

DARNLEY BAY RESOURCES LIMITED

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Management's Discussion and Analysis for the interim period ended September 30, 2006

GENERAL

Darnley Bay Resources Limited was formed in 1993 to explore and develop an area of geophysical significance in the Northwest Territories of Canada. Base metal exploration fortuitously resulted in the discovery of diamonds and the area is now host to both metallic and non-metallic mineral deposit interests. The Company's objectives are to secure and maintain successful financing partnerships to continue exploration for both base metals and diamonds resulting in the development of a profitable mining camp.

BALANCE SHEET AND OPERATIONS

At September 30, 2006, assets totaled \$209,773 compared to \$239,263 at the December 31, 2005 year-end. A deposit of \$83,468 on mining permits advanced by the Company's joint venture partner was forfeited in the nine-month period. During the first nine months of 2006, the Company has not capitalized any mineral property expense (\$83,942 and \$166,521 in the three and nine-month periods in 2005). The current liability increased to \$2,696,922 from \$2,476,915 at the 2005 year-end. The Company issued 468,146 common shares through a debt conversion at \$0.15 per share resulting in a total increase in capital stock of \$70,500 in the three-month period (nil in 2005). The existing stock options incurred a stock-based compensation expense of \$149,272 in the nine-month period. The fair value of the options is recorded into contributed surplus in the nine-month period. The Company reported a loss for the three and nine-month periods of \$240,207 and \$468,991 compared to \$59,294 and \$292,963 in 2005. The ongoing corporate and general expenses required to run a public company continue to be monitored closely.

LIQUIDITY AND CAPITAL RESOURCES

The Company is an exploration and development company and has no revenue. At September 30, 2006, the Company had cash resources of \$51,720 compared to \$3,808 at the December 31, 2005 year-end. Advances of \$70,500 were received in the three-month period and shares were issued through private placements of 705,000 shares at \$0.10 per share on October 23, 2006. The Company has a working capital deficit of \$2,637,150 compared to \$2,471,121 at year-end 2005 and an accumulated deficit of \$20,912,183 (\$20,443,192 at the year-end). The Company is actively working to reduce liabilities through ongoing negotiations with primary creditors plus a debt settlement plan that includes conversion to common shares where allowable is being tabulated.

LIQUIDITY AND CAPITAL RESOURCES continued

The Company is in partnership with Diadem Resources Ltd. to ensure the continuation of the diamond exploration program and is seeking additional funding through equity financing for the base metal project.

The Company's current funding objective is to support a base metal exploration program that will include a review of the available geological and geophysical data relating to the area of interest and to drill the intrusive, and potential sulphide deposit, at its shallowest point. To enable the Company to carry out its plan, additional funds are now being sought. The Company's ability to raise the capital resources to undertake this objective is dependent on the venture capital market, metal prices and the replacement of a former agreement allowing access to the property for the purpose of base metal exploration.

SUMMARY OF QUARTERLY RESULTS

<i>For the quarter ended</i>	<i>Sep. 30</i> <i>2006</i>	<i>Jun. 30</i> <i>2006</i>	<i>Mar. 31</i> <i>2006</i>	<i>Dec. 31</i> <i>2005</i>
Net loss (in thousands)	469	229	102	5,847
Loss per common share	0.01	0.001	0.001	0.001
Total assets (in thousands)	210	159	237	239
Shareholders' equity (deficiency) (in thousands)	(2,487)	(2,466)	(2,340)	(2,238)
 <i>For the quarter ended</i>	 <i>Sep. 30</i> <i>2005</i>	 <i>Jun. 30</i> <i>2005</i>	 <i>Mar. 31</i> <i>2005</i>	 <i>Dec. 31</i> <i>2004</i>
Net loss (in thousands)	59	152	82	216
Loss per common share	0.002	0.004	0.002	0.006
Total assets (in thousands)	6,813	6,731	6,684	6,648
Shareholders' equity (in thousands)	3,489	3,547	3,622	3,704

