

## **Management's analysis of financial condition and results of operations**

### **Nature of operations**

Azimut Exploration Inc. is a mineral exploration company developing leading-edge geoscience data processing methods to better select prospective zones with the objective to discover major ore deposits. The Company has acquired 5 exploration properties following regional-scale assessments in the James Bay region (for gold) and in the Labrador Trough (for nickel-copper-platinum)., The Company was reactivated in June 2003, following the appointment of a new president.

### **Results of operations**

The Company incurred a net loss of \$256,096 for the period ended May 31, 2004, compared to a net loss of \$609,485 for the period ended May 31, 2003. In November 2002, the Company abandoned its option to acquire a 50% interest in the Flavrian property, which resulted in a loss of \$563,696. Expenses in salaries and fringe benefits are related to the appointment of the new president. Expenses related to the search for properties mainly consist in an assessment of the mineral potential in Québec. \$75,000 in compensation has been included in professional fees in order to take into account a grant of 300,000 stock options in February 2004. Office and representation fees increased following Society reactivation.

### **Liquidity and sources of financing**

The Company's working capital was \$101 481 at May 31, 2004, compared to \$58 232 at the beginning of the fiscal year. In November 2003, Azimut concluded two private financings for a total of \$450 000, of which \$250 000 was allocated for exploration programs. A value of \$161 800 has been allocated to warrants and presented separately in the shareholders' equity of the balance sheets.

### **Risks and uncertainties**

The Company is considered to be at the exploration stage, thus it is dependent on obtaining regular financing in order to continue exploration. Despite previous success in acquiring financing, there is no guarantee of obtaining any future financing.

### **Outlook**

Last Winter, the Company finalized the acquisition of five properties namely Retty, Eastmain, Lac Gillet, Opinaca and De Romer including 526 claims. The Company is presently in discussion with potential partners in order to option these properties and to share the risk of exploration. A prospecting campaign was initiated on these new properties. The Company continues to pursue the modeling of mineral potential in various regions of Québec in order to generate new projects of quality.

### **Management's Responsibility for Financial Information**

Azimut's financial statements are the responsibility of the Company's management, and have been approved by the board of directors. The financial statements were prepared by the Company's management in accordance with generally accepted Canadian accounting principles. The financial statements include certain amounts based on the use of estimates and assumptions. Management has established these amounts in a reasonable manner, in order to ensure that the financial statements are presented fairly in all material respects.

(s) Jean-Marc Lulin  
President

(s) Gaétan Mercier  
Controller

Quebec City, Québec, Canada  
July 21, 2004

**AZIMUT EXPLORATION INC.**

(An exploration company)

**Balance Sheets**

	<b>May 31, 2004</b>	<b>August 31, 2003</b>
	\$	\$
	(unaudited)	(audited)
<b>ASSETS</b>		
<b>Current Assets</b>		
Cash	92,508	45,782
Amounts receivable	40,689	29,666
Prepaid expenses	5,957	13,865
	<u>139,154</u>	<u>89,313</u>
<b>Exploration funds</b>	213,329	23,534
<b>Long-term investments</b> (quoted value 18 000 \$; 24 000 \$)	18,000	24,000
<b>Mining properties</b>	53,445	---
<b>Property, plant and equipment</b>	1,051	716
	<u>424,979</u>	<u>137,563</u>
<b>LIABILITIES</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities		
Related companies	---	402
Others	37,673	30,679
	<u>37,673</u>	<u>31,081</u>
<b>SHAREHOLDERS' EQUITY</b>		
<b>Convertible debentures</b>	488,200	350,000
<b>Share capital</b>	4,071,453	3,887,960
<b>Stock options</b>	102,045	24,695
<b>Warrants</b>	161,800	---
<b>Deficit</b>	(4,436,192)	(4,156,173)
	<u>387,306</u>	<u>106,482</u>
	<u>424,979</u>	<u>137,563</u>

**AZIMUT EXPLORATION INC.**

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**Deficit**

For the periods ended May 31, 2004 and 2003 (unaudited)

	<b>2004</b>	<b>2003</b>
	\$	\$
<b>Balance - Beginning of period</b>	4,156,173	3,422,971
Interest on convertible debentures	23,923	36,458
Net loss for the period	<u>256,096</u>	<u>609,485</u>
<b>Balance - End of period</b>	<u><u>4,436,192</u></u>	<u><u>4,068,914</u></u>

