

**AVNEL GOLD MINING LIMITED  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEAR ENDED DECEMBER 31, 2008**

The following management's discussion and analysis (the "MD&A") for Avnel Gold Mining Limited ("Avnel" or "the Company") describes the operating and financial results of the Company for the period from January 1, 2008 to December 31, 2008. Avnel was incorporated under The Companies (Guernsey) Laws 1994 to 2001 on February 18, 2005 with the purpose of becoming the holding company for, and to carry on the business of, Avnel Gold, Limited, a Cayman Islands company ("Avnel Cayman"), pursuant to a reorganization which was completed on February 22, 2005.

This MD&A should be read in conjunction with the audited consolidated financial statements for the year ended December 31, 2008 and related notes thereto. The selected financial information and the discussion of results of operations were prepared in accordance with United States generally accepted accounting principles ("U.S. GAAP"). Reference should be made to Note 15 of the consolidated financial statements of the Company for a reconciliation of Canadian and U.S. GAAP. All amounts in this discussion are expressed in U.S. dollars, unless identified otherwise.

**Forward-Looking Statements**

This MD&A contains forward-looking statements which are based on the Company's expectations, estimates and projections regarding its business and the gold market and economic environment in which it operates. By their nature, forward-looking statements involve numerous assumptions, known and unknown risks and uncertainties, both general and specific, that contribute to the possibility that the predictions, forecasts, projections, and other forward-looking statements will not occur. These assumptions may cause the Company's actual performance and financial results in future periods to differ materially from any estimates or projections of future performance or results expressed or implied by such forward-looking statements. These statements are not guarantees of future performance and involve risks and uncertainties that are difficult to control or predict. Therefore, actual results of the Company could differ materially from those discussed in such forward-looking statements as a result of these risks and uncertainties and readers should not place undue reliance on such statements. The Company disclaims any intention or obligation to update or revise any forward-looking statements, where as a result of new information, future events or otherwise, unless required by applicable law.

**Cautionary Note Regarding Technical Information**

Technical information in this publication regarding the Kalana Gold Mine and the Kalana Permit (as such terms are defined below) is summarized or extracted from technical reports prepared by Snowden Mining Industry Consultants (Pty) Ltd ("Snowden") entitled "Kalana Gold Mine Technical Report" dated February 20, 2005 (the "2005 Snowden Technical Report") and "Kalana Phase I Exploration, Mali, West Africa" dated November 4, 2004 (collectively, the "Technical Reports"). The Technical Reports were prepared by G.M. Greenway, Principal Resource Geologist, and D.H. Kullmann, Principal Consultant Mining Engineer, of Snowden, each of whom is a "Qualified Person" as such term is defined in National Instrument 43-101 — *Standards of Disclosure for Mineral Projects* ("National Instrument 43-101").

Technical information in this publication arising subsequent to the date of the Technical Reports, if any, regarding the Kalana Gold Mine and the Kalana Permit is provided by Avnel management under the supervision of Roy Meade, a Company director, and Andrew Killick, a consultant to the Company, each of whom is a non-independent "Qualified Person" as such term is defined in National Instrument 43-101.

**Overview of the Company**

Avnel's principal assets are an 80% indirect interest in Société d'Exploitation des Mines d'Or De Kalana, S.A. ("SOMIKA") and a 90% indirect interest in the Fougadian exploration and exploitation permit (the "Fougadian Exploration Permit"), through its subsidiary, Avnel Mali SARL. The State of Mali holds the remaining 20% interest in SOMIKA and 10% interest in the Fougadian Exploration Permit. SOMIKA is the owner of a gold mine located in the southwest of Mali (the "Kalana Gold Mine") and is the holder of an exploration permit in respect of 387.4 kilometres squared in south western Mali (the "Kalana Permit"). Avnel's strategic objective, through SOMIKA, is to commercially exploit the underground reserves at the Kalana Gold Mine, and enhance the economics of the

Kalana Gold Mine through the conversion of existing open pit mineral resources into open pit reserves and to increase the resource base of open pit resources.

The Kalana Gold Mine was acquired by Avnel in late 2002 following which the existing plant and infrastructure were upgraded. Mining operations were resumed by SOMIKA in January 2004 with commercial production commencing in March 2004. From 2004 to 2008, Avnel increased gold production at the Kalana Gold Mine from 7,396 ounces in 2004 to 25,359 ounces in 2007. In 2008, production decreased to 21,407 ounces. At the same time, Avnel has invested significantly in the capital expenditures and underground development required to expand production to a planned annual rate of 60,000 tonnes. The Kalana Gold Mine development was behind schedule up to 2007 and it is now anticipated that underground production will increase from 48,000 tonnes in 2008 to 60,000 tonnes in 2009 and 2010. The mineral reserves that can be mined from existing underground infrastructure will be depleted during 2010 and Avnel has commenced addressing strategies for optimising the exploitation of its extensive resource base in and in the immediate proximity of the Kalana Gold Mine.

Initial work on the exploration of the Kalana permit area was carried out by SONAREM and SOGEMORK, (two Malian state companies operating with financial and technical assistance from the former Soviet Union) between 1967 and 1982. In this period, 815 diamond drill holes (totalling 81,524 m) were drilled focusing on an area adjacent to the Kalana village. This area eventually became the Kalana Gold Mine.

