

Annual Report 2005



Exploration

Committed to a three-year, \$10 million annual exploration expenditure



Mining

Balmat Mine to re-open in Q2, 2006



Metals

Un-hedged position provided a strong performance in 2005

HudBay Minerals Inc.
vertically integrated – mines to metals

HUDBAY
MINERALS INC

Corporate profile

HudBay Minerals Inc. is a vertically integrated Canadian mining company producing zinc, copper, gold, silver metal and zinc oxide in Manitoba, Saskatchewan and Ontario, as well as New York and Michigan states in the USA.

HudBay is the third largest producer of both zinc metal and copper metal in Canada and the third largest producer of zinc oxide in North America.

The Manitoba and Saskatchewan operations benefited from a \$435 million capital expenditure completed in 2004 to bring two new mines into production and expand and modernize the metallurgical plant.

Annual production capacity is approximately 115,000 tonnes of zinc, 45,000 tonnes of zinc oxide, 90,000 tonnes of anode copper, 100,000 ounces of gold, and 1,000,000 ounces of silver.

Additionally the Balmat zinc mine in New York state, which is planned to re-open before the end of the second quarter of 2006, will annually produce approximately 60,000 short tons of zinc in concentrates at full production.

In January 2006, the Company completed the purchase of the White Pine Copper Refinery in Michigan, which completes the copper vertical integration of the Company.

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(Left) Shift meeting to discuss safety and operations before going underground. (Right) Remote ore mucking equipment underground at the 777 Mine.

Investor highlights

- Record earnings \$85 million
- Record operating cash flow \$145 million
- Cash on hand \$142 million and net debt \$67 million
- Mineral reserves of 21.4 million tonnes and mineral resources of 4.9 million tonnes
- Aggressive \$10 million annual exploration program
- Committed to outstanding safety, health and environmental performance






Full vertical integration from exploration through to metal sales. Proven mining and metallurgical abilities with an experienced management team and a stable, skilled labour force. Positioned for growth.

Our competitive advantages

Financial position	Mineral reserves and resources	Exploration
<ul style="list-style-type: none"> record earnings of \$85 million (\$1.04 per share) operating cash flow of \$145 million (\$1.77 per share) net debt of \$67 million new \$25 million credit facility metals un-hedged 	<ul style="list-style-type: none"> reserves of 21.4 million tonnes resources of 4.9 million tonnes long history of adding to reserves and resources 25 mines discovered to date in Manitoba and Saskatchewan 	<ul style="list-style-type: none"> \$10 million annual exploration expenditure ~210,000 hectares of exploration land in Flin Flon Greenstone Belt ~20,000 hectares in Balmat district extensive zinc prospect lands in SW Ontario Tom Valley lead/zinc deposit in the Yukon San Antonio copper prospect in Chile

HudBay Minerals Inc. at-a-glance


Mines

777 Mine, Manitoba	Trout Lake Mine, Manitoba	Konuto Mine, Saskatchewan	Chisel North Mine, Manitoba	Balmat Mine, New York
				
<ul style="list-style-type: none"> first production in 2004 HudBay's flagship mine ore production in 2005 was 1.1 million tonnes ore production increased to 1.35 million tonnes as of January 2006 increased production replaces Konuto mine production 	<ul style="list-style-type: none"> first production in 1982 ore production in 2005 was 859,000 tonnes 	<ul style="list-style-type: none"> first production in 1999 mine was closed in October 2005, as planned, due to ore depletion production will be replaced by the 777 mine increased production 	<ul style="list-style-type: none"> first production in 2000 ore production in 2005 was 337,000 tonnes 	<ul style="list-style-type: none"> first ore production before the end of Q2, 2006 will produce up to 60,000 tons of zinc in concentrate when in full production in 2008 majority of concentrate will be treated at the CEZ refinery in Quebec

Concentrators

Flin Flon Concentrator	Snow Lake Concentrator	Balmat Concentrator
<ul style="list-style-type: none"> the Flin Flon concentrator produces copper and zinc concentrates from ore mined at the 777, Trout Lake, and Konuto mines 	<ul style="list-style-type: none"> the Snow Lake concentrator processes Chisel North mine ore and produces zinc concentrate 	<ul style="list-style-type: none"> the Balmat concentrator will process the Balmat mine's ore to produce zinc concentrate

Vertical integration	Mining and metallurgical skills	Growth
<ul style="list-style-type: none"> • full credit for contained metal in concentrates • premium price for metal sales • strong differentiation from competitors • insensitive to metallurgical treatment charges 	<ul style="list-style-type: none"> • industry leading safety performance • long-stayed senior management • stable and skilled labour force • wide range of skills from vertical integration • proven project performance 	<ul style="list-style-type: none"> • annual \$10 million exploration expenditure underway • Balmat zinc mine first ore Q2, 2006 • White Pine purchase complete, January 2006 • financially well positioned

Zinc Plant, Manitoba	Zochem Zinc Oxide, Ontario	Copper Smelter, Manitoba	White Pine Copper Refinery, Michigan
			
<ul style="list-style-type: none"> • leading edge technology with world's first two-stage pressure leaching and state of the art electrolysis • processes HudBay's zinc concentrates with an annual capacity of 115,000 tonnes of special high grade zinc • Canada's third largest production of zinc metal 	<ul style="list-style-type: none"> • annual capacity of 45,000 tonnes of zinc oxide • consumed approximately 32,000 tonnes of HudBay's zinc and sold 43,200 tonnes of zinc oxide in 2005 • North America's third largest production of zinc oxide accounting for approximately 18% of the market 	<ul style="list-style-type: none"> • copper production from HudBay and purchased concentrates • produced 86,300 tonnes of anode copper in 2005 • proven pyro-metallurgical process • Canada's third largest production of copper metal 	<ul style="list-style-type: none"> • purchase complete, January 2006 • provides HudBay with a dedicated refinery and a refining cost of approximately US\$0.06/lb • significantly reduces unit operating costs for copper refining in 2006 and beyond

Marketing

Considar Metal Marketing, Toronto

- | | | | |
|--|---|---|--|
| <ul style="list-style-type: none"> • HudBay's 50% owned marketing company | <ul style="list-style-type: none"> • in the process of contractually changing to an agency arrangement, whereby HudBay will own products until sold to customers | <ul style="list-style-type: none"> • sells zinc, copper, gold, silver and zinc oxide | <ul style="list-style-type: none"> • purchases zinc and copper concentrates, as required, to fill HudBay's metallurgical plants |
|--|---|---|--|

Message from the President & CEO

2005 was a highly successful year of transition and growth as HudBay embarked on its first full year as a publicly traded company.

After acquiring Hudson Bay Mining and Smelting Co., Limited (HBMS) in December 2004, we laid the groundwork for the Company to grow, producing zinc, copper, gold, silver and zinc oxide.

We set ambitious goals entering 2005 and I am pleased to report that we achieved most, if not all of our objectives. We are about delivering results and our first full year as a new company delivered those results.

Completion of the \$435 million 777 group of projects in 2004, together with an excellent safety and operating performance in 2005, and increasing metal prices throughout the year, provided HudBay with an exceptional financial performance. During 2005, we increased the ore production rate at our 777 mine so that in 2006 it will have a production capability of 1.35 million tonnes per annum. This production increase completely offsets the closure of our Konuto mine in October 2005, as planned.

A key growth decision in 2005 was to re-open the Balmat zinc mine in upstate New York. We achieved this goal, after completing a positive feasibility study, in November 2005. We anticipate bringing the mine to production before the end of the second quarter 2006 and when at full production in 2008, it will produce approximately 60,000 tons of zinc in concentrate annually.

Another key growth achievement in 2005 was the acquisition of the White Pine Copper Refinery in Michigan. We exercised our option to acquire 100% ownership of the refinery in October and the purchase was concluded in January 2006 for US\$15.1 million. The refinery has processed our copper anodes to refined copper for many years and now provides us a guaranteed location for anode refining at a significantly reduced unit cost.

The acquisition of the White Pine Refinery further enhances our vertical integration, which sets us apart from other intermediate sized mining companies. Our vertical integration from exploration through to metal sales allows us to gain full credit

for metal contained in concentrates while at the same time capturing significant metal price premiums. In Canada, we are the third largest producer of copper metal and the third largest producer of zinc metal and in North America, we are the third largest producer of zinc oxide.

Strong financial performance

Our financial performance in 2005 was exceptional with a record \$652 million revenue, along with record earnings of \$85 million or \$1.04 per share.

A strong production performance was combined with an un-hedged metals position, so we fully benefited from metal price increases. For the fourth quarter 2005, our production costs were a remarkable US\$0.11/lb. of zinc net of by-product credits.

Our annual operating cash flow in 2005 was \$144.8 million, or \$1.77 per share and it is particularly pleasing to report that at year-end we had reduced our net debt to approximately \$67 million. If year-end metal prices are sustained during 2006, we would expect to be net debt free during the year.



Peter R. Jones
President & Chief Executive Officer

Subsequent to the end of last year, we announced in February, the successful completion of a \$25 million credit facility with The Bank of Nova Scotia. At the same time, we also announced repurchase through the open market of US\$19 million of our 9 5/8% senior secured notes due January 5, 2012.

Safety, health and environment

It gives me great personal pleasure to be able to report that our Manitoba, Saskatchewan and Ontario operations in 2005 achieved the best safety performance in our more than 75 year history with a Lost Time Accident (LTA) frequency of 0.62 based on 200,000 hours worked. Our employees and contractors produced an exceptional performance in an area of critical importance to HudBay.

Our management focus is a systematic approach and we have achieved significant recognition by being the only mining company in Canada to be certified to ISO 14001 for Environmental Management, OHSAS 18001 for Health and Safety

Management and additionally, our products are certified to the ISO 9001 Quality Management Standard.

In addition we constantly strive to minimize environmental emissions and employ the best available technology to ensure compliance with governmental regulations.

Positioned for growth

As we move forward, HudBay is now well positioned to build on our three-pronged growth strategy.

Our first priority is the continuation of an annual exploration expenditure of \$10 million in the prolific Flin Flon Greenstone Belt around our northern Manitoba facilities where we have discovered 25 mines historically and have many high priority targets. A new mine here will be complemented by existing infrastructure and be highly financially beneficial to the Company. During 2006 we plan to expand our exploration activities in Canada and elsewhere, including our lead/zinc deposit in the

Yukon, our zinc prospects in Ontario and our copper prospect in Chile, as well as the approximate 20,000 hectares held by us around the Balmat mine.

Our second thrust is to re-open the Balmat zinc mine and to take full advantage of our new ownership of the White Pine Copper Refinery. These opportunities will increase our production of zinc in concentrate and reduce our unit refining cost for copper.

Our third thrust is to identify merger and acquisition opportunities. Personnel are already evaluating opportunities to grow HudBay, with a focus on zinc, but not to the exclusion of our other products or further vertical integration. Our merger and acquisition plans are a key focus for 2006 and we plan to devote considerable energy ensuring that these activities add real shareholder value.

Consistent with our growth plans in 2006, we plan to continue to improve our financial strength, including, from time to time, deploying cash toward further debt reduction.



The zinc plant uses a state of the art electrolytic cellhouse (shown) and the world's first use of two-stage pressure leaching.

Delivering results

2005 goals	2005 achievements
<ul style="list-style-type: none">• efficient, productive operations• complete Balmat feasibility study• complete copper vertical integration• improve financial strength & liquidity• complete environmental assessment• increase exploration spending	<ul style="list-style-type: none">• four great quarters• Balmat first ore before the end of Q2, 2006• White Pine acquisition complete, January 2006• \$25 million credit facility; cash at year end \$142 million• financial provisions confirmed adequate• \$10 million annual expenditure underway

The Company is financially well positioned to deliver on its growth strategy. Our long-term objective is to grow towards being a major Canadian mining company in base metals, with a focus on zinc. Our financial strength, the intellectual knowledge base of our excellent people and our vertical integration present unique opportunities for us to realize opportunities that will be truly beneficial to the Company and its shareholders.

This last year allowed us to demonstrate that HudBay is a cost effective and consistent producer of zinc, copper, gold, silver and zinc oxide and our performance has built sound credibility within the investment community. These are exciting times for HudBay and as we move ahead through 2006, we do so with great enthusiasm.

The year ahead

Looking forward to 2006, our expectations are for continued price strength in the metals markets with strong underpinnings being in place for copper and especially zinc. The supply of zinc appears to be continuing in deficit and there are expectations that the London Metal Exchange zinc metal inventory will be substantially reduced during 2006. Further, the mine supply of zinc concentrates going forward appears to be in deficit compared to likely consumption demand. I look forward to our Balmat mine starting production and the reduced unit processing costs from the purchase of the White Pine Refinery.

I expect 2006 to be a year when the Company continues to improve its financial strength and growth capability.

Our achievements of the past year were possible by the dedication of our experienced management team, supported by our board of directors as well as our stable and skilled workforce. I also particularly want to thank HudBay shareholders for their continued confidence and support.

(signed) Peter R. Jones

Peter R. Jones
President and Chief Executive Officer



Zinc

- Annual production ~115,000 tonnes of zinc metal
- Third largest producer of zinc metal in Canada
- ~75% of zinc metal sold directly to customers
- Zinc price premium up to US 7¢/lb in 2005.

Copper

- Annual production ~ 90,000 tonnes of copper anode
- Third largest producer of copper metal in Canada
- White Pine Refinery – purchased 2006
- Copper price premium up to US 6¢/lb in 2006

Gold and silver

- Annual production ~100,000 oz. of gold
- Annual production ~1,000,000 oz. of silver
- Most gold and silver produced from HudBay owned mines
- Produced during electrolysis at White Pine Copper Refinery

Zinc oxide

- Annual production ~ 45,000 tonnes of zinc oxide
- Third largest zinc oxide producer in North America
- Produced by 100% owned Zochem division
- ~25% of HudBay zinc metal used by Zochem

Our markets

During 2005, HudBay's zinc, copper, gold, silver and zinc oxide sales were by the Company's 50% owned Consider Metal Marketing Inc. (CMM) based in Toronto. CMM also arranged concentrate purchases for the Company as necessary to fill its metallurgical plants.

CMM sells HudBay's zinc oxide through an established network of distributors and warehouse facilities in the United States and Canada. An important part of CMM's services is the arrangement of transportation for both concentrates to our metallurgical plants and the distribution of metals and oxide products to customers. During 2005 HudBay realized prices of US\$0.65/lb. for zinc,

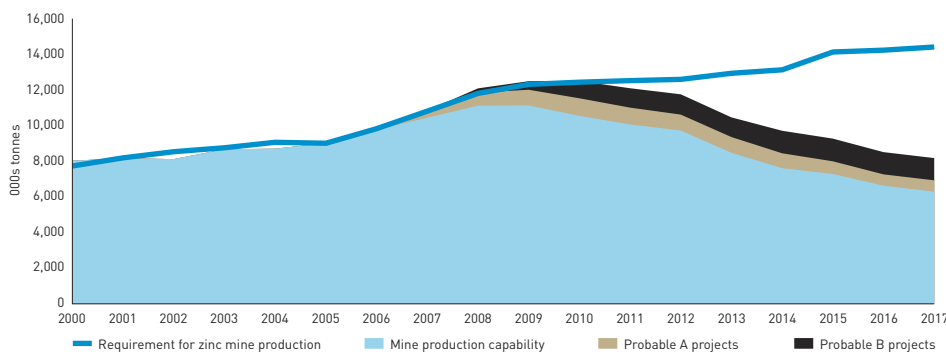
US\$1.72/lb. for copper, US\$445 oz. for gold and US\$7.28 oz. for silver.

To comply with requirements to maximize the size of revolver credit facilities available to the Company as at January 1, 2006, HudBay changed its relationship with CMM from a sales to an agency arrangement, whereby copper and precious metals inventory are owned by the Company until sold to

customers. In the first half of 2006 the Company plans to convert its remaining products of zinc and zinc oxide to the same agency arrangement.

Projections in 2006 and beyond suggest that mine supplied zinc concentrate will be in deficit compared to world projected consumption. HudBay is largely self-sufficient in zinc concentrates.