**Statements of deferred exploration expenses**

For the periods of three (3) and nine (9) months ended May 31, 2004 and 2003 (unaudited)

	<b>2004</b>	<b>2003</b>	<b>2004</b>	<b>2003</b>
	<b>3 months</b>	<b>3 months</b>	<b>9 months</b>	<b>9 months</b>
	\$	\$	\$	\$
<b>Balance - Beginning of period</b>	<u>43,318</u>	<u>0</u>	<u>0</u>	<u>572,038</u>
Expenses incurred during the period				
Claims and permits	9,595	---	52,582	8,147
Geology	1,081	---	1,691	---
	<u>10,676</u>	<u>0</u>	<u>54,273</u>	<u>8,147</u>
Abandoned mining properties	---	---	---	(570,377)
Tax credits and mining rights	(549)	---	(828)	(9,808)
	<u>(549)</u>	<u>0</u>	<u>(828)</u>	<u>(580,185)</u>
<b>Balance - End of period</b>	<u><u>53,445</u></u>	<u><u>0</u></u>	<u><u>53,445</u></u>	<u><u>0</u></u>

**AZIMUT EXPLORATION INC.**

(An exploration company)

**Statements of Earnings**

For the periods of three (3) and nine (9) months ended May 31, 2004 and 2003 (unaudited)

	<b>2004</b>	<b>2003</b>	<b>2004</b>	<b>2003</b>
	<b>3 months</b>	<b>3 months</b>	<b>9 months</b>	<b>9 months</b>
	\$	\$	\$	\$
<b>Revenue</b>				
Interests' income	1,506	306	4,635	868
Gain on sale of mining properties	---	---	---	16,000
Gain on sale of property, plant and equipment	---	---	---	568
	<u>1,506</u>	<u>306</u>	<u>4,635</u>	<u>17,436</u>
<b>Expenses</b>				
Salaries and fringe benefits	20,630	---	55,336	---
Professional and maintenance fees	8,841	4,615	104,485	16,933
Management fees and office expenses	26,707	9,250	58,415	29,719
Travelling and entertainment	3,740	781	8,609	1,011
Interests and bank charges	73	58	182	146
Amortization of property, plant and equipment	92	41	164	166
Loss (gain) on abandonment of a mining property	---	---	---	563,696
Write-off of long-term investments	6,000	---	6,000	10,000
Search for properties	14,936	5,250	62,761	5,250
Tax credits and mining rights	(7,588)	---	(35,221)	---
	<u>73,431</u>	<u>19,995</u>	<u>260,731</u>	<u>626,921</u>
<b>Net loss for the period</b>	<u>(71,925)</u>	<u>(19,689)</u>	<u>(256,096)</u>	<u>(609,485)</u>
<b>Basic and diluted net loss per share</b>	<u>(0.060)</u>	<u>(0.002)</u>	<u>(0.024)</u>	<u>(0.070)</u>
<b>Basic and diluted weighted average number of shares outstanding</b>	<u>11,022,807</u>	<u>8,711,140</u>	<u>10,701,927</u>	<u>8,672,455</u>

**AZIMUT EXPLORATION INC.**

(An exploration company)

**Statements of Cash Flows**

For the periods of three (3) and nine (9) months ended May 31, 2004 and 2003 (unaudited)

