Lucara Diamond Corp.

MD&A and Consolidated Financial Statements

Year Ending: December 31, 2014

LUCARA DIAMOND CORP.
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2014

Management's discussion and analysis ("MD&A") focuses on significant factors that have affected Lucara Diamond Corp. (the "Company") and its subsidiaries performance and such factors that may affect its future performance. In order to better understand the MD&A, it should be read in conjunction with the audited consolidated financial statements of the Company for the year ended December 31, 2014, which are prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). All amounts are expressed in U.S. dollars unless otherwise indicated. The effective date of this MD&A is February 19, 2015.

Some of the statements in this MD&A are forward-looking statements that are subject to risk factors set out in the cautionary note contained herein.

Additional information about the Company and its business activities is available on SEDAR at www.sedar.com.

HIGHLIGHTS

Revenues: During the year the Company had sales totalling 412,136 carats for gross proceeds of $265.5 million at an average price of $644 per carat. The increase in revenues of 47% or $85.0 million compared to the prior year was due to higher prices received for the Karowe diamonds and a larger number of carats being sold in the large exceptional stones tenders, which contributed $135.6 million to revenues. The exceptional stone sales resulted in an average price of $32,471 per carat in 2014 (2013: $24,290 per carat, with the remaining tenders achieving $318 per carat (2013: $249 per carat).

Cash flows and operating margins: The Company's earnings before interest, tax, depreciation and amortization ('EBITDA') (see pages 5 and 9 Non-IRFS measures) for the year were $173.4 million compared to the previous year of $102.9 million. The strong operating margins were largely due to the exceptional stone sales and the Company's focus on cost control, which resulted in a cost per tonne treated (see pages 5 and 9 Non-IRFS measures) of $28 compared to guidance of $31-$33 per tonne.

Net cash position: The Company's year-end cash balance was $100.8 million compared to a cash balance of $49.4 million at the end of 2013. The increase in the Company's cash balance was due to its strong operating cash flows, which more than financed the Company's plant optimization expenditure of $35 million and its dividend payment to shareholders of $27 million during the year. The Company's $50 million credit facility remains undrawn.

Karowe operating performance: Karowe's performance was in line with forecast for the year in terms of ore and waste mined and carats recovered. Karowe recovered 815 special stones (+10.8 carats; 2013 recovery of 732 specials) during the year. This included 27 stones greater than 100 carats (2013: 17 stones) and 4 stones over 200 carats (2013: 4 stones). The plant optimization program is advancing to plan and the plant is expected be commissioned during Q2 2015 within the $55 million forecast cost.

Adjusted Earnings per share and Return on Capital Employed: Adjusted earnings per share (see pages 5 and 9 Non-IRFS measures) was $0.24 per share for the year ended December 31, 2014 (2013: adjusted earnings per share was $0.17) and $0.05 per share for the quarter ended December 31, 2014 (2013: adjusted earnings per share was $0.05).

The Company's strong earnings have resulted in the Company achieving a return on capital employed ('ROCE') (see pages 5 and 9 Non-IRFS measures) of 63% during the year. ROCE increased from 37% in 2013 following the increase in sales from the exceptional stone tender and the Company's operating and capital cost discipline.

Dividends: In 2014, the Company paid a special dividend of CA$ 0.04 per share in addition to its regular dividend of CA$ 0.04 per share. The total dividend paid in 2014 by the Company of US$27 million was equivalent to a dividend yield of 3.7% based on the TSX closing price on December 31, 2014 and a dividend cover of 3.4x using adjusted net income (see page 5 for calculation of adjusted net income).

Mothae divestment: On December 22, 2014, the Company announced it would divest of the Mothae project based on the Company's development strategy and the extensive work conducted on understanding the economics of the asset. The Company does not believe that sufficient shareholder value can be gained through expenditure of current cash reserves on further assessment and development of this project.

Botswana Prospecting Licenses: The Company was awarded two precious stone prospecting licenses within the Orapa Kimberlite field in close proximity to the Karowe Diamond mine during the year. The Company has ordered a bulk sampling plant and will commence work programs on the two prospecting licenses during 2015.

FINANCIAL HIGHLIGHTS

	Three months ended December 31		Year ended December 31	
In millions of U.S. dollars unless otherwise noted	**2014**	2013	**2014**	2013
Revenues [1]	$ 70.5	$ 58.7	$ 265.5	$ 180.5
Average price per carat sold ($/carat)	675	433	644	411
Operating expenses per carat sold ($/carat)	89	109	115	100
Operating margin per carat sold ($/carat)	586	324	529	311
Net income (loss) for the period[2]	(16.8)	21.3	45.7	65.2

(1) Revenue is presented based on cash receipts received during the period and excludes tender proceeds received after each quarter end. See results of operations (page 3) for reconciliation of revenue and total proceeds for tenders received for each quarter.
(2) Net loss in Q4 2014 was mainly generated by the Mothae impairment and restoration charge: $21.2 million in the period.

	Year ended December 31	
In millions of U.S. dollars unless otherwise noted	**2014**	2013
Adjusted net income for the period (see pages 5 and 9 Non-IRFS measures)	90.8	65.2
Earnings per share (basic and diluted)	0.13	0.17
Adjusted earnings per share (see pages 5 and 9 Non-IRFS measures)	0.24	0.17
Cash on hand	100.8	49.4

2015 OUTLOOK

This section of the MD&A provides management's production and cost estimates for 2015. These are "forward-looking statements" and subject to the cautionary note regarding the risks associated with forward-looking statements.

Karowe Mine, Botswana

Karowe is forecast to process 2.3-2.5 million tonnes of ore and to sell 400,000 to 420,000 carats of diamond in 2015. Revenue is forecast between $230 and $240 million.

Ore mined is forecast between 2.5-2.8 million tonnes and waste mined is expected to be between 12.0-12.5 million tonnes.

Karowe's operating cash costs (see page 9 Non-IRFS measures) are expected to be between $33 and $36 per tonne ore treated.

Capital expenditures include the completion of the Karowe's plant optimization project during the second quarter of 2015 for a total cost of $55 million and sustaining capital expenditure is forecast between $7.5-$8.5 million in 2015. This includes a mill relining machine for a full cost of $5 million of which $3 million will be spent in 2014.

The Company has also forecast exploration expenditures of $7.0-$8.0 million for work on its two Botswana prospecting licenses, of which $2.0 million of a forecast total cost of $4.5 million on a bulk sample plant has been spent in 2014.

BUSINESS OVERVIEW

The Company is a diamond mining company focused in Africa. The business of the Company consists of the acquisition, exploration, development and operation of diamond properties. The Company's head office is in Vancouver, BC, Canada and its common shares trade on the Toronto Stock Exchange, the NASDAQ OMX in Sweden and the Botswana Stock Exchange under the symbol "LUC".

The principal assets of the Company and the focus of the Company's operations, development and exploration activities reside in Botswana.

The following summarizes the Company's current land holdings:

Country	Name	Interest Held	Area (km^2)
Botswana	Karowe Diamond License	100%	15.3
Botswana	Prospecting License No. 371/2014	100%	55.4
Botswana	Prospecting License No. 367/2014	100%	1.1
Lesotho	Mothae Diamond Mining Lease	75%	20.0

RESULTS OF OPERATIONS

Karowe Mine, Botswana

	UNIT	Year ended Dec-14	Q4-14	Q3-14	Q2-14	Q1-14	Q4-13
Sales							
Revenues	US$m	265.5	70.5	91.3	71.0	32.7	58.7
Proceeds generated from sales tenders conducted in the quarter are comprised of:	US$m	265.5	70.5	66.5	95.0	33.5	47.8
Sales proceeds received during the quarter	US$m	265.5	70.5	91.3	71.0	32.7	58.7
Q2 2014 tender proceeds received post Q2 2014	US$m	-	-	(24.8)	24.8	-	-
Q1 2014 tender proceeds received post Q1 2014	US$m	-	-	-	(0.8)	0.8	-
Q3 2013 tender proceeds received post Q3 2013	US$m	-	-	-	-	-	(10.9)
Carats sold for proceeds generated during the period	Carats	412,136	104,405	88,364	111,900	107,467	110,635
Carats sold for revenues recognized during the period	Carats	412,136	104,405	115,362	84,915	107,454	127,804
Average price per carat for proceeds generated during the period	US$	644	675	753	849	312	433
Production							
Tonnes mined (ore)	Tonnes	3,327,754	757,672	1,003,312	677,882	888,888	918,765
Tonnes mined (waste)	Tonnes	10,270,720	2,477,687	2,624,067	3,166,644	2,002,322	1,694,134
Tonnes treated	Tonnes	2,421,506	566,681	509,283	664,812	680,730	613,064
Average grade processed	cpht (*)	17.8	20.1	20.8	14.9	16.3	18.9
Carats recovered	Carats	430,292	113,950	106,162	99,142	111,037	116,061
Costs							
Operating costs per carats sold (see page 9 Non-IRFS measures)	US$	115	89	122	132	118	109
Capital expenditures (including capitalized waste)	US$m	50.5	24.8	14.1	9.7	1.9	1.5

(*) carats per hundred tonnes

The second full year of operations at Karowe was a success with all operational and cost targets either being met or exceeded. Safety and Health Lost time injury frequency rates ('LTIFR') for 2014 was 0.99 (measured per 1,000,000 hours), and 500,000 LTI free hours had been worked on the plant optimization project. At year end, Karowe reported 1,064,481 LTI free hours. No reportable environmental incidents occurred during the year.

Mining and process production at Karowe were in line with forecast for 2014. Tonnes of ore mined were in line with forecast, and at a slightly higher grade. Waste stripping was also in line with the mine plan achieving three months of exposed ore for plant feed at year-end. The process plant has dealt with processing the increasingly harder ore encountered at depth and the plant upgrade project has progressed well and delivered two new circuits and the large diamond recovery within 2014 as per schedule.

REVIEW OF PROJECTS

Mothae Diamond Project, Lesotho

The Mothae project is located in northeast Lesotho. On December 22, 2014, the Company announced it would divest of the Mothae project. The Company does not believe that sufficient shareholder value can be gained through expenditure of current cash reserves on further assessment and development of this project.

The Company's decision to cease development resulted in an impairment charge of $18.8 million in 2014, which is included in other expenses and reflects a write-down of Mothae project's carrying value of $18.8 million. The Company also incurred a $2.4 million restoration charge to increase its Mothae closure cost provision to $2.9 million as the Company expects the restoration to be incurred much sooner than initially anticipated.

Karowe, Plant Optimization Project

The plant upgrade project to modify the process plant to treat harder, more dense ore at depth is well advanced. The Company has spent approximately $35 million of the forecasted $55 million as at December 31, 2014. A bleed screen circuit and secondary gyratory crusher have been commissioned along with the Company's large diamond recovery circuit, which has been installed and in operation since September 2014.

SELECT FINANCIAL INFORMATION

In millions of U.S. dollars unless otherwise noted		Year ended December 31, **2014**		2013		2012
Revenues	$	265.5	$	180.5	$	41.8
Operating expenses		(47.2)		(43.8)		(14.0)
Royalty expenses		(26.6)		(18.1)		(4.2)
Operating earnings [1]		**191.7**		**118.6**		**23.6**
Exploration expenditures		(1.2)		(1.3)		(12.8)
Administration		(12.8)		(11.4)		(9.5)
Gain on sale of exploration program diamonds		-		0.5		-
Sales and marketing		(4.3)		(3.5)		(1.5)
EBITDA [2]		**173.4**		**102.9**		**(0.2)**
Depletion, amortization and accretion		(14.6)		(15.0)		(5.9)
Finance income (expenses)		0.8		(3.8)		(3.1)
Foreign exchange gain (loss)		(19.4)		(3.9)		1.7
Impairment charge - Mothae		(18.8)		-		-
Restoration charge - Mothae		(2.4)		-		-
Current income tax expense		(41.6)		-		-
Deferred income tax expense		(31.7)		(15.0)		-
Net income for the year		**45.7**		**65.2**		**(7.5)**
Add back: Foreign exchange loss related to intercompany loan repayment [3]		23.9		-		-
Add back: Impairment and restoration charges for Mothae[4]		21.2		-		-
Adjusted net income for the year [5]		90.8		65.2		(7.5)
Change in cash during the year		**51.5**		**36.1**		**(35.3)**
Cash on hand		**100.8**		**49.4**		**13.3**
Earnings per share (basic and diluted)		**0.13**		**0.17**		**(0.02)**
Adjusted earnings per share (basic and diluted) [6]		**0.24**		**0.17**		**(0.02)**
Per carats sold						
Sales price	**$**	**644**	**$**	**411**	**$**	**274**
Operating expenses		**115**		**100**		**94**
Average grade (carats per hundred tonnes)		**17.7**		**18.7**		**25.4**

(1) Operating earnings is a non-IFRS measure defined as sales less operating expenses and royalty expenses.
(2) EBITDA is a non-IFRS measure defined as earnings before interest, taxation, depreciation and amortization.
(3) Foreign exchange loss related to an intercompany loan repayment between Corporate and Karowe (see foreign exchange loss on page 7)
(4) Impairment and restoration charges for the Mothae project (see Impairment and restoration charges on page 7)
(5) Adjusted net income for the year is a non-IFRS measure defined as earnings before non-cash foreign exchange loss related to an intercompany loan repayment and impairment and restoration charges for the Mothae project.
(6) Adjusted earnings per share for the year is a non-IFRS measure defined as adjusted net income[5] divided by the weighted average number of shares outstanding during the year on both a basic and fully diluted basis.