Global zinc mine production vs primary demand



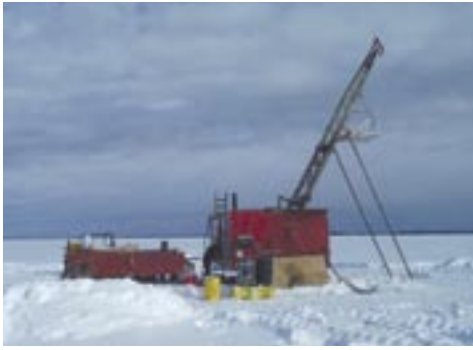
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Skimming dross in the zinc casting plant. At 99.95% pure, the zinc produced is some of the purest in the world.



A man in an orange safety shirt is shown in profile, looking down at a cylindrical diamond drill core sample he is holding with both hands. He is in a laboratory or processing area, with numerous other drill core samples laid out on a table in the foreground. The background is slightly blurred, showing industrial lighting fixtures and a window. The text is overlaid on the left side of the image.

Analyzing diamond drill
core samples. HudBay
has committed to a
\$10 million annual
exploration expenditure.



(Left) Winter drilling on a lake near Flin Flon.
(Right) Summer drilling camp.

Exploration

Historically, HudBay has discovered 25 mines in the Flin Flon Greenstone Belt and presently has a large number of exploration targets in the Belt, including more than 1,200 geophysical targets to drill test.

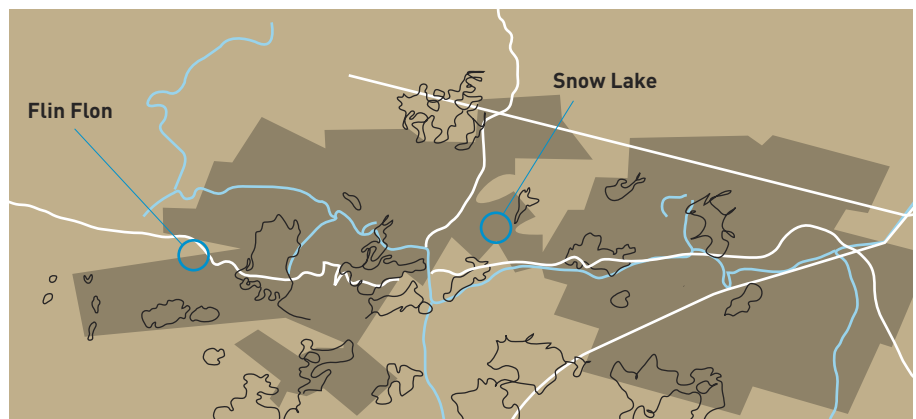
Key exploration properties

- ~210,000 hectares ⁽¹⁾ in the Flin Flon Greenstone Belt, Manitoba/Saskatchewan
- ~20,000 hectares in the Balmat District, New York state
- Tom Valley lead/zinc deposit, Yukon
- Zinc properties, SW Ontario
- San Antonio copper property, Chile
- Gays River property, Nova Scotia ⁽²⁾

(1) at the end of 2005

(2) subject to sale to Acadian Gold Corporation

Flin Flon Greenstone Belt Northern Manitoba and Saskatchewan



The focus of the 2005 Flin Flon Greenstone Belt exploration program was geophysical anomalies, structural re-interpretations, and upgrading of known mineralization. Exploration in the Belt was conducted by Hudson Bay Exploration and Development Company Limited (HBED), a wholly owned subsidiary. HBED has established an exceptional record of success of discovering new ore bodies over many years.

HudBay has committed to a \$10 million annual exploration expenditure in the Belt over three years. During 2005 approximately \$5.9 million was expended, as funding was not available at the start of the year.

Exploration in the Belt is a key part of the Company's growth strategy. A discovery would be in close proximity to existing infrastructure including concentration and metallurgical facilities. A focus of the Belt's 2005 exploration program was the Snow Lake area where 50% of the funding was expended on high priority targets and where the ore concentrator has available capacity.

The Company raised exploration funding by two flow through share issues of \$2.5 million and \$7.5 million respectively in 2005, adequate to support funding through the first quarter of 2006. It is planned that additional flow through funding will be raised for 2006 and

2007 expenditures in the Belt and for exploration elsewhere in Canada.

In 2006 and beyond the Company plans to continue its aggressive Flin Flon Greenstone Belt exploration and also to extend its exploration efforts in Canada and elsewhere including exploring its approximately 20,000 hectares of land holdings in the Balmat district of New York state, its prospective SW Ontario zinc properties as well as the Tom Valley lead/zinc deposit in the Yukon and the San Antonio copper property in Chile.



(Left) The Balmat zinc mine in New York state. (Right) Miners preparing to go underground.

Mines and concentrators

In 2005 HudBay operated four mines in northern Manitoba and Saskatchewan and two ore concentrators, one at Snow Lake and the other at Flin Flon.

Production from our mines was similar to 2004, however the new 777 Mine increased its ore production to 1.1 million tonnes in 2005 and at year end was capable of producing at its full rate of 1.35 million tonnes per annum. Consistent with the 777 mine increase in production, the Konuto mine was depleted and closed late in 2005.

The Konuto mine, located in Saskatchewan, was a very successful mine and the employees have been transferred primarily to the 777 mine. During the year, work started on the re-opening of the Balmat zinc mine in New York state. This mine is expected to commence ore production before the end of the second quarter of 2006.

Both ore concentrators produced well during 2005 and the Flin Flon concentrator improved recovery of both gold and zinc while the Snow Lake concentrator continued its very high zinc recovery at 97.3%, despite lower zinc ore head grades.

A summary of production statistics for the year ended December 31, 2005, together with comparative information for 2004 is shown in the following table:

Mines		Year ended Dec 31	
		2005	2004
777	tonnes	1,093,683	975,895
▪ Copper	%	2.24	2.89
▪ Zinc	%	4.47	4.50
▪ Gold	g/tonne	2.09	2.26
▪ Silver	g/tonne	23.83	23.14
Trout Lake	tonnes	858,751	916,097
▪ Copper	%	1.39	1.46
▪ Zinc	%	5.61	5.32
▪ Gold	g/tonne	1.47	1.47
▪ Silver	g/tonne	14.61	13.58
Chisel North	tonnes	336,731	327,853
▪ Zinc	%	9.00	9.99
Konuto	tonnes	312,465	327,231
▪ Copper	%	3.90	4.07
▪ Zinc	%	1.81	2.08
▪ Gold	g/tonne	1.65	1.92
▪ Silver	g/tonne	9.15	9.60
Total Mines	tonnes	2,601,630	2,547,076
▪ Copper	%	1.89	2.18
▪ Zinc	%	5.11	5.19
▪ Gold	g/tonne	1.64	1.70
▪ Silver	g/tonne	19.40	18.26

Concentrators		Year ended Dec 31	
		2005	2004
Flin Flon Concentrator	tonnes	2,262,555	2,156,051
▪ Copper	%	2.14	2.46
▪ Zinc	%	4.53	4.50
▪ Gold	g/tonne	1.78	1.89
▪ Silver	g/tonne	18.14	17.31
▪ Copper Concentrate Grade	tonnes % Cu	188,851 23.82	208,961 23.60
▪ Zinc Concentrate Grade	tonnes % Zn	164,417 51.51	152,453 50.42
▪ Copper recovery	%	92.8	93.0
▪ Gold recovery	%	74.9	69.6
▪ Silver recovery	%	66.3	68.1
▪ Zn recovery	%	82.6	79.2
Snow Lake Concentrator	tonnes	331,427	327,853
▪ Zinc	%	9.00	9.99
▪ Zinc Concentrate Grade	tonnes % Zn	56,646 51.25	61,825 51.52
▪ Zn recovery	%	97.3	97.3

Mineral reserves as at January 1, 2006

Mine	Tonnes	Au (g/t)	Ag (g/t)	Cu (%)	Zn (%)
777					
▪ Proven	3,474,000	2.5	28.4	2.4	4.7
▪ Probable	12,261,000	2.1	25.7	2.5	4.4
Trout Lake					
▪ Proven	1,433,000	1.0	11.1	1.4	4.7
▪ Probable	1,058,000	1.7	20.5	2.5	4.0
Chisel North					
▪ Proven	661,000	-	-	-	8.9
▪ Probable	761,000	-	-	-	8.4
Balmat					
▪ Proven	686,000	-	-	-	10.6
▪ Probable	1,023,000	-	-	-	11.4
Total Proven	6,254,000	1.6	18.3	1.6	5.8
Total Probable	15,103,000	1.8	22.3	2.2	5.0
Total Reserves	21,357,000	1.8	21.1	2.0	5.3

HudBay estimated proven and probable aggregate mineral reserves as at January 1, 2006 are 21.4 million tonnes.

Separately, as of January 1, 2006, we estimated aggregate inferred mineral resources at our 777, Trout Lake and Chisel North Mines in northern Manitoba and our Balmat Mine in New York state at 4,940,000 tonnes at 1.2 g/t gold 19.1 g/t silver, 1.0% copper and 7.45% zinc.

Balmat zinc mine re-opening ⁽¹⁾

As part of HudBay's growth strategy, in November 2005, after completing a feasibility study, HudBay announced re-opening of the Balmat zinc mine and ore concentrator in New York state. The Balmat mine has been maintained to a high standard, during care and maintenance, since 2001 and includes a 3,200 ft. deep shaft, underground

development to five ore zones and extensive mining equipment as well as a 5,000 ton per day concentrator.

The Balmat mine mineral reserves are estimated at 1,709,000 tonnes at 11.1% zinc and mineral resources estimated at 1,281,000 tonnes at 13.2% zinc, based on high grade selective mining and in compliance with National Instrument 43 – 101.

HudBay expects the mine to be at full production in 2008 when it will produce annually 60,000 tons of zinc in concentrate. Based on mineral reserves and resources the mine life will be approximately seven years, and a planned increase to resources from an underground exploration program is likely to increase the life of the mine. The Balmat mine has a major project capital cost of approximately US\$20 million. Operating costs are expected

to be US\$0.40/lb. of zinc, while total costs including capital, are expected to be US\$0.48/lb. of zinc over the mine life. Based on a zinc price of US\$0.56/lb. for three years and US\$0.50/lb. thereafter, the mine is expected to produce a greater than 20% Internal Rate of Return after tax. Recent zinc prices have been substantially greater than the long-term prices used for the feasibility study.

Balmat zinc concentrate is planned to be processed at the Canadian Electrolytic Refinery in Quebec, some 158 kilometers from the mine, with up to 40% of the concentrate treated at HudBay's zinc plant in Manitoba.

HudBay also holds approximately 52,000 acres of exploration land in the Balmat district and expects to do exploration on these lands in 2006.

(1) Balmat production is shown in short tons, and exploration lands are shown in acres.

The casting wheel in the pyro-metallurgical copper smelter. The smelter has the capacity to produce approximately 90,000 tonnes of copper anode annually.





(Left) The White Pine Copper Refinery in Michigan. (Right) The zinc plant's state of the art electrolytic cellhouse in Flin Flon.

Metallurgical plants

At Flin Flon, in northern Manitoba, HudBay has a hydro-metallurgical zinc plant and a pyro-metallurgical copper smelter.

Additionally in Brampton, Ontario Zochem – a wholly owned subsidiary – off-takes approximately 25% of HudBay's zinc metal and converts it to zinc oxide. In Michigan HudBay owns, as of January 1, 2006, the White Pine Copper Refinery which takes all of the copper smelter

anode production and refines it to industry standard cathode copper, for sale.

Our metallurgical plants' annual production capacity is 115,000 tonnes of zinc, 90,000 tonnes of anode copper, approximately 100,000 ounces of gold,

in excess of 1,000,000 ounces of silver and up to 45,000 tonnes of zinc oxide. Additionally the Balmat mine in New York state will have a capacity of 60,000 tons of zinc metal, in concentrate, when at full production in 2008.

Metal production from HudBay and purchased concentrates

Metal	Units	2005 Dec. 31	2004 Dec. 31	2003 Dec. 31	2002 Dec. 31
Zinc	000s Tonnes	114.7	110.2	117.8	108.1
Copper	000s Tonnes	86.3	76.9	83.4	85.9
Gold	000s Troy Ounces	102.4	79.0	60.6	62.0
Silver	000s Troy Ounces	1,410.5	1,114.6	1,090.8	1,289.3

Metal production from HudBay concentrates only

Metal	Units	2005 Dec. 31	2004 Dec. 31	2003 Dec. 31	2002 Dec. 31
Zinc ⁽¹⁾	000s Tonnes	114.6	108.4	93.0	102.1
Copper	000s Tonnes	49.2	43.7	42.1	45.2
Gold	000s Troy Ounces	100.1	77.6	57.0	57.1
Silver	000s Troy Ounces	916.8	696.5	630.3	802.8

(1) Zochem consumed approximately 35,000 tonnes of zinc of which 31,760 tonnes were from the zinc plant.

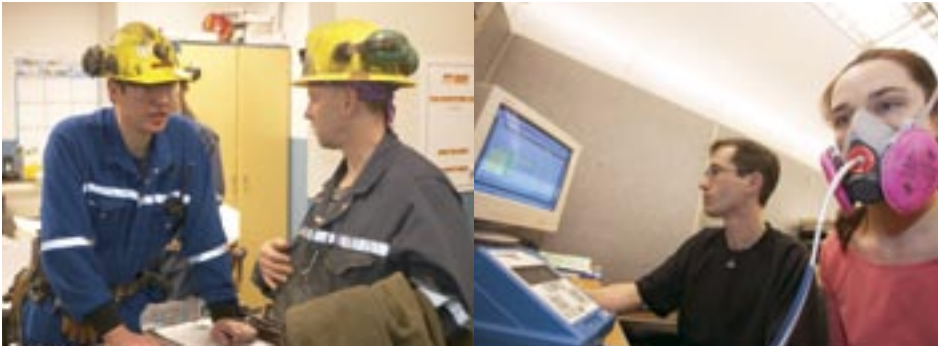
White Pine Copper Refinery acquisition

In October 2005, HudBay announced its intention to acquire 100% ownership of White Pine Copper Refinery Inc., a copper refinery located in the state of Michigan. The purchase was subsequently closed on January 1, 2006 for US\$15.1 million including adjustments.

White Pine has processed copper anode from our northern Manitoba copper smelter into refined copper cathode for a number of years and will continue to do so now that the acquisition is complete. The purchase of White Pine provides a dedicated refining facility for our copper anodes and will significantly reduce HudBay's copper refining unit costs.

In addition, the White Pine acquisition completes the vertical integration of HudBay's copper operations.

White Pine is a modern copper refinery, within effective rail distance of our copper smelter and is close to markets. Additionally, the refinery offers an opportunity to re-process spent copper, from the refinery, after an additional capital expenditure.



(Left) Reviewing safety procedures at shift start. (Right) Employees undergo regular tests to ensure safety compliance.

Health, safety and the environment

HudBay subscribes to the Mining Association of Canada's Total Sustainable Mining initiative, which includes the implementation of practices and policies which contribute to the well being of the environment, the economy and society as a whole, together with the health and safety of employees.

HudBay also publishes an annual sustainability report, describing our health, safety and environmental performance. The 2005 report, together with prior period reports, is available at www.hudbayminerals.com.

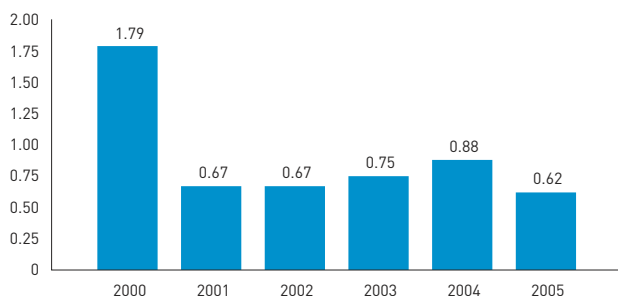
Additionally, HudBay maintains certification to the international programs of OHSAS 18001:1999 (Safety Management) and ISO 14001:2004 (Environmental Management), at our northern Manitoba, Saskatchewan and Ontario operations. The Balmat mine, which re-opens in the second quarter of 2006, and the White Pine Refinery, acquired January 1, 2006, also plan certification to OHSAS 18001:1999 and ISO 14001:2004, by 2008.