In a second phase of drilling between 1989 and 1991, a further 56 holes (totalling 16,000 m) were drilled by SOGEMORK to test the deeper parts of the Kalana Gold Mine. The result of the exploration drilling was a final drill spacing of approximately 50 m by 50 m. Sampling of core was generally only where high gold grades were apparent, (i.e. the gold bearing quartz veins) as the perception was that only the high grade free milling quartz veins could be profitably mined with the technology available in Mali at that time. The quartz veins and their immediate hanging and foot walls were analysed with the result that only a fraction of the core was analysed (likely being significantly less than 10%).

The majority of the drill holes were either vertical or sub vertical as the veins targeted were flat dipping. As such this drilling was not optimally oriented to intersect steeply dipping mineralized zones.

Borehole information was interpreted by SOGEMORK on northeast-southwest sections that are spaced at intervals of between 45 m and 50 m. In addition, there are longitudinal sections aligned northwest-southeast at intervals of approximately 60 m. The SOGEMORK exploration staff interpreted rock types, structure and the mineralized features, such as quartz veins and areas of stockwork, on these sections in great detail.

SONAREM-SOGEMORK also conducted exploration within the Kalanako I prospect area that is approximately 3.0 km to the northeast of the Kalana Gold Mine. SONAREM-SOGEMORK reported a historical resource of 600,000 tonnes at a grade of 3.6 g/t Au. Snowden cannot comment on the reliability of this historical resource as information regarding the estimate was not available for Snowden's review.

From 1963 until the 1980s, intermittent exploration activities were carried out by SONAREM-SOGEMORK on grids in the southern part of the Kalana Permit area. Most of the work within these grids involved mapping, selective sampling, and ground geophysics. No drilling or systematic soil geochemistry was conducted in the southern grid areas.

With this very large technical database Avnel determined during 2008 to commence an optimisation programme entitled the "Kalana Main Project".

### ***Kalana Main Project***

The focus of the Kalana Main Project is to study the potential for non-quartz vein hosted gold mineralization and explore the potential for the mining of the Kalana Gold Mine or parts of it either as an open pit or by underground bulk mining methods.

The objective of the Kalana Main Project is to (i) capture the very large geological database generated in paper form by SONAREM and into a digital database, (ii) re-interpret that data to assess the potential for gold mineralization outside of the flat dipping quartz vein structures mapped and assayed by SONAREM and SOGEMORK and (iii) optimise a future drill program to enhance the existing mineral resource base. These quartz vein structures host substantially all of the Kalana Gold Mine's mineral resources, reported in the 2005 Snowden Technical Report and filed on SEDAR. Avnel has continued underground exploration by development and diamond drilling and this data will be included in the database. Underground mining has exposed numerous quartz vein, stockworks and mineralization in the metasediments that had not been incorporated by SONAREM and SOGEMORK into their geological model of the deposit.

The SONAREM and SOGEMORK exploration in its first and most substantive phase aimed at establishing a high grade free milling gravity gold recoverable underground mine targeting a set of stacked, flatly dipping quartz veins that occur in and around a diorite stock. This has a number of implications in terms of the Russian exploration methodology, being:

- As the target was perceived by SONAREM and SOGEMORK to consist of flatly dipping veins, more than 98% of their drilling was vertical or sub-vertical. The joint venture between Ashanti Gold Fields Ltd. ("Ashanti") and Johannesburg Consolidated Investments Ltd. which studied the mine in 1995/1996 and the surrounding area also drilled predominantly vertical holes.
- With SONAREM and SOGEMORK's perception that only the high grade free milling quartz veins could be profitably mined, they analysed the quartz veins and their immediate hanging and foot walls with the result that only a portion of the core was analysed and incorporated into their geological model.
- All drilling by SONAREM and SOGEMORK was core drilling but the core was not kept, although it was meticulously logged. Ashanti drilled two twin holes (one vertical and one inclined) which had good correlation with the SONAREM and SOGEMORK holes that they twinned.
- As SONAREM and SOGEMORK were only targeting free milling gold, they have neglected the oxide cap (except for the Kalana, I pit) the potential for mineralization in the wallrocks with disseminated sulphides, stockworks and other quartz vein structures.

### Selected Annual Information

(in thousands of U.S. dollars except per share amounts)

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Total Revenue.....	17,800	15,938	11,872
Total Expenses.....	19,062	15,827	13,735
Net Loss.....	(3,457)	(904)	(2,675)
Loss per share	\$(0.05)	\$(0.01)	\$(0.05)
Weighted average shares outstanding	71,068,219	62,382,062	55,920,189
 Balance Sheet			
Working Capital (Deficiency) .....	(639)	(261)	623
Total Assets .....	31,843	30,102	25,821
Long Term Debt .....	10,941	10,941	11,821
Shareholders' Equity .....	12,665	12,982	10,024

### Results of Operations

Revenue has increased to \$17,800,000 in 2008 from \$15,938,000 in 2007. This is as a result of an increase in average sales price of gold from \$629 per ounce in 2007 to \$905 per ounce in 2008, partly offset by a decrease in gold ounces sold from 25,270 ounces in 2007 to 19,614 ounces in 2008.

Avnel recorded a net loss of \$3,457,000 (\$0.05 per share) for the year ended December 31, 2008 compared to a net loss of \$904,000 (\$0.01 per share) in 2007. Lower gold production, delayed gold sales, and higher operating costs were the main contributing factors to the increase in the net loss compared to 2007.

As compared to the balance sheet as at December 31, 2007, Avnel's cash and cash equivalents as at December 31, 2008 decreased by \$730,000. Operating activities generated a negative cash flow of \$3,130,000 with capital expenditure of \$1,782,000. Cash of \$2,000,000 was drawn down on the Loan Facility (as defined below) with \$2.2 million received from the 2008 Private Placement (as defined below).