In millions of U.S. dollars unless otherwise noted	Three months ended December 31, **2014**	2013
Net income (loss) for the quarter	**(16.8)**	**21.3**
Add back: Foreign exchange loss related to intercompany loan repayment [1]	13.6	-
Add back: Impairment and restoration charges for Mothae[2]	21.2	-
Adjusted net income for the quarter [3]	18.0	21.3
Earnings (loss) per share (basic and diluted)	**(0.03)**	**0.05**
Adjusted earnings per share (basic and diluted) [4]	**0.05**	**0.05**

(1) Foreign exchange loss related to an intercompany loan repayment between Corporate and Karowe (see foreign exchange loss on page 7)
(2) Impairment and restoration charges for the Mothae project (see Impairment and restoration charges on page 7)
(3) Adjusted net income for the year is a non-IFRS measure defined as earnings before non-cash foreign exchange loss related to an intercompany loan repayment and impairment and restoration charges for the Mothae project.
(4) Adjusted earnings per share for the quarter is a non-IFRS measure defined as adjusted net income[3] divided by the weighted average number of shares outstanding during the quarter on both a basic and fully diluted basis.

SELECT FINANCIAL INFORMATION (CONTINUED)

Cash operating cost per tonne ore treated reconciliation:

In millions of U.S. dollars with the exception of tonnes treated and cash operating cost per tonne treated		**Year ended December 31, 2014**		2013
Operating expenses	$	47.2	$	43.8
Capitalized production stripping costs[1]		6.2		-
Investment activities: other[2]		2.1		-
Net change in working capital items: inventories[3]		11.8		7.0
Total cash operating costs for ore treated		67.3		50.8
Tonnes treated		2,421,506		2,354,538
Cash operating cost per tonne ore treated[4]		**27.79**		**21.58**

(1) Capitalized production stripping cost in investing activities in the audited consolidated statements of cash flows.
(2) Investment activities: other in the audited consolidated statements of cash flows relates to mobilization costs for MCC, the Company's mining contractor which was paid in Q4 2014 and will be amortized in future periods.
(3) Net change in working capital items: Inventories in operating activities in the audited consolidated statements of cash flows.
(4) Cash operating cost per tonne treated for the period is a non-IFRS measure defined as the sum of operating expenses, capitalized production stripping costs, and net change in working capital items: Inventories divided by the tonnes ore treated for the period.

Return on capital employed (ROCE) reconciliation:

In millions of U.S. dollars with the exception of ROCE			**Year ended December 31, 2014**		2013
Adjustments to net earnings before tax					
Net income before tax		$	119.0	$	80.2
Add back: Finance (income) expenses			(0.8)		3.8
Add back: Foreign exchange loss related to intercompany loan repayment [1]			23.9		-
Add back: Impairment and restoration charges for Mothae[2]			21.2		-
	A		163.3		84.0
Capital employed – beginning of year					
Total assets			247.2		235.4
Less: current liabilities[3]			(15.5)		(14.7)
			231.7		220.7
Capital employed – end of year					
Total assets			317.3		247.2
Less: current liabilities			(28.9)		(15.5)
			288.4		231.7
Average capital employed	B		260.0		226.2
ROCE[4] (%)	A/B		63		37

(1) Foreign exchange loss related to an intercompany loan repayment between Corporate and Karowe (see foreign exchange loss on page 7)
(2) Impairment and restoration charges for the Mothae project (see Impairment and restoration charges on page 7)
(3) 2013 beginning of the year current liabilities is net of current portion of long-term debt ($30.3m)
(4) ROCE is a non-IFRS measure defined as adjusted net income before tax divided by the average capital employed.

Revenues

During the year the Company had sales totalling 412,136 carats for gross proceeds of $265.5 million at an average price of $644 per carat. The increase in revenues of $85.0 million compared to the prior year was due to higher prices received for the Karowe diamonds and a larger number of carats being sold in the large exceptional stones tenders, which contributed $135.6 million to revenues. The exceptional stone sales resulted in an average price of $32,471 per carat in 2014 (2013: $24,290 per carat, with the remaining tenders achieving $318 per carat (2013: $249 per carat).

Operating earnings

Operating earnings before royalty payments for 2014 were $218.3 million resulting in an operating margin (before royalties and depletion, amortization and accretion) of 82%. The margin significantly benefited from the Company's exceptional stone tenders held during the year. Operating expenses during the year were $115 per carat, which resulted in an operating margin of $529 per carat. As anticipated, the full year operating expenses at $115 per carat was higher than the $100 per carat in the prior year due to the increase in non-capitalized waste stripping costs.

Impairment and restoration charges

The Company have proceeded to divest the Mothae project as the project did not meet the Company's investment criteria. This resulted in an impairment charge of $18.8 million and a $2.4 million restoration charge in Q4 2014.

Income Tax expense

The Company's 2014 income tax expense was $73.3 million, which consisted of a current income tax charge of $41.6 million and a deferred income tax charge of $31.7 million for the year. The Company is subject to a variable tax rate in Botswana that increases as profit as a percentage of revenue increases. The lowest variable tax rate is 22% while the highest variable tax rate is 55% only if taxable income were equal to revenue. At the Company's 2014 performance, its tax rate for 2014 was 40%. The Company has paid $27.9 million of its current year tax expense and the remaining current tax accrual of $13.7 million is due on April 30, 2015.

Foreign exchange loss

The Company recorded a foreign exchange loss of $19.4 million in 2014. A loss of $13.6 million was recognized during the fourth quarter which resulted in an accumulated foreign exchange loss of $23.9 million for the year due to an intercompany Pula denominated loan between Corporate and Botswana. Foreign exchange losses following the weakening of the Pula have been previously calculated and reported in the Company's other comprehensive income as this loan has been reported as a net investment in a foreign operation under IAS21. As of January 1, 2014 the Company had determined Boteti was able to continue to be profitable and would repay its intercompany loan. Thus, the Company would no longer report this intercompany loan as a net investment in a foreign operation and as a result previous cumulative foreign exchange losses of $23.9 million reported in other comprehensive income has been reported in the statement of operations as the intercompany loan is repaid. As this intercompany loan has been fully repaid in 2014, the corresponding foreign exchange loss $23.9 million has been fully realized in 2014 and will not occur in 2015.

This $23.9 million foreign exchange loss is entirely due to non-cash foreign exchange movements of the Company's intercompany loan between Corporate and Botswana and has no impact on the value the Company's net assets nor does it result in a cash outflow to the business in the current or future periods. This loss was offset by the Company's $4.5 million foreign exchange gain mainly generated by the appreciation of the US dollar holdings by the Company's Botswana subsidiary.

Earnings before interest, tax, depreciation and amortization (EBITDA)

Full year EBITDA was $173.4 million compared to $102.9 million in 2013. The EBITDA is higher than the prior year as higher prices were received for the Karowe diamonds during the year, which were partially offset by higher costs to reflect increased non-capitalized waste stripping costs.

EBITDA is a non-IFRS measure and is reconciled in the table on page 5.

Cash operating cost per tonne ore treated

The year ended December 31, 2014 cash operating cost per tonne treated was $27.8 per tonne treated compared to $21.6 per tonne treated in the year ended December 31, 2013 and outlook guidance of $31 - $33 per tonne treated. The higher cost compared to the same period in the prior year is largely due to higher non-capitalized waste stripping costs in the current year as anticipated in the mine plan.

Cash operating cost per tonne treated is a non-IFRS measure and is reconciled in the table on page 6 to the most directly comparable measure calculated in accordance with IFRS, which is operating expenses.

Liquidity and Capital Resources

As at December 31, 2014, the Company had cash of $100.8 million compared to $49.4 million at December 31, 2013.

Cash increased during the year by $51.5 million. This increase reflects cash from operating activities of $133.1 million offset primarily by the Company's acquisition of plant and equipment of $42.3 million, largely for the plant optimization project and sustaining capital, $6.2 million of capitalized production stripping costs, and payment of the Company's regular and special dividend of $26.8 million.

The Company has renegotiated its revolving term credit facility with Bank of Nova Scotia. The new agreement is for a three year $50.0 million operating line. The facility contains financial and non-financial covenants customary for a facility of this size and nature. The applicable interest rate of any loan advances under the facility will be determined by the Company's leverage ratio at that time. The Company has maintained the same level of security on the three year facility by way of a charge over the Company's Karowe assets and a guarantee by the Company's subsidiaries, which hold the Karowe assets. As at December 31, 2014 the full amount under this facility was available.

As part of the Company's environmental obligation related to the Karowe Mine, the Government of Botswana required a reclamation bond for the Mine. On July 1, 2014, Standard Chartered Bank Botswana Limited has provided Boteti Mining (Pty) Ltd, a wholly owned subsidiary with a reclamation bond of Botswana Pula 100.0 million ($10.8 million) with respect to the Karowe Mine. Consequently, the Company has provided a guarantee for a maximum amount of Botswana Pula 80.0 million ($8.6 million) with Standard Chartered Bank Botswana Limited. In addition the Company has deposited Botswana Pula 20.0 million ($2.2 million) with Standard Chartered Bank Botswana Limited, accounted for in non-current other assets.

SUMMARY OF QUARTERLY RESULTS

(All amounts expressed in thousands of U.S. dollars, except per share data)

The Company's financial statements are reported under IFRS issued by the IASB. The following table provides highlights, extracted from the Company's financial statements, of quarterly results for the past eight quarters (unaudited):

Three months ended	Dec-14	Sept-14	Jun-14	Mar-14	Dec-13	Sept-13	Jun-13	Mar-13
A. Revenues	70,499	91,253	70,972	32,780	58,683	42,096	47,224	32,504
B. Exploration (expenditures) recovery	(345)	(258)	(135)	(459)	(167)	(389)	(557)	374
C. Administration expenses	(4,536)	(2,290)	(3,841)	(2,107)	(4,871)	(1,851)	(2,761)	(1,946)
D. Net income (loss)(1)	(16,819)	41,846	15,639	5,074	21,331	15,043	22,679	6,169
E. Earnings (loss) per share (basic and diluted)	(0.03)	0.11	0.04	0.01	0.05	0.04	0.06	0.02

(1) Net loss in Q4 2014 was mainly generated by the Mothae impairment and restoration charge: $21.2 million in the period.

Revenues

During the three months ended December 31, 2014, the Company completed three diamond tenders, one of which was an exceptional diamond tender. The exceptional diamond tender generated gross proceeds of $46.4 million and the regular tenders in the fourth quarter achieved winning bids totalling $24.1 million or $234 per carat.

Administration expenses

Administration expenses increased $2.2 million during the quarter when compared to the previous three month period due largely to accrued employee performance payments across the business.

NON-IFRS FINANCIAL MEASURES

This MD&A refers to certain financial measures, such as EBITDA, adjusted net income for the period and adjusted earnings per share for the period, which are not measures recognized under IFRS and do not have a standardized meaning prescribed by IFRS. These measures may differ from those made by other corporations and accordingly may not be comparable to such measures as reported by other corporations. These measures have been derived from the Company's financial statements, and applied on a consistent basis, because the Company believes they are of assistance in the understanding of the results of operations and financial position.

EBITDA (see "Select Financial Information") is the term the Company uses as an approximate measure of the Company's pre-tax operating cash flow and is generally used to better measure performance and evaluate trends of individual assets. EBITDA comprises earnings before deducting interest and other financial charges, income taxes, depreciation and amortization and net loss attributable to non-controlling interests.

Adjusted net income for the period (see "Select Financial Information") is the term the Company uses to describe net income before non-cash foreign exchange loss related to intercompany repayment and Mothae impairment and restoration charge.

Adjusted earnings per share for the period (see "Select Financial Information") is the term the Company uses to describe adjusted net income, as defined above, divided by the basic and fully diluted number of shares at the period end.

Operating costs per carats sold (see "Karowe Mine, Botswana") is the term the Company uses to describe the mining, processing and site administration costs to produce a single carat of diamond. This is calculated as operating costs per carat of diamond sold.

Cash operating cost per tonne ore treated (see "Select Financial Information") is the term the Company uses to describe operating expenses per tonne treated on a cash basis. This is calculated as cash operating cost divided by tonnes of ore treated for the period. This ratio provides the user with the total cash costs incurred by the mine during the period per tonne of ore treated, including waste capitalisation costs, mobilization costs and working capital movements. The most directly comparable measure calculated in accordance with IFRS is operating expenses. A table reconciling the two measures is presented on page 6.

ROCE (see "Select Financial Information") is a non-IFRS financial measure the Company uses to analyze operating performance and the efficiency of the Company's capital allocation. The calculation is earnings before interest and tax ('EBIT') divided by the average capital employed. In the current year EBIT has been adjusted for the non-cash foreign exchange loss related to an intercompany loan repayment and the Mothae impairment and restoration charges. Average capital employed is calculated as an annual average of the capital employed balance at the beginning of the year and end of the year. A table reconciling ROCE is presented on page 6.