HudBay produces products in an environmentally responsible manner, while maintaining a healthy and safe workplace. We are committed to the control of risk to achieve a high level of occupational health and safety and to the protection of the environment.

To fulfil this commitment, we are actively engaged in:

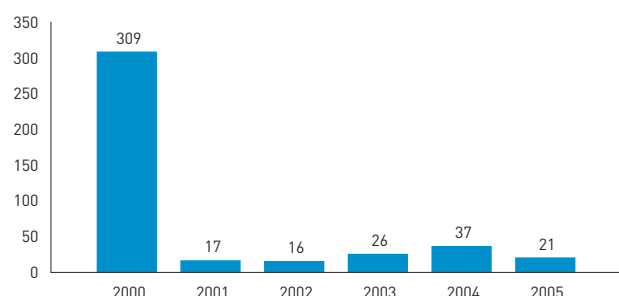
- Developing, implementing and continually improving the effectiveness of safety, health and environmental management systems;
- Meeting, and when practicable, setting targets to surpass all applicable legal and regulatory safety, health and environmental requirements, policies and codes of practice;
- Reducing the risk of injury or occupational health exposure;
- Developing and maintaining a culture of environmental responsibility and an awareness of the primary importance of safety and health;
- Using sustainable processes, practices, procedures and materials that avoid adverse effects on air, water and soil and maintain the environmental health of the communities in which we operate;
- Monitoring effectiveness and reviewing, safety, health and environmental management programs, objectives and targets; and
- Providing adequate resources for safety, health and environmental programs.

Lost time accident frequency rate ⁽¹⁾



(1) Accidents per 200,000 hours worked in Manitoba, Saskatchewan and Ontario.

Lost time accident severity rate ⁽²⁾



(2) Days lost per 200,000 hours worked in Manitoba, Saskatchewan and Ontario.



Checking miners' lamps.



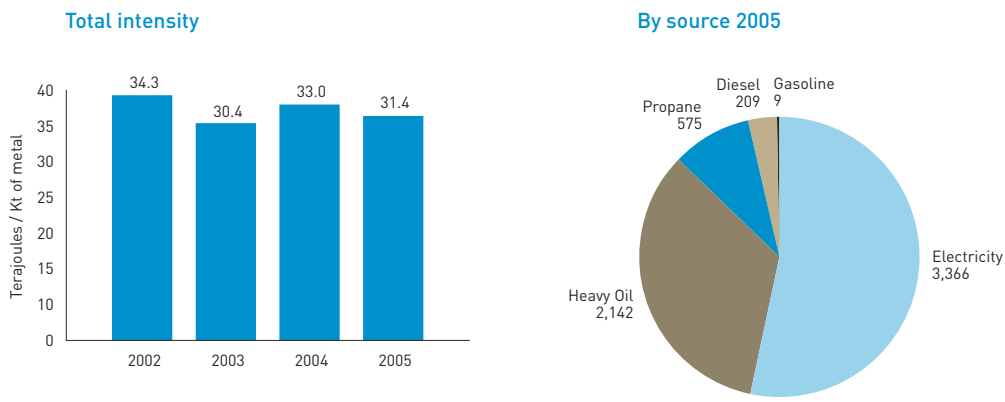
(Left) Spotting diamond drill collars on an exploration geophysical grid.
 (Right) Wildlife flourishes at the Flin Flon Tailings Impoundment Facility.

HudBay, in Manitoba, Saskatchewan and Ontario, achieved an extraordinary safety performance in 2005 of an accident frequency of 0.62 based on 200,000 hours worked, compared to 0.9 in the prior year. This is the best performance in the Company's 76-year history.

Key environmental achievements in 2005 included government approval for expansion of the Flin Flon Tailings Impoundment Facility, successful achievement of energy reduction targets, and maturation of the closure planning process, which included confirming that the closure financial provisions are adequate.

In 2005, HudBay continued to minimize energy use and was successful in reducing total intensity of use compared to 2004. The predominant energy source, electricity, was obtained at some of the lowest costs in North America, from Manitoba Hydro.

HudBay energy intensity and consumption by source – northern Manitoba and Saskatchewan





Message from the Chairman of the Board

2005 has been a year of achievement for HudBay. It was a year during which all factors aligned to generate exceptional results.

The Company achieved a very good safety record, again demonstrating the results of making health and safety of its employees its highest priority. Operationally the Company met or exceeded all of its objectives and the commodity price environment resulted in very solid earnings. The success of any company is dependent upon the people involved and HudBay is fortunate to have a highly skilled and motivated group of employees. All of the employees and particularly the management team have accomplished a great deal this year and I am proud to be associated with them.

I am pleased to report that your Board of Directors (the Board) has built on its commitment of providing best practice corporate governance to enhance shareholder value. To fulfil our commitment, the Board assesses its governance practices regularly to ensure compliance with developing governance standards including the guidelines of the Toronto Stock Exchange.

The Board is comprised entirely of independent Directors, except for the President and CEO of the Company, and all Committee members are also independent Directors. In 2005, the Board discharged many of its responsibilities through Committees, which included the Audit Committee, the Compensation Committee, the Nominating and Environmental, Health and Safety Committee and the Corporate Governance Committee. I am pleased to report that these Committees have developed well throughout this last year and are now very effectively discharging their duties.

I am proud of the way the Company has continued to operate with integrity and transparency during the year and, in particular, that management has established a Disclosure Committee, whose duties include reviewing materials prior to disclosure as well as monitoring the effectiveness of disclosure practices and disclosure transparency to both shareholders and the public.

The year under review has been an exciting and extremely rewarding one which has allowed HudBay to strengthen its balance sheet and broaden its operational base while continuing to make significant progress toward its objective of achieving best practice for corporate governance.

I want to take this opportunity to express my gratitude to my fellow Directors and to management for their commitment, dedication and efforts. I would also like to thank all of our shareholders and other stakeholders for their ongoing support of the Company. I look forward to addressing you and answering any questions you may have at our second Annual General Meeting in Toronto.

(signed) Allen J. Palmiere, CA

Allen J. Palmiere, CA
Chairman of the Board



Allen J. Palmiere, CA
Chairman and Director



Norman M. Anderson, P.Eng.
Director



James W. Aschroft, P.Eng.
Director



Richard W. Brissenden, CA
Director



Ronald P. Gagel, CA
Director



Peter R. Jones, P.Eng.
President, Chief Executive
Officer and Director

Corporate governance

HudBay management and its Board of Directors recognize the importance of sound corporate governance as it relates to the operation and management of the Company's business and affairs. HudBay has, and continues to augment its corporate governance practices with a singular view of ensuring that the business and affairs of the Company are effectively managed so as to enhance shareholder value.

This begins with the election of the Board of Directors. The Board's primary mandate consists of overseeing the business of the Company, and providing guidance to management to attain corporate objectives and maximize shareholder value. There are six Board members, all of whom, except HudBay President and CEO, Peter R. Jones, are independent of the Company under the Toronto Stock Exchange guidelines.

There are four Committees of the Board: the Audit Committee, the Compensation Committee, the Corporate Governance & Nominating Committee, and the Environmental, Health and Safety Committee, and all of them are

comprised entirely of independent Directors. A description of these Committees can be found in the Management Information Circular. The recently formed Disclosure Committee is comprised of senior management personnel.

Several key items comprise the governance documents including:

- Charter of the Board of Directors
- Position Direction for the Independent Chairman or Board Leader
- Code of Business Conduct and Ethics
- Timely Disclosure, Confidentiality and Insider Trading Policy

- Charter of the Environment, Health and Safety Committee
- Charter of the Audit Committee
- Charter of the Compensation Committee
- Charter of the Corporate Governance and Nominating Committee
- Whistleblower Policy, and
- Role Statement of the Chief Executive Officer

Details of each document can be found on the Company's website.

Board of directors

Allen J. Palmiere, CA

Chairman and Director

Mr. Palmiere is a Chartered Accountant, and has served in senior management financial supervisory capacities in the mining industry most of his career. In the past, Mr. Palmiere has been Treasurer of Northgate Exploration Ltd.; President, Chief Executive Officer and Chief Financial Officer of Breakwater Resources Ltd.; and Chief Financial Officer of Zemex Corporation. He is a member of the board of directors of Constellation Copper Corporation and the Chair of its Audit Committee. He is currently the President, Chief Executive Officer and a director of Silk Road Resources Ltd.

Norman M. Anderson, P.Eng.

Director

Mr. Anderson has been involved in the mining industry for over 50 years and is the former Chairman and Chief Executive Officer of Cominco Ltd. Currently, Mr. Anderson is President of the management consulting firm of Anderson & Associates. He has been active in consulting, particularly due diligence consulting and evaluations for financial institutions and mining companies, since 1987. He holds a Bachelor of Science in Geological Engineering from the University of Manitoba in Winnipeg, Manitoba. Mr. Anderson serves on a number of boards of directors of public companies.

James W. Ashcroft, P.Eng.

Director

Mr. Ashcroft is the president of J.W. Ashcroft & Associates, a mining consulting company. As a former President of the Ontario division of INCO Limited, he managed a vertically integrated mining company, which during his tenure completed a \$270 million mining project, improved its safety and environment record and maintained stable labour relations. He received a national diploma in engineering at Wigan Mining College in Lancashire, England and has completed an Executive Management Training Course at the Richard Ivey School of Business. Mr. Ashcroft serves on a number of boards of directors and, in some cases, sits on the health and environment, audit and corporate governance committees of such boards.

Richard W. Brissenden, CA

Director

Mr. Brissenden is a Chartered Accountant. He has been Chairman of Excellon Resources Inc., a mineral exploration and development company, since September 1990. Since February 1996, he has been President of Regal Consolidated Ventures Limited, a mineral exploration and development company. Mr. Brissenden also serves as a director of several other public companies.

Ronald P. Gagel, CA

Director

Mr. Gagel is the Vice President and Chief Financial Officer of FNX Mining Company Inc. Mr. Gagel is a chartered accountant with more than 25 years of professional experience, predominantly in the natural resources sector. From 1988 to 2004, Mr. Gagel was at Aur Resources Inc. and from 1999 to 2004 he served as Vice President and Chief Financial Officer of Aur Resources Inc. He is a director of FNX Mining Company Inc., Glencairn Gold Corporation and the Prospectors and Developers Association of Canada.

Peter R. Jones, P.Eng.

President, Chief Executive Officer and Director

Mr. Jones has been the President and Chief Executive Officer of HBMS since 2002. He joined HBMS in 1995 as Vice President, Mining and has subsequently held the positions of Senior Vice President, Projects and President Metallurgical Division. As Senior Vice President, Projects he was responsible for the 777 Project. Prior to joining HBMS, he held senior positions in operations and projects with Cominco Limited, Cape Breton Development Corporation and Cominco Engineering Services. He has a broad background having worked in potash mines, coal mines, open pit and underground lead zinc mines, gold mines and has directed extensive feasibility studies and management services for a wide range of clients throughout the world. Mr. Jones graduated from the Camborne School of Mines, United Kingdom in 1969 and the Banff School of Advanced Management in 1984. Mr. Jones is a Past President of the Mining Association of Manitoba and is a Director of the Mining Association of Canada.

Management's discussion and analysis

Unless the context otherwise suggests, references to "we," "us," "our" and similar terms, as well as references to "HudBay" or the "Company," refer to HudBay Minerals Inc. and its subsidiaries.

This Management's Discussion and Analysis ("MD&A") is dated March 21, 2006 and should be read in conjunction with the Company's 2005 Annual Information Form ("AIF") and audited annual consolidated financial statements for the year ended December 31, 2005, and related notes thereto and auditors report thereon, which have been prepared in accordance with Canadian Generally Accepted Accounting Principles ("GAAP"). Additional information regarding the Company, is available on SEDAR at www.sedar.com. All figures are in Canadian dollars unless otherwise noted.

HudBay's results for the year ended December 31, 2005 are significantly different from its results for the year ended December 31, 2004 because of its acquisition of HBMS. Therefore, a comparison of the quarter ended December 31, 2005 and September 30, 2005 is included. A comparison of HBMS' results for the twelve month periods ended December 31, 2005 and 2004 is contained in Note 25 to the Company's audited consolidated financial statements for the year ended December 31, 2005.

Our Business

On December 21, 2004, HudBay acquired indirectly all of the outstanding shares of Hudson Bay Mining and Smelting Co., Limited ("HBMS"). The Company is now an integrated mining and metals processing company that operates mines and concentrators in northern Manitoba and Saskatchewan, Canada, is re-opening a mine in New York State, and operates a copper and zinc metal production complex in Flin Flon, Manitoba, exercised an option to purchase a copper refinery in Michigan state, and a zinc oxide production facility in Brampton, Ontario.

Summarized Financial Results

The following table sets out summarized consolidated financial information for the Company as at and for the three-month periods ("quarters") ended December 31 and September 30, 2005 and December 31, 2004, as well as for the year ended December 31, 2005, and 2004.

(\$'000s except per share amounts)	Quarter Ended Dec 31, 2005	Quarter Ended Sept 30, 2005	Quarter Ended Dec 31, 2004 ⁽¹⁾⁽⁴⁾	Year Ended Dec 31, 2005	Year Ended Dec 31, 2004 ⁽¹⁾⁽⁴⁾
Revenue	\$ 173,051	\$ 169,264	\$ 13,308	\$ 652,028	\$ 13,327
Earnings (loss)	\$ 43,941	\$ 23,405	\$ (2,858)	\$ 85,218	\$ (9,920)
Operating cash flow ⁽²⁾	\$ 57,154	\$ 21,814	\$ (2,629)	\$ 144,862	\$ (7,228)
Earnings (loss) per common share: ⁽³⁾					
Basic	\$ 0.52	\$ 0.28	\$ (0.18)	\$ 1.04	\$ (1.12)
Diluted	\$ 0.34	\$ 0.28	\$ (0.18)	\$ 0.70	\$ (1.12)
Operating cash flow per common share: ⁽²⁾					
Basic	\$ 0.68	\$ 0.26	\$ (0.16)	\$ 1.77	\$ (0.81)
Diluted	\$ 0.44	\$ 0.26	\$ (0.16)	\$ 1.20	\$ (0.81)
Total Metal Produced					
	Quarter Ended Dec 31, 2005	Quarter Ended Sept 30, 2005	Quarter Ended Dec 31, 2004	Year Ended Dec 31, 2005	Year Ended Dec 31, 2004
Zinc tonnes	30,520	25,775	28,348	114,687	110,219
Copper tonnes	23,807	20,720	21,908	86,285	76,894
Gold troy oz.	25,860	23,200	26,632	102,371	79,018
Silver troy oz.	401,385	331,829	376,427	1,410,512	1,114,568

Selected Financial Information (\$000s)	Year Ended Dec 31, 2005	Year Ended Dec 31, 2004 ⁽¹⁾
Cash and cash equivalents	\$ 141,660	\$ 64,553
Working capital	209,117	146,952
Free cash flow ⁽⁵⁾	73,938	(12,408)
Net debt ⁽⁶⁾	66,669	176,033
Total assets	728,753	642,697
Shareholders' equity	261,226	152,766

(1) Excludes results of HBMS prior to December 21, 2004.

(2) Operating cash flow is after changes in non-cash capital items. Operating cash flow per common share is considered a non-GAAP measure.

(3) As of March 20, 2006, there were 85,631,503 common shares of the Company issued and outstanding, as well as 1,074,190,157 warrants (pre-consolidated basis at 30 warrants exercisable for one common share) exercisable for an aggregate of 35,806,338 common shares and 992 additional warrants. In addition, options exercisable for an aggregate maximum of 3,106,856 common shares were outstanding.

(4) For 2004, the conversion of stock options and warrants in the calculation of fully diluted resulted in the same earnings per share as basic earnings per share.

(5) Operating cash flows of \$144,862 less capital expenditures of \$70,924.