There was a working capital deficiency of \$639,000 at December 31, 2008 compared to working capital deficiency of \$261,000 as at December 31, 2007 with the main factor being that the Loan Facility becoming a current liability and the high gold bullion inventory held as at December 31, 2008.

Total assets increased from \$30,102,000 as at December 31, 2007 to \$31,843,000 at the end of 2008 with the net value of property, plant and equipment increased by \$132,000. The value of current assets increased by \$1,609,000 mostly as a result of an increase in metal inventories for sale in January held at December 31, 2008.

At December 31, 2007 and December 31, 2008 shareholder loans (as defined below) were \$10,941,000. Short term debt increased by \$2,000,000 resulting from the drawdown of the Loan Facility. Shareholders' equity reduced to \$12,665,000 at December 31, 2008 from \$12,982,000 at the end of 2007. The biggest contributing factor was the net loss for the year of \$3,457,000 partly offset by the increase in shareholders' equity of \$2,952,000 due to shares issued as a result of the 2008 Private Placement and shares issued as payment of interest on the Shareholder Loans (as defined below). Additional Paid in Capital increased by \$182,000 due to stock option charges.

## Mining Operations

The following table shows the production from the Kalana Gold Mine:

	<u>2008</u>	<u>2007</u>
Tonnes milled:		
Underground ore	48,232	35,222
Coarse sand reclaimed	-	-
Total	<u>48,232</u>	<u>35,222</u>
Gold grade - grams per tonne (g/t):		
Underground ore	15.7	24.2
Coarse sand reclaimed	-	-
Total	<u>15.7</u>	<u>24.2</u>
Recovery rate - %	88.0	92.0
Gold production - ounces	21,407	25,359
Cost per tonne milled	\$227	\$296
Operating cost per ounce of gold sold	\$653	\$412
Operating cost per ounce of gold produced	\$513	\$411

Tonnes milled in 2008 were 37% higher than the production achieved in 2007. Gold production at 21,407 ounces in 2008 was 16% lower than 2007 reflecting lower head grade not offsetting higher tonnes milled

Underground mining production increased 37% in 2008 as additional mining faces were made available on 150m and 180m levels.

The gold grade of underground ore mined of 15.7 g/t in 2008 was 35% lower than that obtained in the previous year (24.2g/t). Gold grade decreased as mining moved into lower grade reserve blocks.

Gold recovery in 2008 decreased to 88% as the head grade decreased.

Tonnes milled and gold produced was lower due to the failure of the No 2 Shaft winder gear box in December. The winder returned to operation 24 days later but no ore was hoisted and delivered to the mill from No 2 Shaft. It is estimated that 2,400 tonnes were lost during this period.

Mine development totalled 1,689 metres in 2008 compared to 2,043 metres in 2007. Development exceeded the planned rate for the year. Ore development increased to 440 metres in 2008 from 274 metres in 2007 as new ore reserve blocks were opened up on 150m and 180m level.

On 150m level, development focused on opening up the Vein 17 mineral reserve block and completing access to the diamond drill sites. On 180m level the haulage advanced north towards Vein 18. The haulage intersected a new Vein, 18C, and this was developed between 180m and 150m levels. The haulage intersected Vein 18 and a raise was mined from 180m level towards 150m level. The grade of Vein 18 was disappointing as it was forecast that the grade would be 30g/t between 180m and 150m levels. Diamond drilling from 150m level has shown Vein 18 to be narrower and of a lower grade than forecast using the original model. This has led to a significant reduction in the forecast mining reserve for Vein 18. Vein 18C was included in the mineral resources of Vein 18 but is clearly a separate vein with average grade of 15g/t.

On 180m level, the haulage south was developed to intersect Vein 1. The Vein 1 reserve block above 180m level was mined using this access.

Mine operating costs for the year ended December 31, 2008 amounted to \$13,349,000 compared with \$10,895,000 in 2007. The reasons for the 23% increase were due to higher underground production (37%) and mill tonnes (37%). Cash operating cost of \$227 per tonne milled in 2008 was significantly lower than the cost per tonne in 2007 of \$296 per tonne mainly because of 37% more tonnes milled. Cash operating cost per ounce sold of \$653 per ounce in 2008 increased from \$412 per ounce in 2007 due to the reduction in ounces sold in 2008 compared to 2007 and higher operating costs. The reduction in ounces sold was partly due to gold bullion being held at the year end to meet the January 2009 hedge program, due to the cessation of production in December because of the breakdown of the winder gearbox.

### Gold Sales

Gold sales data is as follows:

	<u>2008</u>	<u>2007</u>
<b>Gold ounces sold</b>		
- at spot price	14,364	18,410
- under forward contracts	5,250	6,860
- total	<u>19,614</u>	<u>25,270</u>
<b>Average realized gold price per ounce</b>		
- at spot price	\$888.26	\$698.90
- under forward contracts	\$952.79	\$441.60
- total	\$905.38	\$629.05
<b>Metal revenue - \$000</b>		
Gold sales if all sales were at spot prices	\$12,756	\$17,403
Net effect of forward sales	5,002	(1,507)
Total gold sales	<u>17,758</u>	<u>15,896</u>
Silver sales	42	42
Metal revenue	<u>\$17,800</u>	<u>\$15,938</u>

Gold spot prices commenced 2008 at \$841 per ounce and ended at \$865 per ounce, with the London AM Fix averaging \$872 per ounce during the year.