RELATED PARTY TRANSACTIONS

For the year ended December 31, 2014, the Company paid $0.5 million, (2013 ☐ $0.5 million) for services provided by a company associated with the Chairman of the Company. The Company also paid $0.2 million for the year ended December 31, 2014 (2013 ☐ $0.3 million) to a charitable foundation directed by members of the Company's directors to carry out social programs on behalf of the Company.

FINANCIAL INSTRUMENTS

Financial assets and liabilities have been classified into categories that determine their basis of measurement and, for items measured at fair value, whether changes in fair value are recognized in the consolidated statements of operations or consolidated statements of comprehensive loss. Those categories are: fair value through profit or loss; loans and receivables; available for sale assets; and, for liabilities, amortized cost.

The fair value of the Company's available for sale financial instruments is derived from quoted prices in active markets for identical assets. The fair value of the Company's long-term debt approximates their carrying amounts due to the fact that there have been no significant changes in the Company's own credit risk. The fair value of all other financial instruments of the Company approximates their carrying values because of the demand nature or short-term maturity of these instruments.

In the normal course of business, the Company is inherently exposed to currency and commodity price risk. For a discussion of certain risks and assumptions that relate to the use of derivatives, including equity market risk, liquidity risk and credit risk, refer to Note 21 in the Company's consolidated financial statements. For a discussion of the methods used to value financial instruments, as well as any significant assumptions, refer also to Note 21 of the Company's consolidated financial statements.

OUTSTANDING SHARE DATA

As at the date of this MD&A, the Company had 379,382,412 common shares outstanding and 2,018,670 stock options outstanding under its stock-based incentive plan. As at the same date, the Company had no stock purchase warrants outstanding.

RISKS AND UNCERTAINTIES

The operations of the Company are speculative due to the high risk nature of its business which includes acquisition, financing, exploration, development and operation of diamond properties. Material risk factors and uncertainties, which should be taken into account in assessing the Company's activities, include, but are not necessarily limited to, those set below. Any one or more of these risks and others could have a material adverse effect on the Company.

Diamond Prices and Marketability

The mining industry, in general, is intensely competitive and there is no assurance that, a profitable market will exist for the sale of diamonds produced. The value of the Company's shares, its financial results and its mining activities are significantly affected by the price and marketability of diamonds. Numerous factors beyond the control of the Company may affect the price and marketability of any diamonds produced which cannot be accurately predicted, such as: international economic and political trends; global or regional consumption and demand and supply patterns; and increased production of other diamond producers, especially due to the small concentration of producers and sellers within the market. There is no assurance that the sale price of diamonds produced from any diamond deposit will be such that they can be mined at a profit.

Economic Conditions

Unfavourable economic conditions may negatively impact the Company's financial ability. Unfavourable economic conditions could also increase the Company's financing costs, decrease estimated income from prospective mining operations, limit access to capital markets and negatively impact the availability of credit facilities to the Company.

Uncertainties Related to Mineral Resource Estimates

There is a high degree of uncertainty attributable to the calculation of mineral resources and corresponding grades being mined or dedicated to future production. Until resources are actually mined and processed, no assurance can be given to the actual quantity of mineral resources and grades. Any material change in the quantity of resources, grades or stripping ratio may affect the economic viability of the Company's properties. In addition, there is no assurance that recoveries in small-scale laboratory tests will be duplicated in larger-scale tests under on-site conditions, or during production. Determining the economic viability of a diamond project is complicated and involves a number of variables. It involves extensive geo-statistical analysis due to the highly variable nature of diamond distribution in kimberlite pipes and the fact that both diamond grade and average diamond value play important roles in determining the viability of any given diamond project. Since no two diamonds are exactly alike, a significant parcel of diamonds is needed to gain confidence levels on diamond size distribution and average diamond value necessary to make any realistic decisions regarding future development.

Licenses, permits and approvals

The Company's operations require licenses, permits and approvals from various governmental authorities. The Company believes that it currently holds and is presently complying in all material respects with all necessary licenses and permits under applicable laws and regulations to conduct its current operations. However, such licenses and permits are subject to change in various circumstances and certain permits and approvals are required to be renewed from time to time. Additional permits or permit renewals will need to be obtained in the future. The granting, renewal and continued effectiveness of these permits and approvals are, in most cases, subject to some level of discretion by the applicable regulatory authority. Certain governmental approval and permitting processes are subject to public comment and can be appealed by project opponents, which may result in significant delays or in approvals being withheld or withdrawn.

There can be no guarantee the Company will be able to obtain or maintain all necessary licenses and permits as are required to explore and develop its properties, commence construction or operation of mining facilities and properties under exploration or development or to maintain continued operations that economically justify the cost.

Currency Risk

Currency fluctuations may impact the Company's financial performance. Diamonds are sold in US dollar with a the Company's costs and expenses being incurred in Botswana Pula, South African Rand, Lesotho Loti, Canadian and U.S. dollar currencies. As a consequence, fluctuations in exchange rates may have a significant effect on the cash flows and operating results of the Company in either a positive or negative direction. In order to mitigate foreign exchange fluctuations the Company hedged a portion of its Botswana pula costs for the 2014 financial year.

Mining and Processing

The Company's business operations are subject to risks and hazards inherent in the mining industry, including, but not limited to, unanticipated variations in grade and other geological problems, water, power, surface conditions, metallurgical and other processing problems, mechanical equipment performance problems, the lack of availability of materials and equipment, the occurrence of accidents, labour force disruptions, force majeure factors, weather conditions which can materially and adversely affect among other things production quantities and rates, development, costs and expenditures and production commencement dates.

The Company periodically reviews its Life of Mine ("LOM") planning. Significant changes in the LOM plans can occur as a result of experience obtained in the course of carrying out its mining activities, changes in mining methods and rates, process changes, investments in new equipment and technology, diamond price assumptions and other factors. Based on this analysis, the Company reviews its accounting estimates and in the event of an impairment may be required to write down the carrying value of its mine or development property. This process continues for the economic life of the mines in which the Company has an interest.

Environmental and Other Regulatory Requirements

All phases of mining and exploration operations are subject to government regulation including regulations pertaining to environmental protection. Environmental legislation is becoming stricter, with increased fines and penalties for non□compliance, more stringent environmental assessments of proposed projects and heightened responsibility for companies and their officers, directors and employees. There can be no assurance that possible future charges in environmental regulation will not adversely affect the Company's operations. As well, environmental hazards may exist on a property that the Company holds an interest in, which were caused by previous or existing owners or operators of the properties and of which the Company is not aware at present. Operations at the Company's mines are subject to strict environmental and other regulatory requirements, including requirements relating to the production, handling and disposal of hazardous materials, pollution controls and health and safety. Any failure to comply with the requirements could result in substantial fines, delays in production, or the withdrawal of the Company's mining licenses.

Foreign Operations Risk

The Company's current significant projects are located in Botswana and Lesotho. Each of these countries exposes the Company to risks that may not otherwise be experienced if its operations were domestic. The risks include, but are not limited to, environmental protection, land use, water use, health safety, labor, restrictions on production, price controls, currency remittance, and maintenance of mineral tenure and expropriation of property. For example, changes to regulations in Botswana and Lesotho relating to royalties, allowable production, importing and exporting of diamonds and environmental protection, may result in the Company not receiving an adequate return on investment capital.

Although the operating environments in Botswana and Lesotho are considered favorable compared to those in other developing countries, there are still political risks. These risks include, but are not limited to terrorism, hostage taking, military repression, expropriation, extreme fluctuations in currency exchange rates, high rates of inflation and labor unrest. Changes in mining or investment policies or shifts in political attitudes in these countries may also adversely affect the Company's business. In addition, there may be greater exposure to a risk of corruption and bribery (including possible prosecution under the federal Corruption of Foreign Public Officials Act). Also, in the event of a dispute arising in foreign operations, the Company may be subject to the exclusive jurisdiction of foreign courts and may be hindered or prevented from enforcing its rights.

There is no assurance that future changes in taxes in any of the countries in which the Company operates will not adversely affect the Company's operations.

Mineral Exploration and Development

The business of exploring for diamonds and mining is highly speculative in nature and involves significant financial and other risks which even careful evaluation, experience and knowledge may not eliminate. There is no certainty that expenditures made or to be made by the Company in exploring and developing diamond properties in which it has an interest will result in the discovery of commercially mineable deposits. Most exploration projects do not result in the discovery of commercially mineable deposits. While discovery of a diamond bearing deposit may result in substantial rewards, few properties which are explored are ultimately developed into producing mines. Major expenses may be required to establish reserves by drilling and to construct mining and processing facilities at a site. There can be no guarantee that exploration programs carried out by the Company will result in the development of profitable mining operations.

Title Matters

Any changes in the laws of Botswana or Lesotho relating to mining could have a material adverse effect to the rights and title to the interests held in those countries by the Company. No assurance can be given that applicable governments will not revoke or significantly alter the conditions of applicable exploration and mining authorizations nor that such exploration and mining authorizations will not be challenged or impugned by third parties.

Infrastructure

The Karowe Mine and the Mothae Project are located in remote areas and the availability of adequate infrastructure is critical. Reliable roads, bridges, power and water supply are important determinants which affect capital and operating costs. Sabotage, government or other interference in the maintenance of provision of such infrastructure could adversely affect activities and profitability of the Company.

Rehabilitation Funds and Mine Closure Costs

Changes in environmental laws and regulations can create uncertainty with regards to future rehabilitation costs and affect the funding requirements. Closing a mine can have significant impact on local communities and site remediation activities may not be supported by local stakeholders. Actual costs realized in satisfaction of mine closure obligations may vary materially from management's estimates.

Community Relations

The Company's relationships with the communities in which it operates and other stakeholders are critical to ensure the future success of its existing operations and the construction and development of its projects. There is an increasing level of public concern relating to the perceived effect of mining activities on the environment and on communities impacted by such activities. Publicity adverse to the Company's operations, or the mining industry generally, could have an adverse effect on the Company and may impact relationships with the communities in which the Company operates and other stakeholders. While the Company is committed to operating in a socially responsible manner, there can be no assurance that its efforts in this respect will mitigate this potential risk.

Uninsured Risks and Insurance Coverage

The mining business is subject to a number of risks and hazards that may not be insured including, but not limited to, environmental hazards, industrial accidents, labor disputes, encountering unusual or unexpected geologic formations or other geological or grade problems, encountering unanticipated ground or water conditions, cave-ins, pit wall failures, flooding, rock bursts, periodic interruptions due to inclement or hazardous weather conditions and other acts of God. Such risks could result in damage to mineral properties or facilities, personal injury or death, environmental damage, delays in exploration, development or mining, monetary losses and possible legal liability.

The Company maintains insurance against certain risks that are associated with its business in amounts that it believes to be reasonable at the current stage of operations. There can be no assurance that such insurance will continue to be available at economically acceptable premiums or will be adequate to cover any future claim.

Competition

The mining industry is intensely competitive in all its phases and the Company competes with other companies that have greater financial resources and technical capacity. The Company continues to compete with a number of companies for the acquisition of mineral properties. The ability for the Company to replace or increase its mineral reserves and mineral resources in the future will depend on its ability to develop its present properties and also to select and acquire economic producing properties or prospects for diamond extraction.

Legal Proceedings

Due to the nature of its business, the Company may be subject to numerous regulatory investigations, claims, lawsuits and other proceedings in the ordinary course of its business. The results of these legal proceedings cannot be predicated with certainty due to the uncertainty inherent in litigation, including the effects of discovery of new evidence or advancement of new legal theories, the difficulty of predicting decisions of judges and juries and the possibility that decisions may be reversed on appeal. There can be no assurance that these matters will not have a material adverse effect on the Company's business.

Conflicts of Interest

The Company's directors and officers may serve as directors or officers, or may be associated with other public companies or have significant shareholdings in other public companies. To the extent that such other companies may participate in business or asset acquisitions, dispositions, or ventures in which the Company may participate, the directors and officers of the Company may have a conflict of interest in negotiating and concluding terms respecting the transactions.

If a conflict of interest arises, directors and officers are subject to the Company's Code of Business Conduct and Ethics and applicable corporate legislation. In accordance with the laws of the Province of British Columbia, the directors and officers of the Company are required to act honestly, in good faith and in the best interests of the Company.

Personnel

The Company is depending on a relatively small number of key senior management employees, the loss of any of whom could have an adverse effect on the Company. The Company does not have key person insurance on these key individuals.

In addition, due to the remoteness of the Company's Karowe mine, there is competition for personnel. The degree to which the Company is not successful in retaining and developing employees at its mine sites could lead to a lack of knowledge, skills and experience required to operate the mine effectively.

Natural Disasters

The occurrence of one or more natural disasters such as a pandemic outbreak or unusually adverse weather conditions could disrupt mining operations and have a material adverse effect on the Company.