(6) Current and long term portion of long term debt, Province of Manitoba loan and capital leases (\$181,428, \$14,065 and \$12,836 respectively less cash and cash equivalents of \$141,660).

Health, Safety, Environment and Product Quality

Our HBMS facilities maintained their certification in the OHSAS 18001 occupational health and safety management system in 2005. HBMS' Lost Time Accident (LTA) frequency rate per 200,000 hours worked dropped from 0.88 in 2004 to 0.62 in 2005 the best performance in the 76 year history of HBMS. Injury severity also dropped from 37 per 200,000 hours worked in 2004 to 21 in 2005. All safety statistics include HBMS employees and HBMS contractors. Total accidents were reduced from 740 in 2004 to 691 in 2005.

HBMS' operations also maintain registration to the ISO 14001 environmental management system standard and the production and supply of its final products are registered to the ISO 9001 quality standard.

The St. Lawrence Zinc Company, LLC operations at Balmat, previously on care and maintenance since 2001, moved to operations re-commissioning during the fourth quarter of 2005. There were no LTAs at Balmat in 2005. The Balmat operations have commenced work on obtaining certification to both OHSAS 18001 and ISO 14001, with registration targeted for first quarter 2007.

A Sustainability Report is published annually that summarizes Environmental, Health and Safety performance for the Company.

Operations Overview

In 2005, our operations consisted of four operating mines, two concentrators, a copper smelter, a zinc plant and a zinc oxide production division.

Mines and Concentrators

777 Mine

The 777 mine is located immediately adjacent to the Company's principal concentrator and metallurgical plant in Flin Flon, Manitoba. In 1999 HBMS commenced development of the 777 mine as part of the \$435 million 777 Project and commercial production commenced in January 2004 at a capacity of 1.0 million tonnes, per annum. At January 2006 the mine production is expected to be approximately 1.35 million tonnes per annum.

Ore production at the 777 mine, for the quarter ended December 31, 2005, increased by 10% compared to the previous quarter, consistent with plans to ramp up production to 1.35 million tonnes per annum by January 1, 2006. Zinc grades improved considerably due to the ability to access higher grade ore. Operating costs in the last quarter increased substantially due to higher operating development and propane costs; however, year-to-year operating costs increased slightly due to increased consumable prices.

Management's discussion and analysis

Overall on a year-to-year basis, ore production increased by 12% while zinc grades were similar in 2005 compared to 2004; however, copper grades reduced by 23% due to mining areas of lower copper as per the overall mine plan. Gold and silver grades mined in 2005 were similar to 2004.

A total of \$25 million in capital expenditures is planned for 2006, compared to \$28 million in expenditures for 2005. Production, grades and unit costs, for 2006, within normal fluctuations, expect to be similar to 2005.

	Year Ended Dec 31, 2004	Quarter Ended Mar 31, 2005	Quarter Ended June 30, 2005	Quarter Ended Sep 30, 2005	Quarter Ended Dec 31, 2005	Year Ended Dec 31, 2005
Production tonnes	975,895	243,248	263,078	279,258	308,099	1,093,683
Copper %	2.89	2.23	2.16	2.28	2.28	2.24
Zinc %	4.50	3.75	4.54	4.34	5.10	4.47
Gold g/tonne	2.26	1.88	2.29	2.18	2.06	2.09
Silver g/tonne	23.14	20.57	25.93	23.93	24.56	23.83
Operating costs \$/tonne	\$ 37.14	\$ 42.20	\$ 36.07	\$ 32.33	\$ 40.46	\$ 37.60

Trout Lake Mine

The Trout Lake mine is located approximately six kilometres from the Company's principal ore concentrator and metallurgical plant in Flin Flon. Commercial production commenced at the Trout Lake mine in 1982. The mine is accessed by a shaft and ramp both from surface and ore from the mine is truck hauled to the Flin Flon concentrator.

Ore production at the Trout Lake mine for the quarter ended December 31, 2005 increased by 2% compared to the previous quarter, copper grade improved and zinc grade decreased consistent with the mining plan. Gold and silver grades also reduced consistent with the mining plan. Operating costs increased in the fourth quarter due to a small increase in operating development due to increased long hole drilling requirements for production and use of propane for the last quarter for heating of mine ventilation.

In 2005, zinc grade improved while copper grade decreased slightly compared with 2004. Gold and silver grades were similar to the prior year. The production grades were consistent with the mine plan. Production tonnage in 2005 was less than 2004 due to the planned reduction in the mining areas available.

A total of \$16 million in capital expenditures are planned for 2006 compared to \$25 million in capital expenditures in 2005. Production, grades and unit costs, for 2006, within normal fluctuations, expect to be similar to 2005.

	Year Ended Dec 31, 2004	Quarter Ended Mar 31, 2005	Quarter Ended June 30, 2005	Quarter Ended Sep 30, 2005	Quarter Ended Dec 31, 2005	Year Ended Dec 31, 2005
Production tonnes	916,097	213,055	219,913	210,802	214,981	858,751
Copper %	1.46	1.28	1.19	1.29	1.79	1.39
Zinc %	5.32	6.37	6.51	5.70	3.86	5.61
Gold g/tonne	1.47	1.55	1.43	1.57	1.32	1.47
Silver g/tonne	13.58	15.96	14.46	14.63	13.35	14.61
Operating costs \$/tonne	\$ 31.21	\$ 36.39	\$ 31.49	\$ 34.81	\$ 39.11	\$ 35.43

Chisel North Mine

The Chisel North mine is approximately 10 kilometres west of the Company's Snow Lake ore concentrator, which is approximately 215 kilometres from Flin Flon. Commercial production commenced at the mine in June 2000. The mine is accessed by ramp and ore from the mine is trucked to the Snow Lake concentrator and concentrate produced is trucked to the metallurgical zinc plant in Flin Flon.

Ore production at the mine for the quarter ended December 31, 2005 decreased by 7% compared to the previous quarter. Production decreased due to less ore being available from mining by long hole stoping. Zinc grade increased slightly consistent with the mine plan. Operating costs also increased slightly due to the usage of propane in winter months and lower production in the fourth quarter.

Ore production increased by 3%, for the year ended December 31, 2005 compared to the prior year, due to availability of production from long hole stopes. Zinc grade declined by 10% consistent with the mine plan. Ore unit costs for 2005 compared to 2004 improved by 8% due to greater availability of ore from long hole stopes.

A total of \$6 million in capital expenditures are planned for 2006 compared to capital expenditures of \$7 million in 2005. Production, grades and unit costs, for 2006, within normal fluctuations, expect to be similar to 2005.

	Year Ended Dec 31, 2004	Quarter Ended Mar 31, 2005	Quarter Ended June 30, 2005	Quarter Ended Sep 30, 2005	Quarter Ended Dec 31, 2005	Year Ended Dec 31, 2005
Production tonnes	327,853	86,545	82,100	87,090	80,996	336,731
Zinc %	9.99	9.64	9.08	8.31	8.97	9.00
Operating costs \$/tonne	\$ 45.99	\$ 36.28	\$ 37.56	\$ 47.62	\$ 48.23	\$ 42.40

Konuto Lake Mine

The Konuto Lake mine is located in Saskatchewan, approximately 24 kilometres from the Company's principal ore concentrator and metallurgical plant in Flin Flon. The Konuto Lake mine was discovered in 1994 and production began in 1999. The mine is accessed by ramp and ore is truck hauled over a dedicated road to the Flin Flon concentrator.

Production at the Konuto mine for the quarter ended December 31, 2005 decreased by 37% compared to the previous quarter. During the quarter, Konuto Lake Mine was closed, as planned, due to the depletion of mineral reserves. The ore grades during the quarter reflect the best grade available from the ore mined. Higher operating costs, in the quarter, are a reflection of lower tonnage mined at the end of the mine life.

Ore grade mined in 2005 was less than in 2004 due to lower grade ore being available to mine towards the end of the mine life. Capital expenditures were minimal however operating costs were higher year-on-year due to lower productivity and higher operating development to access areas necessary to be mined toward the end of the mine life.

The Konuto Lake mine was an excellent source of copper and to a lesser extent zinc, gold and silver for HudBay. The ore tonnage shortfall from the closure of this mine is expected to be substantially supplemented by the planned increase in ore production at the 777 mine in 2006. Konuto was an extremely successful operation with an excellent safety record.

	Year Ended Dec 31, 2004	Quarter Ended Mar 31, 2005	Quarter Ended June 30, 2005	Quarter Ended Sep 30, 2005	Quarter Ended Dec 31, 2005	Year Ended Dec 31, 2005
Production tonnes	327,231	87,062	89,986	82,895	52,522	312,465
Copper %	4.07	4.19	4.47	3.35	3.30	3.90
Zinc %	2.08	1.39	1.66	2.07	2.36	1.81
Gold g/tonne	1.92	1.73	1.84	1.33	1.73	1.65
Silver g/tonne	9.60	8.48	9.28	8.32	11.46	9.15
Operating costs \$/tonne	\$ 33.12	\$ 40.32	\$ 34.81	\$ 31.94	\$ 39.80	\$ 36.42

Flin Flon Concentrator

The Flin Flon concentrator produces zinc and copper concentrates from ore mined at the 777, Trout Lake and Konuto Lake mines. As part of the \$435 million 777 Project, the capacity of the Flin Flon concentrator was increased to 2.18 million tonnes of ore per annum. The concentrator receives ore from each mine separately and blends the ore prior to grinding.

For the fourth quarter of 2005, the Flin Flon concentrator throughput decreased slightly, compared to the historically higher level in the prior quarter. Copper head grade improved 5% in the fourth quarter while zinc head grade decreased 3% principally as a result of changes in the Trout Lake mine ore grades. The lower zinc head grade and the higher copper head grade resulted in a decrease in zinc recovery. Gold and silver recoveries increased slightly. Unit cost of ore processing increased marginally in the fourth quarter as a result of higher maintenance and propane costs for heating requirements.

Management's discussion and analysis

In 2005, processed ore increased by 5% while mine supplied copper head grade was 13% lower and zinc head grade was 1% higher than 2004. Gold recovery improved by 8% as a result of optimization work done on the circuit and zinc recovery improved by 4% due to circuit changes during the year. Operating costs improved slightly due to increased processed ore.

A total of \$4 million in capital expenditures are planned for 2006 compared to capital expenditures of \$2 million in 2005.

	Year Ended Dec 31, 2004	Quarter Ended Mar 31, 2005	Quarter Ended June 30, 2005	Quarter Ended Sep 30, 2005	Quarter Ended Dec 31, 2005	Year Ended Dec 31, 2005
Ore processed tonnes	2,156,051	552,829	558,919	584,362	566,445	2,262,555
Copper ore %	2.46	2.10	2.10	2.13	2.23	2.14
Zinc ore %	4.50	4.52	4.85	4.44	4.32	4.53
Gold g/tonne	1.89	1.71	1.87	1.85	1.75	1.78
Silver g/tonne	17.31	16.95	18.42	18.19	19.01	18.14
Copper concentrate tonnes	208,961	45,666	44,957	48,763	49,465	188,851
Concentrate grade Cu %	23.60	23.06	24.27	23.94	23.99	23.82
Zinc concentrate tonnes	152,453	39,448	44,366	42,488	38,115	164,417
Zinc grade Zn %	50.42	50.34	52.10	51.40	52.15	51.51
Copper recov. to Cu conc %	93.0	90.8	92.9	93.7	93.7	92.8
Gold recov. to Cu conc %	69.6	77.3	78.3	71.8	72.5	74.9
Silver recov. to Cu conc %	68.1	68.1	66.6	64.6	66.1	66.3
Zinc recovery to Zn conc %	79.2	79.4	85.3	84.1	81.2	82.6
Operating costs \$/tonne	\$ 8.29	\$ 8.21	\$ 7.68	\$ 7.88	\$ 7.95	\$ 7.93

Snow Lake Concentrator

The Snow Lake concentrator is approximately 215 kilometres from the Flin Flon metallurgical plants. The facility processes only the Chisel North mine zinc ore and produces zinc concentrate that is trucked to Flin Flon for metallurgical treatment. The concentrator has an ore capacity of approximately 1.2 million tonnes per annum.

For the fourth quarter of 2005, the Snow Lake concentrator's processed ore decreased to match mine production from the Chisel North mine compared to the prior quarter. Zinc recovery increased marginally as a result of a higher zinc head grade from the mine. Unit cost per tonne of ore increased by approximately 25% in the fourth quarter of 2005 as compared to the third quarter, due to minor structural steel repairs of the concentrator building as well as higher costs of reagents.

In 2005, processed ore increased by 1% consistent with ore supply from the Chisel North mine. Ore head grade was 10% lower while metal recovery to concentrate was similar. Operating unit ore processing costs were only 4% higher despite increases in steel, fuel and other commodities.

A total of \$0.3 million in capital expenditures are planned for 2006 compared to an expenditure of \$0.2 million in 2005.

	Year Ended Dec 31, 2004	Quarter Ended Mar 31, 2005	Quarter Ended June 30, 2005	Quarter Ended Sep 30, 2005	Quarter Ended Dec 31, 2005	Year Ended Dec 31, 2005
Ore processed tonnes	327,853	85,632	79,496	83,570	82,729	331,427
Zinc ore %	9.99	9.64	9.09	8.26	9.00	9.00
Zinc concentrate tonnes	61,825	15,827	13,643	13,058	14,118	56,646
Concentrate grade Zn %	51.52	50.91	51.68	51.25	51.21	51.25
Zn recovery to Zn conc %	97.3	97.6	97.5	96.9	97.1	97.3
Operating costs ⁽¹⁾ \$/tonne	\$ 16.69	\$ 16.51	\$ 17.30	\$ 15.82	\$ 19.80	\$ 17.35

(1) Operating costs include the cost of trucking concentrates to the Flin Flon metallurgical plant.

Metallurgical Plants

Copper Smelter

The copper smelter treats copper concentrate and produces copper anodes, which are railed to the White Pine copper refinery, where they are electro-refined into market standard cathode copper.

Both domestic produced copper concentrate and purchased copper concentrate are treated at the smelter. Approximately 35% of the concentrate tonnage treated at the copper smelter was purchased concentrate during 2005. Our Company has long term contracts with both Highland Valley Copper mines and Montana Resources, Butte Mine for the purchase of adequate copper concentrate requirements.

The copper smelter facilities include off-loading of rail cars, concentrate storage sheds, roasters, a reverberatory furnace, three converter furnaces and two anode furnaces and an anode casting wheel together with gas handling systems, electrostatic precipitators and a stack.

Copper anode production for the fourth quarter of 2005 increased by 15% compared to the third quarter, resulting in a new quarterly record for smelter production. On a unit cost basis, operating costs were 5% lower in the fourth quarter of 2005 as compared to the third quarter.

Comparing 2005 with 2004 concentrate treated increased by 12% while copper produced also increased by 12%. Gold production, in copper increased 12% and silver by 26% reflecting the precious metal content in concentrate treated. Operating costs per pound of copper produced was the same as 2004 despite considerable carbon based fuel cost pressures.

The smelter plans to proceed with the previously announced 28 day temporary maintenance shutdown during the second quarter of 2006. The maintenance shutdown is primarily to rebuild the reverberatory furnace, which is used to smelt copper and is rebuilt regularly. Management of copper anode inventory between the copper smelter and the White Pine copper refinery will in part, mitigate the impact on annual sales. HBMS mines and concentrators will continue to operate.

A total of \$10 million in capital expenditures are planned for 2006, compared to \$2 million in 2005, mainly comprising expenditures related to the shutdown.

	Year Ended Dec 31, 2004	Quarter Ended Mar 31, 2005	Quarter Ended June 30, 2005	Quarter Ended Sep 30, 2005	Quarter Ended Dec 31, 2005	Year Ended Dec 31, 2005
Domestic sourced tonnes	185,352	48,352	53,038	49,780	55,172	206,342
Purchased sourced tonnes	98,748	28,839	26,057	28,212	28,828	111,936
Total tonnes	284,100	77,191	79,095	77,992	84,000	318,278
Operating costs ⁽¹⁾ \$/tonne	\$ 147.28	\$ 139.52	\$ 141.93	\$ 153.48	\$ 154.87	\$ 147.59
Copper produced tonnes	76,894	20,698	21,060	20,720	23,807	86,285
Gold troy oz.	79,020	25,774	27,540	23,200	25,860	102,374
Silver troy oz.	1,114,570	338,295	338,998	331,829	401,385	1,410,507
Operating costs ¢/lb. Cu	24.7	23.6	24.2	26.2	24.8	24.7

(1) Represents operating costs per tonne of concentrate treated.