### Other Expenses

General and administrative costs amounted to \$3,135,000 for the year ended December 31, 2008 compared to \$2,699,000 in 2007. This increase was mainly due to legal costs associated with the 2008 Private Placement, tax

issues relating to SOMIKA, salary increases due to appointment of the Company's Chief Operating Officer and travel costs. Stock based compensation charged amounted to \$182,000 in 2008 compared to \$225,000 in 2007.

Depreciation, depletion and reclamation expenses amounted to \$1,650,000 in 2008 compared to \$1,777,000 in 2007. Depletion costs are calculated on the unit-of-production basis and the decrease results primarily from the reduced production in 2008 compared to 2007.

Interest expense was \$713,000 for the year ended December 31, 2008 compared to \$818,000 in 2007. This was mainly as a result of the decrease in the 6-month U.S. dollar LIBOR rate which impacted the rate of interest payable on the Shareholder Loans.

### Exploration

On October 17, 2006, Avnel was awarded the Fougadian Exploration Permit which lies south of the Kalana Permit. The Fougadian Exploration Permit covers an area of 150 square kilometres including a portion of the Niessoumala exploration area. The permit was awarded in accordance with the 1999 Mining Code and a foundation agreement (the "Foundation Agreement") was signed between Avnel Mali, a 100% wholly-owned subsidiary of Avnel, and the Government of the Republic of Mali. Avnel has a 90% indirect interest and the Malian State holds a 10% in the Fougadian Exploration Permit, provided a decision is made to construct a mine. The Foundation Agreement provides for the exploration and exploitation of Group 2 minerals as defined in the 1999 Mineral Code. Group 2 minerals include gold and silver, and base metals, but excludes precious stones, semi-precious stones and fossils.

Avnel advanced its exploration of the Fougadian Exploration Permit by commencing an exploration drilling program in March 2008. The Fougadian Exploration Permit is located directly south of the permit on which the Kalana Gold Mine is operating.

The drill program was focused on the Avnel-1 gold-in-soil geochemical anomaly that is the largest and the most important in terms of gold and arsenic values on the Fougadian Exploration Permit. The anomaly is defined by an area where values generally exceed 32ppb Au and attain a maximum of 1731ppb Au. It extends for almost 4 kilometres in an N-S direction and for 1.5 kilometres in an E-W direction.

Two diamond drill holes were completed to a depth of 190 metres in order to provide information on the bedrock structure that can be used to optimise the orientation of the RC drilling programme. 48 inclined RC drill holes totalling 5,422 metres were completed on a grid pattern during the second quarter of 2008, covering only a small portion of the Avnel 1 anomaly. The holes were drilled in a heel-to-toe fashion to ensure complete coverage across the width of the anomaly. As the budget was inadequate to fully test this large anomaly, the holes were drilled along pairs of lines spaced 200m apart, one pair in the north and a second pair 800m further to the south. Because of encouraging geological indications, an additional three holes were drilled to the south of the latter set of lines. In summary, out of the 50 holes drilled 15 (30%) intersected values above 1g/t Au.

### Consolidated Statement of Operations for the Quarters Ended

Quarter ended	Dec 31 <u>2008</u>	Sep 30 <u>2008</u>	June 30 <u>2008</u>	Mar 31 <u>2008</u>	Dec 31 <u>2007</u>	Sep 30 <u>2007</u>	June 30 <u>2007</u>	Mar 31 <u>2007</u>
Revenue	\$3,382	\$ 5,592	\$ 3,330	\$ 5,496	\$3,516	\$ 3,487	\$ 4,657	\$ 4,278
Net income (loss)	\$(1,101)	\$(455)	\$ (2,102)	\$ 201	\$(633)	\$(1,320)	\$ 280	\$ 769
Income (loss) per share	\$(0.015)	\$ (0.007)	\$ (0.030)	\$ 0.003	\$(0.01)	\$ (0.02)	\$ 0.004	\$ 0.01

Net loss increased in 2008 compared to 2007, resulting from reduced production at higher cost offset by higher gold prices.

## Fourth Quarter Results

Fourth quarter revenue of \$3,382,000 has decreased by 4% compared to revenue of \$3,516,000 in the fourth quarter of 2007 and by 40% compared to the third quarter of 2008 due to holding gold bullion in stock at the year end to meet the January 2009 hedge program. Net loss increased from \$633,000 in the fourth quarter of 2007 to \$1,101,000 in the fourth quarter of 2008. Cash and cash equivalents decreased from \$2,156,000 at the start of the fourth quarter to \$277,000 at December 31, 2008, a decrease of \$1,879,000. Cash utilised by operating activities in the fourth quarter of 2008 was \$2,046,000 and expenditure on property, plant and equipment was \$167,000.

## Liquidity

As of December 31, 2008, Avnel had cash of \$277,000 (2007 - \$1,007,000) and a working capital deficiency of \$639,000 (2007 - working capital deficiency of \$261,000). In the year ended December 31, 2008, operating activities used funds of \$3,130,000 compared to generated cash funds of \$1,743,000 in 2007. This was mainly because the net loss from continuing operations in 2008 of \$3,457,000 was substantially more than the 2007 net loss of \$904,000. Gold bullion stock was high at the year end due to the cessation of production in December due to the breakdown of the winder gearbox and the requirement to hold gold bullion to meet the Company's hedge program in January 2009. Avnel expended \$1,782,000 on mine development and capital additions in 2008 compared to \$4,803,000 in 2007.

