$37,054,998 at December 31, 2009. This increase reflects the acquisition of Silver One (less the goodwill impaired) and the proceeds from financing activities undertaken during the year. Silver One's net assets were valued at \$34,956,166, and Silver One had cash of \$4,048,180 at the time of its acquisition.

At December 31, 2010, current assets were \$30,156,929, an increase from \$3,916,844 at December 31, 2009. This increase is attributable to an increase in cash and accounts receivable (see below). On December 31, 2010, Silvermex had working capital of \$25,438,734, an increase of \$26,059,445 over the working capital deficit at December 31, 2009. The improvement in working capital is primarily as a result of the \$13,916,847 (net of agents' fees and share issuance costs) financing concluded in December 2010, the cash acquired in the Silver One acquisition of \$4,048,180, and the increase in accounts receivable due to the shipment of a larger-than-normal quantity of mineral concentrate. This arose because in July 2010 management commenced a review of available options for the processing of mineral concentrates produced at La Guitarra. While this review was in process, mineral concentrates were not shipped, resulting in an increase in mineral concentrate inventories. The review was completed in the latter part of fourth quarter and the Company began shipping mineral concentrates, resulting in an increase in accounts receivable as of December 31, 2010.

Long-term liabilities were \$13,365,720 on December 31, 2010, which was an increase from \$6,565,985 at December 31, 2009. \$1,387,200 of the increase was attributable to the change in estimate attributable to the asset retirement obligation. The remainder of the increase was primarily attributable to the increase of \$5,011,977 in future income taxes liability, a portion of which can be attributed to the acquisition of Silver One.

The Company recommenced operations at La Guitarra during April 2010, reporting a gross profit of \$838,457, on mineral concentrate sales of \$3,950,957. The mineral concentrate sales for 2009 of \$381,648 were for ore processed in 2008 and sold in 2009. The La Guitarra mine did not operate in 2009 due to mine access issues.

The Company incurred an operating loss of \$5,772,020 in 2010, an increase of the loss over an operating loss of \$3,832,420 for 2009. Administration expenses increased to \$4,601,945 in 2010 from \$2,143,252 in 2009 primarily as a result of increase accounting, legal and consulting fees due to property evaluations, due diligence and merger and acquisition activity, related to and as a result of the acquisition of Silver One, and also due to an increase in wages and benefits in 2010 from \$683,159 in 2009 to \$1,672,628 in 2010. This latter increase is partially as a result of the increase in payroll as a result of the acquisition of Silver One as well as due to bonuses paid to management for service provided in 2010.

The Company's net loss before tax for the year ended December 31, 2010 was \$41,987,419, compared with a net loss before tax of \$10,523,063 during the year ended December 31, 2009. In 2009 an impairment of \$5,391,848 had been recorded for certain property, plant and equipment at La Guitarra, whilst none was taken in 2010. A larger allowance of the Company's VAT receivable asset was also

taken in 2009 (\$2,662,525) than in 2010 (\$525,708). However, an impairment of \$37,468,666 was taken against goodwill in 2010.

Summary of Quarterly Results

The following table summarizes selected Company financial information for the last eight completed fiscal quarters (in thousands, except per share):

	Dec 31, 2010	Sep 30, 2010	Jun 30, 2010	Mar 31, 2010	Dec 31, 2009	Sep 30, 2009	Jun 30, 2009	Mar 31, 2009
		\$	\$	\$	\$	\$	\$	\$
Revenue	3,390	313	248	Nil	382	Nil	Nil	Nil
Net income (loss)	(38,066)	(355)	(1,565)	(1,482)	(14,617)	(1,488)	204	592
Income (loss) per share*	(0.33)	(0.00)	(0.02)	(0.02)	(0.20)	(0.02)	0.00	0.01

*Basic and fully diluted

The revenue figure for the quarter ended December 31, 2010, is significantly higher than the revenue reported in the quarters ended September 30 and June 30, 2010. Revenues for the quarter ended June 2010 reflect the lower grade ores being milled, limited mine production, and less than a full quarter of production. During the quarter ended September 30, 2010, production increased at La Guitarra and the average ore grades increased, but the Company elected to stockpile mineral concentrate and limit mineral concentrate shipments during the quarter while it explored mineral concentrate processing options. During the quarter ended December 31, 2010, the stockpiled mineral concentrates from the prior quarter as well as production from the current quarter were shipped and recovered metal sold. Therefore the revenue figures for the quarters ended September 30 and December 31, 2010 understate and overstate what the revenues for the quarters would have been had the metal produced been sold in the quarter of production. Additionally the prices for silver and gold were significantly higher during the quarter ended December 31, 2010 than during the previous quarters.

The loss was larger in the fourth quarter of 2009 due to an allowance taken against VAT receivable (\$2,662,525), an impairment of property, plant and equipment at La Guitarra (\$5,391,848), and future income taxes of \$4,946,377 increased due to the company taking a full valuation allowance against its carry forward losses.

The loss was larger in the fourth quarter of 2010 primarily due to the goodwill impairment of \$37,468,666.

Fourth Quarter 2010

The acquisition of Silver One closed during the fourth quarter. This resulted in an increase to the Company's net assets of \$34,956,167, after the goodwill impairment of \$37,468,666. Silver One's payment and debt obligations and asset retirement obligation were also recognized upon the completion of the acquisition.

