

MERCATOR GOLD PLC

ANNUAL REPORT AND ACCOUNTS 2005

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CHAIRMAN'S STATEMENT

It is with pleasure that I report on Mercator Gold plc's inaugural year as an AIM-listed company. Mercator was formed to take advantage of a substantial business opportunity (the Annean joint venture) in the gold-rich Meekatharra region of Western Australia. The company has completed its first resource assessments at Bluebird and Surprise where 467,000 ounces have been outlined. I am pleased to inform you that residual low-grade ounces which our exploration team used as pathfinders have now been substantially upgraded. Total resources of the company stand at 690,100 ounces.

Mercator Gold plc aims to acquire quality ground holdings each of substantial size with potential to host more than two million ounces of gold. The Annean joint venture covers an exciting greenstone region that has historically produced more than 3.5 million ounces of gold, about half of which was produced from within the joint venture tenements, from relatively shallow depths.

The company believes the success in our first year and its anticipated ongoing success stem from the conjunction of geological excellence, focus and commitment, maximising the value of the historic data base and the use of the SpaDiS™ technology developed by Vearncombe & Associates Pty Ltd. Target generation is followed by carefully planned drilling programs, results from which have already lead to the definition of new ore resources. Throughout, the company is geology-focused.

Exploration activities to date have been very successful. In the first eleven months from listing, drill programmes totalling 31,000 metres have defined new and exciting resources at Bluebird and Surprise. These resources are 2 million tonnes @ 4.4 g/t Au for a total of 282,000 ounces. In addition, the company identified another 185,000 ounces of lower grade gold resources, surrounding and adjacent to the high-grade resources, at grades ranging 0.7 to 2 g/t. These finds were made at a cost of less than A\$10 (US\$7, £4.20) per ounce. The new resources are located within 1.5 kilometres of a major 3 million tonne per annum plant owned by our joint venture partner St. Barbara Mines Ltd. In terms of the Annean joint venture agreement the company has earned a 45% stake in the Meekatharra properties. This will increase to 51% in calendar 2005.

The data verification and analysis programme has highlighted the area immediately south of Bluebird, at South Junction, and the Great Northern Highway area (also known as Bluebird East) as the more immediate targets for resource enlargement. In addition to the new resources, exploration continues at Meekatharra North (including Maid Marion and Nottingham with ~7km of strike length), Hawk Hill and Stakewell, all of which are giving positive results at the time of writing.

In the coming year the company intends to:

- » upgrade and enlarge resources
- » assess mining suitability at Bluebird and Surprise
- » focus exploration on the Great Northern Highway and South Junction pits
- » add to initial drilling successes at Stakewell and Hawk Hill
- » aggressively explore and define new and additional open pit resources at Meekatharra North
- » use SpaDiS™ technology to identify targets and define resources
- » continue the process of data validation, target generation and discovery in the Meekatharra area
- » review and assess new projects.

Exploration activity and results are regularly reviewed by our independent geological director. The board of the company meets regularly by tele-conference, avoiding the need for expensive air travel. The company has fully functioning Audit and Remuneration committees. Executive and administrative staff, and their performance are carefully monitored. The company is fully cognizant of the corporate governance codes in the UK and Australia to which it strictly adheres.

We look forward to the next year's activities with a sense of keen anticipation.

Terrence Strapp
Chairman

REVIEW OF OPERATIONS

OBJECTIVES

Mercator Gold plc (MCR) manages the Annean Joint Venture comprising approximately 872km² of a near contiguous tenement package in the Meekatharra area of Western Australia. Historic gold production from the tenement area is approximately 1.5 million ounces of gold in a goldfield of more than 3.5 million ounces production. The main areas of historic gold production within the MCR tenements are Yaloginda with about 1.14Moz extracted and Nannine with about 138,000oz extracted.

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Mercator Gold is focused on acquiring substantial, near contiguous ground holdings deemed to have potential to host multiple, greater than 500,000 ounce orebodies. Orebodies that can be grown to the 500,000 ounce level have the potential to become plus million ounce orebodies in their own right, our ultimate ambition. Mercator has placed emphasis on:

- » achieving context and understanding of field geology (structure, alteration, lithology) to marry with drilling data, geophysics and computer-generated technologies
- » effectively managing, processing and integrating inherited data.

These factors are viewed as integral to successful exploration. Mercator aims to:

- » further enlarge its recently discovered resources at Surprise and Bluebird
- » advance South Junction and Great Northern Highway projects to inferred resource level
- » enlarge and develop the mineralisation at Jess for possible inclusion in the Surprise and Surprise Extended resources
- » advance Maid Marion at Meekatharra North to an initial resource evaluation and upgrade the Nottingham prospect
- » continue regional exploration for more >0.5M ounce resources.

Activities from October 2004 - September 2005 have included:

- » approximately 31,000m of drilling (includes rotary airblast, aircore, reverse circulation and diamond)
- » substantial data validation and verification of historic data
- » detailed geological and structural mapping to aid understanding and provide geological control on resource definition
- » SpaDiS™ analysis giving orientation, dip, plunge, repetition, spacing of ore envelopes, key structures and high-grade zones within ore envelopes
- » excellent and coherent drilling results achieved at Surprise, Bluebird, Jess, Maid Marion including high-grade gold
- » new gold zones discovered at Meekatharra North
- » commissioned initial resource assessment for Bluebird and Surprise
- » drilling in progress at Surprise, Great Northern Highway, South Junction, Stakewell and Hawks Hill.

SpaDiS™

SpaDiS™ is a 3-D computer-based technology used by Mercator for rapid and effective evaluation and location of mineralisation. The technology was developed by Vearncombe & Associates Pty Ltd to effectively analyse spatial data free of bias, statistical and algebraic models. Based on fractal principles the technology uses auto-correlation to compare patterns of mineralisation at all scales from the province to details within an ore shoot.

SpaDiS™ is used to determine mineralisation and orebody shape, direction (strike, dip, plunge), spacing, repetition, grade distribution controls, as well as detail within ore envelopes of high-grade zones, their orientation, dimension and distribution. This provides target zones, enables optimisation and prediction of drilling location, direction and spacing, and depth to target.

At Bluebird, Surprise and Surprise Extended, SpaDiS™ identified correctly:

- » orebody strike, dip, plunge and repetitions
- » flat high-grade gold zones and plunging zones within the plane of the steeply dipping ore envelope
- » the keel of the porphyry bearing high-grade gold at Surprise
- » cross-cutting faults that concentrate mineralisation at Surprise
- » change in orientation of the gold-bearing porphyry and the associated change in gold grade.

This information has assisted in reinterpreting drillhole log and assay information, highlighting key structural features and key mineralised vein orientations during field and pit geological mapping and establishing continuity of mineralisation for ore resource evaluations.

The region demonstrates the unifying geological factors that constitute potential for a gold province comparable to the Norseman-Wiluna belt which hosts the largest gold endowment in Australia including the Golden Mile at Kalgoorlie.

The Meekatharra region has the following features, all favourable for gold mineralisation:

- » A fractal dimension between 1.3 and 1.7 (1.4 for the Norseman-Wiluna belt), supporting potential for new deposits away from existing mines
- » A complex rock-type distribution in which no simple stratigraphy can be deduced
- » Iron-rich (high Fe/(Fe+Mg) ratio) and rheologically competent rocks
- » Heterogeneous brittle-ductile deformation, complex folding and faulting that control the emplacement of mineralisation
- » Large alteration systems tens of metres wide of an outer quartz-carbonate-chlorite and inner quartz-carbonate-mica-sulphide assemblage
- » Graphite schists, a rock type associated with most of the world's large gold deposits are now being recognised by Mercator through the Meekatharra area.

MEEKATHARRA GOLD

Mercator's ground holding is almost exclusively on greenschist facies greenstone that is folded into a series of tight synclines and anticlines, bounded by regional- and district- scale shear zones. Right-lateral and reverse motion kinematics of the large-scale shear zones is reflected at pit scale. Granitoid plutons intruded the greenstones and during subsequent deformations generated pressure shadows which are low stress zones excellent for gold accumulation. Yaloginda lies in the northern pressure shadow and Kurara East in the southern pressure shadow of the Norie pluton.

Rock assemblages integral to mineralised packages comprise: high-Mg basalt, basalt, komatiite, andesite, siliciclastics, banded-iron formation, black shales, felsic schists, dolerites, gabbros and layered sills. Gold mineralisation is hosted in:

- » interbedded high-Mg basalt with siliciclastics and banded-iron formation at Meekatharra North and Nannine
- » in porphyry and high-Mg basalt at Yaloginda, and
- » separately in basalt and banded-iron formation at Stakewell.