Share Price Volatility and Future Sales by Existing Shareholders

In recent years, the securities markets have experienced a high level of price and volume volatility, and the market price of securities of many companies, particularly those considered to be development stage companies or early stage production companies without a proven history of sustainable cash flow, have experienced wide fluctuations which have not necessarily been related to the operating performance, underlying asset values or prospects of such companies. There can be no assurance that such fluctuations will not affect the price of the Company's securities. Also, subject to compliance with applicable securities laws, the Company's officers, directors, significant shareholders may sell some or all of their common shares in the future. No prediction can be made as to the effect, if any, such future sales of common shares will have on the market price of the Company's securities. The future sale of a substantial number of common shares by the Company's officers, directors, principal shareholders and their affiliates, or the perception that such sales could occur, could adversely affect prevailing market prices for the Company's securities.

OFF-BALANCE SHEET ARRANGEMENTS

The Company has no off-balance sheet arrangements.

FINANCIAL INFORMATION

The report for the quarter ended March 31, 2015 is expected to be published on May 12, 2015. In addition, the Company's annual general meeting of shareholders will be held on May 13, 2015 in Vancouver, British Columbia.

NEW ACCOUNTING PRONOUNCEMENTS

The Company prepared its financial statements in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). Note 3 of the audited consolidated financial statements for the year ended December 31, 2014 provides details of significant accounting policies and accounting policy decisions for significant or potentially significant areas that have had an impact on our financial statements or may have an impact in future periods.

As of January 1, 2014, the Company adopted the new and amended IFRS pronouncements in accordance with the transitional provisions outlined in the respective standards as listed below.

a) *Pronouncement affecting financial statement presentation or disclosures*

IFRIC 21 provides accounting guidance for an obligation to pay a levy, if that liability is within the scope of IAS 37, Provisions, Contingent Liabilities and Contingent Assets. Levies are imposed by governments in accordance with legislation and do not include income taxes. The interpretation addresses the diversity in practice of when the liability to pay a levy is recognized.

IFRIC 21 defines an obligating event as the activity that triggers the payment of the levy, as identified by legislation. A liability to pay a levy is recognized at the date of the obligating event, which may be at a point in time or over a period of time. The fact that an entity is economically compelled to continue to operate in the future, or prepares its financial statements on a going concern basis, does not create an obligation to pay a levy that will arise in a future period as a result of continuing to operate.

The adoption of IFRIC 21 did not affect the Company's financial results or disclosures.

b) *Pronouncements issued but not yet effective*

New IFRS pronouncements that have been issued but are not yet effective are listed below. The Company plans to apply the new standards or interpretations in the annual period for which it is first required.

IFRS 15 - Revenue from Contracts with Customers

The new revenue standard introduces a single, principles based, five-step model for the recognition of revenue when control of a good or service is transferred to the customer. The five steps are: identify the contract(s) with the customer, identify the performance obligations in the contract, determine transaction price, allocate the transaction price and recognize revenue when a performance obligation is satisfied. IFRS 15 also requires enhanced disclosures about revenue to help investors better understand the nature, amount, timing and uncertainty of revenue and cash flows from contracts with customers and improves the comparability of revenue from contracts with customers.

IFRS 15 will be effective for annual periods beginning on or after January 1, 2017, with early adoption permitted. The Company is currently assessing the effect of this standard on our financial statements.

IFRS 9 - Financial Instruments

IFRS 9, Financial Instruments addresses the classification, measurement and recognition of financial assets and financial liabilities. IFRS 9 requires financial assets to be classified into three measurement categories on initial recognition: those measured at fair value through profit and loss, those measured at fair value through other comprehensive income and those measured at amortized cost. Investments in equity instruments are required to be measured by default at fair value through profit or loss. However, there is an irrevocable option to present fair value changes in other comprehensive income. Measurement and classification of financial assets is dependent on the entity's business model for managing the financial assets and the contractual cash flow characteristics of the financial asset.

IFRS 9 introduces a new three-stage expected credit loss model for calculating impairment for financial assets. IFRS 9 no longer requires a triggering event to have occurred before credit losses are recognized. An entity is required to recognize expected credit losses when financial instruments are initially recognized and to update the amount of expected credit losses recognized at each reporting date to reflect changes in the credit risk of the financial instruments. In addition, IFRS 9 requires additional disclosure requirements about expected credit losses and credit risk.

The completed version of IFRS 9 is effective for annual periods beginning on or after January 1, 2018, with early adoption permitted. The Company is currently assessing the effect of this standard and its related amendments on our financial statements.

CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The application of certain accounting policies requires the Company to make estimates that affect both the amount and timing of the recording of assets, liabilities, revenues and expenses. Some of these estimates require judgments about matters that are inherently uncertain.

Note 3 to the audited consolidated financial statements for the year ended December 31, 2014 includes a summary of the significant accounting policies adopted by the Company. The following policies are considered to be critical accounting policies since they involve the use of significant estimates.

Estimated recoverable reserves and resources

Mineral reserve and resource estimates are based on various assumptions relating to operating matters. These include production costs, mining and processing recoveries, cut-off grades, long term commodity prices and, in some cases, exchange rates, inflation rates and capital costs. Cost estimates are based on feasibility study estimates or operating history. Estimates are prepared by appropriately qualified persons, but will be affected by forecasted commodity prices, inflation rates, exchange rates, capital and production costs and recoveries amongst other factors. Estimated recoverable reserves and resources are used to determine the depreciation of property, plant and equipment at operating mine site, in accounting for deferred stripping costs and in performing impairment testing. Therefore, changes in the assumptions used could affect the carrying value of assets, depreciation and impairment charges recorded in the income statement.

Depreciation, depletion and accretion

Mineral properties and plant and equipment comprise a large component of the Company's assets and as such, depreciation and depletion of these assets have a significant effect on the Company's financial statements. Upon commencement of commercial production, the Company amortizes mineral property and mining equipment and other assets over the life of the mine based on the depletion of the mine's proven and probable reserves. In the case of mining equipment and other assets, if the useful life of the asset is shorter than the life of the mine, the asset is amortized over its expected useful life.

Proven and probable reserves are determined based on a professional evaluation using accepted international standards for the assessment of mineral reserves. The assessment involves geological and geophysical studies and economic data and the reliance on a number of assumptions. The estimates of the reserves may change based on additional knowledge gained subsequent to the initial assessment. This may include additional data available from continuing exploration, results from the reconciliation of actual mining production data against the original reserve estimates, or the impact of economic factors such as changes in the price of commodities or the cost of components of production.

A change in the original estimate of reserves would result in a change in the rate of depreciation and amortization of the related mining assets and could result in an impairment of the mining assets.

Mineral properties

The Company carries the acquisition costs of its mineral properties at cost less any provision for impairment. The costs of each property will be amortized over the economic life of the property on a unit of production basis. Costs are charged to operations when a property is abandoned or when impairment in value, other than temporary, has been determined. Exploration costs are charged to operations as incurred.

The Company undertakes a periodic review of the carrying values of mineral properties and whenever events or changes in circumstances indicate that their carrying value may exceed their fair value. In undertaking this review, management of the Company is required to make significant estimates. These estimates are subject to various risks and uncertainties, which may ultimately have an effect on the expected recoverability of the carrying values of the mineral properties and related expenditures.

Income taxes

Deferred income tax assets and liabilities are determined based on differences between the financial statement carrying values of assets and liabilities and their respective income tax bases ("temporary difference"), and losses carried forward. Deferred income tax assets and liabilities are measured using tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by year end. The effect on deferred income tax assets and liabilities of a change in tax rates is included in operations in the period in which the change is substantively enacted. The amount of deferred income tax assets recognized is limited to the extent that it is probable that future tax profits will be available against which the temporary difference can be utilized.

Management of the Company is required to exercise judgments and make assumptions about the future performance of the Company in determining its ability to utilize loss carry-forwards and realize the benefits of deferred income tax assets.

Stock-based compensation

In calculating the fair value of stock options granted, management is required to make significant estimates in relation to the future volatility of the Company's share price and the period in which stock options will be exercised. Selection of a volatility factor and the estimate of the expected option life will have a significant impact on costs recognized for stock-based compensation. Estimates concerning volatility are made with reference to historical volatility, which is not necessarily an accurate indicator of volatility that will be experienced in the future. Management assumes that stock options will be exercised prior to their expiry date.

Decommissioning and site restoration

The Company has obligations for site restoration and decommissioning related to its diamond properties. The future obligations for decommissioning and site restoration activities are estimated by the Company using mine closure plans or other similar studies which outline the requirements that will be carried out to meet the obligations. Because the obligations are dependent on the laws and regulations of the countries in which the mines operate, the requirements could change as a result of amendments in the laws and regulations relating to environmental protection and other legislation affecting resource companies. As the estimate of obligations is based on future expectations, a number of assumptions and judgments are made by management in the determination of closure provisions. The decommissioning and site restoration provisions are more uncertain the further into the future the mine closure activities are to be carried out.

The Company's policy for recording decommissioning and site restoration provisions is to establish provisions for future mine closure costs at the commencement of mining operations based on the present value of the future cash flows required to satisfy the obligations. The amount of the present value of the provision is added to the cost of the related mining assets and depreciated over the life of the mine. The provision is accreted to its future value over the life of the mine through a charge to operating costs. Actual results could differ from estimates made by management during the preparation of these consolidated financial statements and those differences may be material.

INTERNAL FINANCIAL REPORTING AND DISCLOSURE CONTROLS

Disclosure controls and procedures

Disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed by the Company in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time periods specified in the securities legislation and include controls and procedures designed to ensure that information required to be disclosed by the Company in its annual filings, interim filings or other reports filed or submitted under securities legislation is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Management, including the Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures. As of December 31, 2014, the Chief Executive Officer and Chief Financial Officer have each concluded that the Company's disclosure controls and procedures, as defined in NI 52-109 - Certification of Disclosure in Issuer's Annual and Interim Filings, are effective to achieve the purpose for which they have been designed.

Internal controls over financial reporting

Internal controls over financial reporting are designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with IFRS. Management is also responsible for the design of the Company's internal control over financial reporting in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

The Company's internal controls over financial reporting include policies and procedures that: pertain to the maintenance of records that, in reasonable detail accurately and fairly reflect the transactions and disposition of assets; provide reasonable assurance that transactions are recorded as necessary to permit preparation of the financial statements in accordance with IFRS and that receipts and expenditures are being made only in accordance with authorization of management and directors of the Company; and provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of assets that could have a material effect on the financial statements.

Management, including the Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the design and operation of the Company's internal controls over financial reporting. As of December 31, 2014, the Chief Executive Officer and Chief Financial Officer have each concluded that the Company's internal controls over financial reporting, as defined in NI 52-109 - Certification of Disclosure in Issuer's Annual and Interim Filings, are effective to achieve the purpose for which they have been designed.

Because of their inherent limitations, internal controls over financial reporting can provide only reasonable assurance and may not prevent or detect misstatements. Furthermore, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

CAUTIONARY NOTE REGARDING FORWARD LOOKING STATEMENTS

Certain of the statements made and contained herein in the MD&A and elsewhere constitute forward-looking statements as defined in applicable securities laws. Generally, these forward-looking statements can be identified by the use of forward-looking terminology such as "expects", "anticipates", "believes", "intends", "estimates", "potential", "possible" and similar expressions, or statements that events, conditions or results "will", "may", "could" or "should" occur or be achieved.

In particular, this MD&A may contain forward looking information pertaining to the following: the estimates of the Company's mineral reserve and resources; estimates of the Company's production and sales volumes for the Karowe Mine; estimated costs to complete the Karowe Mine optimization; start-up, exploration and development plans and objectives; production costs; exploration and development expenditures and reclamation costs; expectation of diamond price and changes to foreign currency exchange rates; expectations regarding the need to raise capital; possible impacts of disputes or litigation; and other risks and uncertainties described under the heading "Risks and Uncertainties" in the Company's Annual Information Form dated March 20, 2014 available at http://www.sedar.com (the "AIF").

Forward-looking statements are based on the opinions, assumptions and estimates of management as of the date such statements are made, and they are subject to a number of known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievement expressed or implied by such forward-looking statements. Such assumptions include: the Company's ability to obtain necessary financing; the Company's expectations regarding the economy generally, results of operations and the extent of future growth and performance; and assumptions that the Company's activities will not be adversely disrupted or impeded by development, operating or regulatory risk. The Company believes that expectations reflected in this forward-looking information are reasonable but no assurance can be given that these expectations will prove to be correct and such forward-looking information included in this MD&A should not be unduly relied upon.

There can be no assurance that such statements will prove to be accurate, as the Company's results and future events could differ materially from those anticipated in this forward-looking information as a result of those factors discussed in or referred to under the heading "Risks and Uncertainties" in the Company's AIF, as well as changes in general business and economic conditions, changes in interest and foreign currency rates, the supply and demand for, deliveries of and the level and volatility of prices of rough diamonds, costs of power and diesel, acts of foreign governments and the outcome of legal proceedings, inaccurate geological and recoverability assumptions (including with respect to the size, grade and recoverability of mineral reserves and resources), unanticipated operational difficulties (including failure of plant, equipment or processes to operate in accordance with specifications or expectations, cost escalations, unavailability of materials and equipment, government action or delays in the receipt of government approvals, industrial disturbances or other job actions, adverse weather conditions, and unanticipated events relating to health safety and environmental matters)

Accordingly, readers are cautioned not to place undue reliance on these forward-looking statements which speak only as of the date the statements were made, and the Company does not assume any obligations to update or revise them to reflect new events or circumstances, except as required by law.