The Company also took a further allowance against its VAT receivable with the Mexican Tax Authority of \$525,708 as a result of the tax reassessment, and it also increased its asset retirement obligation at La Guitarra by \$1,235,207.

Liquidity and Capital Resources

On December 31, 2010, the Company had cash on hand of \$17,414,536 and short term investments of \$7,400,203, current assets of \$30,156,929 and working capital of \$25,438,734. The Company believes that the current cash on hand and short term investments are sufficient to meet its cash requirements for the consolidated entity for the next 12 months. In addition to cash used to fund the Company's operations, key events affecting the Company's cash and working capital are as follows:

- During December 2010, the Company completed a private placement of 24,193,548 units at a price of \$0.62 per unit for gross proceeds of \$15,000,000 (net proceeds of \$13,958,924 after agent's commission). Each unit consists of one common share and a one-half warrant to purchase a further share for \$0.90 for a period of three years. Fees of \$1,041,076 were paid and 1,621,655 broker's warrants in the brokered portion of the private placement, and 57,893 warrants in the non-brokered portion of the private placement were issued. The agents' warrants are exercisable to purchase one share at \$0.71 for a period of two years.
- Earlier in 2010, the Company completed a private placement of 14,587,100 units at a price of \$0.33 per unit for gross proceeds of \$4,773,960 (net proceeds of \$4,316,775 after agent's commission and expenses.) As part of this placement the Company issued 10,021,781 units consisting of one common share and a one-half transferable warrant to purchase a further share for \$0.41 for a period of two years, and 4,565,319 units consisting of one common share and a one-quarter transferable warrant to purchase a further share for \$0.41 for a period of two years. The agent was paid \$381,917 and 440,000 broker's warrants exercisable to purchase a further share at \$0.41 for a period of two years.
- During the year, the Company received \$2,000,000 in payments plus interest from Andover Ventures Inc. ("Andover") and amended the existing agreement from 2008 by which the Company had agreed to sell to Andover 6,477,241 convertible common stock and 13,034,769 common stock of Chief Consolidated Mining Company.
- Accounts receivable at December 31, 2010, was \$2,288,506. It includes a higher than average accounts receivable balance due to higher metal prices and above normal concentrate shipments during the fourth quarter. This was as a result of concentrate inventory stockpiled during a review of concentrate processing options available to the Company initiated in July of 2010. During the review the Company elected to stockpile the majority of concentrate produced and following the completion of the review the stockpiled inventories were shipped along with the majority of the fourth quarter's production during the fourth quarter of 2010. Full payment on the accounts receivable was received subsequent to December 31, 2010.

The following table summarizes the Company's contractual obligations as at December 31, 2010:

Contractual Obligations ⁽¹⁾	Payments Due by Period				
	Total	<1 Year ⁽²⁾	1-3 Years ⁽³⁾	4-5 Years	>5 Years
Long-Term Debt	7,497,000	499,000 ⁽²⁾	6,998,000 ⁽³⁾	-	-
Operating Leases	623,647	217,270	406,377	-	-
Other Long-Term Obligations	4,199,535	-	-	-	4,199,535 ⁽⁴⁾
Total Contractual Obligations	12,320,182	716,270	7,404,377	-	4,199,535

- (1) Potential royalty payments based on future production are excluded from the table as they cannot be estimated at this time. We do not believe we will be required to make royalty payments on our mineral properties in the next five years.
- (2) Consists of the final US\$500,000 (\$487,147 discounted, accrued in the financial statements) payment to be made for the purchase of the La Guitarra Mine within the next year. This obligation may be settled in shares. Historically the Company has elected to settle this payment by the issuance of shares.
- (3) Consists of two payments of US\$500,000 (\$917,493 discounted, accrued in the financial statements) to be made in 2012 to Aurcana Corporation, and the final option payment to Silver Standard for the San Marcial property. Silver Standard may elect to receive its payments in shares..
- (4) Consists of the Company's undiscounted future asset retirement obligation estimate of \$4,159,567 (\$1,492,940 discounted, provision included in the financial statements) and the labour severance liability in Mexico of \$39,968..

The Company also has the following royalty obligations:

La Guitarra Property - Mario Héctor Gottfried Joy receives what the Company considers to be advance on royalties. The agreement with Mr. Gottfried Joy calls for a payment to him of \$2,000 per month, subject to an inflation adjustment after September 2003. To date, over US\$210,000 has been advanced to Mr. Gottfried Joy. Once the concessions are in production the monthly royalty payment will be reduced by US\$500 if the calculated monthly royalty is US\$3,500 or less; and by US\$1,000 if the royalty is US\$3,501 or more. Royalty payments of 1.5% of the amount received in final payment for the silver and gold produced is payable when the properties are in production. If the price of silver is more than US\$15 per ounce, the royalty increases to 2%. An additional, one-time payment to Mr. Gottfried Joy of US \$200,000 is payable when production has totalled 30,000 equivalent ounces of gold.