Zinc Plant

The Flin Flon zinc plant facility utilizes leading edge technology and includes a two-stage pressure leach plant, oxygen plant, four steps of solution purification, a new electrolysis plant and a casting plant. An oxygen plant supplies oxygen to the pressure leach process. The facility produces special high grade zinc as the final product.

For the fourth quarter of 2005, operating costs in the zinc plant, on a unit cost of zinc metal produced basis, decreased by 6% compared to the third quarter as zinc production increased by approximately 4,700 tonnes (or 18%), the difference reflecting the lower production and maintenance activities that were carried out in the third quarter. In the fourth quarter, the zinc plant achieved a quarterly record for zinc cathode metal production.

Management's discussion and analysis

In 2005, zinc concentrate treated increased by 2% and zinc produced increased by 4% resulting from higher concentrate zinc grade treated and improved metal recovery. Unit operating cost per pound of metal produced was similar to the prior year.

During the second quarter of 2006 and similar to 2005, a routine ten-day annual maintenance shutdown is planned for the oxygen plant, autoclave, thickener and cellhouse maintenance. No impact on annualized zinc metal production as a result of the maintenance shutdown is expected. HBMS' mines, concentrators and other process plants will continue to operate.

A total of \$5 million in capital expenditures are planned for 2006, compared to \$3 million in 2005.

	Year Ended Dec 31, 2004	Quarter Ended Mar 31, 2005	Quarter Ended June 30, 2005	Quarter Ended Sep 30, 2005	Quarter Ended Dec 31, 2005	Year Ended Dec 31, 2005
Domestic tonnes	219,561	58,809	58,105	51,339	59,856	228,109
Purchased tonnes	3,488	-	-	-	-	-
Total tonnes	223,049	58,809	58,105	51,339	59,856	228,109
Operating costs ⁽¹⁾ \$/tonne	\$ 278.69	\$ 272.32	\$ 275.45	\$ 304.76	\$ 290.98	\$ 285.31
Zn produced tonnes	110,219	29,204	29,188	25,775	30,520	114,687
Operating costs €/lb. Zn	25.6	24.9	24.9	27.5	25.9	25.7

(1) Represents operating costs per tonne of zinc concentrate treated.

Zinc Oxide Facility – Zochem

Zochem is the zinc oxide production facility of HBMS, located in Brampton, Ontario. Zochem is a stand-alone operation that off-takes between 32,000 tonnes and 41,000 tonnes of our Flin Flon zinc plant zinc metal production per annum.

In 2005, Zochem was the third largest producer of zinc oxide in North America, accounting for approximately 20% of the North American market.

The Zochem facilities have a total capacity of 45,000 tonnes per annum of zinc oxide. In 2005, Zochem consumed approximately 35,000 tonnes of the zinc of which 31,760 tonnes was from HBMS, and sold 43,230 tonnes of zinc oxide.

A total of \$2 million in capital expenditures is planned for 2006, compared to \$0.3 million in 2005. The increased expenditure is related to productivity improvement by the installation auto palletizing machines to bag zinc oxide.

Commodity Markets

The following market analysis is provided by HudBay and is obtained from various information sources, which reflects the views of HudBay management.

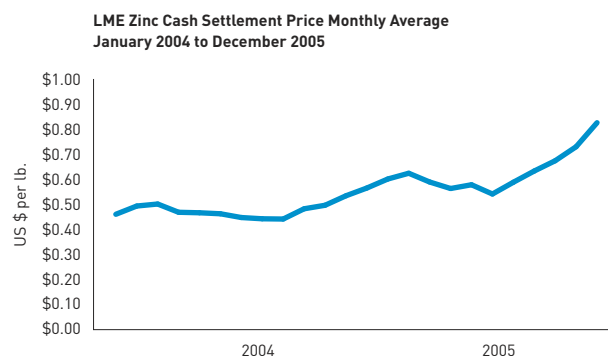
Zinc

Of the five products the Company produces, earnings are most sensitive to fluctuations in the price of zinc (see Sensitivity Analysis). In 2005, the LME price of zinc averaged US \$0.63 a pound, increasing over the year to US \$0.87 a pound at year end. In early 2006, zinc continued its upward trend and reached a high of \$1.12.

Zinc inventories on the London Metal Exchange (LME) fell by 235,300 tonnes or almost 40% during the year as zinc consumption exceeded production capacity.

The tight supply of zinc in 2005 and early 2006 is evidenced by the increase in the associated premiums received for the direct sale of zinc metal.

The outlook for zinc price remains positive with world zinc metal demand expected to continue to exceed supply.



Management's discussion and analysis

Inflationary Cost Pressures

Similar to other mining companies, HudBay has experienced significant inflationary cost pressures with increasing prices of consumables such as steel, explosives and rubber products. We plan to continue focusing on procurement and continuous improvement initiatives to mitigate the impact of consumables, including controlling usage and extending the life of plant and equipment, where possible.

Other Capital Expenditures

In addition to the capital expenditures at the mines and plants described in the Operations Overview section and excluding the reopening of the Balmat mine, the Company plans to spend approximately \$12 million in 2006 (\$7 million of which relates to the expansion of the Flin Flon tailings impoundment system) compared to \$3 million in 2005.

Sensitivity Analysis

The following table shows the approximate impact of metal prices and exchange rates, using 2005 as a basis, on the Company's 2005 net income.

	A change of	Would change our 2005 net income by: (Cdn \$ million)	Would change our 2005 earnings per share by: ⁽¹⁾ (Cdn \$/share)
Metal Prices			
Zinc (lb.)	US\$ 0.10	\$ 29	\$ 0.35
Copper (lb.)	US\$ 0.10	\$ 12	\$ 0.14
Gold (troy oz.)	US\$ 10.00	\$ 1	\$ 0.01
Silver (troy oz.)	US\$ 1.00	\$ 1	\$ 0.01
Exchange Rates			
US \$1 to C \$1	C\$ 0.01	\$ 3	\$ 0.04

(1) Based on undiluted common shares outstanding of 84 million.

Mineral Reserves and Inferred Mineral Resources

Estimated January 1, 2006 mineral reserves at our 777, Trout Lake and Chisel North Mines in Northern Manitoba and our Balmat Mine project in New York State, in compliance with NI 43-101, was 21,357,000 tonnes at 1.8 g/t gold, 21.1 g/t silver, 2.0% copper and 5.3% zinc.

Mine	Tonnes	Au (g/t)	Ag (g/t)	Cu (%)	Zn (%)
777					
Proven	3,474,000	2.5	28.4	2.4	4.7
Probable	12,261,000	2.1	25.7	2.5	4.4
Trout Lake					
Proven	1,433,000	1.0	11.1	1.4	4.7
Probable	1,058,000	1.7	20.5	2.5	4.0
Chisel North					
Proven	661,000	–	–	–	8.9
Probable	761,000	–	–	–	8.4
Balmat					
Proven	686,000	–	–	–	10.6
Probable	1,023,000	–	–	–	11.4
Total Proven	6,254,000	1.6	18.3	1.6	5.8
Total Probable	15,103,000	1.8	22.3	2.2	5.0
Total Reserves	21,357,000	1.8	21.1	2.0	5.3

Separately, as of January 1, 2006, we estimated aggregate inferred mineral resources at our 777, Trout Lake and Chisel North Mines in Northern Manitoba and our Balmat Mine project in New York state at 4,940,000 tonnes at 1.2 g/t gold 19.1 g/t silver, 1.0% copper and 7.45% zinc.

The categorization of measured and indicated mineral resource is determined in a 12-step process, which includes determination of the integrity and validation of the data collected, including, confirmation of specific gravity, assay results and methods of data recording. The process also includes determining the appropriate geological model, selection of data and the application of statistical models including probability plots and restrictive kriging to establish continuity and model validation. The resultant estimates of measured and indicated mineral resources are converted to proven and probable mineral reserves by the application of mining dilution and recovery, as well as the determination of economic viability using historical operating costs. Other factors such as depletion from production are applied as appropriate. Long term metal prices, including premiums used for economic viability of the 2006 mineral reserves, were US \$400 oz. gold, US \$6.00 oz. silver, US \$0.91 lb. copper and US \$0.52 lb. zinc.

Prior period mineral reserves are filed in the Canadian Securities Administrators SEDAR filing system in the Renewal Annual Information Form of HudBay Minerals Inc., March 29, 2005.

Financial Review

The following table sets forth our selected consolidated financial information for each of the eight most recently completed quarters. Note that the results reflect the acquisition of HBMS as of December 21, 2004.

(\$000s, except per share information)	Q4	Q3	Q2	2005 Q1	Q4	Q3	Q2	2004 Q1
Net Revenue	\$173,051	\$169,264	\$158,188	\$151,525	\$ 13,308	\$ 6	\$ 7	\$ 6
Earnings (loss)	43,941	23,405	8,691	9,181	(2,891)	(3,282)	(2,083)	(1,664)
Per Common Share								
Basic	\$ 0.52	\$ 0.28	\$ 0.11	\$ 0.12	\$ (0.18)	\$ (0.45)	\$ (0.30)	\$ (0.29)
Diluted ⁽¹⁾	0.34	0.28	0.11	0.12	(0.18)	(0.45)	n/a	n/a

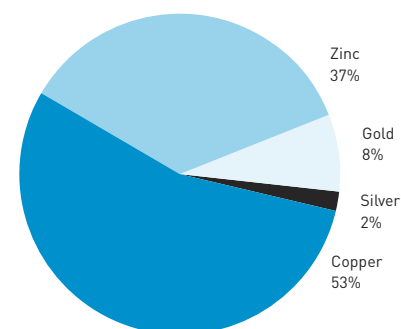
(1) Based on the treasury method of calculating diluted shares outstanding.

With the exception of ten days in December 2004, HudBay had no production and was essentially a development stage enterprise. As such, discussion and analysis of 2005 compared to 2004 has been limited and, additionally, a comparison of results achieved in the third and fourth quarters of 2005 has been provided.

Revenue

Revenues are affected by sales volumes, commodity prices and currency exchange rates. For 2005, total revenue was \$652.0 million, resulting from the sale of 114,682 tonnes of zinc (which includes 31,760 tonnes to our Zochem division), 78,070 tonnes of copper, 95,511 ounces of gold and 1,321,784 ounces of silver.

Total sales revenue for the quarter ended December 31, 2005 was \$173.0 million from sales of approximately 17,644 tonnes of copper, and 29,598 tonnes of zinc which included 9,226 tonnes to our Zochem facilities for use in the production of zinc oxide. In the fourth quarter of 2005, Zochem had sales of approximately 11,010 tonnes of zinc oxide. Revenues for the quarter also included sales of approximately 21,783 ounces of gold, and 358,434 ounces of silver. The Company's re-negotiated contract with CMM for conversion to an agency agreement from a sales agreement for sale of copper and precious metals resulted in lower sales volume of these products in the fourth quarter (refer to HudBay's Agency Arrangement section below).



Over the quarter, realized prices averaged US \$2.04/lb. copper, US \$0.79/lb. zinc, US \$465/troy oz. gold, and US \$7.66/troy oz. silver. The Canadian to US dollar exchange rate averaged Cdn \$1.17 per US \$1.00 for the quarter.

Management's discussion and analysis

Realized Metal Prices

	2005	Average Prices ⁽¹⁾	2004 ⁽²⁾
Zinc (US \$/lb.)	\$ 0.65	\$ 0.63	\$ 0.49
Copper (US \$/lb.)	1.72	1.67	1.35
Gold (US \$/troy oz.)	445	445	387
Silver (US \$/troy oz.)	7.28	7.31	6.66

HudBay's Agency Arrangement

Previous to this change, HudBay's operating subsidiary HBMS recognized 100% of its sales when its product was shipped from the Flin Flon operations and sold to its 50% owned metal sales joint venture, Considar Metal Marketing ("CMM").

In order to enhance the Company's credit capacity under its credit facility, by increasing account receivables and inventory, the Company re-negotiated its contractual relationship with CMM.

As at January 1, 2006, the Company changed its relationship with CMM from a sales to an agency arrangement, whereby copper and precious metal inventory are owned by the Company until sold to customers.

Under the agency contractual arrangement, HudBay will retain title to these metals until they are sold to third party customers. The associated one-time change in sales at HBMS's Flin Flon location to the third party customer arrangement is approximately 7 weeks. The approximate financial impact on this contractual change with CMM for copper and precious metals for the fourth quarter and year ended 2005 is shown in the following table.

Proforma Impact of Agency Arrangement on Selected Items

	As Reported Q4	Financial Impact	Proforma Q4	Proforma 2005
Sales	\$ 170,000	\$ 36,000	\$ 206,000	\$ 685,000
Operating Expenses	\$ 122,000	\$ 27,000	\$ 149,000	\$ 506,000
Net Earnings	\$ 44,000	\$ 9,000	\$ 53,000	\$ 94,000
EPS – Basic	\$ 0.52	\$ 0.10	\$ 0.62	\$ 1.15
EPS – Diluted	\$ 0.34	\$ 0.07	\$ 0.41	\$ 0.78
Accounts Receivable	\$ 45,000	\$ 36,000	\$ 81,000	\$ 81,000
Inventories	\$ 117,000	\$ (27,000)	\$ 90,000	\$ 90,000
Copper Tonnes Sold	17,644	5,500	23,144	83,570
Gold Ounces Sold	21,783	8,000	29,783	103,511

In the first half of 2006, the Company plans to convert the remaining products of zinc and zinc oxide to the same agency arrangement. The financial impact of a similar delay is estimated to be 3 to 4 weeks of revenue of \$8 to \$9 million and \$7 to \$8 million in costs resulting in lower earnings of \$1 to \$2 million.

Total revenue for the fourth quarter of 2005 remained similar to the third quarter, despite the impact of changes to the CMM agency arrangements as described above, primarily due to higher metal prices.

Expenses

Operating Expenses

Total operating expenses in 2005 were \$480.5 million. Operating expenses in the fourth quarter of 2005, of \$123.3 million, decreased by approximately 3% compared to the third quarter of \$125.4 million. This decrease primarily related to lower sales volumes from the relationship change with the Company's joint venture marketing company offset by increased profit sharing expenses (10% of net profit distributed among eligible employees) of \$2.0 million due to higher profits, an increase in concentrate purchase costs of \$7.4 million, primarily due to increases in metal prices, and other cost increases of \$5.5 million in operations and mining, offset partly by increased production. For the quarter ended December 31, 2005, operating costs in the mines and concentrators increased by approximately 13% related to increased operation development and the zinc plant and copper smelter increased by approximately 10% compared to the previous quarter, due partly to record quarterly production for copper anode and zinc cathode. This increase resulted from additional maintenance costs and higher costs of consumables (steel, heavy fuel oil, grinding media, etc.)

General and Administration

Total general and administrative ("G&A") expenses for 2005 were \$19.6 million. G&A expense for the quarter ended December 31, 2005 was \$8.2 million compared to \$3.1 million for the quarter ended September 30, 2005. Costs for the fourth quarter of 2005 were higher as total G&A expenses included consulting costs for the fair valuation of the acquisition of HBMS of approximately \$0.9 million, stock based compensation of \$2.7 million, and additional legal and audit fees associated with both recent compliance requirements and the fair valuation of HBMS in the amount of approximately \$0.5 million.

Exploration Expenses

The previously announced program of exploration on the Company's lands in Manitoba and Saskatchewan continued during the quarter. The program provides for \$10 million of planned exploration in the Flin Flon greenstone belt during 2005 and the first quarter of 2006, of which approximately \$5.9 million has been spent as of December 31, 2005. For the year ended December 31, 2005, exploration expenditures of \$11.3 million as shown on the income statement include \$5.9 million relating to flow-through activity, \$4.1 million for Balmat feasibility costs (including exploration), and \$1.3 million of other costs (primarily non flow-through related expenses).