February 19, 2015

Independent Auditor's Report

To the Shareholders of Lucara Diamond Corp.

We have audited the accompanying consolidated financial statements of Lucara Diamond Corp., which comprise the consolidated balance sheets as at December 31, 2014 and December 31, 2013 and the consolidated statements of operations, comprehensive income, cash flows and changes in equity for the years then ended, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

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 International Financial Reporting Standards, 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 Lucara Diamond Corp. as at December 31, 2014 and December 31, 2013 and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

signed "PricewaterhouseCoopers LLP"

Chartered Accountants

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LUCARA DIAMOND CORP.
CONSOLIDATED BALANCE SHEETS
(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

	December 31, 2014	December 31, 2013
ASSETS		
Current assets		
Cash and cash equivalents	$ 100,839	$ 49,364
Investments	56	90
VAT receivables and other (Note 6)	5,017	3,593
Inventories (Note 7)	32,019	21,132
	137,931	74,179
Plant and equipment (Note 8)	122,016	100,886
Mineral properties (Note 9)	52,729	72,061
Other non-current assets	4,349	62
TOTAL ASSETS	$ 317,025	$ 247,188
LIABILITIES		
Current liabilities		
Trade payables and accrued liabilities	$ 12,384	$ 15,491
Taxes payable (Note 17)	13,681	-
Current portion of restoration provisions (Note 10)	2,857	-
	28,922	15,491
Restoration provisions (Note 10)	15,902	14,515
Deferred income taxes (Note 17)	43,646	14,258
TOTAL LIABILITIES	88,470	44,264
EQUITY		
Share capital (Note 11)	286,138	283,609
Contributed surplus (Note 12)	4,713	5,108
Deficit	(25,128)	(45,516)
Accumulated other comprehensive loss	(37,182)	(41,820)
Total equity attributable to shareholders of the Company	228,541	201,381
Non-controlling interests (Note 13)	14	1,543
TOTAL EQUITY	228,555	202,924
TOTAL LIABILITIES AND EQUITY	$ 317,025	$ 247,188

Commitments (Note 23)

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

Approved on Behalf of the Board of Directors:

"Marie Inkster"
Director

"William Lamb"
Director

LUCARA DIAMOND CORP.
CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE YEARS ENDED DECEMBER 31
(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

		2014		2013
Revenues	$	265,504	$	180,507
Cost of goods sold				
Operating expenses		47,169		43,835
Royalty expenses (Note 9)		26,550		18,051
Depletion, amortization and accretion		14,681		14,979
		88,400		76,865
Income from mining operations		177,104		103,642
Other expenses				
Exploration expenditures (Note 14)		1,197		1,323
Administration (Note 15)		12,774		11,429
Gain on sale of exploration program diamonds		-		(584)
Sales and marketing		4,355		3,523
Finance (income) expenses (Note 16)		(813)		3,785
Foreign exchange loss		19,372		3,953
Restoration charge (Note 5)		2,415		-
Impairment charge (Note 5)		18,783		-
		58,083		23,429
Net income before tax		119,021		80,213
Income tax expense (Note 17)				
Current income tax		41,589		96
Deferred income tax		31,692		14,895
		73,281		14,991
Net income for the year	$	45,740	$	65,222
Attributable to:				
Shareholders of the Company	$	47,317	$	65,317
Non-controlling interests	$	(1,577)	$	(95)
Income per common share (Note 18)				
Basic	$	0.13	$	0.17
Diluted	$	0.13	$	0.17
Weighted average common shares outstanding (Note 18)				
Basic		378,198,299		376,392,625
Diluted		380,011,269		376,512,990

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

LUCARA DIAMOND CORP.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
FOR THE YEARS ENDED DECEMBER 31
(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

		2014		2013
Net income for the year	$	45,740	$	65,222
Other comprehensive income (loss)				
Items that may be subsequently reclassified to net income				
Change in fair value of available-for-sale securities		(29)		11
Currency translation adjustment		4,620		(20,816)
		4,591		(20,805)
Comprehensive income	$	50,331	$	44,417
Comprehensive income attributable to:				
Shareholders of the Company		51,955		44,878
Non-controlling interests		(1,624)		(461)
	$	50,331	$	44,417

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

LUCARA DIAMOND CORP.

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

FOR THE YEARS ENDED DECEMBER 31

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

	Number of shares issued and outstanding	Share capital	Contributed surplus	Cumulative deficit	Accumulated other comprehensive loss	Non-controlling interests	Total
Balance, January 1, 2013	376,292,749	$ 282,796	$ 4,874	$ (110,740)	$ (21,381)	$ 1,911	$ 157,460
Exercise of stock options	606,666	813	(283)	-	-	-	530
Stock-based compensation	-	-	517	-	-	-	517
Effect of foreign currency translation	-	-	-	-	(20,450)	(366)	(20,816)
Unrealized gain on investments	-	-	-	-	11	-	11
Free-carried non-controlling interests (Note 13)	-	-	-	(93)	-	93	-
Net income for the year	-	-	-	65,317	-	(95)	65,222
Balance, December 31, 2013	376,899,415	$ 283,609	$ 5,108	$ (45,516)	$ (41,820)	$ 1,543	$ 202,924
Balance, January 1, 2014	376,899,415	$ 283,609	$ 5,108	$ (45,516)	$ (41,820)	$ 1,543	$ 202,924
Exercise of stock options	2,469,664	2,529	(727)	-	-	-	1,802
Stock-based compensation	-	-	332	-	-	-	332
Effect of foreign currency translation	-	-	-	-	4,667	(47)	4,620
Unrealized loss on investments	-	-	-	-	(29)	-	(29)
Free-carried non-controlling interests (Note 13)	-	-	-	(95)	-	95	-
Dividends paid[1]	-	-	-	(26,834)	-	-	(26,834)
Net income for the year	-	-	-	47,317	-	(1,577)	45,740
Balance, December 31, 2014	379,369,079	$ 286,138	$ 4,713	$ (25,128)	$ (37,182)	$ 14	$ 228,555

(1) On June 19, 2014, the Company paid a cash dividend of CA$ 0.02 per share. On December 18, 2014, the Company paid a cash dividend of CA$ 0.06 per share.

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

LUCARA DIAMOND CORP.

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31
(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

		2014		2013
Cash flows from (used in):				
Operating Activities				
Net income for the year	$	45,740	$	65,222
Items not involving cash and cash equivalents:				
Depletion, amortization and accretion		15,128		15,402
Foreign exchange loss		23,879		-
Stock-based compensation		332		517
Deferred income taxes		31,692		14,895
Finance costs		184		3,527
Restoration charge		2,415		-
Impairment charge		18,783		-
		138,153		99,563
Net changes in working capital items:				
VAT receivables and other current assets		(2,094)		2,060
Inventories		(11,814)		(6,953)
Trade payables and other current liabilities		(3,094)		3,893
Taxes payable		11,908		
		133,059		98,563
Financing Activities				
Repayments of debt		-		(50,000)
Repayments of revolving credit facility		-		(4,500)
Dividends paid		(26,834)		-
Proceeds from exercise of stock options		1,802		530
Other		(2,298)		-
		(27,330)		(53,970)
Investing Activities				
Acquisition of plant and equipment		(42,271)		(7,865)
Capitalized production stripping costs		(6,162)		-
Other		(2,051)		54
		(50,484)		(7,811)
Effect of exchange rate change on cash and cash equivalents		(3,770)		(679)
Increase in cash and cash equivalents during the year		51,475		36,103
Cash and cash equivalents, beginning of year		49,364		13,261
Cash and cash equivalents, end of year	$	100,839	$	49,364
Supplemental Information				
Interest received (paid)		739		(109)
Taxes (paid) received		(26,708)		96
Changes in trade payable and accrued liabilities related to plant and equipment		(272)		(2,870)

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

1. NATURE OF OPERATIONS

Lucara Diamond Corp. together with its subsidiaries (collectively referred to as the "Company") is a diamond mining company focused on the development and operation of diamond properties in Africa. The Company holds a 100% interest in the Karowe Mine (previously named AK6 Diamond Project) located in Botswana and a 75% interest in Mothae Diamond Project located in Lesotho.

The Company's common shares are listed on the TSX, NASDAQ OMX First North and Botswana Stock Exchanges. The Company was continued into the Province of British Columbia under the Business Corporations Act (British Columbia) in August 2004 and its registered office is located at Suite 2000 – 885 West Georgia Street, Vancouver, British Columbia, V6C 3E8.

2. BASIS OF PRESENTATION

The Company prepared its financial statements in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). The same accounting policies have been consistently applied in all periods presented.

These financial statements were approved by the Board of Directors for issue on February 19, 2015.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies used in the preparation of these consolidated financial statements are as follows:

(a) Basis of measurement

These consolidated financial statements have been prepared under the historical cost convention, except for investments in equity securities, which are measured at fair value.

(b) Consolidation

These consolidated financial statements include the accounts of the Company and all of its subsidiaries. (See Note 13 Principal subsidiaries)

Subsidiaries are entities controlled by the Company. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Subsidiaries are included in the consolidated financial statements from the date control is obtained until the date control ceases. Where the Company's interest is less than 100%, the Company recognized non-controlling interests. All intercompany balances, transactions, income, expenses, profits and losses, including unrealized gains and losses have been eliminated on consolidation. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Company.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Non-controlling interests represent the equity in a subsidiary not attributable, directly and indirectly, to the Company and is presented separately within equity in the consolidated balance sheet, separately from equity attributable to the shareholders of the Company. Losses within a subsidiary continue to be attributed to the non-controlling interests even if that results in a deficit balance. Changes in the Company's ownership interest in subsidiaries that do not result in a loss of control are accounted for as equity transactions.

(c) *Critical accounting estimates and judgments*

The preparation of consolidated financial statements requires management to use judgment in applying its accounting policies and estimates and assumptions about the future. Estimates and other judgments are continuously evaluated and are based on management's experience and other factors, including expectations about future events that are believed to be reasonable under the circumstances. The following discusses the most significant accounting judgments and estimates that the Company has made in the preparation of the consolidated financial statements:

Estimated recoverable reserves and resources – Mineral reserve and resource estimates are based on various assumptions relating to operating matters. These include production costs, mining and processing recoveries, cut-off grades, long term commodity prices and, in some cases, exchange rates, inflation rates and capital costs. Cost estimates are based on feasibility study estimates or operating history. Estimates are prepared by appropriately qualified persons, but will be affected by forecasted commodity prices, inflation rates, exchange rates, capital and production costs and recoveries amongst other factors. Estimated recoverable reserves and resources are used to determine the depreciation of property, plant and equipment at operating mine site, in accounting for deferred stripping costs and in performing impairment testing. Therefore, changes in the assumptions used could affect the carrying value of assets, depreciation and impairment charges recorded in the income statement.

Valuation of mineral properties – The Company carries the acquisition costs of its mineral properties at cost less any provision for impairment. The Company undertakes a periodic review of the carrying values of mineral properties and whenever events or changes in circumstances indicate that their carrying values may exceed their fair value. In undertaking this review, management of the Company is required to make significant judgments. These judgments are subject to various risks and uncertainties, which may ultimately have an effect on the expected recoverability of the carrying values of the mineral properties and related expenditures.

Stock based compensation – The fair value of stock options is determined using the Black-Scholes option pricing model and are expensed over their vesting periods. In estimating fair value, management of the Company is required to make certain assumptions and estimates regarding the life of the options, volatility and forfeitures rates. Changes in the assumptions used could result in materially different results.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Decommissioning and site restoration – The Company has obligations for site restoration and decommissioning related to its diamond properties. The future obligations for decommissioning and site restoration activities are estimated by the Company using mine closure plans or other similar studies which outline the requirements that will be carried out to meet the obligations. Because the obligations are dependent on the laws and regulations of the countries in which the mines operate, the requirements could change as a result of amendments in the laws and regulations relating to environmental protection and other legislation affecting resource companies. As the estimate of obligations is based on future expectations, a number of assumptions and judgments are made by management in the determination of closure provisions. The decommissioning and site restoration provisions are more uncertain the further into the future the mine closure activities are to be carried out.

The Company's policy for recording decommissioning and site restoration provisions is to establish provisions for future mine closure costs at the commencement of mining operations based on the present value of the future cash flows required to satisfy the obligations. The amount of the present value of the provision is added to the cost of the related mining assets and depreciated over the life of the mine. The provision is accreted to its future value over the life of the mine through a charge to operating costs. Actual results could differ from estimates made by management during the preparation of these consolidated financial statements and those differences may be material.

(d) Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the person that makes strategic decisions. The CEO is deemed the chief operating decision-maker of the Company.