San Marcial Property – 1% net smelter royalty capped at \$13,750,000 less the \$6,000,000 payment and the value of the 1,000,000 shares due to be issued to Silver Standard in February 2011 (unissued). The Company is obligated to pay Silver Standard US\$100,000 per month if commercial production commences on the San Marcial Project while the project is still under option from Silver Standard. These payments will be credited against the purchase price. There is also a 3% net smelter return on the property, and the Company is also obligated to pay US\$100,000 to International American Resources Inc. as a production payment.

Rosario Property - When Aurcana Corporation ("Aurcana") purchased the Rosario property from Industrial Minera Mexico, S.A. de C.V. the acquisition agreement stipulated that Aurcana was to use its "best commercial efforts" to initiate commercial production within 18 months from the date of signing the agreement (i.e., August 2, 2007). If no commercial production is undertaken by such date due to a cause attributable to Aurcana, a 25% advance royalty payment is to be paid on an annual basis based on estimates of production. As Aurcana did not commence production by August 2, 2007, the Company has accrued an amount of \$147,427 based on the limited information available to it.

Subsequent to December 31, 2010, the Company posted a bond of approximately \$3,200,000 with the Servicio de Administracion Tributaria ("SAT"), the Mexican Tax Authority, against the Company's tax reassessment in Mexico of approximately \$3,100,000 for the calendar year 2003 plus interest and penalties. These funds will be unavailable to the Company unless and until the matter is resolved by the courts in the Company's favour, which has not yet been determined.

In order to implement long-term plans for the Temascaltepec Mining District, and take advantage of other business opportunities, Silvermex may need to raise additional funds. At this time, the Company does not know of any demands, commitments, or future events, which will materially affect its liquidity. As in many

resource companies, cash flows are directly affected by the success and failure of exploration and development work, and until such time that prices, grades, throughput, reduced costs or a combination of these factors provides sufficient cash flows to support all exploration and development work the Company may be required to look for alternate sources of financing. No assurance can be given that if additional funding is required it will be available, or if available, will be on terms acceptable to the Company.

Off-Balance Sheet Arrangements

The Company does not have any off-balance sheet arrangements that have, or are reasonably likely to have, a current or future effect on its results of operations or financial condition including, without limitation, such considerations as liquidity and capital resources.

Transactions with Related Parties

During the year ended December 31, 2010, Mr. Anderson, a director of the Company participated in a private placement subscribing for 5,150,290 common shares and 500,000 warrants at a price of \$0.33 per unit.

During the year, the Company provided a loan to Mr. Nelson, a director of the Company for \$93,000, bearing interest at 5.0% per annum, due on demand, with the principal and interest due on or before March 10, 2011 (subsequently repaid in early 2011).

The above transactions were in the normal course of operations, occurring on terms and conditions that are similar to those of transactions with unrelated parties and, therefore, are measured at the exchange amount.

Critical Accounting Policies and Estimates

In the preparation of its audited consolidated financial statements, Silvermex uses Canadian GAAP, which requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying disclosure. Management bases its estimates on knowledge of current events and actions that the Company may undertake in the future; actual results may differ significantly from these estimates, and accordingly affect the results of operations.

The critical accounting policies include but are not limited to:

Mineral concentrate inventory

Mineral concentrate inventory is valued at the lower of cost and net realizable value. Mineral concentrate inventory includes all direct costs of extracting the ore, direct labour, and all indirect pro-rated costs associated with operating La Guitarra mine. When circumstances that previously caused inventories to be written down below cost no longer exist, the amount of the write-down is to be reversed.

Property, plant and equipment

Significant costs related to property acquisitions including undeveloped mineral interests are capitalized until the viability of the mineral interest is determined. The costs are capitalized until such time that it has been determined that a mineral deposit is commercially recoverable and a decision has been made to prepare a mining plan (which occurs upon completion of a positive economic analysis of the mineral deposit). Major development expenditures incurred to expose the ore, increase production or extend the life of an existing mine are capitalized. Mine infrastructure is amortized using the unit-of-production method based on the estimated total recoverable ounces contained in proven and probable reserves at the related mine when operating levels intended by management have been reached. Capitalized costs are written down to their estimated recoverable amount if the properties are determined to be uneconomic or are placed for sale.

Interest and finance costs relating to the construction of plant and equipment are capitalized prior to the commencement of commercial production of a new mine. Depletion of the mine properties is charged on a unit of production basis over the estimated useful life of the mine.

Evaluations of the carrying values of each operation and development property are undertaken in each reporting period to determine if estimated undiscounted future net cash flows are less than the carrying value. Estimated undiscounted future net cash flows are calculated using estimated production sales prices and operating costs, capital costs and reclamation and closure costs. If it is determined that the future net cash flows from an operation or development property are less than the carrying value a write down is recorded with a charge to operations.

Impairment of long-lived assets

The Company reviews the recoverability of its long-lived assets annually and when events and circumstances indicate an impairment event may have occurred. The Company assesses the recoverability of its long-lived assets by determining whether their carrying value can be recovered over their remaining lives through undiscounted future cash flows. In the event that future recoverability is not supported, an impairment loss is measured and recorded based on the extent that the estimated future cash flows on a discounted cash flows are less than the carrying value.