Gold mineralisation is associated with brittle-ductile shear zones with quartz-vein systems akin to the Golden Mile, Jundee and Sunrise, and sheeted quartz vein arrays akin to Mt Charlotte, Kalgoorlie. There is a superposition of vein-type lodes on shear-zone lodes. The shear-zone lodes are up to 50 metres wide in which gold mineralisation has developed parallel to the shear zone. The vein-type lodes comprise fault-controlled, flat to gently dipping quartz vein sets (tension gash arrays) within, but, orthogonal to the strike of the shear zones. The shear zones are mostly strike-slip, whereas the vein-type lodes relate principally to reverse oblique-slip motion, hence the two developed in different structural régimes. Late or reactivated high-angle cross-cutting northwest-trending faults also influence the position of mineralisation. Quartz-carbonate veins are ubiquitous and pyrite common with gold mineralisation.

DRILLING Historic drilling through the tenement area is mostly shallow (<100m vertical depth) comprising rotary airblast and aircore for bedrock sampling, reverse circulation and diamond drilling, the latter restricted primarily to Yaloginda. Drilling to greater than 100m vertical depth is confined to mining operations with negligible drilling to greater than 200m depth.

Mercator's drilling programme has seen most reverse circulation drillholes drilled to between 100m and 300m vertical depth and diamond drilling, mostly as "tails" to reverse circulation extend to 500m vertical depth. In two campaigns between October and August 2005, Mercator has drilled 30,610 metres of rotary air blast, aircore, reverse circulation and diamond drilling for a total of 297 drillholes.

DRILLHOLE TYPE	NO OF HOLES	METRES
Rotary Airblast	91	5,550
Aircore	103	7,177
Reverse Circulation	77	14,450
Diamond	26	3,433
Total	297	30,610

GEOLOGY OVERVIEW

The Archaean Yilgarn Craton is the largest tectonic unit in Western Australia consisting of granitoid-greenstone terrain of between ca. 2950 and 2600 Ma. Crustal components exhibit evidence of intense volcanic, plutonic, tectonic and mostly low-grade metamorphic activity between ca. 2750 Ma and 2600 Ma. Gold mineralisation was most prevalent between ca. 2640 and 2630 Ma.

MURCHISON PROVINCE The Murchison Province forms the northwestern part of the Yilgarn Craton, covering an area of almost 100,000 km². The terrain is characterised by north-northwest to north-northeast -trending greenstone belts, major, tectonic lineaments and granitic intrusions. The Murchison Province is bounded by the 3.7 Ga to 2.3 Ga Narryer Gneiss Complex in the northwest, Proterozoic rocks of the Napperu Basin to the north and ill-defined boundaries to the east and south with Archaean rocks of the Southern Cross Province and South West Province respectively. More than 270 Moz and 13 Moz of gold has been mined from the Yilgarn Craton and Murchison Province respectively.

MEEKATHARRA GREENSTONE BELT The Meekatharra greenstone belt is located in the northern part of the Murchison Province. The landscape is generally flat, climate semi-arid with less than 5% of supracrustal rocks exposed at surface. Much of the belt is obscured by laterite or surficial deposits. The gold-mining centres are accessible via sealed and unsealed roads linked to the Great Northern Highway.

Gold was first discovered in 1891 at Nannine. To the end of 1997, gold production of 406t (~13 Moz), almost 10% of Western Australia's total production, was produced from the Murchison Province. By 1930, all of the major mining centres had been located and the Meekatharra-Mount Magnet region was the most important mining field outside of the Eastern Goldfields Province. After the Second World War, gold-mining activity decreased, and by 1960, Hill 50 mine at Mount Magnet was the only major operating gold mine. In the early to mid 1990's mining commenced at Paddy's Flat, Meekatharra township, and at Bluebird in the Yaloginda group of deposits 15km south-southwest of Meekatharra. Mining finished in all areas by 2002.

STRUCTURE AND METAMORPHISM The most prominent regional structures in the greenstone belt are northeast to northwest-trending elongate belts of upright regional folds, intrusions of syn- and post-tectonic granitoids and regional-scale shear zones. The metamorphic pattern is similar to the gold-rich Eastern Goldfields Province and consists of intensely deformed amphibolite-facies domains along the margins and variably deformed greenschist facies domains in the interior of the greenstone belts.

MEEKATHARRA NORTH

Meekatharra North tenements are located immediately north of Meekatharra township and extend northeast for about 15kms. The Great Northern Highway traverses much of the tenement area; in conjunction with station tracks and historic exploration activity, access is excellent in flat terrain.

MINERALISATION AND ALTERATION Gold mineralisation occurs as two parallel lodes on an anticlinal fold, dipping moderately east and plunging northeast changing to east-northeast as the fold swings to the east. Mineralisation is underlain by a shear zone hosting semi-massive sulphides and quartz veins. The rocks are mostly sheared, some mylonitic and strongly weathered locally to greater than 250m depth.

Data compilation, digitisation and evaluation of historic aircore, rotary air blast and reverse circulation drilling has outlined a 3km long geochemical anomaly in the area of Maid Marion prospect and a further 3.5km long geochemical anomaly of greater than 0.5g/tAu to the south at the newly named Nottingham prospect. The anomalous zones in both areas are open to the north and south.

Mercator's exploration drilling results from Maid Marion prospect, demonstrate consistent gold mineralisation across a series of exploration drill fences. Mineralisation to date has been located in drilling over a strike length of more than 450m, up to 160m down-dip and greater than 100m vertical depth. Two gold lodes were intersected in most holes, the upper zone containing true widths to 15m of low grade gold and a lower zone to 5m true width, down-dip with narrower higher grade mineralisation.

Highlights - Meekatharra North

AIRCORE

04MMAC019	4m @ 2.13g/t, 1m @ 8.9g/tAu
04MMAC060	4m @ 1.5g/t, 4m @ 7.66g/tAu
04MMAC061	4m @ 1.6g/t, 1m @ 6.3g/tAu
05MMAC084	3m @ 3.8g/tAu
04MMAC091	4m @ 2.14g/tAu

REVERSE CIRCULATION

05MMRC006	15m @ 1.6g/t, 6m @ 2.2g/tAu
05MMRC007	9m @ 1.4g/t, 2m @ 3.27g/tAu
05MMRC009	8m @ 1.4g/t, 5m @ 1.35g/t, 10m @ 1.9g/tAu
05MMRC010	11m @ 1.6g/tAu
05MMRC013	6m @ 1.7g/tAu

DIAMOND

05MMDD001	2m @ 11.16g/t, 4m @ 3.5g/tAu
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The Maid Marion gold target has been upgraded to a priority greenfields target as recent drilling has demonstrated gold mineralisation that may fulfil Mercator's 500,000 ounce gold potential.

YALOGINDA

The Yaloginda project area hosts many small, mined-out gold pits oriented to the north-northeast on at least two parallel trends. Most previous production was extracted from Great Northern Highway, South Junction and Bluebird. Host rocks to gold mineralisation vary, however, the structural controls on gold mineralisation remain similar from pit to pit. Most pits are shallow (<70m depth), the two exceptions being the deeper South Junction and Great Northern Highway pits.

In the Yaloginda area, Mercator's drilling effort has concentrated at Bluebird and Surprise with lesser drilling at Surprise Extended, Jess and Great Northern Highway. Drillcore from Bluebird, Surprise and Great Northern Highway contains visible nuggets of gold in high-Mg basalt and in porphyry.

Bluebird

Bluebird is an existing pit, from which oxide ore was mined to a depth of 70m then abandoned in the mid 1990's. Bluebird is located 15kms south of Meekatharra and less than 300m from the Bluebird mill.

A SpaDISTM analysis of mineralisation at Bluebird indicated the mineralised envelope strikes NE at about 030° and dips near vertical (85°E). The mineralised envelope remains relatively homogeneous until about 40g.m/t above which the pattern breaks up into a series of flat zones repeated vertically. Flats have a 01°-08° plunge to the

northeast that remains robust with increasing grade. Flat zones of mineralisation are interpreted to be ~120-130m apart.

Of the three main alteration zones at Bluebird, the Edin Hope (western) and Polar Star (eastern) zones are up to 25m & 30m wide respectively, and are northern extensions of the mineralised zones in South Junction. Gold grade increases substantially in these zones toward the southern end of Bluebird pit.