	<b>2004</b>	<b>2003</b>	<b>2004</b>	<b>2003</b>
	<b>3 months</b>	<b>3 months</b>	<b>9 months</b>	<b>9 months</b>
	\$	\$	\$	\$
<b>Cash flows from operating activities</b>				
Net loss for the period	(71,925)	(19,689)	(256,096)	(609,485)
Items not affecting cash				
Amortization of property, plant and equipment	92	41	164	166
Cost of compensation in stock options	---	---	77,350	---
Loss on abandonment of a mining property	---	---	---	563,696
Write-off of long-term investments	6,000	---	6,000	10,000
Gain on sale of mining properties	---	---	---	(16,000)
Gain on sale of property, plant and equipment	---	---	---	(568)
	<u>(65,833)</u>	<u>(19,648)</u>	<u>(172,582)</u>	<u>(52,191)</u>
Change in non-cash working capital items				
Amounts receivable	20,725	(833)	(1,597)	14,605
Prepaid expenses	12,120	1,703	7,908	(2,832)
Accounts payable and accrued liabilities	(3,979)	797	(2,528)	4,961
	<u>28,866</u>	<u>1,667</u>	<u>3,783</u>	<u>16,734</u>
	<u>(36,967)</u>	<u>(17,981)</u>	<u>(168,799)</u>	<u>(35,457)</u>
<b>Cash flows from financing activities</b>				
Variation in exploration funds	15,986	---	(189,795)	---
Convertible debenture contracted	---	---	138,200	---
Variation in share capital	(1,329)	(6,517)	159,570	(6,517)
Increase in warrants	---	---	161,800	---
	<u>14,657</u>	<u>(6,517)</u>	<u>269,775</u>	<u>(6,517)</u>
<b>Cash flows from investing activities</b>				
Variation of mining properties	(10,433)	---	(53,751)	8,342
(Acquisition) Sale on property, plant and equipment	(499)	---	(499)	1,274
	<u>(10,932)</u>	<u>0</u>	<u>(54,250)</u>	<u>9,616</u>
<b>Net change in cash</b>	<b>(33,242)</b>	<b>(24,498)</b>	<b>46,726</b>	<b>(32,358)</b>
<b>Cash - Beginning of period</b>	<b>125,750</b>	<b>65,257</b>	<b>45,782</b>	<b>73,117</b>
<b>Cash - End of period</b>	<b><u>92,508</u></b>	<b><u>40,759</u></b>	<b><u>92,508</u></b>	<b><u>40,759</u></b>
<b>Additional information</b>				
Items not affecting cash and cash equivalents related to financing and investing activities				
Interests cashed	1,299	306	4,261	868
Shares issued and to be issued in consideration of the payment of interest on convertible debentures	9,578	12,159	23,923	36,458
Shares received in consideration of sale of a mining property	---	---	---	16,000
Tax credit and mining rights receivable related to exploration costs applied against mining properties	9,426	---	9,426	---
Purchase of mining properties included in accounts payable and accrued liabilities	9,120	---	9,120	---

**AZIMUT EXPLORATION INC.**

(An exploration company)

**Notes to Interim Financial Statements (unaudited)**

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**1 Summary of significant accounting policies**

**Interim financial information**

The financial information as at May 31, 2004 and for the periods ended May 31, 2004 and 2003 is unaudited; however, in the opinion of management, all adjustments necessary to present fairly the results of these periods have been included. The adjustments made were of a normal recurring nature. Interim results may not necessarily be indicative of results anticipated for the year.

These interim financial statements are prepared in accordance with generally accepted accounting principles in Canada and use the same accounting policies and methods used in the preparation of the Company's most recent annual financial statements. All disclosures required for annual financial statements have not been included in these financial statements. These interim financial statements should be read in conjunction with the Company's most recent annual financial statements.

**Stock option plan and new accounting policy**

On December 15, 2003, the company adopted the new recommendations of the Canadian Institute of Chartered Accountants relating to accounting for stock-based compensation and other stock-based payments. It has elected to apply the fair value method prospectively. This method is applied to the awards granted, modified or settled from the start of the fiscal year in which the Company adopted this method for these awards. Compensation expenses is recorded for the excess, if any, of the fair value of the shares of the date of grant over the exercise price of the options. The Company provides pro-forma earnings and earnings per share information for these awards of stock-based compensation to employees who are not accounted for at fair value during one or many periods for which a statement of results is presented.