Foreign Exchange Loss

In 2005, the Company incurred a foreign exchange loss of \$2.3 million (including amortization of deferred option premiums). This relates primarily to the change in the value of the Company's cash balance which is held largely in US \$ deposits, and was converted to Canadian dollars at a year-end exchange rate of Cdn \$1.16 per US \$1.00, compared to higher rates earlier in the year. For the quarter ended December 31, 2005, there was a slight overall movement in foreign exchange rates resulting in a small loss.

Operating Earnings

For the quarter ended December 31, 2005, operating earnings were \$25.5 million compared to \$19.1 million for the three months ended September 30, 2005. The favourable variance of \$6.4 million is attributable to higher metal prices and a receipt of business interruption insurance of \$2.0 million from a prior claim, more than offset by the cost associated with the Company's relationship change with CMM of \$9 million and increased costs for concentrates and operating expenses.

Foreign Exchange – Long Term Debt

For the year, the Company recorded a foreign exchange gain on long-term debt of \$6.8 million on the dollar movements related to the US dollar denominated debt. For the quarter ended December 31, 2005, the Company recorded a minor foreign exchange loss on long-term debt compared to a gain of \$11.0 million in the previous quarter. This gain was a result of the change in US \$ denominated debt as valued at month end exchange rates.

Management's discussion and analysis

Gain on Derivative Instruments

In the quarter ended December 31, 2005, the Company recorded a \$3.2 million gain on derivative instruments compared to a \$1.5 million gain for the quarter ended September 30, 2005. The derivatives are forward contracts of zinc and to a lesser extent zinc oxide, placed in conjunction with CMM fixed price sales contracts to convert the fixed price zinc sales contract to floating prices.

Tax Recovery

For the year, the Company recorded a recovery of taxes of \$10.8 million, primarily related to the increase in the tax asset. The tax asset has been adjusted to reflect the future income tax assets at an amount that the Company considers is more likely than not to be realized. Since HBMS had many years of tax losses, the tax asset has been based on only one future year of earnings. One year is considered appropriate due to the uncertainties of future metal prices, exchange rates and the magnitude of prior losses, but will continue to be reviewed as circumstances change.

As a result of this adjustment being made in the quarter ended December 31, 2005, the Company recorded a non-cash tax recovery of \$20.0 million compared to an expense of \$3.8 million in the quarter ended September 30, 2005. The Company has sufficient tax pools to shelter income and does not anticipate significant cash income taxes in the foreseeable future.

Quarter Ended December 31, 2005 Compared to Quarter Ended September 30, 2005

For the quarter ended December 31, 2005, net earnings were \$43.9 million compared to \$23.4 million for the three months ended September 30, 2005. The net \$20.5 million variance is summarized broadly as follows: decreased sales volumes due to change in agency arrangements offset by increased metal sales prices, increase in derivative gains of \$1.7 million, and a settlement of a business interruption claim from prior years of \$2.0 million; a reduction in foreign exchange losses on operating of \$2.7 million and a reduction in foreign exchange gains on long-term debt of \$11.0 million; an increase to the tax asset of \$13.3 million and a reduction to previously recorded tax expense of \$6.7 million (as compared to a tax expense of \$3.8 million in the third quarter); and cost increases for G&A of \$2.5 million, increases to the profit sharing expenses of \$2.0 million due to higher profits, increases in concentrate purchase costs of \$7.4 million primarily due to increases in metal prices, and other cost increases of \$5.5 million in the operating areas primarily related to production volume and amount of mine operating development.

The following shows the variances from third quarter to fourth quarter net earnings:

(\$ millions)

Earnings – Third Quarter	\$	23.4
CMM Agency contractual change with CMM		(9.0)
Increase in revenue		31.4
Foreign exchange		(8.3)
Tax recovery		23.8
General and administrative expenses		(2.5)
Other		(14.9)
Earnings – Fourth Quarter	\$	43.9

Quarter Ended December 31, 2005 Compared to Quarter Ended December 31, 2004

Net income for the quarter ended December 31, 2005 was \$43.9 million compared with a loss of \$2.9 million for the quarter ended December 31, 2004.

Total sales revenue for the quarter ended December 31, 2005 was \$169.7 million from sales of metals produced. The Company had minimal metal sales in the fourth quarter of 2004 resulting from the acquisition of HBMS on December 21, 2004.

Operating costs for the quarter ended December 31, 2005 increased to \$121.9 million from \$11.5 million for the quarter ended December 31, 2004. Costs in the fourth quarter of 2004 primarily related to care and maintenance costs of the Balmat mine and the Gays River mine property, together with 10 days operations of HBMS.

Cash Cost per Pound of Zinc Sold

HudBay's cash cost of zinc sold, net of by-product credits, 2005 was US \$0.16 per pound. The Company had minimal metal sales in 2004 with the acquisition of HBMS on December 21, 2004.

Non-GAAP Reconciliation of Cash Cost per Pound of Zinc Sold, Net of By-Product Credits

(\$000)	Quarter Ended Mar 31, 2005	Quarter Ended June 30, 2005	Quarter Ended Sep 30, 2005	Quarter Ended Dec 31, 2005	Quarter Ended Dec 31, 2005 (excluding CMM change to Agency)	Year Ended Dec 31, 2005	Year Ended Dec 31, 2005 (excluding CMM change to Agency)
Expenses	C\$135,049	C\$136,726	C\$150,140	C\$147,554	C\$174,554	C\$569,469	C\$596,469
Non-cash operating costs							
Depreciation and amortization	(12,724)	(13,228)	(13,618)	(13,530)	(13,530)	(53,100)	(53,100)
Stock-based compensation	0	(1,354)	(591)	(729)	(729)	(2,674)	(2,674)
Accretion and other non-cash	(652)	(649)	(655)	(656)	(656)	(2,612)	(2,612)
Exploration	(569)	(3,216)	(3,930)	(3,566)	(3,566)	(11,281)	(11,281)
Foreign exchange gain (loss)	250	424	(2,850)	(162)	(162)	(2,338)	(2,338)
	121,354	118,703	128,496	128,911	155,911	497,464	524,464
Less: By-product credits ⁽¹⁾	(106,263)	(111,408)	(120,812)	(111,615)	(147,615)	(450,097)	(486,097)
Cash cost net of by-products	C\$ 15,091	C\$ 7,295	C\$ 7,684	C\$ 17,296	C\$ 8,296	C\$ 47,367	C\$ 38,367
Exchange rate (C\$/US\$) ⁽²⁾	1.227	1.244	1.200	1.176	1.176	1.211	1.211
Cash cost net of by-products	US\$ 12,299	US\$ 5,864	US\$ 6,403	US\$ 14,707	US\$ 7,054	US\$ 39,114	US\$ 31,682
Zinc sales (000 lbs)	59,739	62,754	65,015	65,252	65,252	252,760	252,760
Cash cost per pound of zinc, net of by-product credits	US\$ 0.21	US\$ 0.09	US\$ 0.10	US\$ 0.23	US\$ 0.11	US\$ 0.16	US\$ 0.13⁽¹⁾

(1) By-product credits include revenues from sale of copper, gold, silver, the premium on zinc oxide sales and the Company's proportionate share of by-product sales by its marketing joint venture.

(2) Weighted average exchange rate for sales during the period.

Cash cost per pound of zinc, net of by-product credits, is furnished to provide additional information and is a non-GAAP measure that does not have a standardized meaning and is therefore unlikely to be comparable to similar measures presented by other issuers. This measure should not be considered in isolation as a substitute for measures of performance prepared in accordance with generally accepted accounting principles and is not necessarily indicative of operating expenses as determined under generally accepted accounting principles. This measure is intended to provide investors with information about the cash generating capabilities of HBMS' operations. HBMS uses this information for the same purpose. Mining operations are capital intensive. This measure excludes capital expenditures. Capital expenditures are discussed throughout the MD&A and the consolidated financial statements.

All per pound value in the following section are rounded to the closest cent.

The table on the previous page shows a US \$0.13 per pound net increase in the cash cost per pound of zinc for the quarter ended December 31, 2005 compared to the quarter ended September 30, 2005. For comparative purposes, the information for the quarter has been adjusted for the impact of the CMM agency change, which would result in only a US \$0.01 per pound increase from the prior quarter. The US \$0.13 increase per pound of zinc is comprised of unfavourable variances of approximately US \$0.31, and a benefit of US \$0.18 from by-product credits and changes in volumes and inventories.

Management's discussion and analysis

Unfavourable variances include approximately US \$0.11 increase in copper concentrate purchases, a US \$0.10 increase in mining and processing costs, a US \$0.03 increase in general and administrative, a US \$0.02 exchange impact on Canadian dollar costs, and an increase of approximately US \$0.05 for profit sharing expenses due to the higher earnings. Increased mining and processing costs have been influenced by higher cost of consumables such as heavy fuel oil, grinding media, and steel products.

The calculation of cash cost per pound of zinc is strongly influenced by by-product metal prices, which may fluctuate going forward.

Operating Costs

	Quarter Ended Mar 31, 2005	Quarter Ended June 30, 2005	Quarter Ended Sep 30, 2005	Quarter Ended Dec 31, 2005	Year Ended Dec 31, 2005
Mines					
777 \$/tonne	\$ 42.20	\$ 36.07	\$ 32.33	\$ 40.46	\$ 37.60
Trout Lake \$/tonne	36.39	31.49	34.81	39.11	35.43
Chisel North \$/tonne	36.28	37.56	47.62	48.23	42.40
Konuto \$/tonne	40.32	34.81	31.94	39.80	36.42
Total mines \$/tonne	\$ 39.16	\$ 34.55	\$ 35.09	\$ 40.92	37.36
Concentrators					
Flin Flon \$/tonne	\$ 8.21	\$ 7.68	\$ 7.88	\$ 7.95	\$ 7.93
Snow Lake \$/tonne	\$ 16.51	\$ 17.30	\$ 15.82	\$ 19.80	\$ 17.35
Metallurgical Plants					
Copper Smelter \$/lb Cu	\$ 0.24	\$ 0.24	\$ 0.26	\$ 0.25	\$ 0.25
Zinc Plant \$/lb Zn	\$ 0.25	\$ 0.25	\$ 0.28	\$ 0.26	\$ 0.26
Non-GAAP Reconciliation of Operating Expenses (\$000)					
Mines					
777	\$ 10,136	\$ 9,488	\$ 9,029	\$ 12,466	\$ 41,119
Trout Lake	7,754	6,926	7,338	8,407	30,425
Chisel North	3,141	3,084	4,147	3,906	14,278
Konuto	3,510	3,132	2,648	2,090	11,380
Concentrators					
Flin Flon	4,538	4,290	4,605	4,501	17,934
Snow Lake	1,414	1,375	1,322	1,638	5,749
Metallurgical Plants					
Copper Smelter	10,770	11,226	11,970	13,009	46,975
Zinc Plant	16,015	16,005	15,646	17,416	65,082
Other					
Purchased Concentrate Treated	34,555	32,747	43,606	50,998	161,906
Anode Freight & Refining	6,313	5,931	5,713	4,936	22,893
Services & Administration	6,059	6,186	7,024	7,084	26,353
Care & Maintenance	820	1,122	878	620	3,440
Zochem (excluding zinc purchases from HBMS)	4,131	4,279	3,081	2,396	13,887
Other ⁽¹⁾	8,557	8,319	8,359	(6,138)	19,097
Total Operating Expenses, per financials	\$ 117,713	\$ 114,110	\$ 125,366	\$ 123,329	\$ 480,518

(1) Includes profit sharing, changes in domestic inventory, share of CMM and miscellaneous provisions.

Cash Flows, Liquidity, and Capital Resources

The following table summarizes our cash flows for the three and twelve-month periods ended December 31, 2005, and 2004.

Operating Activities	Quarter Ended Dec 31, 2005	Quarter Ended Sept 30, 2005	Quarter Ended Dec 31, 2004⁽¹⁾	Year Ended Dec 31, 2005	Year Ended Dec 31, 2004⁽¹⁾
(\$'000s except per share amounts)					
Earnings (loss) for the period	\$ 43,941	\$ 23,405	\$ (2,858)	\$ 85,218	\$ (9,920)
Items not affecting cash	(10,739)	9,758	(729)	37,953	705
Net change in non-cash items	23,952	(11,349)	959	21,691	1,987
Cash generated by (required for) operating activities	57,154	21,814	(2,628)	144,862	(7,228)
Cash generated by (required for) investing activities	(19,478)	(15,341)	346,855	(57,430)	(274,084)
Cash generated by (required for) financing activities	(22,736)	201	(281,937)	(7,368)	344,440
Foreign exchange gain (loss)					
on cash held in foreign currency	840	(4,761)	(689)	(2,957)	(689)
Increase in cash and cash equivalents	15,780	1,913	61,601	77,107	62,439

(1) Excludes results of HBMS prior to December 21, 2004.

With the exception of ten days in December 2004, HudBay had no production and was essentially a development stage enterprise. As such, discussion and analysis of 2005 compared to 2004 has been limited and, additionally, a comparison of results achieved in the third and fourth quarters of 2005 has been provided.

Quarter Ended December 31, 2005 Compared to Quarter Ended September 30, 2005

As of December 31, 2005, HudBay had cash and cash equivalents of \$141.7 million compared to \$125.9 million as at September 30, 2005. As at December 31, 2005, there were outstanding letters of credit in the amount of \$35.2 million unchanged from September 30, 2005.

Cash flow from operating activities totaled \$57.2 million for the quarter ended December 31, 2005 compared to \$21.8 million for the quarter ended September 30, 2005. During the third quarter additional cash outlays were made of approximately \$11.5 million for interest, \$10.9 million due to timing of purchase concentrates, and \$4.6 for insurance premiums which were not incurred in the last quarter. The remaining difference of \$3.9 million was a result of normal working capital fluctuations.

In the fourth quarter of 2005, a net total of \$19.5 million was required for investing activities, which related largely to capitalized mine development and other sustaining capital expenditures at HBMS. Also, Balmat capital expenditures started in November 2005 and approximately \$1.9 million was spent in the fourth quarter. This compares to \$15.3 million required for investment in development and other sustaining capital in the third quarter of 2005. As planned, the third quarter decrease in investing activities partially related to equipment purchases rescheduled into the fourth quarter. Financing activities in the fourth quarter of 2005 resulted in cash outlays of \$21.3 million which included a US \$19.0 million repurchase of debt at a premium of \$1.5 million, a \$0.9 million repayment under capital lease obligations, offset by approximately \$1.6 million proceeds from the exercise of warrants. Financing activities in the third quarter of 2005 generated \$0.2 million, which included approximately \$1.1 million proceeds from the exercise of warrants, and a \$0.9 million repayment under capital lease obligations.

As at December 31, 2005, HudBay had long-term financial debt (excluding the current portion) of \$200.5 million compared to \$223.4 as at September 30, 2005. The change in the amount outstanding arises from a change in the quarter-end exchange rate used to convert US \$ denominated debt, and the repurchase of debt described above, and repayments of capital leases. The Company will continue to consider, from time to time, reducing debt further.

Net cash flow for the quarter ended December 31, 2005 was \$15.8 million compared to \$1.9 million for the quarter ended September 30, 2005. Aside from the repurchase of debt of \$22 million, and an increase in capital expenditures of approximately \$6.0 million as indicated above, working capital changes were primarily the reason for the changes from quarter to quarter. The third quarter included significant cash expenditures as described above. Other changes were in the normal course of working capital variances.

New cash requirements for the near term include approximately US \$15 million (US \$13 million plus US \$2 million of adjustments), incurred in early 2006, for the purchase of the White Pine Refinery, and an estimated 2006 expenditure of US \$19 million for the Balmat mine.

Management's discussion and analysis

Quarter Ended December 31, 2005 Compared to Quarter Ended December 31, 2004

As of December 31, 2005, HudBay had cash and cash equivalents of \$141.7 million compared to \$64.6 million as at December 31, 2004. As at December 31, 2005, there were outstanding letters of credit in the amount of \$35.2 million, while there were \$22.8 million of outstanding letters of credit in 2004.