Bluebird (central) zone, the primary mineralised zone at Bluebird, is consistently about 50m wide. Toward the southern half of the Bluebird pit, Bluebird zone splits into two parallel gold zones, both steeply east dipping, trending to about 020°. The Eastern Zone is narrow (5-10m wide), contains high-grade gold and appears to split again at shallower depth. The Western Zone is wider and of lower gold grade overall, but does contain multiple zones of anastomosing high-grade gold mineralisation.

High-grade zones of gold mineralisation comprise subvertical, narrow (5-6 metres) sheets of massive alteration that host quartz veins oriented northeast (030°) in the plane of the overall mineralised envelope. Very high grades are associated with flat to south-southwest dipping quartz veins and tension gash arrays with sulphide-rich quartz selvages.

HIGHLIGHTS Mercator has drilled a total of 23 holes for 7,184 metres at Bluebird, some being re-entry holes to historic drilling that had terminated short of the ore zones. A summary of selected gold intersections are as follows:

05BBRC004	10m@2.3g/t	05BBRC005	6m@2.2g/t
05BBRC009	5m@5.7g/t	05BBRC010	3m@3.4g/t
05BBRC011	24m@4.1g/t	05BBRC012	8m@4.8g/t
04BBRD002	9m@4.8g/t	RCB201	10m@7.7g/t
RCB260	7m@5.5g/t, 4.5m@4.0g/t		

RESOURCES An independent Joint Ore Reserve Committee (JORC) compliant announcement of a resource estimation of the Bluebird deposit has resulted in 5.28Mt@1.9g/t Au for 326,000 ounces of indicated and inferred gold resources. This includes 1,698,000 tonnes@4.5g/t for 244,000 ounces and 510,000 tonnes@6.9g/t Au for 114,000 ounces.

PROPOSED ACTIVITIES Mercator is working to extend the resource north and south of Bluebird pit, consolidate the high-grade mineralisation in the Edin Hope alteration zone between Bluebird and South Junction, track the Bluebird mineralised envelope south and Polar Star mineralisation northward.

Surprise, Surprise Extended and Jess

Surprise, Surprise Extended and Jess lie north-south respectively along strike within the Yaloginda group of historic mining pits next to the Great Northern Highway and about 300 metres from the Bluebird mill.

The Surprise pit was mined in late 1997 - early 1998 by St Barbara Mines Ltd from which ~13,000 ounces was produced (200,000 tonnes of ore at a grade of ~2g/t Au). The pit is about 300m long, 150m wide and 50m deep.

MINERALISATION AND ALTERATION Mineralisation is contained primarily within the porphyry and at the sheared contact zones with high-Mg basalt. High-grade gold intersections are associated with subhorizontal quartz vein packages in the porphyry and on the western porphyry-high-Mg basalt contact. At this position the basalt is highly carbonated, silicified and veined.

SpaDiSTM analysis of data from the greater Surprise area indicates mineralisation is oriented 160° at Surprise Extended, rotating to 180° at Surprise Pit. Mineralisation dips steeply at 80° northwest and plunges southwest at 45° to 210°. The high-grade mineralised envelope is oriented northeast at about 030°. The low-grade mineralised envelope is oriented north-northeast at about 010°. Within the ore envelope, high-grade ore zones comprise multiple flat zones oriented northeast-southwest plunging about 00°-05° southwest.

HIGHLIGHTS Mercator has drilled a total of 36 holes for 5,490 metres at Surprise and Surprise Extended and 17 holes for 2,363 metres at Jess. Results show moderate to high-grades of mineralisation at Surprise and low-grade gold values at Surprise Extended where the orientation of mineralisation changes by about 200. Individual assay results are up to 10.7 ounces (333g/t Au). Most of the very high grade values have been excluded or topcut to 50g/t in the current resource calculation.

A summary of selected gold intersections are as follows:

04SURC002	8m@5.5g/t	04SURC009	17m@2.7g/t
04SURC010	2m@22.7g/t	04SURC012	15m@45g/t
04SURC013	5m@6.3g/t	04SURC014	6m@36g/t
04SURC026	7m@2.3g/t, 4m@3.9g/t		
04SURC027	4m@5.7g/t, 4m@2.4g/t		

At Jess, preliminary drilling returned the following selected intersections:

05JSRC010 4m@2.6g/t, 3m@2g/t, 8m@1.9g/t, 8m @1.2g/t, 8m@1.0g/t
05JSRC017 8m@4.0g/t

RESOURCES An independent Joint Ore Reserve Committee (JORC) compliant announcement of a resource estimation of the Surprise deposit has resulted in 4.185Mt@1.0g/t Au for 141,000 ounces of indicated and inferred gold resources. This includes 1,121,000 tonnes@2.2g/t for 80,000 ounces and 283,000 tonnes@4.2g/t Au for 38,000 ounces.

PROPOSED ACTIVITIES In order to accurately estimate any interpreted high-grade at Surprise there is a requirement to have more detailed sampling. This will enable future modelling of both the grade and volume of the high-grade shoot. It is Mercator's plan to drill the high-grade shoot in the next twelve months with the expectation of an increase in grade and better control on the high-nugget gold variability.

SURPRISE TABULATION OF HIGH GRADE CUT AND UNCUT ESTIMATES >0.3G/T GOLD

CATEGORY	VOLUME	TONNES	HIGH CUT GOLD G/T	UNCUT GOLD G/T	HIGH CUT METAL	UNCUT METAL (OZ)
Indicated	494,000	1,220,000	0.9	1.0	34,000	40,000
Inferred	1,129,000	2,965,000	1.1	1.4	107,000	131,000
TOTAL	1,623,000	4,185,000	1.0	1.3	141,000	171,000

SURPRISE TABULATION > 1.0 G/T GOLD

CATEGORY	VOLUME	TONNES	GOLD G/T	METAL (OZ)
Indicated	133,000	326,000	1.5	15,000
Inferred	303,000	795,000	2.5	65,000
TOTAL	436,000	1,121,000	2.2	80,000

SURPRISE TABULATION > 2.5 G/T GOLD

CATEGORY	VOLUME	TONNES	GOLD G/T	METAL (OZ)
Indicated	8,000	18,000	3.1	2,000
Inferred	100,000	265,000	4.3	36,000
TOTAL	108,000	283,000	4.2	38,000

Great Northern Highway

The Great Northern Highway gold deposit is located on the eastern side of the Great Northern Highway opposite the Bluebird ore processing facility. This deposit was previously known as Bluebird East. The Great Northern Highway mine contains three gold lodes located around a south plunging synform-antiform and are named herein the Western, Eastern and Northern Lodes. Past gold production amounts to approximately 420,000 ounces.

MINERALISATION AND ALTERATION There are three main lodes: western, northern and eastern quartz lodes hosted in high-Mg basalts and felsic porphyries above an altered granite stock.

The western lode is made up of a main vein striking northeast, dipping 65° southeast. Gold grades in the western lode are commonly greater than 10g/t, and typically less than 2g/t in the subordinate veins.

The eastern lode has a strike length of nearly 700 metres and is the largest and most complicated of the lodes.

The northern lode has about 170 metres strike length; the southern part of the lode strikes northeast, dips southeast and the northern part strikes north-northwest dipping steeply west. The highest grade and widest part of the lode is situated north of the inflection point (as shown in the diagram below).

Drilling to pierce a potential southerly plunge to the central breccia zone as shown in the diagram below has resulted in intersecting over 150 metres of moderately to strongly altered, sulphidic basalt and porphyry, with visible gold in one section of porphyry.

A second hole directed to test the northern lode at depth intersected 60 metres of strongly altered, sulphidic basalt and graphite schist.

HIGHLIGHTS Mercator has drilled 2 diamond holes with reverse circulation precollars for 715.6 metres. A summary of selected gold intersections are as follows:

05GNRDD001 2m@18.5g/t, 3m@2.4g/t,
4m@3.8g/t, 4m@2.2g/t Au
05GNRDD002 2m@4.6g/t, 5m@5.7g/t Au

South Junction

South Junction is located about 100-150 metres south, along strike from Bluebird. South Junction deposit was discovered in mid 1989; actual gold production is unclear, but, in the order of 180,000 ounces.

MINERALISATION AND ALTERATION Gold mineralisation is related to the development of intense alteration. Alteration has exploited the margins of quartz porphyry bodies and failed limb/hinge shear zones of large-scale folds. There are three main alteration zones at South Junction – Edin Hope in the west, Polar Star is central and Archenar in the east. Higher gold grades tend to be where quartz vein density is high and vein selvages contain sulphides.