**AZIMUT EXPLORATION INC.**

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**Notes to Interim Financial Statements (unaudited)****2 Mining properties**

	<b>Undivided participation %</b>	<b>Balance as at Sept. 1, 2003 \$</b>	<b>Costs incurred \$</b>	<b>Tax credits and abandoned mining properties \$</b>	<b>Balance as at May 31, 2004 \$</b>
Retty (130 claims)	100				
Mining property		---	12,220	---	12,220
Exploration costs		---	581	(288)	293
		---	12,801	(288)	12,513
Eastmain (218 claims)	100				
Mining property		---	22,890	---	22,890
Exploration costs		---	230	(112)	118
		---	23,120	(112)	23,008
Lac Gillet (87 claims)	100				
Mining property		---	8,178	---	8,178
Exploration costs		---	356	(173)	183
		---	8,534	(173)	8,361
Opinaca (65 claims)	100				
Mining property		---	6,825	---	6,825
Exploration costs		---	230	(112)	118
		---	7,055	(112)	6,943
De Romer (26 claims)	100				
Mining property		---	2,469	---	2,469
Exploration costs		---	294	(143)	151
		---	2,763	(143)	2,620
		---	54,273	(828)	53,445

**AZIMUT EXPLORATION INC.**

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**Notes to Interim Financial Statements (unaudited)**

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**3 Convertible debentures**

	2003	2002
	\$	\$
Debentures convertible at the company's option into common shares		
At a conversion price of \$0.40 per share, 14%, interest payable by half-yearly instalments through common shares of the company, at the base rate on the date of payment, non-interest bearing if the share is traded at \$0.80 and over during the twenty business days preceding the dates of interest instalments, maturing in May 2003.	0	250,000
At a conversion price of \$0.15 per share, 14%, interest payable by half-yearly instalments through common shares of the company at the base rate on the date of payment, non-interest bearing if the share is traded at \$0.36 and over during the twenty business days preceding the dates of interest instalments, maturing in March 2005.	100,000	100,000
At a conversion price of \$0.425 per share, 12%, interest payable by half-yearly instalments through common shares of the company at the base rate on the date of payment, non-interest bearing if the share is traded at \$0.15 and over for the first/second six-month period, and \$0.20 and over for the subsequent six-month period during the twenty business days preceding the dates of interest instalments, maturing in March 2006.	250,000	0
At a conversion price varying from \$0.33 to \$0.44 per share, 12%, interest payable by half-yearly instalments through common shares of the company at the base rate on the date of payment, non-interest bearing if the share is traded at more than \$0.37 for the first/second six-month period, at more than \$0.45 for the third/forth six-month period, at more than \$0.55 for the fifth/sixth six-month period, at more than \$0.65 for the seventh/eighth six-month period and at more than \$0.75 for the ninth/tenth six-month period during the twenty business days preceding the dates of interest instalments, maturing in November 2008.	138,200	0
	<u>488,200</u>	<u>350,000</u>

**4 Share Capital**

## Authorized

Unlimited number of commons shares, without par value, voting and participating  
11 032 256\* shares issued and fully paid

\*482 685 shares are subject to escrow and cannot be released without the consent of regulatory authorities.

**AZIMUT EXPLORATION INC.**

(An exploration company)

**Notes to Interim Financial Statements (unaudited)**

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**5 Variation of warrants**

	Number	Weighted average exercise price \$
Outstanding - beginning of period	0	0.00
Granted	1,492,858	0.42
Exercised	0	0.00
Matured or cancelled	0	0.00
Outstanding and exercisable - end of period	1,492,858	0.42

The following table summarizes the expiry date of outstanding warrants :

600 000 warrants at \$0,45 expire in May 2005

892 858 warrants at \$0,40 expire in May 2005

Warrants are recorded at their fair value, which was determined using the Black-Scholes model.

**6 Stock Option Plan**

The Company established a stock option plan as described in note 9 of the audited annual financial statements. On December 15, 2003, the Company chose to replace its present method of accounting by the fair value method and to apply it in a prospective way. The following tables present the stock option activity since September 1, 2003 and summarize information about fixed stock options outstanding and exercisable as at May 31:

	<u>9 months</u>	
	Number	Weighted average exercise price \$
Outstanding - Beginning of period	795,000	0.18
Exercised	(155,000)	0.16
Granted	310,000	0.30
Outstanding - End of period	<u>950,000</u>	<u>0.22</u>
Exercisable - End of period	<u>430,000</u>	<u>0.19</u>

**AZIMUT EXPLORATION INC.**

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**Notes to Interim Financial Statements (unaudited)**

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exercise prices	Options outstanding		Options currently exercisable
	Number	Weighted average remaining contractual life (years)	Number
\$0.16	380,000	2.23	170,000
\$0.18	140,000	5.64	140,000
\$0.24	120,000	4.05	120,000
\$0.30	310,000	4.72	0
	<u>950,000</u>	<u>3.57</u>	<u>430,000</u>