Goodwill

Business combinations are accounted for under the acquisition method of accounting whereby acquired assets and liabilities are recorded at fair value as of the date of acquisition. The excess of the purchase price over the fair value of the net assets acquired is recorded as goodwill and allocated to the applicable reporting unit. Goodwill is not amortized, it is tested annually for impairment or more frequently if current events or changes in circumstances indicate that the carrying value of the goodwill of a reporting unit may exceed its fair value. A two-step impairment test is used to identify potential impairment in goodwill and to measure the amount of goodwill impairment, if any. In the first step, the fair value of a reporting unit is compared with its carrying value, including goodwill. When the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is considered not to be impaired and the second step of the impairment test is not undertaken. When the carrying amount of a reporting unit exceeds its fair value, the fair value of the reporting unit's goodwill (determined on the same basis as the value of goodwill is determined in a business combination) is compared with its carrying amount to measure the amount of the impairment loss, if any. When the carrying amount of reporting unit goodwill exceeds the fair value of the goodwill, an impairment loss is recognized in an amount equal to the excess.

Exploration, development expenditures and acquisition of mineral properties

Significant mineral property acquisition costs and exploration and development expenditures are capitalized. For the acquisition of mineral properties, the fair value is determined by estimating the value of the property's reserves, resources and exploration potential. Capitalized costs are written down to their estimated recoverable amount if the properties are determined to be uneconomic, abandoned, or are placed for sale.

Other critical accounting estimates include but are not limited to:

- the carrying value of the note receivable;
- the outcome of litigation;
- the value of future income taxes and any allowances;
- the valuation of financial instruments;
- the carrying values of receivables; and
- the valuation of stock-based compensation.

Litigation and Contingencies

Tax Reassessment

During the year ended December 31, 2010 the Company received a tax reassessment from the Mexican tax authorities in the amount of approximately \$3,100,000. The reassessment is attributable to (a) VAT refunds collected by the Company that SAT argues that the Company was not entitled to, and (b) SAT argues that certain inter-company loans should have been treated as income. The Company has contested the claim and its claim has been admitted to the Tax Court. Although management believes the reassessment is without merit and that it will ultimately be successful in having it reversed, subsequent to December 31, 2010, the Company posted a surety bond of \$3,136,701 with SAT in the amount of the reassessment, and interest and penalties. Due to the uncertainty of the timing of a final judgement and the collectability, the Company has recorded a valuation allowance for the full amount of the tax receivable as of December 31, 2010. Any amount received in the future will be recorded as income.

Payment Dispute

A payment related lawsuit was filed during the year ended December 31, 2010, against the Company's Mexican subsidiary relating to work done under contract. Subsequent to December 31, 2010, the Supreme Court of Guanajuato ruled that the Company's damages are limited to approximately US\$81,000 (CAD \$80,500) plus interest at a rate of 5% calculated monthly. The Company has recorded US\$81,000 as a liability but believes that the interest portion of the claim (approximately US\$120,000) is without merit.

Employee Lawsuit

During the year ended December 31, 2010 the Company received a notice informing them that a former employee had sued the Company's Mexican subsidiary claiming unpaid salary and expense reimbursements. An accurate amount of the potential liability cannot be determined but based on the information available, the Company has recorded a liability in the amount of \$220,096 (MXN 2,700,000).

Future Changes in Accounting Policies

International Financial Reporting Standards (“IFRS”)

In February 2008, the Canadian Accounting Standards Board (AcSB) announced 2011 is the changeover date for publicly listed companies to adopt IFRS, in place of Canadian generally accepted accounting principles (GAAP). The date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011.

In 2009, we commenced our plan to convert our consolidated financial statements to IFRS at the changeover date of January 1, 2011 with comparative financial results for 2010. The Company's IFRS transition plan addressing the IFRS conversion impact on financial reporting consists of three phases: scoping and planning, design and build, and implementation and reviewing.

- The scoping and planning phase was completed in the first quarter of 2010. This phase included a high-level impact assessment to identify key areas that may be impacted by the transition to IFRS. This resulted in the prioritization of high, medium and low impact areas of focus for the Company based on potential to significantly impact our consolidated financial statements.
- The second phase was initiated during the second quarter of 2010. The progress in detailed analysis and evaluation on high and medium impact areas was slower than our plan, mainly due to certain historical data not being readily available for analysis and priority for the management team to focus on successfully closing the acquisition of Silver One and securing private placements throughout the year. Recognizing the importance of executing the IFRS transition plan, the Company engaged an external advisor in the fourth quarter of 2010 to assist. This phase is now substantially complete with documentation assessing the differences between GAAP and IFRS prepared as well as preparation of shell financial statements, including notes near completion.
- We are currently engaged in the implementation phase. This phase includes implementation of changes identified in second phase two affecting financial reporting, internal controls and businesses, finalization and approval of accounting policy choices and IFRS 1 exemptions, and training of accounting and other staff, as necessary. The preparation of an opening consolidated IFRS balance sheet as of January 1, 2010 is nearing completion and 2010 comparative interim financial statements are underway. The overall IFRS transition is expected to be completed on schedule and we will issue our first interim consolidated financial statements in accordance with IFRS as issued by the IASB beginning with the first quarter ending March 31, 2011 with comparative interim IFRS financial results for 2010.

Our audit committee has been informed of the significant policy decisions, and our auditors are reviewing those areas that are complete.