The Edin Hope and Polar Star alteration zones can be related to equivalent zones at Bluebird with mineralisation potentially extending between the pits, as well as into an as yet untested zone positioned beneath the ramp at South Junction. The Archenar alteration zone trends to the northeast and requires drilling to define possible gold extensions to the northeast.

PROPOSED ACTIVITIES In the second half of calendar 2005, the Company will drill the previously untested extensions of the Bluebird lodes into South Junction along the line of the historic haul road. Drill testing for southern extensions of mineralisation will be made in 2006.

OTHER GREENFIELDS EXPLORATION PROJECTS

Stakewell

Stakewell is located immediately west of the Great Northern Highway, 60km south of Meekatharra. Past gold production has been from the Kohinoor mine, which was mined variously between 1897-1911 for 9,563oz, 1988-1989 for 5,943oz and again as an underground operation from 1993-1995 for which there are no production figures. Underground mining went to 150 metres vertical depth. Outcrop within the area is limited, although banded-iron formation crops out extensively as prominent ridges.

MINERALISATION AND ALTERATION Kohinoor is located at an east-west to northeast flexure in stratigraphy. Gold mineralisation is structurally and metasomatically controlled (replacement of magnetite in banded-iron formation by pyrrhotite and pyrite), associated with near vertical plunging shoots within banded-iron formation and enclosed within mafic schist. The lode system is dominated by fine- to medium-grained quartz-pyrite-pyrrhotite schist and associated chlorite-biotite-epidote-haematite alteration and chalcopyrite.

East of the Kohinoor pit in an area devoid of outcrop is a series of closely spaced, mineralised near vertical quartz veins trending northwest, in line with northwest-trending faults. Previous aircore drilling across these veins returned highly anomalous intersections with grades to 6.4g/t Au and mineralisation open in all directions. At the time of writing, a reverse circulation drill programme to test the depth and along strike extent of these mineralised veins was in progress.

PROPOSED ACTIVITIES In the second half of calendar 2005, the Company plans to drill test the stacked veins at depth and along strike to test potential dimensions of the mineralised system.

Nannine

Nannine was discovered in 1891 and mining peaked in the early 1900's with underground production from the Aladdin, Nannine, Champion and Caledonian reefs that were mined to about 60 metres depth. In 1983, alluvial gold was extracted at Baileys Island and in 1987 open pit production from Aladdin and Caledonian amounted to about 36,000 ounces and 189,000 ounces respectively. Approximately 19,350 ounces was extracted from the Nannine reef. The area as a whole is dotted by numerous historic prospecting pits and shafts from which auriferous quartz veins were mined.

MINERALISATION AND ALTERATION Economic mineralisation occurs on or about the western and eastern contacts of an intercalated basalt-meta-sedimentary sequence with tonalite and amphibolite respectively, and where the contacts are intersected by about north-south faults. Concordant and cross-cutting, steeply dipping quartz veins are prevalent within and about the zones of mineralization in the pits.

Exploration activities have involved surface and pit geological mapping, aeromagnetic interpretations and initial assessment of historic drilling data. Structural features are being used to define detailed exploration focus. The Company is planning drill programmes for calendar 2006.

NEW ZEALAND

Mercator Gold holds a large tenement in the Gisborne area of the North Island, New Zealand. The Lottin Point tenement is 1,167km² in size and encompasses the historic gold and base metal workings at Te Kumi and surrounds known gold-bearing volcanogenic massive sulphide (VMS) mineralisation near the coast, indicative of Eskay Creek style mineralisation.

At Sulphide Bay, located on the coast west of Lottin Point, altered basalts, sulphidic red argillite and cherts are exposed at surface. Historic reports indicate gold grades to 50g/t, copper to 0.5% and Fe to 28%. A small exclusion within the tenement is known to host significant levels of copper in massive sulphide, zinc and gold in barytes-quartz. Samples from "B 13" creek have returned values up to 2.5% Cu, 2.55% Pb, 11.4% Zn, 58g/t Au, 75g/tAg and 58% Ba.

Mercator is currently compiling and digitising all historic information relating to the Lottin Point area prior to an on-ground exploration programme.

Dr J Vearncombe *Director*

Dr S Vearncombe *Director*

DIRECTORS' BIOGRAPHIES

Terrence John Strapp

Non-executive Chairman (aged 61)

Terry Strapp was appointed as a Director and Chairman on 7 July 2004. He has extensive experience in banking, finance and corporate risk management and has been actively involved in the mining industry for the last twenty years. He is currently Executive Chairman of Oakvale Capital Limited, a leading independent specialist financial risk management business in Australia. He has held, over the years, numerous positions on public company boards, including as Executive Chairman of Zapopan N.L., Chairman of Pac Min Limited (formerly Camelot Resources N.L.) and as a director of Mount Gibson Mining Limited. He is a Certified Practising Accountant (CPA), a Fellow of the Australian Institute of Banking and Finance (FAIBF), an Affiliate of the Securities Institute of Australia (AffSIA) and a member of the Australian Institute of Company Directors (MAICD).

Patrick Aloysius Harford BSc (Hons)

Managing Director (aged 53)

Patrick Harford was appointed as Managing Director on 22 March 2004. He graduated with Honours in Geomorphology from Melbourne University in 1973. He has had experience in gold and diamond exploration and production in Australia and southern Africa. His past roles have seen Patrick involved with Grants Patch Mining Limited (as Managing Director, when that company operated an alluvial gold mine in the Northern Territory), Zapopan N.L. (during the period that it located and developed the Mt. Todd and Tanami mines in the Northern Territory) and Auridiam Consolidated N.L. (during that company's successful construction of a two million ton per annum diamond mine in Zimbabwe).

Michael John de Villiers B.Comm CFA (SA)

Finance Director (aged 42)

Michael de Villiers was appointed Finance Director on 22 March 2004. He qualified as a Commercial and Financial Accountant with Ernst & Young in Cape Town. Michael gained his experience as financial manager at mining and chemical operations in Namibia, Botswana, Ghana and Bulgaria. He was previously Finance Director of Oxus Gold plc and Navan Mining plc.

Julian Vearncombe

BSc (Hons), PhD, FGS, RPGeo, FAIG

Exploration Director (aged 50)

Dr Julian Vearncombe was appointed Exploration Director on 15 April 2004. He is an experienced geologist, with expertise in finding gold, base metals and kimberlites - he has been a crucial member of exploration teams that have located over five million ounces of gold. His career has involved academia, management, exploration and mine geology; he has established structural controls on mineralisation and developed predictive technologies for the mineral exploration and mining industries. Upon leaving academia, Julian worked as a consultant to various exploration and mining companies. Mine geology projects have included resource geometry evaluation, structural geology and staff training. Exploration projects have included due diligence, geological mapping, special pattern analysis, target generation and the identification of joint venture partners and projects.

Susan Vearncombe

B.Soc.Sci, MSc (Hons), PhD, MAIG, RPGeo

Executive Director (aged 48)

Dr Susan Vearncombe was appointed Business Development Director on 2 March 2005. She is an experienced explorationist, having worked with companies, research organisations and as a consultant. Her experience covers most Australian States and Territories, Africa, Indonesia, New Zealand, South America and the USA, and on projects covering geology from Archaean through to modern active systems. She has published in the areas of petrogenesis, structural geology and regional tectonics, volcanogenic massive sulphide and gold systems, and spatial analysis. Dr Vearncombe is the past Chairperson of the Western Australia branch of the Australian Institute of Geoscientists (AIG) and an AIG Federal Councillor.

Richard Nicholas Allen

Non-executive Director (aged 69)

Nick Allen was appointed as a non-executive Director on 7 April 2004. He has worked in the mining industry for over 40 years, primarily in diamond mining and marketing, including lengthy periods with Consolidated African Selection Trust and D Drukker & Zn, a De Beers Industrial distributor in the UK and India.

Michael Elias BSc (Hons), FAusIMM, CPGeo

Non-executive Director (aged 54)

Michael Elias was appointed as a non-executive Director on 7 July 2004. He is a geologist with over 30 years' of experience in the mining industry. He has worked with WMC Resources (mainly in nickel projects, including as Chief Geologist Resource Development, Nickel Division) and Geological Survey of Western Australia. He is currently a director of CSA Australia.

Paul Robert Loudon ASI

Non-executive Director (aged 43)

Paul Loudon was appointed a non-executive Director on 22 March 2004. He has over 20 years experience in mining finance, corporate management and stockbroking in Australia, Canada and the UK. He is currently the non-executive Chairman of BDI Mining Corp (formerly BM Diamond Corp (AIM - BMG)) and is a Director and Head of Equity Finance at Loeb Aron & Company Ltd.

