

DARNLEY BAY RESOURCES LIMITED

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MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE SECOND QUARTER AND HALF YEAR OF 2005

This Management's Discussion and Analysis for the 2nd quarter and half year of 2005 is a follow up of the MD&A for the year 2004, which provided background on the Company's objectives and operations since its commencement. In conjunction with this up date on current operations, it is suggested that reference be made to the MD&A for the year ended December 31, 2004 and to Note 3 of the relative financial statements. Note 3 covers both the governing agreements with the Inuvialuit Land Corporation and the joint venture agreement with Diadem Resources Ltd. for exploration of diamonds.

Introduction

Darnley Bay Resources Limited's main focus is exploration for base metals and diamonds in an Area of Mutual Interest (AMI) comprising some 14 million acres surrounding the Hamlet of Paulatuk in the Inuvialuit Settlement Region, Northwest Territories, Canada.

The area is the site of the strongest isolated gravity anomaly in North America which, together with a coinciding magnetic anomaly, is termed the "Anomaly."

The Geological Survey of Canada (GSC) has assigned a moderate to a high rating for the cause of the Anomaly to be a major mineral complex comparable to the Sudbury Basin in Ontario, Norilsk in Russia, or to the Bushveld Complex in South Africa. These are mining districts known primarily for their great nickle and copper production and are also prime platinum/palladium producers.

Ref.: 1994 GSC, Open File Report 2789

Company's Completed Exploration

In 1997, the Company flew an aeromagnetic survey over the Anomaly that indicated the main source to be a buried intrusive body lying 1,000-3,000 metres below surface. The survey indicated that the main intrusive has 4 upward extending feeder pipes. The feeder pipes give way to 9 laterally trending shallow magnetic zones within 300 metres of surface which are referred to as intrusive "Offshoots" that could contain economic mineral deposits. Also, numerous kimberlite targets were disclosed which prompted the Company to embark on a diamond program in addition to the base metals.

These kimberlite targets show characteristic circular signatures similar to those at Lac de Gras in the Northwest Territories where some of the richest diamond deposits in the world are now being mined or prepared for production. Follow up till sampling contained many kimberlite indicator minerals and three samples carried diamonds. This is significant on a worldwide basis, only one in 30,000 till sampling programs actually yield diamonds.

In 1999 and 2000, ground geophysical surveys and geological investigation were carried out. The ground surveys revealed 5 electromagnetic conductors within 250 metres of the surface that are coincident with the gravity and magnetic responses, 3 of the conductors are horizontal and 2 are vertical. The 2 vertical conductors are along fault shear structures with possible associated mineralization, having strike lengths of 1,500 metres and widths of 450-800 metres respectively, that are centred 250 metres below surface and extend to over 1,000 metres in depth.

In 2000 a drill hole on the Thrasher Zone of the Anomaly prior to reaching its targeted depth at 2,300 m was terminated at 1,812 m due to extreme ground water pressure and gravel run-in from aquifers. However, the drill hole revealed geological information of the region such as the contact between the Precambrian and younger overlying sediments at a depth of 1,167.50 m. The Precambrian formation outcrops just east of the Anomaly suggesting that the igneous intrusive to be shallower to the east.

Also, a 17,000 km aeromagnetic survey of the Parry Peninsula identified 76 kimberlite targets, 10 of which were drilled and 6 contain diamonds. This is a statistically significant result as only 14% of the world's known kimberlite contain diamonds. The relationship between the kimberlite pipes and the mafic intrusives is unknown.

Diamond Exploration

The Company's agreements with the Inuvialuit Land Corporation and with Diadem Resources Ltd. are set out in Note 3 to the financial statements dated December 31, 2004.

Diadem has undertaken a 50,000 line km airborne magnetic survey. Thus far, 26,000 kms have been flown over the Parry Peninsula. An additional 24,000 kms are to be flown. The project will include till sampling. The objective is to drill in 2006.

The Company's view is that the area has a potential for diamonds similar to those at Lac de Gras, N.W.T.