IFRS changeover plan status

The Company expects the transition to IFRS to impact financial statement preparation, infrastructure and control environment, as well as certain business activities. Management has developed an IFRS conversion plan covering activity areas, and the status of the changeover plan in the key activity areas is as follows:

Key activities	Status
<p>Financial statement preparation:</p> <ul style="list-style-type: none"> • Identification of differences in IFRS and Canadian GAAP accounting policies • Selection of the Company's ongoing IFRS policies • Selection of the Company's IFRS 1 choices • Quantification of effects of change in initial IFRS 1 disclosures and IFRS compliant 2010 financial statements 	<ul style="list-style-type: none"> • The Company has identified differences between our accounting policies under Canadian GAAP and accounting policy choices under IFRS, both on an ongoing basis and with respect to certain choices available on conversion under IFRS 1. • See the sections below for discussion of optional exemptions under IFRS 1 that the Company expects to elect on transition to IFRS and accounting policy changes that management considers most significant to the Company. • An update on management's choices on accounting policies and IFRS 1 elections is to be presented to the Audit Committee in April 2011.
<p>Infrastructure: Development of IFRS expertise</p>	<ul style="list-style-type: none"> • The Company has been providing training for head office staff. • Training of operating staff commenced in September of 2010.
<p>Infrastructure: Development of systems solution for transition period and post-conversion period in:</p> <ul style="list-style-type: none"> • Processing changes • Program upgrades/changes • Gathering data for disclosures • Scope of consolidation package • Budget/plan/forecast monitoring process 	<ul style="list-style-type: none"> • The Company has assessed the impact on system requirements for the conversion and post-conversion periods and expect there will be no significant impact on applications arising from the transition to IFRS. • Additional modules for accounting software and sub-ledgers necessary for post-conversion period are being identified as accounting policy choices are analyzed.
<p>Control Environment: Internal Control over Financial Reporting ("ICFR")</p> <ul style="list-style-type: none"> • For all accounting policy changes identified, assessment of ICFR design and effectiveness implications • Implementation of appropriate changes 	<ul style="list-style-type: none"> • We have identified the required accounting process changes that result from the application of IFRS accounting policies; these changes are not considered significant. • As part of the transition project, we will complete the design, implementation and documentation of the accounting process changes that result from the application of IFRS accounting policies.
<p>Control Environment: Disclosure Controls and Procedures ("DC&P")</p> <ul style="list-style-type: none"> • For all accounting policy changes identified, assessment of DC&P design and effectiveness implications • Implementation of appropriate changes, in particular: <ul style="list-style-type: none"> ▪ Revision of MD&A communications package ▪ Development of IFRS related queries response process in investor relations 	<ul style="list-style-type: none"> • We continue to provide IFRS project updates in quarterly and annual disclosure document.

Key activities	Status
Business Policy Assessment: Financial Covenants <ul style="list-style-type: none"> • Identification of impact on financial covenants and business practices • Completion of any required renegotiations/changes 	<ul style="list-style-type: none"> • No financial covenants exist on current agreements; therefore, there is no impact on the financial covenants and business practices due to changeover.
Business Policy Assessment: Customer and Supplier Contracts <ul style="list-style-type: none"> • Evaluation of impact on customer and supplier contracts • Completion of any required renegotiations/changes 	<ul style="list-style-type: none"> • Major customer contracts have been reviewed. • The terms of contracts are not impacted by IFRS and thus, no changes are required. • The Company does not have any supplier contracts.
Business Policy Assessment: Taxation <ul style="list-style-type: none"> • Identification of impact on taxation in foreign jurisdiction • Revision of tax planning as required 	<ul style="list-style-type: none"> • Identification of the tax impact in Mexico is in progress.
Business Policy Assessment: Compensation Arrangements <ul style="list-style-type: none"> • Identification of impact on compensation arrangements • Implementation of required changes 	<ul style="list-style-type: none"> • Review of compensation has been completed. • Compensation arrangements that are in effect are not impacted by changeover to IFRS. • Management is aware of IFRS impact to share-based payments. The changes to the share-based payment requirements will be taken into consideration when designing the terms and conditions of future share option issuances. • The Company monitored new or changes to compensation arrangements in 2010.

Summary of impact on key areas

1. IFRS 1 - First-time adoption IFRS

First-Time Adoption of International Financial Reporting Standards (“IFRS 1”) provides entities adopting IFRS for the first time a number of optional exemptions and mandatory exceptions, in certain areas, to the general requirement for full retrospective application of IFRS. The following are the optional exemptions available under IFRS 1 that the Company expects to elect on transition to IFRS. The Company continues to review all IFRS 1 exemptions and will implement those determined to be most appropriate in our circumstances on transition to IFRS and up to the audit of the year-end audit as of December 31, 2011. The list below and associated comments should not be regarded as a complete list of IFRS 1 exemptions that are available to the Company as a result of the transition to IFRS.