REPORT OF THE DIRECTORS

The Directors present their report and audited financial statements for the period ended 30 June 2005.

Incorporation

The Company was incorporated in England and Wales on 22 March 2004 as Western Australia Gold Mines Limited.

Change of name and admission to AIM

The name of the Company was changed to Mercator Gold Limited on 21 May 2004 and subsequently to Mercator Gold plc on 17 September 2004. The Company gained admission to the Alternative Investment Market (AIM) on 08 October 2004.

Principal Activities

The principal activity of the Group is exploration for gold in Australia. The principal activity of the company is that of a holding company.

Directors

The Directors who served during the period were:

T J Strapp	appointed 7 July 2004
P A Harford	appointed 22 March 2004
M J de Villiers	appointed 22 March 2004
J R Vearncombe	appointed 15 April 2004
S Vearncombe	appointed 2 March 2005
R N Allen	appointed 7 April 2004
M Elias	appointed 7 July 2004
P R Loudon	appointed 22 March 2004
Cobbetts Limited	appointed 22 March 2004; resigned 17 April 2004

Directors' Interests

Share Interests

The directors of the Company who held office at 30 June 2005 held the following beneficial interests (including interests held by spouses and minor children) in the ordinary shares of the Company:

	30 June 2005 No. of Shares	On appointment
T J Strapp	200,000	-
P A Harford	16,500,100	-
M J de Villiers	600,000	100
J R Vearncombe	1,500,000	-
S Vearncombe	1,500,000	1,500,000
R N Allen	-	-
M Elias	100,000	-
P R Loudon	2,140,000	-
Total	22,540,100	1,500,100

JR Vearncombe and S Vearncombe also have a beneficial interest in a further 200,000 shares through the Vearncombe Superannuation Fund.

Share Options

The directors of the Company held share options granted under the Company's Share Option Scheme, as indicated below. No share options were exercised during the period.

	Options issued	Date issued	Expiry date	Exercise price	30 June 2005 Balance
T J Strapp – total	750,000	19 Nov 2004	18 Nov 2014	£0.10	750,000
P A Harford	100,000	29 Sept 2004	7 Oct 2009	£0.08	100,000
	8,150,000	29 Sept 2004	7 Oct 2009	£0.08	8,150,000
	750,000	19 Nov 2004	18 Nov 2014	£0.10	750,000
P A Harford – total	9,000,000				9,000,000
M J de Villiers	750,000	19 Nov 2004	18 Nov 2014	£0.10	750,000
	1,250,000	14 April 2005	13 April 2015	£0.12	1,250,000
M J de Villiers – total	2,000,000				2,000,000
J Vearncombe	750,000	29 Sept 2004	7 Oct 2009	£0.08	750,000
	750,000	19 Nov 2004	18 Nov 2014	£0.10	750,000
J Vearncombe – total	1,500,000				1,500,000
S Vearncombe	750,000	29 Sept 2004	7 Oct 2009	£0.08	750,000
	750,000	30 June 2005	29 June 2015	£0.10	750,000
S Vearncombe – total	1,500,000				1,500,000
N Allen – total	500,000	19 Nov 2004	18 Nov 2014	£0.10	500,000
M Elias – total	500,000	19 Nov 2004	18 Nov 2014	£0.10	500,000
P R Loudon	1,000,000	29 Sept 2004	7 Oct 2009	£0.08	1,000,000
	500,000	19 Nov 2004	18 Nov 2014	£0.10	500,000
P R Loudon – total	1,500,000				1,500,000
Total Directors' options	17,250,000				17,250,000

Warrant Interests

The directors of the Company who held office at 30 June 2005 held the following beneficial interests (including interests held by spouses and minor children) in warrants to subscribe for ordinary shares of the Company:

	Warrants issued	Date issued	Expiry date	Exercise price	30 June 2005 Balance
T J Strapp – total	400,000	29 Sept 2004	7 Nov 2005	£0.08	400,000
M J de Villiers – total	670,000	29 Sept 2004	7 Nov 2005	£0.08	670,000
J and S Vearncombe Superannuation Fund	400,000	29 Sept 2004	7 Nov 2005	£0.08	400,000
M Elias	200,000	29 Sept 2004	7 Nov 2005	£0.08	200,000
P R Loudon	280,000	29 Sept 2004	7 Nov 2005	£0.08	280,000
Total Directors' warrants	1,950,000				1,950,000

Further details of share options and share warrants are in Note 16.

Business Review

A review of the Group's business and prospects is set out in the Chairman's Statement.

Share Capital

The authorised share capital of the Company at 30 June 2005 was £9,000,000 divided into 900,000,000 Ordinary Shares of 1 penny each ("Shares").

Section 95 of the Companies Act 1985 provides that any shares being issued for cash must in general be issued to all existing shareholders pro-rata to their holding. However, where directors have a general authority to allot shares they may be given power by the Articles or by a special resolution to allot shares pursuant to the authority as if the statutory pre-emption rights did not exist.

On 7 June 2004 the Company passed the following resolutions:

- (a) An ordinary resolution to authorise the Directors, pursuant to section 80 of the Companies Act, to allot relevant securities up to an aggregate nominal amount of £9,000,000 provided that the authority shall expire upon the date falling five years after the passing of the resolution;
- (b) A special resolution that the Directors be empowered to allot or agree to allot equity securities pursuant to the authority referred to in sub-paragraph (a) above as if section 89(1) of the Companies Act did not apply to such allotment.

The Company's share price varied between 6.25 pence and 10.75 pence during the period. At 30 June 2005 the mid-market price was 7.38 pence.

Substantial Share Interests

The Company had been notified of the following interests in Shares held as at 22 September 2005:

	Ordinary Shares	%
Caledonian Capital Limited	16,300,000	18.7
First International Resources Limited	16,500,000	18.94
Artemis Investment Group Limited	3,750,000	4.3
Drs Julian & Susan Vearncombe	3,200,000	3.67

Statement of Directors' Responsibilities

Company law requires the Directors to prepare financial statements for each financial period which give a true and fair view of the state of affairs of the Company and Group and of the profit or loss for that period. In preparing those financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and to enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for ensuring that the Directors' Report and other information included in the annual report is prepared in accordance with company law in the United Kingdom.

Corporate Governance and Financial Control

The Board of Directors

The Directors support the highest standards of corporate governance and aim to observe the requirements of the Combined Code to the extent that they consider appropriate in light of the Company's size, stage of development and resources.

The Directors are responsible for the Group's system of internal control and for reviewing its effectiveness. The risk management process and systems of internal control are designed to manage rather than eliminate the risk of failure to achieve the Company's objectives. Any such system of internal financial control can only provide reasonable but not absolute assurance against material misstatement or loss.

At least six Board meetings are held per year at which reports relating to the Group's operations, together with financial reports, are considered. The executive Directors meet regularly to review operational reports from all the Group's areas of operations. The process is used to identify major business risks and evaluate their financial implications and ensure an appropriate control environment. Certain control over expenditure is delegated to on site project managers subject to Board control by means of monthly budgetary reports. Internal financial control procedures include:

- Preparation and regular review of operating budgets and forecasts
- Prior approval of all capital expenditure
- Review and debate of treasury policy
- Unrestricted access of non-executive Directors to all members of senior management.

The Board, in conjunction with members of the Audit Committee, has reviewed the effectiveness of the system of internal control for the period from 22nd March 2004 to the date of this report.

Audit Committee

The Audit Committee comprises Terry Strapp as Chairman, and Nick Allen with Michael de Villiers as Advisor. The committee meets twice a year and at any other time when it is considered appropriate to consider and discuss audit and accounting related issues. The committee will make recommendations on the appointment of the auditors and the audit fees, be responsible for ensuring the financial performance of the Group is properly monitored and reported on and will receive and review reports from management and auditors relating to the interim reports, the annual report and accounts and internal control systems of the Group. The committee will have the opportunity to meet the auditors without other executive Board members being present.

Remuneration Committee

The Remuneration Committee comprises Nick Allen as Chairman, Michael Elias and Paul Loudon. The committee will meet at any time when it is considered appropriate to review and make recommendations on the remuneration arrangements for Directors and senior management, including any bonus arrangements and the award of share options, having regard to the performance of the Group and the interests of shareholders. The remuneration and terms of appointment of non-executive Directors will be set by the Board.

Total Directors' emoluments are disclosed in note 6 to the financial statements and the Directors' options are disclosed above. During the reporting period 250,000 options were granted to employees.

The Directors will comply with Rule 19 of the AIM rules relating to Directors' dealings and will take all reasonable steps to ensure compliance by the Company's Directors and applicable employees.