On April 14, 2008, Avnel completed three transactions with its principal shareholders and two other shareholders of the Company. First, a non-brokered private placement, ( the "2008 Private Placement") of 6,542,857 Common Shares was made to Elliott International L.P. and The Liverpool Limited Partnership, an affiliate of Elliott International L.P., and two other Avnel shareholders, at a price of CDN\$0.35 per Common Share for gross proceeds of CDN\$2,290,000 (US\$2,231,000). Second, a secured term loan in the principal amount of US\$3,000,000 was provided by Manchester Securities Corp., an affiliate of Elliott International L.P., to Avnel (the "Loan Facility"), which is to be repaid on December 31, 2009. As at December 31, 2008 US\$2,000,000 was drawn down. The Loan Facility is secured by a security interest granted over all of the ordinary shares of Avnel Cayman held by the Company and Avnel's interest under an intercompany loan agreement among Avnel, Avnel Cayman and SOMIKA. Third, the maturity date of the term loan notes (the "Term Loan Notes") previously issued by Avnel on June 30, 2005 to each of Elliott (as defined below) and the Fern Trust was extended from December 31, 2008 to December 31, 2009. The Term Loan Notes continued on the same terms in all other respects.

The consolidated financial statements have been presented on the basis that the Company is a going concern. Accordingly, the financial statements do not include adjustments relating to the carrying value of assets, the amounts and classification of liabilities, or other adjustments that might result should the Company be unable to continue as a going concern. The Company has current liability debts of \$2.9 million due for repayment on December 31, 2009, and this debt repayment and continuing operations of the Company are dependent on its ability to generate future cashflows from its mining operations or obtain additional financing. There is a risk that additional financing will not be available on a timely basis or on acceptable terms. Management are actively looking at several re-financing and restructuring options to address this issue and expect that financing options will be available to enable the Company to continue to operate as a going concern. In the event that the Company is unable to repay this debt, refinance such debt, or secure additional financing and continue as a going concern, material adjustments would be required to the carrying value of the assets and liabilities and the balance sheet classifications used.

## Contractual Obligations

The Company has the following contractual obligations at December 31, 2008:

Contractual Obligations - \$000	Total	Less than 1 year	1-3 years	4-5 years	After 5 years
Current portion of long-term debt (1)	2,880	2,880	-	-	-
Long-term Debt (1)	10,941	-	10,941	-	-
Operating Leases (2,3)	390	116	274	-	-
Total Contractual Obligations	\$ 14,211	\$ 2,996	\$ 11,215	\$ -	\$ -

Notes:

- (1) The long term debt of Avnel consists entirely of the Shareholder Loans.
- (2) The Company has entered into operating leases for office space and equipment with a company related to Fern. Pursuant to these leases which expire in June 2012, future minimum payments will amount to £265,000 up until the end of the lease, which at the 2008 year end exchange rate, is equivalent to \$384,000 per annum.

- (3) The Company has entered into an operating lease for an office building in Bamako, Mali. The lease expires in June 2009. The remaining commitment as at December 31, 2008 was \$6,000.

### **Capital Resources**

Long term debt of the Company consists mainly of convertible loans provided by Elliott International L.P. and Elliott Associates L.P. (collectively "Elliott") and the Fern Trust, the two major shareholders of Avnel (the "Shareholder Loans") with an aggregate principal amount outstanding of \$10,941,000. Each shareholder loan note is convertible by the holder into Common Shares at CDN\$0.898299 per Common Share and bears interest at the six month U.S. LIBOR rate plus 2% payable bi-annually. The Company may elect to pay the interest in Common Shares in lieu of cash and may, upon maturity, elect to repay the outstanding principal amount in Common Shares at CDN\$0.898299 per Common Share if the 40-day weighted average trading price of the Common Shares prior to the conversion date is equal to or greater than \$1.20. The Shareholder Loans notes mature on June 30, 2010.

The Company also has the Term Loan Notes with an aggregate principal amount outstanding of \$880,000, bearing interest at a rate of 8% payable bi-annually. The Term Loans Notes are due for repayment on December 31, 2009.

In addition the Company has the Loan Facility of \$3,000,000 with an aggregate principal of \$2,000,000 drawn at December 31, 2008. The loan matures on December 31, 2009 and bear interest at a rate of 10% per annum, payable bi-annually.

The Company expended \$1,782,000 on capital in 2008 compared to \$4,803,000 on capital in 2007. The Company forecasts that capital expenditure in 2009 will be \$2,800,000. At December 31, 2008, there were commitments for capital expenditure of \$205,000.

### **Related Party Transactions**

SOMIKA purchases explosives from African Explosives Limited ("AEL"). Mr. Ibrahim Kantao is a director of the Company, SOMIKA and AEL and is also the Director-General of AEL Mali SARL. Such purchases amounted to \$466,000 in the year ended December 31, 2008. The Company has an ongoing supply agreement with AEL Mali SARL.

Avnel entered into a forward sales agreement on March 4, 2008 in respect of 10,000 ounces for the period through to April 2009 at an average price of \$956 per ounce with Elliott. As at December 31, 2008, the Company had met all its obligations under this agreement. During the year ended December 31, 2008, forward sales of \$5,002,000 were recorded.

The premises occupied by Avnel and Kalana Mine Services in London are leased from a company associated with the Fern Trust, a significant shareholder. The Company incurred \$153,000 in rental costs during the year ended December 31, 2008. The Company's lease expires in June 2012.

### **Business Risks**

The risks associated with Avnel and the effect on future operating results and financial position of the Company are set out in detail under the section entitled "Risk Factors" in the Company's Annual Information Form dated March 30, 2008 ("the AIF"), which section is incorporated by reference into and forms an integral part of this MD&A. A copy of the AIF can be found on the System for Electronic Document Analysis and Retrieval (SEDAR) at [www.sedar.com](http://www.sedar.com).