Optional exemptions	Description
Business combination	<p>Under this exemption, the Company has the option to apply IFRS 3, retroactively to all business combinations or may elect to apply the standard prospectively only to those business combinations that occur after the date of transition.</p> <p>The Company intends to use this exemption which removes the requirement to retrospectively restate all business combinations prior to the date of transition to IFRS 3, which are equivalent to the principles of CICA Section 1582 under Canadian GAAP which we adopted effective January 1, 2010 on a prospective basis.</p>
Share-based payment transactions	<p>IFRS 1 encourages application of IFRS 2 to equity instruments that were granted on or before November 7, 2002, but permits the application only to equity instruments granted after November 7, 2002 that had not vested by the transition date.</p> <p>The Company intends to apply this exemption to equity instruments that were granted on or before November 7, 2002 and those granted after November 7, 2002 and vested before the date of opening IFRS balance sheet.</p>
Fair value or revaluation as deemed cost	<p>This exemption allows the Company to initially measure an item of property, plant and equipment upon transition to IFRS at its fair value and use that fair value as its deemed cost at that date.</p> <p>The Company intends to use this exemption and deem the fair value of specifically identified items of property, plant and equipment on the date of transition to be the deemed costs. An opening balance sheet adjustment to reflect the fair value of specific assets with an offset to retained earnings is expected. The calculation is in the process of being finalized.</p>
Cumulative translation differences	<p>This exemption permits the Company to reset the cumulative translation differences to zero by recognizing the full amount in the retained earnings of the opening IFRS balance sheet.</p> <p>The Company intends to use this exemption and deem all cumulative translation differences to be zero at transition date.</p>
Decommissioning liabilities included in the cost of property, plant and equipment	<p>IFRS 1 provides the option to measure the restoration provision at the transition date in accordance with the requirements of IAS 37. Accordingly the Company can choose to re-measure the provisions as at transition date under IAS 37 Provisions, Contingent Liabilities and Contingent Assets, and estimate the amount to be included in the cost of the related asset by discounting the liability to the date which the liability first arose. The Company is permitted to calculate this using the best estimates of the historical rate-adjusted discount rates, and recalculate the accumulated depreciation under IFRS up to the transition date.</p> <p>The Company intends to use this exemption. The asset retirement obligation (ARO) liability was recalculated under IFRS which is expected to result in an opening balance sheet adjustment to increase the ARO liability and decrease retained earnings by approximately \$5,352.</p>

Optional exemptions	Description
Borrowing costs	<p>This exemption allows the Company to adopt IAS 23, which requires the capitalization of borrowing costs on all qualifying assets, prospectively from the date of the opening IFRS balance sheet.</p> <p>The Company intends to use this exemption and not retroactively capitalize borrowing costs.</p>

2. Impact on key financial statement areas

Based on an analysis of Canadian GAAP and IFRS in effect as at December 31, 2010, we have identified several differences between our current accounting policies and those expected to apply in preparing IFRS financial statements. Information on the key differences that management considers most significant to our financial statements are summarized below. The impact from IFRS 1 exemption choices is not included in the summary below

Financial statement area	Differences between IFRS and Canadian GAAP and Status
Exploration for and evaluation of mineral resources ("E&E")	<p>IFRS 6 permits a reporting entity to choose an accounting policy to expense or capitalize E&E expenditures, while capitalizing other E&E expenditures, as long as the accounting policy is applied consistently. IFRS 6 requires us to value E&E assets using a cost or a revaluation model subsequent to initial recognition. E&E assets may be disclosed as either tangible or intangible asset under IFRS. Entities may test impairment of E&E assets on a multiple cash-generating unit basis under IFRS, as long as such policy is established.</p> <p>Under Canadian GAAP, the Company capitalizes resource property acquisition as mineral interests and exploration and development costs as a component of property, plant and equipment. Under IFRS, the Company has decided to expense E&E costs. This is expected to result in an opening balance sheet adjustment to reduce property, plant and equipment by approximately \$16.9 million. We will capitalize our E&E expenditures incurred subsequent to establishing economic recoverability and we currently intend to elect the cost model for subsequent measurement of E&E assets and to disclose E&E assets as tangible assets.</p>
Property, plant and equipment ("PP&E")	<p>IAS 16 requires entities to value PP&E using a cost or a revaluation model subsequent to initial recognition. Where a significant component of PP&E has a cost that is significant in relation to the cost of the item as a whole, it must be depreciated separately from the remainder of the item.</p> <p>The Company intends to apply the cost model for subsequent valuation of PP&E. The Company has identified differences arising from the additional componentization of PP&E and quantification of the difference is in process.</p>