ANALYSIS OF MINERAL PROPERTY EXPENDITURES

	<i>Sept. 30,</i> <i>2006</i>	<i>Sept. 30,</i> <i>2005</i>	<i>June30,</i> <i>2006</i>	<i>June 30,</i> <i>2005</i>
Project management	-	14,667	-	15,998
Engineering services	-	(71)	-	4,969
Project consulting fees	-	-	-	-
Property access and services	<u>-</u>	<u>69,346</u>	<u>-</u>	<u>27,321</u>
	-	83,942	-	48,288

ANALYSIS OF CORPORATE AND GENERAL EXPENSES

	<i>Sept 30, 2006</i>	<i>Sept. 30, 2005</i>	<i>June 30, 2006</i>	<i>June 30, 2005</i>
Project consulting fees/services	11,697	-	18,837	-
Stock based compensation	149,272	2,100	-	76,600
Accounting services	7,500	21,000	14,620	19,500
Management services	25,250	6,000	15,500	8,400
Premises rent	10,351	2,251	13,801	15,000
Audit fees	-	8,125	17,650	11,550
Legal fees	-	-	-	-
Office services & supplies	13,500	2,988	6,482	2,184
Administration services	8,800	5,293	8,000	5,400
Stock transfer/exchange fees	7,942	3,893	5,497	8,058
Shareholder communication	4,150	4,801	4,536	1,069
Interest	1,745	2,843	21,554	3,906
Miscellaneous	<u>-</u>	<u>-</u>	<u>38</u>	<u>-</u>
	240,207	59,294	126,515	151,667

COMMON SHARES ISSUED

Common shares issued at September 30, 2006 were 37,584,752 (37,116,606 at the year-end). The additional 468,146 shares at \$0.15 were issued in the three-month period through the conversion of \$70,222 in debt. There are share purchase options for directors, officers and consultants at an exercise price of \$0.13 (3,500,000) and \$0.10 (100,000) expiring on November 4, 2009 and in accordance with the Company's Stock Option Plan (see note 5b of the interim financial statements). The Company will make 500,000 shares available to Carnarvon Capital Corporation when the Darnley Bay/Diadem diamond joint venture meets a \$2 million exploration expenditure target. The Company has 41,866 shares in escrow. At the time of this report an additional 705,000 shares were issued at \$0.10 per share for a total of 38,294,752 issued shares.

ACCOUNTING POLICIES

The Company's accounting methods are based upon Canadian Generally Accepted Accounting Principles (GAAP) applicable to resource issuers, which are applied on a consistent basis. These are outlined in full detail in note 2 of Company's audited financial statements for the year ended December 31, 2005.

The recovery of amounts capitalized as Mineral Property expenditures is dependent upon the discovery of economically recoverable ore reserves, the ability of the Company to obtain necessary financing to explore and develop potential ore reserves, future profitable production, or alternatively, upon the Company's ability to dispose of its interests on an advantageous basis. At the 2005 year end, the carrying value of the mineral exploration

ACCOUNTING POLICIES continued

property was considered unrecoverable and written down to \$1 due to uncertainties in financing. The Company continues to retain interest in its property and looks to future funding opportunities and ongoing exploration for both base metals and diamonds.

The Company uses the fair value method of accounting for all stock options awarded. Compensation expense is recognized based on the fair value of the option on the date of the grant and is expensed over the vesting period of the option (see note 5c of the 2005 annual statement)