### *Going Concern*

The Company has a significant going concern risk in that it relies on the cash flow of one operating mine. The mine has in excess of a one million ounce mineral resource, but has reached a stage in its development that extraction by underground mining and gravity recovery methods may not be the most economical and it is considering very carefully its future strategy.

The consolidated financial statements have been presented on the basis that the Company is a going concern. Accordingly, the financial statements do not include adjustments relating to the carrying value of assets, the amounts and classification of liabilities, or other adjustments that might result should the Company be unable to continue as a

going concern. The continuing operations of the Company are dependent on its ability to generate future cash flows from its mining operations or obtain additional financing, although there is a risk that additional financing will not be available on a timely basis or on acceptable terms. In the event that the Company is unable to secure additional financing and continue as a going concern, material adjustments would be required to the carrying value of the assets and liabilities and the balance sheet classifications used.

#### *Exploration, Development and Operating Risk*

The Company faces risks associated with underground mining such as rock conditions, water, geological faults, variable vein widths, dilution, power supply and equipment failures. The international mining industry is facing a shortage of skilled personnel and the Company faces risks in attracting and retaining skilled employees. The Company operates in a remote location in Mali and is reliant on the transport systems to deliver equipment and materials which are purchased in South Africa or Europe. There is a risk that such equipment and materials may not always be available on site when required.

#### *Gold Prices*

The Company also faces risk in respect of its exposure to gold prices.

#### *Hedging Activities*

All gold revenues and a portion of operating costs are in U.S. dollars. The Company has not hedged its foreign exchange risk relating to its non-U.S. dollar expenses.

#### *Capital Requirements*

Avnel will require significant capital in order to fund its operating costs, to service existing and future indebtedness and to carry out plans to develop the Kalana Gold Mine and the Kalana Permit. As well, a portion of Avnel's activities will be directed towards the search for, and development of, new mineral deposits which will require significant capital investment to achieve commercial production from any successful exploration efforts. Avnel will require additional financing from external sources to meet such requirements. There can be no assurance that such financing will be available to Avnel or, if it is, that it will be offered on acceptable terms. If additional financing is raised through the issuance of equity or convertible debt securities of Avnel, the interests of shareholders in the net assets of Avnel may be diluted. Any failure of Avnel to obtain required financing on acceptable terms could have a material adverse effect on Avnel's financial condition, results of operations and liquidity and require Avnel to cancel or postpone planned capital investments.

#### *Insurance and Uninsured Risks*

Avnel maintains insurance against risks that are typical in the gold mining industry. Although the Company maintains insurance in amounts that it believes to be adequate, the insurance coverage maintained may not be adequate in the event of unforeseen circumstances, and Avnel does not maintain political risk insurance.

#### *Environmental Risks and Hazards*

The Company is committed to environmental protection, to safe operations and to the control of environmental risks. The Company adheres to the requirements of the Malian Government and has adopted policies and procedures as expected in the mining industry. The Company is committed to maintaining the aforementioned risks at levels as low as can be reasonably achieved, taking into account social and economic factors, and that continued improvement in environmental and health and safety performance be achieved.

#### *Governmental Regulation*

All phases of Avnel's operations are subject to environmental regulation in the jurisdiction in which it operates. These regulations mandate, among other things, the maintenance of air and water quality standards and land reclamation. They also set forth limitations on the generation, transportation, storage and disposal of solid and hazardous waste. Environmental legislation is evolving in a manner which will require stricter standards and enforcement, increased fines and penalties for non-compliance, more stringent environmental assessments of proposed projects and a heightened degree of responsibility for companies and their officers, directors and employees. There is no assurance that future changes in environmental regulation, if any, will not adversely affect Avnel's operations. Environmental hazards may exist on the property which are unknown to Avnel at present and which have been caused by previous or existing owners or operators of the properties.

### *Hazardous Materials*

Certain hazardous materials are presently stored on the Kalana Gold Mine site, including diesel fuel, arsenic trioxide and sulphide concentrates tailings that remain from the SOGEMORK operations in the 1980s. SOMIKA is currently conducting test programs to assess the optimum process to ameliorate the risks associated with production, storage and disposal of these hazardous materials.

### *Global Financial Risk*

Current global financial conditions have been characterized by increased volatility and several financial institutions have either gone into bankruptcy or have had to be rescued by governmental authorities. Access to public financing has been negatively impacted by both the rapid decline in value of sub-prime mortgages and the liquidity crisis affecting the asset-backed commercial paper market. These factors may impact the ability of the Company to obtain equity or debt financing in the future on terms favourable to the Company. Additionally, these factors, as well as other related factors, may cause decreases in asset values that are deemed to be other than temporary, which may result in impairment losses. If such increased levels of volatility and market turmoil continue, the Company's operations could be adversely impacted and the trading price of the Common Shares may be adversely affected.

### **Critical Accounting Estimates**

The consolidated financial statements of the Company have been prepared in accordance with U.S. GAAP. Management is required to make various estimates and judgements in determining the reported amounts of assets and liabilities, revenues and expenses for each period presented and in the disclosure of commitments and contingencies. Management believes the following critical accounting policies reflect its more significant estimates and judgements used in the preparation of the consolidated financial statements.

The consolidated financial statements have been presented on the basis that the Company is a going concern. Accordingly, the financial statements do not include adjustments relating to the carrying value of assets, the amounts and classification of liabilities, or other adjustments that might result should the Company be unable to continue as a going concern.