Financial statement area	Differences between IFRS and Canadian GAAP and Status
Impairment of assets	<p>Under IAS 36, we are required to assess, at the end of each reporting period, whether there is any indication that an asset may be impaired. If such an indication exists, the entity shall estimate the recoverable amount of the asset by performing a one-step impairment test, which requires a comparison of the carrying value of the asset to the higher of value in use and fair value less costs to sell. Value in use is defined as the present value of future cash flows expected to be derived from the asset in its current state. IAS 36 allows reversal of impairment losses where circumstances have changed such that the impairments have been reduced.</p> <p>Under Canadian GAAP, there is a two-step impairment test in which (1) undiscounted future cash flows are compared to the carrying value; and (2) if those undiscounted cash flows are less than the carrying value, the asset is written down to fair value. The use of a one-step process to test for impairment under IFRS as compared to a two-step process under Canadian GAAP may result in more frequent impairment charges where carrying amounts of mining interests may have been supported under Canadian GAAP on an undiscounted cash flow basis, but cannot be supported on a discounted cash flow basis under IFRS.</p> <p>The Company's assessment of impairment indicators did not result in any additional requirement for impairment tests on transition to IFRS. However, the impairment that was recorded under Canadian GAAP for the La Guitarra mineral property was recalculated under IAS 36. This resulted in an estimated further impairment of \$1.9 million which is expected to reduce the mining property asset in the opening balance sheet with an offset to retained earnings.</p>
Share-based payment ("SBP")	<p>IFRS 2 requires each instalment of share-option grant to be measured as a separate award, if share options vest at different times. We are required to estimate forfeitures upfront in the valuation of share options, whereas under Canadian GAAP, they can be recorded upfront or recorded as they occur.</p> <p>The Company has calculated the measurement differences for the share options that were unvested as of January 1, 2010. The adjustment will be to decrease contributed surplus and increase the deficit. Quantification of this adjustment is in process.</p>
The effects of changes in foreign exchange rates	<p>Under Canadian GAAP, there are various indicators to be considered in determining the appropriate functional currency of a foreign operation and such indicators are similar to those under IFRS. When the assessment of functional currency under IFRS provides mixed indicators and the functional currency is not obvious, priority is given to certain specific indicators. Since the determination of the functional currency requires the exercise of judgment based on the evaluation of all relevant information, differences in assessment under IFRS and Canadian GAAP may arise.</p> <p>The Company has completed its assessment and determined that a change in the functional currency of some of the foreign operations is required on conversion to IFRS. There is no impact on the opening balance sheet.</p>

Financial statement area	Differences between IFRS and Canadian GAAP and Status
Provision, contingent liabilities and contingent assets	<p>IAS 37 requires a provision be recognized when there is a present obligation as a result of a past transaction or event; it is probable that an outflow of resources will be required to settle the obligation; and a reliable estimate can be made of the obligation. Under Canadian GAAP, we recognize a provision when an outflow of resources is “likely”, which is a higher threshold than “probable”. IAS 37 measures the provisions using a mid-point of a range, whereas Canadian GAAP uses the lowest value. For material provisions, IFRS requires the provisions to be discounted.</p> <p>The Company has completed its assessment and determined that no additional provisions require recognition on adoption of IFRS.</p>
Income taxes	<p>Canadian GAAP does not recognize deferred tax assets or liabilities arising from the effect of exchange rate movements on the tax base of non-monetary assets or liabilities measured in a functional currency that is different than the presentation currency; these are all recognized under IFRS. IFRS also has a different approach to recognizing and measuring uncertain tax positions (falling within the approach set out for provisions above). Other differences may also arise in specific circumstances.</p> <p>In accordance with IAS 12, deferred income taxes are not recognized for temporary differences that arise from differences between the fair values and tax bases of assets acquired in a transaction other than a business combination. Under Canadian GAAP, deferred income taxes are recognized for such temporary differences</p> <p>Major new deferred tax assets and liabilities might be recognized on adopting IFRS. The tax provision might also become more volatile because of the more active measurement of uncertain tax positions. Quantification of the impact is ongoing, including the potential impact on the future income tax liability which arose on the acquisition of Silver One.</p>

There are other differences between IFRS and Canadian GAAP that may be applicable to the Company, but we do not anticipate these will have a significant impact. The IASB continues to amend and add to current IFRS with several projects underway. The Company’s transition plan includes monitoring actual and anticipated changes to IFRS and related rules and regulations and assessing the impact of these changes on the Company and its financial statements, including expected dates of when such impacts are effective.

Financial Instruments and Other Instruments

The Company’s financial instruments consist of cash, short-term investments, accounts receivable, note receivable, accounts payable, and long term debt.

It is management’s opinion that the Company’s exposure to significant currency, credit, liquidity, or price risks as follows:

Currency Risk

The Company is exposed to the financial risk related to the fluctuation of foreign exchange rates. The Company operates in Mexico, its revenues are generated in United States ("US") dollars and its cost of sales are incurred in Mexican pesos. A significant change in the currency exchange rates between the Canadian dollar relative to the US dollar and the Mexican peso would have an effect on the Company's results from operations, financial position or cash flows. The Company has not hedged its exposure to currency fluctuations.

As at December 31, 2010, the Company is exposed to currency risk through the following assets and liabilities denominated in US dollars and Mexican pesos:

	<u>US Dollars</u>	<u>Mexican Pesos</u>
Cash	1,742,064	940,282
Accounts receivable	1,766,421	2,938,397
Accounts payable and accrued liabilities	(223,638)	(13,220,652)
Long term debt	(1,404,640)	—
Future income taxes	—	(145,752,284)
Asset retirement obligations	(142,256)	(16,721,294)
	<u>1,737,951</u>	<u>(171,815,551)</u>

Based on the above net exposures as at December 31, 2010, and assuming that all other variables remain constant, a 10% depreciation or appreciation of the Canadian dollar against the US dollar would result in a decrease/increase of \$173,447 in the Company's net earnings. Likewise, a 10% depreciation or appreciation of the Canadian dollar against the Mexican peso would result in a decrease/increase of \$1,400,141 in the Company's net earnings.