Base Metal Exploration

The Company has reviewed all the available geophysical and the geological data for the area of the anomaly and the surrounding area. This has been compared with the base metal data over the Sudbury Basin, the Norilsk Deposits, and the Bushveld Complex.

The Company plans a base metal exploration program to be carried out on a year-round schedule to include:

1. drilling two vertical electromagnetic conductors to intersect possible mineralization with the anomaly;
2. drilling the kimberlite targets within the anomaly to reveal sulphide fragments (xenoliths) revealing the composition of the anomaly and to upgrade the potential for additional diamondiferous kimberlites;
3. ground geophysical surveys and drilling of the anomaly for major nickel, copper, platinum and palladium information..

Financial Review

The attached “Financial Summary”, Schedule 1, summarizes the balance sheet, administrative expenses and cash flow for the 2nd Quarter and Half Year of 2005 with comparisons to same periods of 2004. An analysis of quarterly operations is provided by the “Summary of Quarterly Results”, Schedule 2. This summary covers administrative operations for the first two quarters of 2005 and the eight previous quarters of 2004 and 2003. The MD&A for the year ended December 31, 2004 contains general comments on quarterly operations for the eight quarters of 2004 and 2003. Bottom line, the quarterly results for 2005 indicate a “stand still” situation pending additional funding for base metals and anticipated success from the joint venture partner in its diamond exploration.

Quarterly expenditures cover current charges for rent, stock transfer and legal and audit services, interest payable to the Inuvialuit and other creditors and ongoing technical reviews conducted by various professionals. The professional services are being provided chiefly by the senior officers and directors and the reader will note from Note 2 to the half year Financial Statements, “Related Party Transactions,” that payments to senior officers and directors have been deferred.

A new charge to operations is that in connection with options granted to officers and directors. Under new accounting standards, when options are granted, an estimate is made of the fair present value of the options and this estimate is recorded as an operating expense at the time when the options become effective. This recording is in addition to the subsequent recording of the applicable subscriptions. In the present situation, as disclosed by Note 1 to the financial statements for the half year ended June 30, 2005, while options were granted on November 5, 2004, they were not exercisable until May 4, 2005 and therefore the relative Company expense, for \$76,600, was deferred until the 2nd quarter of 2005.

FINANCIAL SUMMARY

BALANCE SHEET

	June 30		December 31
	2005	2004	2004
	\$	\$	\$
Current assets and deposits	247,439	242,382	246,915
Less payables and advances	-2,317,533	-1,944,794	-2,077,359
<u>Working capital deficit</u>	<u>-2,070,094</u>	<u>-1,702,412</u>	<u>-1,830,444</u>
Mineral property and related expenditures	6,483,889	6,487,441	6,401,310
Less applicable income taxes	-867,145	-953,701	-867,145
<u>Net assets</u>	<u>3,546,650</u>	<u>3,831,328</u>	<u>3,703,721</u>
Share capital	18,083,110	17,787,280	18,006,510
<u>Deficit</u>	<u>-14,536,460</u>	<u>-13,955,952</u>	<u>-14,302,789</u>
<u>Net equity</u>	<u>3,546,650</u>	<u>3,831,328</u>	<u>3,703,721</u>

	2nd Quarter		Half Year	
	2005	2004	2005	2004

LOSS & DEFICIT

Administrative and general expenses	151,667	125,753	233,671	226,704
Future income tax (reduction) payable	nil	nil	nil	nil
<u>Loss for period</u>	<u>151,667</u>	<u>125,753</u>	<u>233,671</u>	<u>226,704</u>
Deficit at beginning of period	14,384,793	13,830,199	14,302,789	13,729,248
<u>Deficit at end of period</u>	<u>14,536,460</u>	<u>13,955,952</u>	<u>14,536,460</u>	<u>13,955,952</u>
<i>loss per share</i>	<i>0.004</i>	<i>0.003</i>	<i>0.006</i>	<i>0.006</i>
<i>diluted loss per share</i>	<i>0.004</i>	<i>0.003</i>	<i>0.006</i>	<i>0.006</i>