The Company's primary reporting segments are based on individual diamond properties, being the Karowe Mine and the Mothae Diamond Project and Corporate. The Corporate office provides support to the diamond properties with respect to sales, treasury and finance, technical support, regulatory reporting and corporate administration.

(e) Foreign currency translation

Functional and presentation currency

Items included in the financial statements of each of the Company's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in U.S. dollars. The functional currency of the parent company, Lucara Diamond Corp., is the Canadian dollar.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at exchange rates of monetary assets and liabilities denominated in currencies other than an entity's functional currency are recognized in the statement of operations.

Group companies

The functional currency of the significant subsidiaries of the Company are Boteti Mining (PTY) Ltd., which has a Pula functional currency and Mothae Diamonds (Pty) Ltd, which has a Loti functional currency. The results and financial position of the group companies, which have a functional currency different from the presentation currency, are translated into the presentation currency as follows:

(i) Assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet
(ii) Income and expenses for each statement of operation are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the rate on the dates of the transactions).
(iii) All resulting exchange differences are recognized in other comprehensive income as cumulative translation adjustments.

(f) Cash and cash equivalents

Cash and cash equivalents include cash on hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less.

(g) Financial instruments

Financial assets and liabilities are recognized when the Company becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership. Financial liabilities are derecognized when the obligation specified in the contract is discharged, cancelled or expires.

At initial recognition, the Company classifies its financial instruments in the following categories:

(i) Financial assets and liabilities at fair value through profit or loss: A financial asset or liability is classified in this category if acquired principally for the purpose of selling or repurchasing in the short-term. Derivatives are also included in this category unless they are designated as hedges.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments in this category are recognized initially and subsequently at fair value. Transaction costs are expensed in the consolidated statement of operations. Gains and losses arising from changes in fair value are presented in the consolidated statement of operations within "other gains and losses" in the period in which they arise. Non-derivative financial assets and liabilities at fair value through profit or loss are classified as current except for the portion expected to be realized or paid beyond twelve months of the balance sheet date, which are classified as non-current.

(ii) Available-for-sale investments: Available-for-sale investments are non-derivatives that are either designated in this category or not classified in any of the other categories.

Available-for-sale investments are recognized initially at fair value plus transaction costs and are subsequently carried at fair value. Gains or losses arising from re-measurement are recognized in other comprehensive income. When an available-for-sale investment is sold or impaired, the accumulated gains or losses are moved from accumulated other comprehensive income to the statement of operations and are included in "other gains and losses". Available-for-sale investments are classified as non-current, unless an investment matures within twelve months, or management expects to dispose of it within twelve months.

(iii) Loans and receivables: Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The Company's loans and receivables comprise cash and trade receivables and are included in current assets due to their short-term nature. Loans and receivables are initially recognized at the amount expected to be received, less, when material, a discount to reduce the loans and receivables to fair value. Subsequently, loans and receivables are measured at amortized cost using the effective interest method less a provision for impairment.

(iv) Financial liabilities at amortized cost: Financial liabilities at amortized cost include trade payables. Trade payables are initially recognized at the amount required to be paid, less, when material, a discount to reduce the payables to fair value. Subsequently, trade payables are measured at amortized cost using the effective interest method.

Impairment of financial assets

At each reporting date, the Company assesses whether there is objective evidence that a financial asset (other than a financial asset classified as fair value through profit or loss) is impaired.

The criteria used to determine if objective evidence of an impairment loss exists include:

(i) significant financial difficulty of the obligor;
(ii) delinquencies in interest or principal payments; and
(iii) it becomes probable that the borrower will enter bankruptcy or other financial reorganization.

For equity securities, a significant or prolonged decline in the fair value of the security below its cost is also evidence that the assets are impaired.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

If such evidence exists, the Company recognizes an impairment loss, as follows:

(i) Financial assets carried at amortized cost: The loss is the difference between the amortized cost of the loan or receivable and the present value of the estimated future cash flows, discounted using the instrument's original effective interest rate. The carrying amount of the asset is reduced by this amount either directly or indirectly through the use of an allowance account.

(ii) Available-for-sale financial assets: The impairment loss is the difference between the original cost of the asset and its fair value at the measurement date, less any impairment losses previously recognized in the statement of operations. This amount represents the loss in accumulated other comprehensive income that is reclassified to net loss.

Impairment losses on financial assets carried at amortized cost and available-for-sale debt instruments are reversed in subsequent periods if the amount of the loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized. Impairment losses on available-for-sale equity instruments are not reversed.

(h) Inventories

Inventories, which include rough diamonds, ore stockpile and parts and supplies, are measured at the lower of cost and net realizable value. The amount of any write-down of inventories to net realizable value and all losses, are recognized in the period the write-down of loss occurs. Cost is determined using the weighted average method. Cost includes directly attributable mining overhead but excludes borrowing costs.

Net realizable value represents the estimated selling price in the ordinary course of business, less all estimated costs to completion and selling expenses.

(i) Plant and equipment

Plant and equipment are stated at cost less accumulated depreciation and impairment losses. The cost of an asset consists of its purchase price, any directly attributable costs of bringing the asset to its present working condition and location for its intended use and an initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located.

Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably.

Depreciation of each asset is calculated using the straight line or unit of production method to allocate its cost less its residual value over its estimated useful life. The estimated useful lives of plant and equipment are as follows:

Machinery	5 to 10 years
Plant facilities	based on resources on a unit of production basis
Furniture and office equipment	2 to 3 years

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognized within "other gains and losses" in the statement of operations.

(j) Exploration and evaluation expenditures and mineral properties

Exploration and evaluation expenditures relate to the search for mineral resources, the determination of technical feasibility and the assessment of commercial viability of an identified resource. Exploration and evaluation activities include:

- Researching and analyzing historical exploration data;
- Gathering exploration data through topographical, geochemical and geophysical studies;
- Exploratory drilling, trenching and sampling;
- Determining and examining the volume and grade of the resource; and
- Surveying, transportation and infrastructure requirement

Exploration and development expenditures are expensed as incurred on mineral properties not sufficiently advanced as to identify their development potential. When it has been established that a mineral property is considered to be sufficiently advanced and an economic analysis has been completed, all further expenditures for the current year and subsequent years are capitalized as incurred. Costs associated with acquiring a mineral property are capitalized as incurred.

(l) Impairment of non-financial assets

Long lived assets are reviewed for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(m) Provisions

Asset retirement obligations

The Company recognizes a liability for an asset retirement obligation on long-lived assets when a present legal or constructive obligation exists, as a result of past events and the amount of the liability is reasonably determinable. Asset retirement obligations are initially recognized and recorded as a liability based on estimated future cash flows discounted at a risk free rate. This is adjusted at each reporting period for changes to factors including the expected amount of cash flows required to discharge the liability, the timing of such cash flows and the risk free discount rate. Corresponding amounts and adjustments are added to the carrying value of the related long-lived asset and amortized or depleted to operations over the life of the related asset.

Environmental expenditures

Environmental expenditures that relate to current operations are expensed or capitalized as appropriate. Expenditures that relate to an existing condition caused by past operations and which do not contribute to current or future revenue generation are expensed. Liabilities are recorded when environmental assessments and/or remedial efforts are probable, and the costs can be reasonably estimated.

Other provisions

Provisions are recognized when:

- the Company has a present legal or constructive obligation as a result of a past event;
- a reliable estimate can be made of the obligation.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation, using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to the passage of time is recognized as finance costs.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(n) Deferred income taxes

Deferred tax is recognized using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized for the following temporary differences: the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable income, and differences relating to investments in subsidiaries and jointly controlled entities to the extent that it is probable that they will not reverse in the foreseeable future. In addition, deferred tax is not recognized for taxable temporary differences arising on the initial recognition of goodwill.

Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the year end.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities where there is a legal right to do so, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized to the extent that it is probable that future tax profits will be available against which the temporary difference can be utilized. Deferred tax assets are reviewed at each year end and are reduced to extent that is no longer probable that the related tax benefit will be realized.

(o) Share capital

Common shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

(p) Revenue recognition

Revenues from diamond sales are recognized when the risks and rewards of ownership pass to the customer, which is when proceeds are received and title is transferred to the purchaser.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(q) Royalties

Royalties and revenue-based taxes are accounted for under IAS 12 when they have the characteristics of income tax. This is considered to be the case when they are imposed under Government authority and the amount payable is based on taxable income – rather than based on quantity produced or as a percentage of revenue. For such arrangements, current and deferred tax is provided on the same basis as described above for other forms of taxation. Obligations arising from royalty arrangements that do not satisfy these criteria are recognized as current provisions and disclosed as part of royalty expenses. The royalties incurred by the Company are considered not to meet the criteria to be treated as part of income tax.

(r) Stock-based compensation

The Company has a stock-based compensation plan, under which the entity receives services from employees and non-employees as consideration for equity instruments (options) of the Company.

Stock options granted to employees are measured on the grant date. Stock options granted to non-employees are measured on the date that the goods or services are received.

The fair value of the employee and non-employee services received in exchange for the grant of the options is recognized as an expense. The total amount to be expensed is determined by reference to the fair value of the options granted and the vesting periods. The total expense is recognized over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied.

The cash subscribed for the shares issued when the options are exercised is credited to share capital, net of any directly attributable transaction costs.

(s) Income per share

Income per share is calculated by dividing the income attributable to the shareholders of the Company by the weighted average number of common shares issued and outstanding during the year. Diluted income per share is calculated using the treasury stock method.

(t) Leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the statement of operations on a straight-line basis over the period of the lease.

(u) Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset are capitalized as part of the cost of that asset. Other borrowing costs not directly attributable to a qualifying asset are expensed in the period incurred.

4. ADOPTION OF NEW IFRS PRONOUNCEMENTS

As of January 1, 2014, the Company adopted the new and amended IFRS pronouncements in accordance with the transitional provisions outlined in the respective standards as listed below.

a) *Pronouncement affecting financial statement presentation or disclosures*

IFRIC 21 provides accounting guidance for an obligation to pay a levy, if that liability is within the scope of IAS 37, Provisions, Contingent Liabilities and Contingent Assets. Levies are imposed by governments in accordance with legislation and do not include income taxes. The interpretation addresses the diversity in practice of when the liability to pay a levy is recognized.

IFRIC 21 defines an obligating event as the activity that triggers the payment of the levy, as identified by legislation. A liability to pay a levy is recognized at the date of the obligating event, which may be at a point in time or over a period of time. The fact that an entity is economically compelled to continue to operate in the future, or prepares its financial statements on a going concern basis, does not create an obligation to pay a levy that will arise in a future period as a result of continuing to operate.

The adoption of IFRIC 21 did not affect the Company's financial results or disclosures.

b) *Pronouncements issued but not yet effective*

New IFRS pronouncements that have been issued but are not yet effective are listed below. The Company plans to apply the new standards or interpretations in the annual period for which it is first required.

IFRS 15 - Revenue from Contracts with Customers

The new revenue standard introduces a single, principles based, five-step model for the recognition of revenue when control of a good or service is transferred to the customer. The five steps are: identify the contract(s) with the customer, identify the performance obligations in the contract, determine transaction price, allocate the transaction price and recognize revenue when a performance obligation is satisfied. IFRS 15 also requires enhanced disclosures about revenue to help investors better understand the nature, amount, timing and uncertainty of revenue and cash flows from contracts with customers and improves the comparability of revenue from contracts with customers.

IFRS 15 will be effective for annual periods beginning on or after January 1, 2017, with early adoption permitted. The Company is currently assessing the effect of this standard on our financial statements.

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

4. ADOPTION OF NEW IFRS PRONOUNCEMENTS (continued)

IFRS 9 - Financial Instruments

IFRS 9, Financial Instruments addresses the classification, measurement and recognition of financial assets and financial liabilities. IFRS 9 requires financial assets to be classified into three measurement categories on initial recognition: those measured at fair value through profit and loss, those measured at fair value through other comprehensive income and those measured at amortized cost. Investments in equity instruments are required to be measured by default at fair value through profit or loss. However, there is an irrevocable option to present fair value changes in other comprehensive income. Measurement and classification of financial assets is dependent on the entity's business model for managing the financial assets and the contractual cash flow characteristics of the financial asset.

IFRS 9 introduces a new three-stage expected credit loss model for calculating impairment for financial assets. IFRS 9 no longer requires a triggering event to have occurred before credit losses are recognized. An entity is required to recognize expected credit losses when financial instruments are initially recognized and to update the amount of expected credit losses recognized at each reporting date to reflect changes in the credit risk of the financial instruments. In addition, IFRS 9 requires additional disclosure requirements about expected credit losses and credit risk.

The completed version of IFRS 9 is effective for annual periods beginning on or after January 1, 2018, with early adoption permitted. The Company is currently assessing the effect of this standard and its related amendments on our financial statements.

5. IMPAIRMENT OF MOTHAE PROJECT

During the year ended December 31, 2014, the Company concluded that the Mothae project in Lesotho did not meet the Company's investment criteria. The Company's decision to cease development resulted in a charge of $18.8 million, which is included in other expenses and reflects a write-down of the Company's carrying value of the Mothae project. The Company also recorded a $2.4 million restoration charge to increase its Mothae closure cost provisions to $2.9 million and classified the resulting restoration obligation as a current liability based upon the planned timing of these expenditures (Note 10).