Dividends and Profit Retention

No dividend is proposed in respect of the period and the retained loss for the period of £867,319 has been taken to reserves.

Policy on Payment of Suppliers

The Company's policy is to settle terms of payment with its suppliers when agreeing the terms of each transaction, ensuring that suppliers are made aware of the terms of payment, and abiding by the agreed terms. The number of days of trade creditors outstanding at the period end was 22 days.

Auditors

PKF were appointed as first auditors of the company. On 23 May 2005 PKF transferred their business to PKF (UK) LLP, a limited liability partnership. Under section 26(5) of the Companies Act 1989, the company consented to extend the audit appointment to PKF (UK) LLP from 23 May 2005. Accordingly, the audit report has been signed in the name of PKF (UK) LLP and a resolution for the reappointment of PKF (UK) LLP will be proposed at the forthcoming annual general meeting.

By order of the Board



M J de Villiers
Secretary
26 September 2005

INDEPENDENT AUDITORS' REPORT

REPORT OF THE INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF MERCATOR GOLD PLC

We have audited the financial statements of Mercator Gold plc for the period ended 30 June 2005 which comprise the consolidated profit and loss account, the consolidated balance sheet, the company balance sheet, the consolidated cash flow statement and the related notes. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report and the financial statements in accordance with application law and United Kingdom Accounting Standards are set out in the statement of directors' responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions with the group is not disclosed.

We read other information contained in the annual report and consider whether it is consistent with the audited financial statements. This other information comprises only the chairman's statement, review of operations and the report of the directors. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of opinion

We conducted our audit in accordance with United Kingdom auditing standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's and group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the financial statements.

Going concern

In forming our opinion, we have considered the adequacy of the disclosures made in note 1 of the financial statements concerning the uncertainty as to the adequacy of the Group's funding and its ability to continue as a going concern.

In view of this uncertainty we consider that it should be drawn to your attention but our opinion is not qualified in this respect.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the company and the group at 30 June 2005 and of the loss of the group for the period then ended and have been properly prepared in accordance with the Companies Act 1985.

PKF (UK) LLP
REGISTERED AUDITORS
London

PKF (UK) LLP

26 September 2005

CONSOLIDATED PROFIT AND LOSS ACCOUNT

For the period from 22 March 2004 to 30 June 2005

	2005 Notes	£
Administrative expenses		(926,654)
Operating loss	5	(926,654)
Net interest receivable & similar items	7	59,335
Loss on ordinary activities before taxation		(867,319)
Taxation	8	-
Loss on ordinary activities after taxation		(867,319)
Loss per share	9	(2.03)p

All amounts relate to continuing activities

The Group has no recognised gains or losses other than the loss of £867,319 for the period

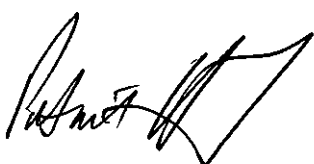
CONSOLIDATED BALANCE SHEET

At 30 June 2005

	Notes	2005 £
Fixed assets		
Intangible	11	1,453,885
Tangible	10	65,934
Total fixed assets		1,519,819
Current assets		
Debtors	13	194,972
Cash at bank and in hand	15	954,467
Total current assets		1,149,439
Creditors – amounts falling due within one year	14	572,611
Net current assets		576,828
Total assets less current liabilities		2,096,647
Capital and reserves		
Called-up share capital	16	871,198
Share premium account	16	2,492,599
Merger Reserve	12	(399,831)
Profit and loss account	17	(867,319)
Equity shareholders' funds		2,096,647

The financial statements were approved by the Board on 26 September 2005 and signed on their behalf by:

P A Harford
Director



M J De Villiers
Director



COMPANY BALANCE SHEET

At 30 June 2005

	Notes	2005 £
Tangible	10	5,622
Investment	12	450,000
Long term loan – subsidiary	12	1,720,422
Total fixed assets		2,176,064
Current assets		
Debtors	13	60,539
Cash at bank and in hand		681,246
Total current assets		741,785
Creditors - amounts falling due within one year	14	125,216
Net current assets		616,569
Total assets less current liabilities		2,792,633
Capital and reserves		
Called-up share capital	16	871,198
Share premium account	16	2,492,599
Profit and loss account	17	(571,164)
Equity shareholders' funds		2,792,633

The financial statements were approved by the Board on 26 September 2005 and signed on their behalf by:

P A Harford
Director



M J De Villiers
Director



CONSOLIDATED CASH FLOW STATEMENT

For the period from 22 March 2004 to 30 June 2005

	Notes	2005 £
Net cash outflow from operating activities	18(a)	(526,834)
Returns on investments and servicing of finance	18(b)	29,718
Capital expenditure and financial investment	18(c)	(1,541,831)
Net cash outflow before management of liquid resources and financing:		(2,038,947)
Management of liquid resources		(647,000)
Financing:		
Issue of ordinary shares		2,963,797
Increase in cash in the period		277,850
Reconciliation of net cash flow to movement in net funds	18(d)	
Increase in cash in the period		277,850
Change in net funds resulting from cash flows		277,850
Exchange differences		29,617
Movement in short term deposits		647,000
Movement in net funds in the period		954,467
Net funds at 22 March 2004		-
Net funds at 30 June 2005		954,467

SHAREHOLDERS' FUNDS

For the period from 22 March 2004 to 30 June 2005

	2005 £
Loss for the period	(867,319)
Merger reserve arising on consolidation	(399,831)
New share capital issued	3,363,797
Net addition to shareholders' funds	2,096,647
Opening shareholders' funds	-
Closing shareholders' funds	2,096,647

NOTES TO THE FINANCIAL STATEMENTS

For the period ended 30 June 2005

1 Accounting policies

Accounting convention and basis of preparation of financial statements and going concern

The financial statements have been prepared under the historical cost convention and in accordance with applicable accounting standards. The principal accounting policies of the Group are set out below.

These financial statements are prepared on a going concern basis, notwithstanding the loss for the period to 30 June 2005 of £867,319, which the Directors believe to be appropriate for the following reasons:

In common with many exploration companies, the Company raises finance for its exploration and appraisal activities in discrete tranches to finance its activities for limited periods only. Further funding is raised as and when required, the most recent being in September 2005.

The Directors are of the opinion that the Company will need to raise additional financial resources to enable the Group to undertake an optimal programme of exploration and appraisal activity over the next twelve months. Accordingly, the Directors intend to raise further funds during the course of the next twelve months. Whilst the Directors are confident that the Group will be able to secure additional funding to enable it to continue to meet its debts as they fall due and to undertake the programme described above for at least the next twelve months from the date of approval of these financial statements, there can be no guarantee that this will be the case. The financial statements do not include any adjustments, particularly in respect of fixed assets, investments, loans and provisions for winding up which would be necessary if the Company and Group ceased to be a going concern.

Basis of consolidation

Details of principal subsidiaries are given in note 12. The Group accounts consolidate the accounts of Mercator Gold plc and its subsidiary undertakings. The acquisition by the Company of Mercator Gold Australia Pty Ltd in August 2004 was accounted for in accordance with the principles of Merger accounting set out in Financial Reporting Standards 6 on "acquisitions and mergers". Accordingly, the consolidated financial statements are presented as if Mercator Gold Australia Pty Ltd has been controlled by the Company throughout the period from its incorporation on 19 January 2004.

Exploration and development costs

All costs associated with mineral exploration and investments are capitalised on a project-by-project basis, pending determination of the feasibility of the project. Costs incurred include appropriate technical and administrative expenses but not general overheads. If an exploration project is successful, the related expenditures will be transferred to mining assets and amortised over the estimated life of the commercial ore reserves on a unit of production basis. Where a licence is relinquished or a project abandoned, the related costs are written off. Where the Group maintains an interest in a project, but the value of the project is considered to be impaired, a provision against the relevant capitalised costs will be raised.

The recoverability of all exploration and development costs is dependent upon the discovery of economically recoverable reserves, the ability of the Company to obtain necessary financing to complete the development of reserves and future profitable production or proceeds from the disposition thereof.

Computer Software

Computer software is initially capitalized at cost and amortization is provided on a straight line basis over the estimated useful life of 3 years. The company reviews the carrying value on a regular basis and a provision is made in the year that any impairment is determined by management.

Tangible fixed assets

Tangible fixed assets are included at cost less depreciation. Depreciation is calculated to write off office furniture, equipment and vehicles on a straight line basis over their estimated useful lives, which range from three to five years.

Investments

Investments are included at cost, less amounts written off.