CASH FLOW

Funds received				
subscriptions for shares	nil	nil	nil	116,443
Less disbursements on				
exploration	48,290	52,404	82,579	97,791
administration	75,067	125,753	157,071	226,704
	<u>123,357</u>	<u>178,157</u>	<u>239,650</u>	<u>324,495</u>
Increase (decrease) in working capital	-123,357	-178,157	-239,650	-208,052
<u>Working capital (deficit) at beginning of period</u>	<u>-1,946,737</u>	<u>-1,524,255</u>	<u>-1,830,444</u>	<u>-1,494,360</u>
<u>Working capital (deficit) at end of period</u>	<u>-2,070,094</u>	<u>-1,702,412</u>	<u>-2,070,094</u>	<u>-1,702,412</u>

SUMMARY OF QUARTERLY RESULTS

	1st Quarter \$	2nd Quarter \$	3rd Quarter \$	4th Quarter \$	Year \$
LOSS & DEFICIT					
Year 2003					
Revenue	nil	nil	nil	nil	nil
Administrative & general expenses	106,117	128,392	142,415	122,349	499,273
Write down of mineral property				6,500,000	6,500,000
Future income tax (reduction) payable	117,156	96,298	13,200	-2,852,295	-2,625,641
Loss for period	223,273	224,690	155,615	3,770,054	4,373,632
Share issue expense			-2,223		-2,223
Deficit for period	223,273	224,690	153,392	3,770,054	4,371,409
<i>loss per share</i>	0.007	0.007	0.004	0.113	0.132
<i>diluted loss per share</i>	0.007	0.006	0.004	0.111	0.129
Year 2004					
Revenue	nil	nil	nil	nil	nil
Administrative & general expenses	100,951	125,753	130,608	106,067	463,379
Write down of mineral property	nil	nil	nil	196,718	196,718
Future income tax (reduction) payable	nil	nil	nil	-86,556	-86,556
Loss for period	100,951	125,753	130,608	216,229	573,541
Share issue expense					
Deficit for period	100,951	125,753	130,608	129,673	486,985
<i>loss per share</i>	0.003	0.003	0.004	0.006	0.016
<i>diluted loss per share</i>	0.003	0.003	0.004	0.005	0.016
Year 2005					
			Year to date		
Revenue	nil	nil	nil		
Administrative & general expenses	82,004 *	151,667	233,671		
Write down of mineral property					
Future income tax (reduction) payable					
Loss for period	82,004	151,667	233,671		
Share issue expense					
Deficit for period	82,004	151,667	233,671		
<i>loss per share</i>	0.002	0.002	0.006		
<i>diluted loss per share</i>	0.002	0.004	0.006		

* 2nd Quarter 2005 includes "Stock based compensation \$76,600"

	1st Quarter \$	2nd Quarter \$	3rd Quarter \$	4th Quarter \$	Year \$
CASH FLOW					
Year 2003					
Share subscriptions, less commissions	266,266	234,690	47,224	nil	548,179
Expenditures					
Administrative	106,117	128,392	142,414	122,350	499,273
Mineral property expenditures	110,843	75,310	132,361	217,429	535,943
	216,960	203,702	274,775	339,779	1,035,216
Change in working capital	49,306	30,988	-227,551	-339,779	-487,037
Year 2004					
Share subscriptions, less commissions	116,443	nil	219,230	nil	335,673
Expenditures					
Administrative	100,951	125,753	130,608	106,067	463,379
Mineral property expenditures	45,387	52,405	50,528	60,059	208,379
	146,338	178,158	181,136	166,126	671,758
Change in working capital	-29,895	-178,158	38,094	-166,126	-336,085
Year 2005					
			Year to date		
Share subscriptions, less commissions	nil	nil	nil		
Expenditures					
Administration	82,004	75,067	116,295		
Mineral property expenditures	34,291	48,290	150,586		
	116,295	123,357	266,881		
Change in working capital	-116,295	-123,357	-266,881		