All costs, other than acquisition costs, are expensed prior to the establishment of proven and probable reserves. Gains or losses resulting from the sale or abandonment of properties are included in operations. Acquisition and development costs associated with properties brought into production are charged to operations using the units of production method based on estimated proven and probable reserves which can be recovered. Costs of start-up activities and on-going costs to maintain production are expensed as incurred. Production facilities and equipment are stated at cost and are amortized over the estimated proven and probable reserves which can be recovered from the related property.

The Company evaluates the carrying value of its properties and equipment when events or changes in circumstances warrant and tests for recoverability of the long life asset value. With respect to properties, a test for recoverability is performed to determine if the estimated future cash flows exceed the carrying amount of the asset. Measurement of any impairment loss is determined by the estimated fair value of the assets based on the best information available, including comparable asset values in the market and the use of valuation techniques. Any estimates of future cash flows are subject to risks and uncertainties and it is reasonably possible that changes in estimates could occur which may affect the expected recoverability of investments in mining properties. The carrying value of the Company's estimate of mineral resource has been estimated as at in excess of the net book value of the Company's assets at the balance sheet date using comparative market value of resources, taken from recent mine transactions conducted at arms length between willing parties. Based on these estimates management believe that no impairment to the carrying values exist at the balance sheet date. The Company has not recorded any impairment losses in any of the periods.

The fair value of a retirement or rehabilitation obligation is recognised as an asset and a liability in the period when it is incurred. The liability is discounted and an accretion expense is recognised using the credit-adjusted risk free rate in effect when the liability is incurred. The retirement asset is included in mining properties and charged to operations using the units of production method based upon estimated proven and probable reserves which can be recovered.

During 2006, the Company commissioned an environmental report by an independent party. This estimated an increase in estimated cash flow for the retirement and rehabilitation of the Kalana Gold Mine from \$1,000,000 to \$2,236,000. The increase in fair value of this liability was calculated at \$325,000. The environmental liability is based on the work required to be carried out on the tailings facilities to ensure stabilisation of the facility and re-vegetation of the tailings surface area, the capping of the underground shafts and the reclamation of plant, workshops and buildings where appropriate. The area disturbed by mining operations will then be re-vegetated. There will then be an ongoing monitoring of the water quality and re-vegetation programmes.

The Company has used a credit-adjusted risk-free rate of 8.5% to discount future cash flows in arriving at the fair value of its asset retirement and rehabilitation obligations. This is also the rate at which shareholders advanced funds to the Company in 2004. The Company still considers that 8.5% is an appropriate credit-adjusted risk-free rate.

Transactions expressed in foreign currencies are translated into U.S. dollars at the rate of exchange prevailing on the date of transaction. Monetary assets and liabilities expressed in foreign currencies are re-converted into U.S. dollars at the rates of exchange prevailing on the balance sheet date.

The financial statements of overseas subsidiaries are remeasured into their functional currency. Mining properties and other non-current assets are remeasured at historical rates. Monetary assets and liabilities are remeasured at current rates. Revenue and expense transactions are remeasured at the average rate for the period. Remeasurement gains and losses are included in income.

#### **Financial Instruments**

In 2008, the Company sold forward 10,000 ounces of gold at an average price of \$956 per ounce. The Company believes that these forward sales qualify as normal sales contracts under SFAS 133 and recorded the revenues when the gold sold forward was delivered. These forward sales agreements were entered into with Elliott. At December 31, 2008, the Company had 4,750ozs remaining to be delivered into the forward sales agreements.

The Company has no other financial instruments or long-term commitments outstanding.

#### **Disclosure of Outstanding Share Data**

As at March 30, 2009, the Company had issued 79,187,189 common shares.

The following table shows the number of options or rights to purchase common shares of the Company as at December 31, 2008.

Warrants issued through the IPO on June 30, 2005	6,518,713
Convertible Loan Notes	14,893,320
Minority shareholder warrants	1,411,042
CEO Compensation Options	2,500,000
Long Term Incentive Plan	2,874,000
<b>Total as at March 30, 2009</b>	<b>28,197,075</b>

#### **Outlook**

For 2009, Avnel is planning gold production of 25,000 ounces at an average operating cost of approximately \$557 per ounce of gold produced, net of royalties. Tonnes milled is planned to be 60,000 tonnes, 24% higher than 2008, at an average grade of 15.7g/t.

It is planned to advance development 1,107 metres during 2009. The main development will be 180m haulage north to access Vein 19.

It is forecast that the mineable reserves available from the current mine infrastructure is approximately 120,000 tonnes containing 51,000 ounces. This will provide approximately 24 months of operations to end 2010.

There remains approximately 1,740,000 tonnes containing over 600,000 ounces in underground mineral resources (measured and indicated). In addition the open pit mineral resources (measured, indicated and inferred) contain approximately 400,000 ounces in 3 million tonnes. Underground mining and underground diamond drilling have exposed additional mineralised zones that may contain gold to extract by open pit mining or underground bulk mining. The Company has commenced a study to evaluate the optimum method to exploit the mineral resources that will be available beyond 2010. The Kalana Main Project will initially create a comprehensive data base of all geological data available from exploration and mining over the last 30 years. This will be utilised to review the existing geological model and to prioritise a surface drill program.

Avnel believes the optimum method to exploit these mineral resources will require the development of an open pit with a new gold plant. The development of the underground mine between 180m and 300m level will be postponed until this study is completed. Avnel has revised the mineral reserves of the Kalana Gold Mine in line with the strategic decision to proceed with the Kalana Main Project Study which is more fully explained on pages 2 to 3 above.

## **Disclosure Controls and Procedures and Internal Control over Financial Reporting**

### **Disclosure controls and procedures**

The Company's disclosure controls and procedures are designed to provide reasonable assurance that material items requiring disclosure by the Company are identified and reported in a timely manner.