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

**Period ended May 31, 2004**

Risk-free interest rate	3.27%
Expected volatility	120%
Dividend yield	zero
Weighted average expected life	60 months
Weighted average fair value of options granted	0.249 \$

**AZIMUT EXPLORATION INC.**

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**Notes to Interim Financial Statements (unaudited)**

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The Company recognizes, as a compensation cost arising from awards to key employees, officers and directors the excess, if any, of the fair value of the shares at the date of grant over the exercise price of the options. \$75 000 compensation cost has been accounted for in the financial statements for the period ended May 31, 2004. The fair value of stock options granted to key employees, officers and directors during the previous year amounts to \$9 720. If the fair value based method had been used to account for stock-based compensation costs related to stock options granted to key employees, officers and director, the loss and related loss per share for the previous year would be as follows:

**Period ended May 31, 2003**

	\$
Pro-forma loss for the period	619,205
Pro-forma basic and diluted loss per share	0,071

The pro-forma loss considers the impact of awards granted to key employees, directors and administrators on June 19, 2003.

The compensation cost arising from stock options granted to suppliers amounts to \$2 350 for the period ended May 31, 2004. The compensation cost has been included in general exploration cost and the related credit has been recognized in the stock options recorded under Shareholders' Equity.

## **AZIMUT EXPLORATION INC.**

(An exploration company)

### **Notes to Interim Financial Statements (unaudited)**

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#### **7 Subsequent events**

- a) On July 7, 2004, the company signed a strategic agreement with Kennecott Exploration Company to develop an exploration strategy for gold and base metals over a vast region in Quebec. Agreement includes three phases :

Phase I : Azimut will deliver to Kennecott a mineral potential assessment study for a territory covering almost 500,000 km<sup>2</sup> with the objective of identifying major exploration targets. Kennecott will fund this phase by paying \$40,000 CAD to Azimut as follows : \$20,000 upon signing the Letter Agreement and \$20,000 upon delivery of the Target Report. Work commences immediately and will be completed in four months.

Phase II : For targets that require further appraisal, Kennecott will invest \$5,000 to \$30,000 per target during a subsequent one-year assessment period to establish a portfolio of Identified Targets. Azimut will be the Operator.

Phase III : For each Identified Target, Kennecott will have an exclusive right to enter into a Joint Venture with Azimut under the following conditions :

- Kennecott will earn a 60 % interest per selected property by investing \$1,000,000 of exploration work over a four year period or less according to the following exploration expenditures : \$150,000 during the first year and a minimum of \$250,000 per year thereafter. Kennecott will be the Operator.
- Kennecott will pay a \$50,000 bonus to Azimut for each selected property that reaches the drilling stage.
- Upon forming the Joint Venture, Kennecott will have the option to acquire an additional 20 % interest, for a total interest of 80 %, by delivering a Feasibility Study within a five-year period with a minimal investment of \$100,000 per year.

- b) On July 21, 2004, the Fonds régional de solidarité FTQ, Nord du Québec, subscribed to 500,000 common shares of the Company at a price of \$0,30 per share and to 250,000 purchase warrants. Each whole purchase warrant entitles the holder to purchase one (1) common share of the Company at a price of \$0,40 per share at any time. the purchase warrant is valid for 18 months form the closing date.

**Board of Directors**

Jacques Bonneau, Eng., M.Sc., Chairman of the Board (Quebec City)

Jean-Marc Lulin, Ph.D., geologist, Director (Montreal)

Jean-Charles Potvin, B.Sc., M.B.A., Director (Toronto)

Louis P. Salley, B.A., LL.B., Director (Vancouver)

**Management**

Jean-Marc Lulin, President and Chief Executive Officer

Gaétan Mercier, Controller and Secretary

**Management Advisors**

Jacquelin Gauthier, Eng.

Jack Stoch, B.Sc., geologist

**Legal Counsel**

Pothier Valiquette (Montreal)

**Auditors**

PricewaterhouseCoopers LLP (Quebec)

**Transfer Agent**

Trust CIBC Mellon Company (Montreal)

**Listing**

TSX Venture

Symbol: AZM

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