6. VAT RECEIVABLES AND OTHER

	2014	**2013**
VAT	$ 2,712	$ 2,694
Other	1,335	233
Prepayments	970	666
	$ 5,017	$ 3,593

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

7. INVENTORIES

	2014	2013
Rough diamonds	$ 11,703	$ 9,026
Ore stockpile	13,849	6,674
Parts and supplies	6,467	5,432
	$ 32,019	$ 21,132

Inventory expensed during the year ended December 31, 2014 totaled $47.2 million (2013 – $43.8 million).

8. PLANT AND EQUIPMENT

Cost	**Construction in progress**	**Mine and plant facilities**	**Vehicles**	**Furniture and office equipment**	**Total**
Balance, January 1, 2013	$ -	$ 126,430	$ 1,542	$ 2,361	$ 130,333
Additions	-	5,212	100	293	5,605
Disposals and other	-	(964)	(36)	334	(666)
Translation differences	-	(14,748)	(187)	(281)	(15,216)
Balance, December 31, 2013	-	115,930	1,419	2,707	120,056
Additions	41,154	245	228	372	41,999
Disposals and other	-	-	(19)	-	(19)
Impairment (Note 5)	-	(5,171)	(111)	(106)	(5,388)
Translation differences	(2,473)	(9,277)	(123)	(238)	(12,111)
Balance, December 31, 2014	$ 38,681	$ 101,727	$ 1,394	$ 2,735	$ 144,537
Accumulated depreciation					
Balance, January 1, 2013	$ -	$ 10,752	$ 598	$ 588	$ 11,938
Depletion, amortization and accretion for the year	-	8,515	382	619	9,516
Disposals and other	-	(33)	(35)	12	(56)
Translation differences	-	(2,042)	(90)	(96)	(2,228)
Balance, December 31, 2013	-	17,192	855	1,123	19,170
Depletion, amortization and accretion for the year	-	9,170	388	628	10,186
Disposals and other	-	-	(13)	-	(13)
Impairment (Note 5)	-	(4,746)	(75)	(74)	(4,895)
Translation differences	-	(1,713)	(89)	(125)	(1,927)
Balance, December 31, 2014	$ -	$ 19,903	$ 1,066	$ 1,552	$ 22,521
Net book value					
As at December 31, 2013	$ -	$ 98,738	$ 564	$ 1,584	$ 100,886
As at December 31, 2014	$ 38,681	$ 81,824	$ 328	$ 1,183	$ 122,016

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

9. MINERAL PROPERTIES

Cost		Capitalized production stripping asset		Karowe Mine		Mothae Diamond		Mothae mining license		Total
Balance, January 1, 2013	$	-	$	65,504	$	17,688	$	3,177	$	86,369
Additions		-		2,324		-		-		2,324
Disposals and other		-		(500)		(74)		-		(574)
Translation differences		-		(7,459)		(1,773)		(609)		(9,841)
Balance, December 31, 2013		-		59,869		15,841		2,568		78,278
Additions		6,162		1,881		-		-		8,043
Impairment (Note 5)		-		-		(15,502)		(2,487)		(17,989)
Translation differences		(370)		(5,040)		(339)		(81)		(5,830)
Balance, December 31, 2014	$	5,792	$	56,710	$	-	$	-	$	62,502
Accumulated depletion										
Balance, January 1, 2013	$	-	$	1,724	$	-	$	-	$	1,724
Depletion for the year		-		4,896		-		-		4,896
Translation differences		-		(403)		-		-		(403)
Balance, December 31, 2013		-		6,217		-		-		6,217
Depletion for the year		213		4,116		-		-		4,329
Translation differences		(13)		(760)		-		-		(773)
Balance, December 31, 2014	$	200	$	9,573	$	-	$		$	9,773
Net book value										
As at December 31, 2013	$	-	$	53,652	$	15,841	$	2,568	$	72,061
As at December 31, 2014	$	5,592	$	47,137	$	-	$	-	$	52,729

a) *Karowe Mine*

A royalty of 10% of the sales value of diamonds produced from Karowe is payable to the government of Botswana. During the year, the Company had a royalty expense of $26.6 million. (2013: $18.1 million)

b) *Mothae Diamond Project*

Pursuant to the terms of the mining agreement, Mothae Diamonds, an indirect 75% owned subsidiary of the Company has a 100% interest in the project. The remaining 25% of Mothae Diamonds is held by the Government of Lesotho (Note 13). One half of the project interest held by the Government is a free carried interest and one half is funded by the Government through its share of project dividends.

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

10. RESTORATION PROVISIONS

The Company's restoration provisions relate to the rehabilitation of its diamond properties. The provisions have been calculated based on total estimated rehabilitation costs and discounted back to their present values. The pre-tax discount rates and inflation rates are adjusted annually and reflect current market assessments. The Company has applied a pre-tax discount rate of 8.4% at December 31, 2014 (10.8% at December 31, 2013) and an inflation rate of 5.3% at December 31, 2014 (5.8% at December 31, 2013) at the Karowe Mine project. The Karowe rehabilitation costs are expected to be incurred in the year 2022. The Company's decision to divest Mothae resulted in a present value accretion and a re-estimation of the Mothae restoration provision (Note 5). The Mothae rehabilitation costs are expected to be incurred in 2015. The estimated total liability for reclamation and remediation costs on an undiscounted basis is approximately $23.0 million (December 31, 2013 - $21.9 million).

		2014		2013
Balance, beginning of year	$	14,515	$	12,242
Revision to provisions		2,415		-
Changes due to discount rate changes		1,881		2,250
Accretion of liability component of obligation		1,484		1,628
Foreign currency translation adjustment		(1,536)		(1,605)
Balance, end of year		18,759		14,515
Less: Current portion		2,857		-
Long-term portion of restoration provisions	$	15,902	$	14,515

11. SHARE CAPITAL

The authorized share capital consists of an unlimited number of common shares, with no par value.

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

12. STOCK OPTIONS

The Company has one rolling stock option plan (the "Plan") approved by the shareholders of the Company on May 13, 2011 which reserves an aggregate of 10% of the issued and outstanding shares of the Company for issuance upon the exercise of options granted. Vesting and terms of the option agreement are at the discretion of the Board of Directors.

Movements in the number of stock options outstanding and their related weighted average exercise prices are as follows:

	Number of shares issuable pursuant to stock options		Weighted average exercise price per share (CA$)
Balance at December 31, 2012	**2,665,000**	**$**	**0.88**
Granted	2,775,000		0.72
Forfeited	(50,000)		1.03
Expired	(575,000)		0.91
Exercised	(606,666)		0.92
Balance at December 31, 2013	**4,208,334**		**0.76**
Granted	300,000		2.11
Exercised(1)	(2,469,664)		0.80
Balance at December 31, 2014	**2,038,670**	**$**	**0.92**

(1) The weighted average share price on the exercise dates for the 2014 stock option exercises was CA$2.20.

Options to acquire common shares have been granted and are outstanding at December 31, 2014 as follows:

	Outstanding Options				**Exercisable Options**			
Range of exercise prices CA$	Number of options outstanding	Weighted average remaining contractual life (years)		Weighted average exercise price CA$	Number of options exercisable	Weighted average remaining contractual life (years)		Weighted average exercise price CA$
$0.61 - $0.70	1,638,670	1.3973	$	0.70	763,643	1.3973	$	0.70
$0.71 - $1.00	100,000	1.6795		0.99	50,000	1.6795		0.99
$1.01 - $2.25	300,000	2.3822		2.11	100,000	2.3822		2.11
	2,038,670	1.5560	$	0.92	913,641	1.5205	$	0.87

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

12. STOCK OPTIONS (continued)

During the year ended December 31, 2014, an amount of $0.3 million (2013 – $0.5 million) was charged to operations in recognition of stock-based compensation expense, based on the vesting schedule for the options granted.

The fair value of each option granted is estimated on the date of grant using the Black-Scholes option pricing model with weighted average assumptions and resulting values for grants as follows:

	2014	**2013**
Assumptions:		
Risk-free interest rate *(%)*	1.03	1.00
Expected life *(years)*	3.00	3.00
Expected volatility *(%)*	51.00	52.85
Expected dividend	CA$0.02/share semi annually	Nil
Results:		
Weighted average fair value of options granted *(per option)*	$ 0.68	$ 0.25

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

13. PRINCIPAL SUBSIDIARIES

The Company had the following subsidiaries at December 31, 2014:

Name	Country of incorporation and place of business	Nature of business	Proportion of shares directly held by the Company (%)	Proportion of shares held by the group (%)	Proportion of shares held by non-controlling interests (%)
African Diamonds Ltd.	UK	Intermediate holding company	100	-	-
Lucara Management Services Ltd.	UK	Intermediate services company	100	-	-
Lucara Diamond Holdings (I) Inc.	Mauritius	Intermediate holding company	100	-	-
Mothae Diamond Holdings Inc.	Mauritius	Intermediate holding company	-	100	-
Boteti Diamond Holdings Inc.	Mauritius	Intermediate holding company	-	100	-
Lucara Diamond South Africa (Pty) Ltd.	South Africa	Intermediate holding company	-	100	-
Wati Ventures (Pty) Ltd.	Botswana	Intermediate holding company	-	100	-
Debwat Exploration (Pty) Ltd.	Botswana	Intermediate holding company	-	100	-
Boteti Mining (Pty) Ltd.	Botswana	Mining of diamonds	-	100	-
Mothae Diamonds (Pty) Ltd.	Lesotho	Exploration of diamond properties	-	75	25

All subsidiary undertakings are included in the consolidation. The proportion of the voting rights in the subsidiary undertakings held directly by the parent company do not differ from the proportion of ordinary shares held.

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

13. PRINCIPAL SUBSIDIARIES (continued)

The total non-controlling interest at December 31, 2014 is $14 thousand (2013 - $1.5 million).

As consideration for acquiring a mining license from the Government of Lesotho ("GOL"), the Company issued the GOL 25% ownership in Mothae Diamonds (Pty) Ltd. ("Mothae Diamonds"). One half of the interest held by the GOL is a free-carried interest and the other 12.5% will ultimately be paid for by the GOL through its share of future dividends paid by Mothae Diamonds, if any.

The GOL's equity interest must be kept at 25% and cannot be diluted by further equity issuances. As such, the 12.5% free-carried interest portion of the Company's capital contributions into Mothae Diamonds is accounted for as an equity transaction between shareholders.

Set out below is the summarized financial information for Mothae Diamonds.

Summarized balance sheet

		2014		2013
CURRENT				
Assets	$	115	$	890
Liabilities		(38)		(77)
		77		813
NON-CURRENT				
Assets		-		8,953
Liabilities		(3,478)		(608)
		(3,478)		8,345
NET ASSETS (LIABILITIES)	$	(3,401)	$	9,158

Summarized statement of operations

		2014		2013
Revenue	$	-	$	-
Depreciation		-		-
Loss from operations		(12,379)		(758)
Other comprehensive loss		(90)		(2,174)
Comprehensive loss		(12,469)		(2,932)
Attributable to non-controlling interests		(1,559)		(367)
Dividends paid to non-controlling interests		-		-

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

13. PRINCIPAL SUBSIDIARIES (continued)

Summarized statement of cash flows

		2014		2013
Cash used in operating activities	$	(1,161)	$	(538)
Cash generated from financing activities		910		742
Cash generated from (used in) investing activities		(26)		54
Effect of exchange rate on cash		50		(46)
Net increase (decrease) in cash		(227)		212
Cash, beginning of year		340		128
Cash, end of year		113		340

The information above is the amount before inter-company eliminations.

14. EXPLORATION EXPENDITURES

		2014		2013
Resource development	$	170	$	-
Office and other		578		849
Care and maintenance		449		474
	$	1,197	$	1,323

15. ADMINISTRATION

		2014		2013
Salaries and benefits	$	5,822	$	5,275
Professional fees		1,972		1,490
Office and general		1,904		1,313
Travel		945		894
Stock exchange, transfer agent, shareholder communication		668		775
Stock based compensation		332		517
Management fees		457		489
Depreciation		447		423
Donations		227		253
	$	12,774	$	11,429

16. FINANCE INCOME

The Company generated $0.8 million in interest income during 2014 from its cash and cash equivalents holdings. In 2013, the Company had incurred $3.8 million in interest expenses from its debenture financing which was fully repaid in 2013.