RELATED PARTY TRANSACTIONS

Technical and administrative support is received from directors and officers of the Company. In the absence of financial resources to pay for these services, the allowable issuance of common shares for debt is undertaken. In the three and nine-month periods ended June 30, 2006, amounts charged for management fees, office services and rent by La Prairie Ltd. (controlled by Leon La Prairie, CEO/director) were \$23,419 and \$70,514 (\$22,779 and \$75,341 in 2005). Mr. La Prairie charged \$19,250 and \$44,250 for consulting services (2005 - \$12,999 and \$33,666). Accounting services were provided in the amount of \$25,500 in the nine-month period (\$19,500 in the three-month and \$58,500 in the nine-month period in 2005) by the Company's former CFO, Richard La Prairie. William Allen, director, provides legal services to the Company; no services were provided in the nine-month period in 2006 and 2005 however, an accrual of \$15,000 was made in 2005. Patricia Mannard provided corporate maintenance and accounting management services in the amount of \$7,500 and \$16,120 in the three and nine-month periods (\$640 and \$9,640 in 2005). John Dowsett, a director, provided geophysical and project development services in the amount of \$4,775 and \$11,275 (\$nil and \$6,244 in 2005). George Kent, a director, provided geological consulting services in the amount of \$442 and \$2,990 (nil in 2005). As at September 30, 2006, accounts payable to the above total \$648,745 (2005 - \$591,824).

COMMITMENTS

Note 3 of the financial statements for the year ended December 31, 2005 covers both the governing agreements with the Inuvialuit Land Corporation and the joint venture agreement with Diadem Resources Ltd. for exploration of diamonds.

Effective November 26, 2003 the Company entered into an agreement to form a joint venture with Diadem Resources Ltd., formerly an agreement held with Carnarvon Capital Corporation, to operate diamond exploration in an area near Paulatuk in the Northwest Territories. Diadem has not met earn in requirements outlined in the agreement at the time of this report.

The joint venture entered into a letter agreement with the Inuvialuit Regional Corporation allowing access to the property that lies within the Inuvialuit Settlement Region. The

COMMITMENTS continued

Company's joint venture partner has, at the time of this report, not confirmed that the conditions of the agreement have been met however; the Company has not received a notice of default as required by the agreement.

A debt settlement arrangement has been made with a former officer of the Company. An initial amount of \$70,222 was converted to 468,146 shares at \$0.15. A balance of \$134,000 can be paid in cash at any time or be converted to shares, as permitted, on an annual schedule at the then market price. The former CFO is retained as a consultant to the Company.

RISKS AND UNCERTAINTIES

The inherent risks, which most profoundly affect the Company's activities, are metal prices and the ability of the Company to obtain venture capital necessary to establish economic ore reserves. Further, the Company is relying on its joint venture partner to fulfill its obligations as operator of the diamond exploration project and the Inuvialuit Regional Corporation to allow property access for diamond exploration.

OUTLOOK

The ongoing rally in metal prices and the influx of major mining companies participating in diamond exploration in the area surrounding our interests in the Northwest Territories has bolstered financing possibilities. Renewed interest from the investment community including third party interest in the diamond exploration and continuing support from the Inuvialuit and other local participants is encouraging. The Company anticipates the commencement of diamond target drilling by its joint venture partner. A base metal exploration schedule is in place to further define the property's potential contingent upon the receipt of funds through equity financing or joint ventures on terms most favourable for our shareholders.

This MD&A contains certain forward-looking statements related but not limited to the Company's operations, anticipated financial performance, business prospects and strategies. Forward-looking information typically contains statements with words such as "anticipate", "believe", "expect", "plan" or similar words suggesting future outcomes. Readers are cautioned to not place undue reliance on forward-looking information because it is possible that the Company will not achieve predictions, forecasts, projections and other forms of forward-looking information.

THE MANAGEMENT'S DISCUSSION AND ANALYSIS SHOULD BE READ IN CONJUNCTION WITH THE COMPANY'S AUDITED FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2005 AND THE INTERIM STATEMENTS FOR THE NINE-MONTH PERIOD ENDED SEPTEMBER 30, 2006 WHICH ACCOMPANY THIS ANALYSIS AND, ALTERNATELY ARE AVAILABLE ALONG WITH ALL THE COMPANY'S PUBLIC DOCUMENTS ON

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