Based on current securities legislation in Canada, management, including the Chief Executive Officer of the Company ("CEO"), who also performs functions similar to the Chief Financial Officer of the Company, evaluated the design and effectiveness of the Company's disclosure controls and procedures as of December 31, 2008, and concluded that such disclosure controls and procedures were operating effectively at that date. There were no significant changes to the Company's disclosure controls process during the year ended December 31, 2008.

It should be noted that, while the Company's CEO believes that the Company's disclosure controls and procedures provide a reasonable level of assurance and that they are effective, it is not expected that the disclosure controls and procedures can prevent all errors or mistakes. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

### **Internal controls over financial reporting**

Management is responsible for designing, establishing and maintaining a system of internal controls over financial reporting to provide reasonable assurance that the financial information prepared by the Company for external purposes is reliable and has been recorded, processed and reported in an accurate and timely manner.

The board of directors of the Company (the "Board") is responsible for ensuring that management fulfills its responsibilities. The audit committee of the Company (the "Audit Committee") fulfills its role of ensuring the integrity of the reported information through its review of the interim and annual financial statements.

Due to the small size of the Company, there are certain aspects of the Company's internal control systems that are not ideal. This is not uncommon in a company the size of Avnel. Due to the limited number of staff at Avnel, it is not feasible or cost effective to achieve complete segregation of duties.

The control framework the Company used to design its internal controls over financial reporting is based on the principles set out in the *Risk Management and Governance: Guidance on Control* (COCO Framework), formerly known as *Guidance of the Criteria of Control Board*, published by The Canadian Institute of Chartered Accountants.

The Company made certain changes to its systems of internal controls over financial reporting in 2008, including changes in accounting personnel and reporting procedures. These changes are not reasonably likely to materially affect internal control over financial reporting.

The Company has paid particular attention to segregation of duties matters surrounding its internal controls over financial reporting as the Company has only limited staff resources at the present time such that "ideal" segregation of duties is not feasible. This risk is mitigated by management and Board review where appropriate.

The Company's management, including the CEO, who also performs functions similar to the Chief Financial Officer of the Company, have evaluated the design and operating effectiveness of internal controls over financial reporting as at December 31, 2008, and concluded that the Company's internal control over financing reporting was not effective during the fiscal year ended 2008. During this process, the CEO identified certain deficiencies in internal control over financial reporting resulting primarily from a significant turnover of key management and accounting personnel during the year, lack of accounting expertise at the Company's remote Malian operations, and lack of segregation of duties. None of these deficiencies were individually or cumulatively considered to be material weaknesses and the risks arising from these deficiencies are not considered to be significant.

During 2008 Avnel appointed the current Chairman of the Board of Directors as the CEO of the Company. This creates a potential conflict as there is an inherent lack of segregation of duties and absence of oversight between management and the Board. To alleviate any potential conflict between the Board and management, a Lead Director has been appointed who is also Chairman of the Audit Committee.

During the year a new Chief Operating Officer was appointed in March 2008 and was terminated in September 2008. A new General Manager of Mine Operations was appointed in May 2008 and resigned in December 2008 when Mr. Roy Meade, an executive director of the Company, took on the duties of Director Mining responsible inter-alia for mining in Mali. The Company appointed a new Chief Financial Officer in August 2008 who resigned due to ill health in January 2009. Mr. Alan McFarlane was appointed VP Finance with effect from February 1, 2009. The Company's Financial Controller of its Malian operations was on maternity leave for a substantial part of the year. High turnover in senior personnel, and the absence for extended periods of appropriate approval authorities and signing officers, created deficiencies which impacted internal control procedures. The Company is aware that turnover of key management and accounting personnel represents a significant risk to internal control over financial reporting and is endeavouring to put in place policies to retain key personnel.

The Company has taken such action as it considers appropriate to minimize any potential risks from these deficiencies, including increased Director and Audit Committee oversight when deemed appropriate. The Company continues to review and assess its internal controls over financial reporting and is seeking to put enhanced procedures and controls in place. At the present time, the Company does not anticipate hiring additional accounting or administrative staff and accordingly, will continue to rely on review procedures to detect potential misstatements in reporting of material to the public.

The Company believes that its internal controls over financial reporting need to be enhanced to provide reasonable, but not absolute, assurance that the objectives of the control system are met. The design of a control system must reflect that there are staffing and financial resource constraints, and that the benefits of controls must be considered relative to their costs to the Company.

The Company's management believe that any internal controls over financial reporting, including those systems determined to be effective and no matter how well conceived and operated, have inherent limitations and can provide only reasonable, not absolute, assurance that the objectives of the control system are met with respect to financial statement preparation and presentation. Because of the inherent limitations in all control systems, they cannot provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been prevented or detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by unauthorized override of the control. The design of any system of controls is also based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Accordingly, because of the inherent limitations in a cost effective control system, misstatements due to error or fraud may occur and not be detected.

There are inherent limitations in the effectiveness of internal controls over financial reporting, including the possibility that misstatements may not be prevented or detected. Accordingly, even effective internal controls over financial reporting can provide only reasonable assurance with respect to financial statement preparation. Furthermore, the effectiveness of internal controls can change with circumstances.

**Additional Information**

This MD&A has been prepared as of March 30, 2009. Additional information about the Company, including the Company's Annual Information Form, is available at [www.avnelgold.com](http://www.avnelgold.com) or the website of the System for Electronic Document Analysis and Retrieval at [www.sedar.com](http://www.sedar.com).