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

17. INCOME TAXES

		2014		**2013**
Current	$	41,589	$	96
Deferred		31,692		14,895
Income tax expense	$	73,281	$	14,991

Income tax expense differs from the amount that would result from applying the Canadian federal and provincial income tax rates to net income before tax. These differences result from the following items:

		2014		**2013**
Basic statutory tax rate		26.00%		25.75%
Net income before tax		119,021		80,213
Computed income tax expense		30,945		20,655
Differences between Canadian and foreign tax rates		(6,819)		(3,962)
Non-deductible expenses and other permanent differences		4,493		1,331
Current tax effect of Botswana variable tax rate in excess of Botswana standard tax rate		18,534		-
Deferred tax effect of Botswana variable tax rate in excess of Botswana standard tax rate		15,717		-
Change in deferred tax rates		-		(376)
Benefits from previously unrecognized tax benefits		-		(8,458)
Change in deferred benefits not recognized		3,961		4,461
Exchange rate differences		5,772		1,144
Other		678		196
	$	73,281	$	14,991

The Company is subject to a variable tax rate in Botswana based on a profit and revenue ratio which increases as profit as a percentage of revenue increases. The lowest variable tax rate is 22% while the highest variable tax rate is 55% only if taxable income were equal to revenue. The Company has estimated the variable tax rate for the deferred income taxes following the updated Karowe 43-101 technical report and current financial performance. The Company recorded a deferred tax liability during the year, which resulted in a corresponding non-cash deferred income tax expense of $32.0 million.

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

17. INCOME TAXES (continued)

The movement in deferred tax liabilities during the year, without taking into consideration the offsetting balances within the same tax jurisdiction, is as follows:

		2014		2013
Balance, beginning of year	$	14,258	$	-
Deferred income tax expense		31,692		14,895
Foreign currency translation adjustment		(2,304)		(637)
Balance, end of year	$	43,646	$	14,258

Deferred income tax assets and liabilities recognized		**2014**		**2013**
Deferred income tax assets				
Non-capital losses	$	590	$	7,659
Restoration provisions		5,467		3,060
Total deferred income tax assets		6,057		10,719
Deferred income tax liabilities				
Mineral properties, plant and equipment		47,283		24,751
Other		2,420		226
Deferred income tax liabilities		49,703		24,977
Deferred income tax liabilities, net	$	43,646	$	14,258

Deferred income tax assets not recognized		**2014**		**2013**
Tax losses	$	20,305	$	19,229
Mineral property, plant and equipment		2,104		58
Other deductible temporary differences		484		1,045
	$	22,893	$	20,332

As at December 31, 2014, the Company has non-capital losses for income tax purposes which expire as follows:

		2015		2016		2017		Subsequent to 2018		No expiry date		Total
Canada	$	-	$	-	$	-	$	47,969	$	-	$	47,969
United Kingdom		-		-		-		-		5,832		5,832
Lesotho		-		-		-		-		21,475		21,475
	$	-	$	-	$	-	$	47,969	$	27,307	$	75,276

No tax benefit has been recorded for the Canadian, United Kingdom and Lesotho non-capital losses.

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

18. INCOME PER COMMON SHARE

a) Basic

Basic earnings per common share are calculated by dividing the net income attributable to the shareholders of the Company by the weighted average number of common shares outstanding during the year:

	2014	2013
Income for the year – attributable to Shareholders of the Company	$ 47,317	$ 65,317
Weighted average number of common shares outstanding	378,198,299	376,392,625
	$ 0.13	$ 0.17

b) Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of common shares outstanding to assume conversion of all dilutive potential common shares. For stock options, a calculation is done to determine the number of shares that could have been acquired at fair value (determined as the average market share price of the Company's outstanding shares for the year), based on the exercise prices attached to the stock options. The number of shares calculated above is compared with the number of shares that would have been issued assuming the exercise of stock options.

	2014	2013
Income for the year – attributable to Shareholders of the Company	$ 47,317	$ 65,317
Weighted average number of common shares outstanding	378,198,299	376,392,625
Adjustment for stock options	1,812,970	120,365
Weighted average number of common shares for diluted earnings per share	380,011,269	376,512,990
	$ 0.13	$ 0.17

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

19. RELATED PARTY TRANSACTIONS

a) Key management compensation

Key management personnel are those persons having the authority and responsibility for planning, directing and controlling the activities of the Company, directly or indirectly. Key management personnel include the Company's executive officers, vice-presidents and members of its Board of Directors.

The remuneration of key management personnel were as follows:

		2014		2013
Salaries and wages	$	3,058	$	2,142
Short term benefits		77		49
Stock based compensation		239		402
	$	3,374	$	2,593

b) Other related parties

For the year ended December 31, 2014, the Company paid $0.5 million, (2013 ☐ $0.5 million) for services provided by a company associated with the Chairman of the Company. The Company also paid $0.2 million for the year ended December 31, 2014 (2013 ☐ $0.3 million) to a charitable foundation directed by members of the Company's directors to carry out social programs on behalf of the Company.

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

20. SEGMENT INFORMATION

The Company's primary business activity is the development and operation of diamond properties in Africa. The Company has three operating segments: Karowe Mine, Mothae Diamond Project and Corporate and other.

2014

	Karowe Mine	Mothae Diamond Project	Corporate and other	Total
Revenues	$ 265,504	$ -	$ -	$ 265,504
Income from mining operations	177,331	-	(227)	177,104
Exploration expenditures	-	(1,197)	-	(1,197)
Finance income (expenses)	1,298	-	(485)	813
Other expenses	(5,016)	(4)	(31,481)	(36,501)
Taxes	(73,281)	-	-	(73,281)
Restoration and Impairment charges	-	(21,198)	-	(21,198)
Net income (loss) for the year	100,332	(22,399)	(32,193)	45,740
Capital expenditures	(42,190)	(22)	(59)	(42,271)
Total assets	306,668	115	10,242	317,025

2013

	Karowe Mine	Mothae Diamond Project	Corporate and other	Total
Revenues	$ 180,507	$ -	$ -	$ 180,507
Income from mining operations	103,899	-	(257)	103,642
Exploration expenditures	-	(1,323)	-	(1,323)
Gain on sale of exploration program diamonds	-	584	-	584
Finance income (expenses)	96	(67)	(3,814)	(3,785)
Other income (expenses)	(4,836)	48	(14,117)	(18,905)
Taxes	(14,991)	-	-	(14,991)
Net income (loss) for the year	84,168	(758)	(18,188)	65,222
Capital expenditures	(7,822)	-	(43)	(7,865)
Total assets	222,031	19,845	5,312	247,188

The geographic distribution of non-current assets is as follows:

	Plant and equipment		Mineral properties		Other	
	2014	2013	2014	2013	2014	2013
Canada	$ 127	$ 142	$ -	$ -	$ 202	$ -
Lesotho	-	486	-	18,408	-	62
Botswana	121,889	100,258	52,729	53,653	4,147	-
	$ 122,016	$ 100,886	$ 52,729	$ 72,061	$ 4,349	$ 62

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

21. FINANCIAL INSTRUMENTS

a) *Measurement categories and fair values*

As explained in Note 3, financial assets and liabilities have been classified into categories that determine their basis of measurement and, for items measured at fair value, whether changes in fair value are recognized in the consolidated statements of operations or consolidated statements of comprehensive loss. Those categories are: fair value through profit or loss; loans and receivables; available for sale assets; and, for liabilities, amortized cost.

The fair value of the Company's available for sale financial instruments is derived from quoted prices in active markets for identical assets. The fair value of the Company's long-term debt approximates their carrying amounts due to the fact that there have been no significant changes in the Company's own credit risk. The fair value of all other financial instruments of the Company approximates their carrying values because of the demand nature or short-term maturity of these instruments.

The Company's financial assets and liabilities are categorized as follows:

		December 31, 2014		December 31, 2013
ASSETS				
Loans and receivables				
Cash and cash equivalents	$	100,839	$	49,364
Other receivables		445		233
	$	101,284	$	49,597
Available for sale				
Investments		56		90
	$	56	$	90
LIABILITIES				
Amortized cost				
Trade payables and accrued liabilities	$	12,384	$	15,491
	$	12,384	$	15,491

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

21. FINANCIAL INSTRUMENTS (continued)

b) Fair value hierarchy

The following table classifies financial assets and liabilities that are recognized on the balance sheet at fair value in a hierarchy that is based on significance of the inputs used in making the measurements. The levels in the hierarchy are:

Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities
Level 2 - Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices)
Level 3 - Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs).

	December 31, 2014	December 31, 2013
Level 1		
Investments	$ 56	$ 90
Level 2 and Level 3 – N/A		

c) Financial risk management

The Company's financial instruments are exposed to certain financial risks, including commodity price, currency, credit, liquidity and price risks.

Commodity price risk

The Company is subject to commodity price risk. Diamonds are not a homogenous product and the price of rough diamonds is not monitored on a public index system. The fluctuation of prices is related to certain features of diamonds such as quality and size. Diamond prices are marketed in U.S. dollars and long term U.S. dollar per carat prices are based on external market consensus forecasts. The Company does not have any financial instruments that may fluctuate as a result of commodity price movements.

Currency risk

The Company is exposed to the financial risk related to fluctuating foreign exchange rates. All sales revenues are denominated in U.S. dollars, while directly related costs are denominated in Botswana Pula. At December 31, 2014, the Company is exposed to currency risk relating to U.S. dollar cash held within the Company. Based on this exposure, a 10% change in the U.S. dollar exchange rate would give rise to an increase/decrease of approximately $4.7 million in net income for the year.

(All amounts expressed in thousands of U.S. Dollars, unless otherwise indicated.)

21. FINANCIAL INSTRUMENTS (continued)

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. The majority of the Company's cash and cash equivalents is held through a large Canadian financial institution with a high investment grade rating. Considering the nature of the Company's ultimate customers and the relevant terms and conditions entered into with such customers, the Company believes that credit risk is limited as customers pay on receipt of goods.

The carrying amount of financial assets recorded in the financial statements, net of any allowance for losses, represents the Company's maximum exposure to credit risk.

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. Cash flow forecasting is performed in the operating entities of the Company and aggregated in head office which monitors rolling forecasts of the Company's liquidity requirements to ensure it has sufficient cash to meet operational needs at all times. Such forecasting takes into consideration the Company's debt financing plans.

The Company's estimated minimum contractual undiscounted cash flow requirements for financial liabilities were:

December 31, 2014	**Less than 3 months**	**3 months to 1 year**	**2-5 years**	**Over 5 years**
Trade payables and accrued liabilities	$ 12,384	$ -	$ -	$ -

December 31, 2013	**Less than 3 months**	**3 months to 1 year**	**2-5 years**	**Over 5 years**
Trade payables and accrued liabilities	$ 15,491	$ -	$ -	$ -

Guarantee

As part of the Company's environmental obligation related to the Karowe Mine, the Government of Botswana required a reclamation bond for the Mine. On July 1, 2014, Standard Chartered Bank Botswana Limited has provided Boteti Mining (Pty) Ltd, a wholly owned subsidiary, with a reclamation bond of Botswana Pula 100.0 million ($10.8 million) with respect to the Karowe Mine. Consequently, the Company has provided a guarantee for a maximum amount of Botswana Pula 80.0 million ($8.6 million) with Standard Chartered Bank Botswana Limited. In addition, the Company has deposited Botswana Pula 20.0 million ($2.2 million) with Standard Chartered Bank Botswana Limited, accounted for in non-current other assets.

21. FINANCIAL INSTRUMENTS (continued)

Revolving credit facility

In May 2014, the Company had renewed its credit facility with the Bank of Nova Scotia. The credit facility was increased to a $50 million revolving term credit facility with a maturity date of May 5, 2017, which may be extended if both parties agree. Funds drawn under the revolving credit facility are due in full at maturity. The facility contains financial and non-financial covenants customary for a facility of this size and nature. As at December 31, 2014, the Company is in compliance with all financial and non-financial covenants. Outstanding amounts under the facility bear interest at LIBOR or an alternative base rate plus an applicable margin based on the Company's leverage ratio.

The Company has provided security on the three year facility by way of a charge over the Company's Karowe assets and a guarantee by the Company's subsidiaries, which hold the Karowe assets.

The Bank of Nova Scotia has first ranking security over the Karowe assets.

As at December 31, 2014, the full amount under this facility was available. As a result, the deferred finance charges have been classified under other assets.

Interest rate risk

The Company's exposure to interest rate risk results from the effects that changes in interest rates may have on the reported value of cash. There is minimal risk that the Company would recognize any loss as a result of a decrease in the fair value of any short-term investments included in cash due to their short-term nature. Based on the balance of cash and cash equivalents at December 31, 2014, and assuming that all other variables remain constant, a 0.25% change in the U.S. prime rate would result in an increase/decrease of $0.3 million in the interest accrued by the Company per annum.

Equity market risk

The Company is exposed to equity price risk arising from its marketable securities, which are classified as available-for-sale.

22. CAPITAL MANAGEMENT

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order to pursue the development of its mineral properties and to maintain a flexible capital structure which optimizes costs of capital at an acceptable risk.

In the management of capital, the Company considers items included in equity attributable to shareholders and its debt facility to be capital.

The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the Company's assets. In order to maintain or adjust the capital structure, the Company may attempt to issue new shares or debt instruments, acquire or dispose of assets, or to bring in joint venture partners.

In order to facilitate the management of its capital requirements, the Company prepares annual expenditures budgets and life-of-mine plans which are updated as necessary depending on various factors, including successful capital deployment and general industry conditions. The annual and updated budgets and life-of-mine plan are approved by the Board of Directors.

23. COMMITMENTS

In conjunction with the building and commissioning of a plant upgrade at the Karowe Mine, the Company has committed to approximately $7.4 million in capital expenditures.

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