Taxation

The charge for taxation is based on the profit or loss for the period and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes.

Deferred tax is recognised, without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes which have arisen but not reversed by the balance sheet date, except as otherwise required by FRS 19. Deferred tax assets are recognised when it is more likely than not that they will be recovered.

Foreign currencies

Assets and liabilities in foreign currencies are translated into sterling at the rates of exchange ruling at the balance sheet date. Transactions in foreign currencies are translated into sterling at the rate of exchange ruling at the date of transaction. Exchange differences are taken into account in arriving at the operating result. For the purpose of consolidation the balance sheets of the foreign subsidiaries are translated at the closing rate and the profit and loss accounts at the average rate during the year.

Pension schemes

The Group does not operate any pension schemes for the benefit of its employees.

Financial instruments

Financial assets are recognised in the balance sheet at the lower of cost and net realisable value. Provision is made for diminution in value where appropriate.

Income and expenditure on financial instruments is recognised on the accruals basis and credited to the profit and loss account in the financial period to which it relates.

Operating lease

Rentals payable under operating leases are charged to the profit and loss account as they fall due, unless such a payment relates to exploration and evaluation costs in which case it is capitalised.

Liquid resources

In accordance with FRS 1 (revised 1996) on "Cash Flow Statements", for cash flow purposes, cash includes net cash in hand and bank deposits payable on demand within one working day and liquid resources include all of the Group's other bank deposits.

2 Operating environment and risks

The Company's operations are located principally in Australia. Australia has stable, advanced economic and legal infrastructures, and hosts extensive and long established mining industries.

3 Segmental analysis

By geographical location:

	Loss before taxation - £	Net Assets - £
UK	(623,606)	672,191
Australia	(243,713)	1,424,456
Total	(867,319)	2,096,647

4 Employees

2005

£

Staff costs:

Salaries and wages	425,074
Social security costs	10,231
Total	435,305

The average number of persons employed by the Group was as follows:

	Number
Management	8
Others	5
Total	13

5 Operating loss

2005

£

The operating loss is stated after charging:

Depreciation of tangible fixed assets	12,512
Computer software amortisation	
Auditors remuneration	
Audit services – UK	19,250
Audit services – overseas	5,750
Non-audit services – UK	33,500
Operating leases	5,995

The Board reviews the nature and extent of non-audit services to ensure that independence is maintained.

6 Directors' emoluments

2005

£

Directors' emoluments	311,998
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The highest paid director received remuneration of £77,636.

7 Net interest (payable)/receivable and similar items

2005

£

Foreign exchange gain	29,617
Interest payable on bank loans and overdrafts	(2,162)
Interest receivable	31,880
Total	59,335

Foreign exchange gains and losses principally relate to exchange differences on intra-group balances denominated in Pounds Sterling and owing to the Company by its Australian subsidiaries. The latter prepare their financial statements in Australian Dollars, which consequently recognise in profit and loss account terms any Australian Dollar movement in the corresponding opening intra-group balances, resulting from changes in the Australian Dollar/Pound Sterling exchange rate over the period. For accounting purposes, such exchange gains and losses are also recognised in the Group's consolidated financial statements.

8 Taxation

The Company has made a loss in the United Kingdom. Consequently no liability to United Kingdom taxation arises.

No other company in the Group has made profits liable to taxation.

	2005
Current tax reconciliation	£
Loss on ordinary activities before tax	(867,319)
Current tax at 30% (2003: 30%)	(260,196)
Effects of:	
Capital allowances in excess of depreciation	(610)
Expenses not deductible for tax purposes	15,757
UK tax losses carried forward	159,959
Losses on overseas subsidiary	85,090
Current tax charge	-

There was no tax payable for the period ended 30 June 2005 due to the Company having taxable losses.

The Group's business operations currently comprise mining projects in Australia, which are all currently at an exploration stage. The Group has tax losses carried forward on which no deferred tax asset is recognised that may affect the future tax position, as and when its mining projects reach a development stage. At the year-end deferred tax assets of £245,049 have not been recognised because there is insufficient evidence of the timing of future taxable profits against which they can be recovered.

9 Loss per share

Loss per share is calculated by reference to the loss for the period of £867,319 and the weighted average number of ordinary shares in issue during the period of 42,807,238. There is no dilutive effect of share options or warrants

10 Tangible fixed assets

Group	Plant and Machinery £	Office equipment £	Motor vehicles £	Total £
Cost				
As at 22 March 2004	-	-	-	-
Additions	29,781	9,552	39,113	78,446
At 30 June 2005	29,781	9,552	39,113	78,446
Depreciation				
As at 22 March 2004	-	-	-	-
Depreciation charge for the period	8,586	1,010	2,916	12,512
At 30 June 2005	8,586	1,010	2,916	12,512
Net book value				
At 30 June 2005	21,195	8,542	36,197	65,934
At 22 March 2004	-	-	-	-
Company			Office equipment £	
Cost				
As at 22 March 2004			-	
Additions			5,983	
At 30 June 2005			5,983	
Depreciation				
As at 22 March 2004			-	
Depreciation charge for the period			361	
At 30 June 2005			361	
Net book value				
At 30 June 2005			5,622	

At 22 March 2004

11 Intangible fixed assets

Group	Exploration and development costs £	Computer software £	Total £
Cost			
As at 22 March 2004	-	-	-
Additions	1,430,282	33,103	1,463,385
At 30 June 2005	1,430,282	33,103	1,463,385
Amortisation			
As at 22 March 2004	-	-	-
Amortisation for the period	-	9,500	9,500
At 30 June 2005	-	9,500	9,500
Net book value			
At 30 June 2005	1,430,282	23,603	1,453,885
At 22 March 2004	-	-	-

12 Fixed asset investments

Company	Shares £	Loans £
Cost		
As at 22 March 2004	-	-
Acquisition of subsidiaries - shares in group undertakings and funds advanced	450,000	1,720,442
At 30 June 2005	450,000	1,720,442

The amount due from subsidiary undertaking has no fixed terms of repayment

Acquisition of subsidiaries

(a) **Mercator Gold Australia Pty Limited** (formerly Aurogenic Resources Pty Limited). The Company acquired the entire share capital of Mercator Gold Australia Pty Limited, a company incorporated in Australia, via a share for share exchange. In terms of the acquisition agreement, on 4 August 2004 the Company issued 20,000,000 ordinary shares of £0.01 each for the purchase of the company and subsequently, on 26 January 2005 issued 20,000,000 shares of £0.01 each as a bonus in terms of the agreement.

This transaction has been accounted for by the merger method of accounting.

Equity acquired :	£
Shares issued at par	(400,000)
Share capital acquired	169
Merger Reserve	(399,831)

(b) **Island Gold Plc.** On the 11 December 2004, the company incorporated and subscribed for the entire share capital of Island Gold Plc for £50,000. The company has not traded since incorporation.

At 30 June 2005, the Company and the Group had interests in the following material subsidiaries, which are included in the consolidated financial statements.

Subsidiary undertakings	Registration	Country of Incorporation/ Principal Activity	Principal Country of Operation	Description and Effective Proportion of Shares Held
Mercator Gold Australia Pty Limited (formerly Aurogenic Resources Pty Limited)	Australia	Mineral Evaluation & Production	Australia	100% Ordinary
Island Gold Plc	United Kingdom	Dormant	United Kingdom	100% Ordinary

13 Debtors

	Group 2005 £	Company 2005 £
Trade debtors	3,703	3,703
Other debtors	80,372	17,520
Other taxes	87,250	15,669
Prepayments and accrued income	23,647	23,647
	<u>194,972</u>	<u>60,539</u>

14 Creditors - amounts falling due within one year

	Group 2005 £	Company 2005 £
Trade creditors	475,980	20,253
Amounts owed to subsidiary undertakings	-	37,500
Taxes and social security	23,530	2,487
Other Creditors	600	600
Accruals and deferred income	72,501	64,376
	<u>572,611</u>	<u>125,216</u>

During the period, non-interest bearing, Unsecured Convertible Loan Notes were issued and subsequently converted to ordinary shares as follows:

Issue of Loan Notes:

- (i) Notes to the value of £180,000 were issued on 8 April 2004, equivalent to 3,000,000 shares upon conversion.
- (ii) Notes to the value of £300,000 were issued on 1 June 2004, equivalent to 5,000,000 shares upon conversion.

Conversion at £0.06 per share to ordinary shares of £0.01, plus share premium of £0.05:

7,476,667 shares on 4 August 2004

523,333 shares on 10 August 2004

Directors' interests in the Loan Notes and their conversion amounted to £50,400 in respect of 840,000 shares.