Credit Risk

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

Financial instruments that potentially subject the Company to a concentration of credit risk consist of cash, accounts and the note receivable. The Company deposits cash with financial institutions it believes to be creditworthy. Cash balances at these financial institutions may exceed the federally guaranteed amount.

The Company's accounts receivable are primarily derived from input tax credits receivable and trade receivables for sales of mineral concentrate ore. The Company maintains an allowance for doubtful accounts receivable in those cases for which the expected collectability of accounts receivable is in question, including against certain VAT receivables.

Note receivable due from Andover Ventures Inc. relates to the sale of shares from Chief Consolidated Mining Company. As the collectability of the note was uncertain in 2009, the Company has recorded a valuation allowance in 2009 against the note with the fair value determined to be the value of the underlying security. For 2010, the amount of the remaining note receivable is less than the securitized amount therefore no valuation allowance has been recorded.

Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company manages liquidity by maintaining adequate cash balances and by raising equity or debt financing. The Company has no assurance that such financing will be available on favourable terms. The Company believes it is subject to liquidity risk through its working capital. In general, the Company attempts to avoid exposure to liquidity risk by obtaining corporate financing through the issuance of common shares.

Although the Company has completed private placements, it will still need to target sources of additional financing through alliances with financial, exploration and mining entities, or other business and financial transactions to assure continuation of the Company's exploration and development programs. There can be no assurance that the Company will be able to continue to raise funds, in which case the Company may be unable to meet its obligations. The net realizable value of the Company's assets may be materially less than the amounts recorded in these financial statements should the Company be unable to secure sufficient additional financing in the future and therefore be in a position to realize its assets and discharge its liabilities in the normal course of business.

Price Risk

The Company is subject to price risk from fluctuations in the market price of silver and gold, which in turn is affected by numerous factors including central bank policies, producer hedging activities, the value of the US dollar relative to other major currencies, global demand and supply and global political and economic conditions. The carrying value of the Company's mine infrastructure and exploration costs could be adversely affected by any reductions in the long term prices of silver and gold.

Additional Disclosure Requirements

Disclosure Controls and Procedures

An evaluation of the effectiveness of the Company's disclosure controls and procedures, as defined under the rules of the Canadian Securities Administrators, was conducted as of December 31, 2010 under the supervision of the Company's Audit Committee and with the participation of management. Based on the results of that evaluation, the Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this report in providing reasonable assurance that the information required to be disclosed in the Company's annual filings filed or submitted by it under securities legislation is recorded, processed, summarized and reported in a timely manner.

Management's Report on Internal Control over Financial Reporting

As of December 31, 2010, management has evaluated the design and the operating effectiveness of the internal control over financial reporting ("ICFR") as defined by National Instrument 52-109. This evaluation was performed under the supervision of and with the participation of the CEO and the CFO. Based on this evaluation, management, the CEO and the CFO concluded that the Company's ICFR were not effective due to the material weakness noted below.

The Company uses the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") internal control framework to design ICFR. Due to its inherent limitations, ICFR may not prevent or detect misstatements on a timely basis as such systems can only be designed to provide reasonable as opposed to absolute assurance. Also projections of any evaluation of the effectiveness of ICFR to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Ineffective controls at the entity level - As evidenced by the material weaknesses described below, the Company determined that several design deficiencies existed within the entity-level controls related to the control environment, risk assessment, monitoring function and dissemination of information and communication activities, resulting in a material weakness in each of these respective components. The deficiency in each of these individual COSO components represents a separate material weakness. The Company's management determined that the weaknesses were primarily attributable to a lack of a code of conduct and other policies and procedures manuals, as well as the lack of formally established audit, compensation, governance and other Board of Directors committees. This lack of formalization was the result of changes in both the management team and the Board of Directors which relates specifically to the business combination transaction. These changes in close proximity to year-end did not allow adequate time for the establishment of formal policies and procedures.

The Company has enhanced its corporate governance policies in the first quarter of 2011 as the board of directors has revised or implemented, and approved new corporate governance charters or policies (as applicable) addressing the audit committee, code of business conduct and ethics, compensation and corporate governance, and insider trading which have been or are being adopted going forward. The Company is also looking to adopt health and safety, environmental, and whistleblower policies. Management believes that the material weaknesses have been remediated, subject to testing in fiscal 2011 as part of the Company's annual assessment of the effectiveness of internal control over financial reporting.

Changes in Internal Control over Financial Reporting

During the period the Company completed a business combination transaction which resulted in changes to governance processes, operations and management personnel. These changes for the Company have had a material effect on our internal control over financial reporting. In response, the Company appointed external advisors to review the internal controls over financial reporting. CEO, CFO and Audit Committee have reviewed the advisors findings and will incorporate their recommendations into the control remediation plan during the first half of 2011.

Disclosure of Outstanding Share Data

The Company has an unlimited number of common shares authorized, with 231,303,256 common shares outstanding on December 31, 2010 and 233,781,843 as of the date of this MD&A.

On December 31, 2010, options to purchase 12,628,340 common shares, and warrants to purchase 51,654,908 common shares were outstanding. As of the date of this MD&A, options to purchase 15,035,250 common shares and warrants to purchase 50,697,813 common shares were outstanding, and 643,244 agents' common share units were outstanding.