Cash flow from operations totaled \$57.1 million for the quarter ended December 31, 2005.

This relates primarily to HBMS operations, and compares with \$2.6 million cash required for operating activities in the same period in 2004 when the Company incurred a loss of \$2.9 million primarily in relation to management fees, mine care and maintenance activities and debenture interest expense, along with only 10 days operations of HBMS.

Year Ended December 31, 2005 Compared to Year Ended December 31, 2004

Cash flow from operations totaled \$144.9 million for the year ended December 31, 2005. This relates primarily to HBMS operations, which contributed \$153.3 million, and compares with \$7.2 million cash required for operating activities in the same period in 2004 when the Company incurred a loss of \$9.9 million primarily in relation to management fees, mine care and maintenance activities and debenture interest expense.

Financial Condition

Financial Condition at December 31, 2005 Compared to Financial Condition as at December 31, 2004

Cash and cash equivalents at December 31, 2005 increased to \$77.1 million compared to December 31, 2004.

Working capital improved by \$61.8 million, reflecting the improved cash position net of \$13.0 million of restricted cash and routine fluctuations in other working capital items.

Common share capital increased by \$23.5 million, which included \$12.9 million from exercise of warrants, \$1.1 million from exercise of options and \$10.0 million from flow-through shares net of \$0.6 million share issue costs.

Restricted cash decreased by \$13 million as funds placed in trust for the Provinces of Manitoba and Saskatchewan as financial assurance for the Company's asset retirement obligations were replaced with letters of credit. As at December 31, 2005, there were outstanding letters of credit in the amount of \$35.2 million unchanged from September 30, 2005.

HudBay's contractual obligations at December 31, 2005 are materially unchanged from December 31, 2004 except that, for the mutual benefit of both parties, the agreement to purchase from Compania Minera Dona Ines de Collahuasi was terminated effective June 30, 2005. Pursuant to the agreement, the Company purchased 40,000 dmt of copper concentrate per year. The termination of the agreement, which would otherwise have expired in 2008, is not expected to impact the Company's ability to obtain copper concentrate for its Flin Flon copper smelter.

The Company entered into a long-term agreement for the purchase of 10% of another mine's concentrate, or approximately 13,000 dry metric tonnes in 2006, and 20% of annual production or approximately 26,000 dry metric tonnes each year thereafter. The term of this agreement is from 2006 to 2015 and is subject to certain termination rights effective after December 31, 2008.

The Company committed to acquire 100% ownership of White Pine Copper Refinery Inc., through HBMS, by exercising an option held by its joint venture marketing Company Considar Metal Marketing Inc. (CMM) effective January 1, 2006.

Pursuant to a previous commitment to exchange HBMS' outstanding 9 5/8% Senior Secured Notes due January 15, 2012 (issued on December 21, 2004 in a private placement), a prospectus was filed in Ontario and a registration statement on Form F-10 (for which that prospectus formed a part) was filed with the SEC in August 2005. The Form F-10 registration statement registered the exchange of HBMS's outstanding notes for 9 5/8% Senior Secured Exchange Notes due January 15, 2012 under the United States Securities Act of 1933, as amended (the "Securities Act of 1933"). The terms of the exchange notes are identical in all material respects to those of the previously outstanding notes, except that the exchange notes are not subject to the same transfer restrictions. The exchange offer was both commenced and completed during the quarter ended September 30, 2005. 100% of the notes were exchanged.

The Company has received a commitment from the Bank of Nova Scotia to establish a revolving credit facility in the total amount of C\$ 25 million. In addition, the bank may consent to increasing the credit facility to C \$50 million if HBMS satisfies certain conditions. The facility closed in February 2006.

The Collective Bargaining Agreements (CBA's) with the unionized HBMS' Flin Flon/Snow Lake workforce expired on December 31, 2005 and negotiations are underway. In 1998, and in support of the \$435 million 777 Project, HBMS entered into a Amending Agreement in respect of certain of its collective bargaining agreements. The amending agreement prohibits strikes and lockouts through 2012 and provides for binding arbitration in the event that negotiated CBA settlements are not achieved.

Risk Management

The Company uses forward exchange contracts to limit the effects of movements in exchange rates on foreign currency denominated assets and liabilities and future anticipated transactions. At December 31, 2005 the Company held US dollar put options giving it the right, but not the obligation, to sell up to US \$56.9 million in equal quarterly amounts at \$1.20482 per US dollar, from January 2006 and continuing to January 2009.

From time to time the Company maintains price protection programs and conducts commodity price risk management to reduce risk through the use of financial instruments. The Company manages risk associated with forward physical sales that are made on a fixed price basis regarding zinc and zinc oxide and, accordingly, enters into forward zinc purchase contracts. These contracts effectively offset the Company's forward sales price commitments. In the current environment of strong base metal market prices, the Company has benefited from full exposure to metal price movements, but may consider implementing protection to limit the effects of future price changes.

Closure and Environmental Reclamation Provisions

HBMS has completed an evaluation of the closure and reclamation plans for its Manitoba and Saskatchewan operations and a review of other potential environmental costs to a feasibility level of accuracy. The closure plans have been updated and completed to the feasibility level of accuracy by major Canadian environmental engineering firms.

Based on the results of the evaluations to date, HudBay is satisfied that current financial statement provisions for closure and environmental reclamation obligations in Manitoba, Saskatchewan and elsewhere, are adequate and appropriate. The HudBay financial statement provision for closure and environmental reclamation has been adjusted to reflect the estimates of \$55.1 million, which has been recorded as a net present value of \$29.2 million. These provisions may be modified based on the review process currently being done by the governments of Manitoba and Saskatchewan.

Contractual Obligations and Commitments

Contractual Obligations

The following table summarizes, as at December 31, 2005, certain of our contractual obligations for the period specified.

Contractual Obligations (as at December 31, 2005) (\$000)	Total	Payments Due by Period			
		Less than 1 Year	1-3 Years	3-5 Years	After 5 Years
Interest on long-term debt obligations	\$ 113,503	\$ 17,462	\$ 34,924	\$ 34,924	\$ 26,193
Long-term debt obligations	195,493	4,000	11,500	-	179,993
Capital lease obligations	12,836	4,436	8,400	-	-
Operating lease obligations	3,939	2,515	1,282	142	-
Purchase obligations	11,700	11,700	-	-	-
Pension and other employee future benefits obligations	20,386	20,386	-	-	-
Asset retirement	55,059	462	1,833	2,400	50,364
Total	\$ 412,916	\$ 60,961	\$ 57,939	\$ 37,466	\$ 256,550

Management's discussion and analysis

Commitments

(a) Buy-sell commitments:

The Company has a commitment to purchase copper concentrate for payment based on a deemed delivery rather than a required physical delivery. The contract requires delivery of 72,000 tonnes annually from 2006 to 2008.

The Company also has a long-term agreement for the purchase of 10% or approximately 13,000 dry metric tonnes in 2006, and 20% of annual production or approximately 26,000 dry metric tonnes each year thereafter. The term of this agreement is from 2006 to 2015 and is subject to certain termination rights effective after December 31, 2008.

Payment for purchased concentrates is based on the market price of contained metal during a quotational period following delivery of the concentrate, less a fixed treatment and refining credit. If the Company cannot process the deemed tonnage in a timely manner, management believes the Company will be able to negotiate alternate arrangements for the sale or diversion of the tonnage.

The Company relies partly on processing purchased concentrates to achieve a portion of profits. The continued availability of such concentrates at economic terms beyond the expiry of current existing contracts cannot be determined at this time.

(b) Other commitments and agreements:

- (i) On January 1, 2006 the Company entered into an agency agreement with CMM for the Company's copper and precious metals products. As a result of this agreement, the Company retains title to the copper and precious metals until they are ultimately sold to the customers. In order to facilitate this agreement, the Company, in effect, on December 31, 2005 acquired the inventory of CMM. This purchase resulted in a reversal of the originating sales transactions associated with these products. Therefore the net result was the removal of any associated profit margin and inclusion of the associated inventories in the financial statements of the Company.
- (ii) On the majority of the 777 mine, the Company is subject to a royalty payment of \$0.25 per ton of ore milled and a net profits interest of 6-2/3% of the net proceeds of production if cumulative and aggregate cash flow for the year is positive. To date, the aggregate cash flow has been negative.
- (iii) HBMS has a profit-sharing plan, whereby 10% of the Company's after-tax earnings (excluding provisions for future income tax) calculated in accordance with Canadian generally accepted accounting principles for any given fiscal year will be distributed to all employees in the Flin Flon/Snow Lake operations, with the exception of executive officers and key management personnel. This expense has been accrued in these financial statements.
- (iv) The Company entered into a security agreement dated March 31, 1999 in favour of the Province of Saskatchewan in respect of its reclamation undertakings in Saskatchewan. As security for the implementation of decommissioning plans in respect of its undertakings in Saskatchewan, the Company has granted to the Province of Saskatchewan a first priority security interest in its mining equipment, buildings and fixtures and a first charge on all proceeds derived from any dealings with such mining equipment, buildings and fixtures. In addition, the Company has a security agreement dated May 7, 2004 in favour of the Province of Manitoba in respect of its reclamation undertakings in Manitoba. As security for the implementation of a decommissioning plan in respect of its undertakings in Manitoba, the Company has granted to the Province of Manitoba a first priority security interest in its mining equipment, buildings and fixtures owned by the Company and located on the lands and a first charge on all proceeds derived from any dealings with such mining equipment, buildings and fixtures. The security interests granted to the Provinces of Saskatchewan and Manitoba rank *pari passu*.

The Company has substantially completed a study of reclamation costs. The Company believes the existing security provided is adequate and sufficient. However, the Company has provided additional security to the provinces in the form of a letter of credit in the amount of \$13 million. Upon completion of the review of the study by the Provinces, the appropriate security may be reassessed.

- (v) In the normal course of operations, the Company provides indemnifications that are often standard contractual terms to counterparties in transactions, such as purchase and sale contracts, service agreements and leasing transactions. These indemnification agreements may require the Company to compensate the counterparties for costs incurred as a result of various events, including environmental liabilities, changes in (or in the interpretation of) laws and regulations, or as a result of litigation claims or statutory sanctions that may be suffered by the counterparty as a consequence of the transaction. The terms of these indemnification agreements will vary based upon the contract, the nature of which prevents the Company from making a reasonable estimate of the maximum potential amount that could be required to pay to counterparties. Historically, the Company has not made any significant payments under such indemnifications. Management estimates that there are no significant liabilities with respect to these indemnification guarantees.
- (vi) The Company has outstanding letters of credit in the amount of \$35.2 million (including the above-mentioned amount for environmental reclamation).
- (vii) In 2003, the Company established a wholly-owned subsidiary, St. Lawrence Zinc Company LLC ("St. Lawrence"). St. Lawrence was incorporated in the State of New York for the purposes of acquiring the Balmat zinc mine ("Balmat"). On September 24, 2003, St. Lawrence purchased the Balmat zinc mine and related assets located in upper New York State. Total consideration paid consisted of a cash deposit of U.S. \$1 million required to assume an environmental bond. In addition, contingent consideration, consisting of US \$20 million, was provided for in connection with the acquisition. The contingent consideration will be accounted for as additional purchase price as the contingencies are resolved and the amounts payable become fixed and/or determinable. The contingent consideration is payable out of 30% of the net future cash flow from operations after allowing for reasonable capital and exploration expenditures. A further \$5 million is payable if the monthly average special high grade settlement price of zinc, as quoted by The London Metal Exchange, averages \$0.70 or greater during any consecutive 24-month period after the closing date and prior to the fifth anniversary of the date on which the seller receives payment of the \$20 million.
- (viii) Pursuant to a Purchase Agreement dated February, 2002, the Company acquired from Regal Mines Limited certain properties and other assets located in Nova Scotia, including lead and zinc mining and milling operations (collectively the "Gays River"). A component of the purchase price was a 2% of net smelter return payable based on operations. The Company has entered into a letter of intent to sell its holding in Scozinc Limited to Acadian Gold Corporation for \$7.5 million. The potential sales transaction with Acadian Gold Corporation of Halifax is subject to the satisfaction of certain conditions, including the provision of certain cash deposits, board approvals, the purchaser completing satisfactory financing agreements, due diligence, the entering into of a definitive sale and purchase agreement and receipt of all necessary regulatory approvals.

Critical Accounting Estimates

The preparation of the financial statements in accordance with Canadian GAAP requires management to make estimates and judgements that affect the reported amounts of assets, liabilities, revenues and expenses. We evaluate the estimates periodically, including those relating to mineral reserve determinations, asset impairment, in-process inventory quantities, future income tax valuation reserves, asset retirement obligations, pension obligations and other employee future benefits. Actual results could differ from these estimates by material amounts.

Mineral Reserves and Mineral Resources

Mineral reserves and mineral resources are estimated to determine future recoverable mine production based on assessment of geological, engineering and metallurgical analyses, estimates of future production costs, capital costs and reclamation costs as well as metal prices. The costs of mineral properties and mine development are capitalized and amortized by the unit-of-production basis based on related proven and probable mineral reserves.

Impairment

The carrying value of our operating mines and plant and equipment is periodically reviewed for impairment when events or changes in circumstances indicate that the carrying amounts of related assets or groups of assets may not be recoverable. If total estimated future cash flows on an undiscounted basis are less than the carrying amount of the asset, an impairment loss is measured and recorded to write down the asset to its fair value.

Management's discussion and analysis

In-Process Inventories

In-process concentrates and metal inventory quantities comprise the majority of our inventories by value, and represent materials that are in the process of being converted into saleable product. Measurement of in-process inventories is based on assays of material received at our metallurgical plants and estimates of recoveries in the production processes. Realizable value of in-process inventories is estimated at financial statement dates and inventories are carried at the lower of cost and net realizable value.

Future Tax Assets and Liabilities

We use the liability method of tax allocation for accounting for income taxes. Under the liability method, future tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities. Future tax assets are reduced by a valuation allowance if it is more likely than not that some or all of the future tax assets will not be realized. We evaluate the carrying value of our future tax assets periodically by assessing its valuation allowance and by adjusting the amount of such valuation allowance, if necessary. The factors used to assess the likelihood of realization are forecasts of future taxable income and available tax planning strategies that could be implemented to realize future tax assets.

Asset Retirement Obligations

Asset retirement obligations are estimated based on environmental plans, in compliance with current environmental and regulatory requirements. Decommissioning costs are estimated and provided for, along with an identical decommissioning asset, when a new mine or plant is placed into commercial production. The decommissioning asset is amortized on a straight-line basis over the life of the mine or plant. Accretion costs are estimated and accrued over the life of each operating mine. The accrued amounts are increased by an annual interest component such that at the end of the asset life the provision is equal to the balance estimated to be paid at that date.

In view of the uncertainties concerning these future obligations, the ultimate timing and cost of reclamation and mine closure may differ materially from our estimates.

Pensions and other Employee Future Benefits

Our on-going health care benefit plans comprise the majority of post-retirement obligations. The obligations relating to these plans, together with pension plans maintained by us, are estimated based on actuarial determinations, which incorporate assumptions using management's best estimates of factors including plan performance, salary escalation, retirement dates of employees and drug cost escalation rates.

Disclosure Controls

As of December 31, 2005 management has evaluated the effectiveness of the disclosure controls and procedures as defined under the rules adopted by the U.S. Securities and Exchange Commission (SEC) and the Canadian securities regulatory authorities. This evaluation was performed under the supervision of and with the participation of the Chief Executive Officer and the Chief Financial Officer. Based on this evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the design and operation of the disclosure controls and procedures were effective.

2006 Outlook

The Company plans to focus on the following key areas for 2006:

- Growth opportunities
- Balmat re-opening
- Exploration
- Purchase of White Pine
- Divestiture of Scozinc
- Improve financial strength
- Relationship change with CMM
- 2006 expected production

Growth Opportunities

In 2006, the Company will look at opportunities to identify and evaluate strategic growth, focusing on zinc but not to the exclusion of copper, precious metals or secondary products. Opportunities synergistic with the Company's fully vertically integrated operations will be of particular interest.