15 Financial instruments

The Group is at an early stage of development and has yet to commence commercial production. Two risks which the Group encounters are currency exposure and liquidity risk. Currency exposure is managed as far as is practical by financing the Group's development and exploration activity in hard currency and to match the currency of borrowing to the expected revenue stream. Liquidity risk is managed by tight controls over expenditure. The Board determines, as required, the degree to which it is appropriate to use financial instruments or hedging contracts or techniques to mitigate risks. During the period ended 30 June 2005 the Group has not entered into any hedging or forward exchange rate contracts.

There is no material difference between fair value and book value of financial instruments.

The information below describes the Group's financial instruments. Short-term debtors and creditors are excluded from the numerical disclosures below with the exception of the currency risk disclosures.

(a) Financial assets

The currency profile of the financial assets is set out below:

Group	2005
Cash:	£
Pounds Sterling	693,746
Australian Dollars	260,721
	<u>954,467</u>

Financial assets are at floating rate, comprising cash earning interest at various rates set with reference to the prevailing LIBOR or equivalent for the relevant country.

(b) Financial liabilities

As at 30 June 2005 the Group had no financial liabilities, as distinct from short-term creditors such as trade creditors and accruals.

As at 30 June 2005 there were no un-drawn committed facilities.

(c) Currency risk

The table below shows the extent to which Group companies have monetary assets and liabilities in currencies other than their functional currency. Foreign exchange differences on re-translation of such assets and liabilities are taken to the profit and loss account.

Group Net Foreign Currency Monetary Assets/(Liabilities)

Functional currency of Group operation	Denomination GBP £	Denomination AUD\$
GBP £	-	-
AUD \$	(1,720,442)	-
30 June 2005	(1,720,442)	-

16 Share Capital and Share Premium Accounts

	2005 Number of shares	2005 Nominal value £
(a) Authorised share capital		
On incorporation – ordinary shares of £1 each	1,000	1,000
Sub-divided into ordinary shares of £0.01 each on 7 June 2004	100,000	1,000
Creation of additional ordinary shares of £0.01 each on 7 June 2004	899,900,000	8,999,000
At 30 June 2005 - Ordinary Shares of 1p each	900,000,000	9,000,000

(b) Changes in issued Share Capital and Share Premium:

For the period ended 30 June 2005

	Number of shares	Nominal value £	Share premium £	Total £
Subscriber share issued upon incorporation 22 March 2004	1	1	-	1
Share issue on 24 March 2005	1	1	-	1
	2	2	-	2
Sub-division into £0.01 shares on 7 June 2004	200	2	-	2
Conversion of loan notes – 4 August 2004	7,476,667	74,767	373,833	448,600
Share issue costs charged to share premium	-	-	(26,916)	(26,916)
Conversion of loan notes – 10 August 2004	523,333	5,233	26,167	31,400
Share issue costs charged to share premium	-	-	(1,884)	(1,884)
Shares issued at £0.06 each – placing on 20 September 2004	14,766,600	147,666	738,330	885,996
Share issue costs charged to share premium	-	-	(53,160)	(53,160)
Shares issued at £0.06 each – placing on 23 September 2004	8,728,000	87,280	436,400	523,680
Share issue costs charged to share premium	-	-	(31,421)	(31,421)
Shares issued at £0.01 each for purchase of Mercator Gold Australia Pty on 29 September 2004	20,000,000	200,000	-	200,000
Shares issued at £0.01 each for purchase of Mercator Gold Australia Pty – 26 January 2005	20,000,000	200,000	-	200,000
Shares issued at £0.08 each – placing on 16 February 2005	12,500,000	125,000	875,000	1,000,000
Share issue costs charged to share premium	-	-	(50,000)	(50,000)
Shares issued at £0.08 each – placing on 25 February 2005	3,125,000	31,250	218,750	250,000
Share issue costs charged to share premium	-	-	(12,500)	(12,500)
Ordinary Shares of 1p each	87,119,800	871,198	2,492,599	3,363,797

All shares were issued for cash apart from those related to the Mercator Gold Australia Pty Ltd acquisition.

Potential issues of ordinary shares:

Share options and warrants

At 30 June 2005 the Company had 26,750,000 options and 37,294,600 warrants outstanding for the issue of ordinary shares, as follows:

Options

Date of grant	Exercisable from	Exercisable to	Exercise price	Number Granted	Number at 30.06.06
29 September 2004	8 October 2004	7 October 2009	£0.08	20,000,000	20,000,000
19 November 2004	19 November 2004	18 November 2014	£0.10	4,500,000	4,500,000
15 December 2004	15 December 2004	14 December 2014	£0.10	100,000	100,000
30 June 2005	30 June 2005	29 June 2015	£0.10	900,000	900,000
14 April 2005	14 April 2005	13 April 2015	£0.12	1,250,000	1,250,000
				26,750,000	26,750,000

Warrants

Date of grant at 30.06.06	Exercisable from	Exercisable to	Exercise price	Number Granted	Number
23 September 2004	8 October 2004	7 October 2007	£0.06	2,300,000	2,300,000
23 September 2004	8 October 2004	7 October 2007	£0.08	500,000	500,000
29 September 2004	8 October 2004	7 November 2005	£0.08	34,494,600	34,494,600
				37,294,600	37,294,600
Total contingently issuable shares at 30 June 2005					64,044,600

17 Profit and loss account

	Group £	Company £
At 22 March 2004	-	-
Loss for the period	(867,319)	(571,164)
At 30 June 2005	(867,319)	(571,164)

Mercator Gold plc has taken advantage of the exemption permitted by section 230 of the Companies Act 1985 and has not presented its own profit and loss account.

18 Cash flow statement

	2005			
	£			
(a) Reconciliation of Operating Loss to Operating Cash Flows				
Operating loss	(926,654)			
Depreciation and amortisation charges	22,013			
(Increase) in debtors	(194,972)			
Increase in creditors	572,611			
<u>Net cash outflow from operating activities</u>	<u>(527,002)</u>			
(b) Returns on investments and servicing of finance				
Interest received	31,880			
Interest paid	(2,162)			
<u>Net cash outflow from returns on investments and servicing of finance</u>	<u>29,718</u>			
(c) Capital expenditure and financial investment				
Purchase of intangible fixed assets	(1,463,385)			
Purchase of tangible fixed assets	(78,446)			
<u>Net cash outflow for capital expenditure and financial investment</u>	<u>(1,541,831)</u>			
(d) Analysis of Net Funds				
	At 22 March 2004	Cash flow	Exchange	At 30 June 2005
	£	£	£	£
Cash in hand, at bank	-	277,850	29,617	307,467
Short-term deposits (included within cash at bank and in hand in the balance sheet)	-	647,000	-	647,000
<u>Net funds</u>	<u>-</u>	<u>924,850</u>	<u>29,617</u>	<u>954,467</u>

19 Contingencies and operating lease commitments

The Group had no contingent liabilities at 30 June 2005.

At 30 June the Group and the Company had commitments under operating leases that expire as follows:

Office	
Premises	2005
	£
Within 2 – 5 years	31,980

Lease commitments relate to assets used by the Group in the United Kingdom.

20 Related party transactions

During the period, fees and commissions totalling £93,407 were paid to Loeb Aron & Co. of which Paul Loudon is a Director.

During the period, the Company paid £5,001 to Mr T Strapp and £1,875 to Mr M Elias as consultancy fees, prior to their appointment as directors.

Legal fees of £51,000 were paid to Cobbetts, a firm connected with Cobbetts Limited, the company director that resigned in the period.

During the period an amount of £110,990 was paid as a licence fee for the use of SpaDiST™ technology to Vearncombe & Associated Pty Ltd, a company owned and controlled by Drs Julian and Susan Vearncombe.

Other transactions with Directors are disclosed in Note 6.

21 Post balance sheet events

On 5 August 2005 the Company made an offer to all warrant holders to exercise their 8p warrants early and receive a further warrant allocation in addition to their original warrant entitlement. This offer was limited to 12,500,000 warrants only, consequently a pro rata allocation of 12,500,000 new shares and 12,500,000 10 pence warrants, expiring on 7 November 2006, are being issued during September 2005. This exercise is raising a £1,000,000 before expenses and underwriting costs of approximately £63,000.

On 8 September 2005 the Company announced that it has expended A\$3 million under the Annean Joint Venture and it had advised its joint venture partner, St. Barbara Mines Ltd, that it had now earned a 45% interest and will proceed to stage 3 of the joint venture by spending an additional A\$1 million on exploration to secure a 51% interest.