Balmat Re-opening

HudBay decided to re-open its wholly owned Balmat mine and concentrator after completion of an internal feasibility study.

The Balmat zinc mine is strategically located near a multi-modal transportation system, which includes truck, rail and ocean transportation options for concentrate. Most of the mine's production will be treated at the CEZ refinery close to Montreal, some 158 kilometres from the mine.

The Company plans to continue in-fill ore definition drilling, as well as extension drilling, to upgrade our mineral reserve and resource base. Drilling to date has shown good ore body consistency.

The Balmat mine has been maintained to a high standard while on care and maintenance since October 2001. It includes a 3,200 foot deep shaft, underground excavations to access the ore zones, extensive mining equipment and a 5,000 ton per day ore concentrator. Recovery of zinc to concentrate is expected to be 96%, producing a concentrate containing 55.5% zinc. At full production in 2008, the mine is expected to produce close to, approximately 60,000 tons of zinc metal in concentrate, which is planned to be processed at the CEZ Refinery in Quebec, with the capability for the Company to process 40% of the concentrate at its zinc plant in Manitoba.

Life of mine total unit zinc production costs, including concentrate treatment and capital expenditures, are expected average US \$0.48 lb. (US \$0.57 per lb. for 2006 to 2008, and US \$0.43 per lb. thereafter).

At year end, we have hired approximately 100 permanent employees and have some 25 underground development and diamond drill contractors at site. Several of the professional skills were available in the mine area. At full production the mine is expected to have approximately 190 employees.

We expect Balmat's first ore in the second quarter of 2006 and then increasing to full production in 2008.

Exploration

Our focus for 2006 is on exploration activities in the Flin Flon greenstone belt. In 2005, the Company raised \$10 million through an issue of flow through common shares. This provided the funding for the \$10 million planned expenditure during 2005 and Q1 2006 for exploration on its approximately 210,000 hectares of prime exploration land holdings in the Flin Flon greenstone belt. We plan to continue the \$10 million per year program throughout 2006 and 2007.

Exploration includes targets that could feed the Snow Lake concentrator which is operating under capacity. HudBay has historically discovered 25 mines in the Flin Flon greenstone belt and further discoveries are an excellent opportunity for organic growth.

The exploration program includes electromagnetic anomaly drill testing, drilling of known mineral deposits as well as drilling of structural re-interpretations of prior ore bodies. During the recent winter months, we had six diamond drills operating.

Exploration is being managed by Hudson Bay Exploration and Development Company Limited (HBED), a wholly owned subsidiary of HBMS.

Historically, the Flin Flon greenstone belt ore bodies have grown by an average of 2.5 times the mineral reserve at commencement of mining. Further growth of ore bodies currently being mined is expected.

In addition, the company also expects to be exploring the approximate 20,000 hectares of land adjacent to its Balmat mine in New York State and its lead/zinc deposit, Tom Valley in the Yukon Territory, as well as its zinc holdings in Ontario and copper holdings in Chile.

Management's discussion and analysis

Purchase of White Pine

On January 1, 2006, we completed the purchase of all the outstanding common shares of White Pine Copper Refinery Inc. (White Pine) for a total purchase price of US \$13.0 million plus US \$2.1 million in adjustments. The acquisition of this refinery, which processes all of the Company's anode copper into cathode quality copper, completes HudBay's vertical integration, provides a dedicated processing facility for our copper anodes, as well as lowers the Company's operating costs by approximately two cents per pound of copper processed. We expect to spend total of \$5 million in capital expenditures for 2006.

Divestiture of Scozinc

In December 2005, we announced we had entered into a letter of intent to sell Scozinc (Gays River's lead and zinc mineral property) to Acadian Gold Corporation for \$7.5 million. The transaction is expected to be completed in 2006 subject to satisfaction of certain conditions.

Relationship Change with CMM

On January 1, 2006, the Company changed its relationship with CMM from a sales to an agency arrangement, whereby 100% of copper and precious metal inventory are owned by the Company until sold to customers. In the first half of 2006, the Company plans to convert the remaining products of zinc and zinc oxide under the same arrangement.

Improve Financial Strength

Early in 2006, our HBMS subsidiary received a commitment from the Bank of Nova Scotia to establish a revolving credit facility in the total amount of C \$25 million. The Bank may consent to increasing the credit facility to C \$50 million if the Company satisfies certain conditions.

As at year end we repurchased \$19 million of the 9.625% US notes to reduce the outstanding amount of this debt to US \$156 million. In 2006, the Company, may, from time to time, divert cash toward further debt reduction.

2006 Expected Production

Estimated production for 2006 is:

Zinc tonnes	120,000	to	140,000
Copper ⁽¹⁾ tonnes	45,000	to	55,000
Gold troy oz.	85,000	to	100,000
Silver troy oz.	1,000,000	to	1,300,000

(1) Domestic copper production only.

Forward-looking Statements

This MD&A contains certain forward-looking statements. All statements, other than statements of historical fact, included herein, including without limitation, statements regarding the Company's future plans and objectives are forward-looking statements that involve various risks and uncertainties. There can be no assurance that such statements will prove accurate, and actual results and future events could differ materially from those anticipated in such statements.

Important factors that could cause actual results to differ materially from the Company's expectations are disclosed in documents that we have filed from time to time with the Canadian and other regulatory authorities.

Certain items of financial information in this MD&A, including free cash flow, operating cash flow per common share, unit operating expenses, and cash cost per pound of zinc, net of by-product credits, are non-GAAP measures and are furnished to provide additional information. As non-GAAP measures they neither have standardized meanings nor are they necessarily comparable with similar measures presented by other companies. These measures should not be considered in isolation or as a substitute for measures of performance prepared in accordance with generally accepted accounting principles and are not necessarily indicative of operating expenses as determined under generally accepted accounting principles. These measures are intended to provide investors with information about the cash generating capabilities of the Company's operations. HudBay uses this information for the same purpose. Mining operations are capital intensive. These measures exclude capital expenditures. Capital expenditures are discussed throughout the MD&A and the consolidated financial statements.

Appendix – HBMS Production

A summary of production statistics for the fourth quarter of 2005, as well as year-to-date data, together with comparative information for 2004 is shown in the following table.

	Quarter Ended Dec 31, 2005	Quarter Ended Sept 30, 2005	Quarter Ended Dec 31, 2004	Year Ended Dec 31, 2005	Year Ended Dec 31, 2004
777					
Ore tonnes	308,099	279,258	245,695	1,093,683	975,895
Copper %	2.28	2.28	2.54	2.24	2.89
Zinc %	5.10	4.34	4.22	4.47	4.50
Gold g/tonne	2.06	2.18	2.03	2.11	2.27
Silver g/tonne	24.56	23.93	21.25	23.84	23.14
Trout Lake					
Ore tonnes	214,982	210,802	226,630	858,751	916,097
Copper %	1.79	1.29	1.36	1.39	1.46
Zinc %	3.86	5.70	6.06	5.61	5.32
Gold g/tonne	1.32	1.57	1.47	1.47	1.46
Silver g/tonne	13.35	14.63	15.69	14.59	13.57
Chisel North					
Ore tonnes	80,995	87,090	83,158	336,731	327,853
Zinc %	8.97	8.31	8.89	9.00	9.99
Konuto⁽¹⁾					
Ore tonnes	52,522	82,895	74,953	312,465	327,231
Copper %	3.30	3.35	3.91	3.90	4.07
Zinc %	2.36	2.07	2.13	1.81	2.08
Gold g/tonne	1.73	1.33	1.66	1.65	1.91
Silver g/tonne	11.46	8.32	9.71	9.17	9.61
Total Mines:					
Ore tonnes	656,598	660,045	630,436	2,601,630	2,547,076
Copper %	1.94	1.83	1.97	1.89	2.18
Zinc %	4.95	5.01	5.25	5.11	5.19
Gold g/tonne	1.59	1.65	1.57	1.64	1.70
Silver g/tonne	19.95	18.63	17.78	19.40	18.26

(1) Konuto mine closed in the fourth quarter of 2005.

Management's discussion and analysis

Fourth Quarter Results

	Quarter Ended Dec 31, 2005	Quarter Ended Sept 30, 2005	Quarter Ended Dec 31, 2004	Year Ended Dec 31, 2005	Year Ended Dec 31, 2004
Concentrators					
Flin Flon Concentrator:					
Ore tonnes	556,445	584,362	529,875	2,262,555	2,156,051
Copper %	2.23	2.13	2.22	2.14	2.46
Zinc %	4.32	4.44	4.71	4.53	4.50
Gold g/tonne	1.75	1.85	1.79	1.80	1.89
Silver g/tonne	19.01	18.19	17.48	18.15	17.33
Copper Concentrate Produced tonnes	49,465	48,763	47,081	188,851	208,961
Grade % Cu	23.99	23.94	22.95	23.82	23.60
Zinc Concentrate Produced tonnes	38,115	42,488	39,476	164,416	152,453
Grade % Zn	52.15	51.40	50.76	51.51	50.42
Copper recovery to Cu Conc %	93.7	93.7	91.8	92.8	93.0
Gold recovery to Cu Conc %	72.5	71.8	79.5	74.9	69.6
Silver recovery to Cu Conc %	66.1	64.6	76.4	66.3	68.1
Zn recovery to Zn Conc %	81.2	84.1	80.2	82.6	79.2
Snow Lake Concentrator:					
Ore tonnes	82,729	83,570	85,580	331,427	327,853
Zinc %	9.00	8.26	8.91	9.00	9.99
Zinc Concentrate Produced tonnes	14,118	13,058	14,431	56,646	61,825
Grade % Zn	51.21	51.25	51.48	51.25	51.52
Zn recovery to Zn Conc %	97.1	96.9	97.4	97.3	97.3

	Quarter Ended Dec 31, 2005	Quarter Ended Sept 30, 2005	Quarter Ended Dec 31, 2004	Year Ended Dec 31, 2005	Year Ended Dec 31, 2004
Smelter					
Copper Concentrate Treated					
Domestic tonnes	55,172	49,780	55,068	206,343	185,349
Purchased tonnes	28,828	28,212	28,252	111,935	98,750
Total tonnes	84,000	77,992	83,320	318,278	284,099
Zinc Plant					
Zinc Concentrate Treated					
Domestic tonnes	59,856	51,339	56,784	228,107	219,561
Purchased tonnes	0	0	0	0	3,488
Total tonnes	59,856	51,339	56,784	228,107	223,049
Metal Produced					
From HBMS Mines					
Copper tonnes	13,822	11,538	12,557	49,179	43,653
Zinc tonnes	30,485	25,733	28,323	114,557	108,404
Gold troy oz.	25,311	22,759	26,220	100,144	77,611
Silver troy oz.	264,259	205,144	240,336	916,810	696,454
From Purchased Concentrates					
Copper tonnes	9,985	9,182	9,351	37,106	33,241
Zinc tonnes	35	43	24	131	1,815
Gold troy oz.	546	441	412	1,927	1,407
Silver troy oz.	137,131	126,685	136,091	493,702	418,114
Total Metal Produced					
Copper tonnes	23,807	20,720	21,908	86,285	76,894
Zinc tonnes	30,520	25,775	28,348	114,687	110,219
Gold troy oz.	25,860	23,200	26,632	102,371	79,018
Silver troy oz.	401,385	331,829	376,427	1,410,512	1,114,568
HBMS Metal Sold⁽¹⁾					
Copper tonnes	17,644	19,800	20,815	78,070	73,905
Zinc, incl sales to Zochem tonnes	29,598	29,500	27,973	114,682	111,319
Gold troy oz.	21,783	21,800	25,403	95,511	75,578
Silver troy oz.	358,434	309,500	343,144	1,321,784	1,054,998

Management's responsibility for financial reporting

All information in the Annual Report, including the accompanying financial statements and management's discussion and analysis of the consolidated financial position and results of operations ("MD&A") of the Company, is the responsibility of the management of the Company. The consolidated financial statements and the MD&A were prepared by management in accordance with accounting principles and MD&A disclosure requirements generally accepted in Canada, and the financial information contained elsewhere in the Annual Report conforms to the consolidated financial statements and MD&A.

The preparation of financial statements and MD&A requires the selection of appropriate generally accepted accounting principles and the use of estimates and judgment by management to present fairly and consistently the consolidated financial position and results of operations of the Company. Estimates are necessary when transactions affecting the current accounting period cannot be finalized with certainty until future periods. In management's opinion, such estimates have been properly reflected in the consolidated financial statements and MD&A. Systems of internal accounting controls are designed and maintained by management in order to provide reasonable assurance, on a cost-effective basis, of the reliability of this financial information.

The Board of Directors is responsible for ensuring that management fulfils its responsibilities for financial reporting and is ultimately responsible for reviewing and approving the consolidated financial statements and MD&A. The Board carries out this responsibility principally through its Audit Committee composed of three directors, none of whom are members of management. The Committee meets periodically with management and the Company's independent auditors to discuss internal controls over the financial reporting issues and to review the consolidated financial statements, the MD&A and the independent auditors' report to shareholders. The Committee reports its findings to the Board for consideration when approving the consolidated financial statements and MD&A for issuance to shareholders. The Committee also considers, for review by the Board and approval by the shareholders, the engagement or re-appointment of the Company's independent auditors.

The consolidated financial statements have been audited on behalf of the shareholders by the Company's independent auditors, Deloitte & Touche LLP, Independent Registered Chartered Accountants, in accordance with Canadian generally accepted auditing standards. The auditors' report, dated March 17, 2006, outlines the scope of their examination and their opinion on the consolidated financial statements.

(signed) Peter R. Jones, P.Eng.

(signed) Jeff A. Swinoga, CA

Peter R. Jones, P.Eng.

President & Chief Executive Officer

Jeff A. Swinoga, CA

Vice-President & Chief Financial Officer

Report of Independent Registered Chartered Accountants

To the Shareholders of HudBay Minerals Inc.

We have audited the consolidated balance sheet of HudBay Minerals Inc. as at December 31, 2005 and the consolidated statements of earnings, retained earnings and cash flows for the year ended December 31, 2005. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2005, the results of its operations and cash flows for the year ended December 31, 2005 in accordance with Canadian generally accepted accounting principles.

The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion.

The consolidated financial statements as at December 31, 2004 and for the year then ended were audited by other auditors who expressed an opinion without reservation on those statements in their report dated March 30, 2005.

(signed) Deloitte & Touche LLP

Deloitte & Touche LLP

Independent Registered Chartered Accountants
Winnipeg, Manitoba, Canada

March 17, 2006

Consolidated statements of earnings (loss)

(In thousands of Canadian dollars, except share and per share amounts)
Years ended December 31, 2005 and 2004

	2005	2004
Revenue	\$ 652,028	\$ 13,327
Expenses:		
Operating	480,518	14,081
Depreciation and amortization	53,100	1,443
General and administrative	19,620	5,127
Exploration	11,281	1,734
Accretion of asset retirement obligation	2,612	138
Foreign exchange loss	2,338	-
	569,469	22,523
Operating earnings (loss)	82,559	(9,196)
Interest expense	(21,939)	(2,320)
Foreign exchange gain on long term debt	6,825	1,562
Gain on derivative instruments (note 16c)	5,319	78
Interest and other income	3,996	103
Amortization of deferred financing fees	(2,342)	(620)
Earnings (loss) before income taxes	74,418	(10,393)
Tax recovery (note 13)	10,800	473
Earnings (loss) for the year	\$ 85,218	\$ (9,920)
Earnings (loss) per share:		
Basic	\$ 1.04	\$ (1.12)
Diluted (note 14d)	0.70	(1.12)
Weighted average number of common shares outstanding		
Basic	82,008,190	8,894,235
Diluted (note 14d)	121,116,832	8,894,235

See accompanying notes to consolidated financial statements.

Consolidated statements of retained earnings (deficit)

(In thousands of Canadian dollars) Years ended December 31, 2005 and 2004

	2005	2004
Deficit, beginning of year:		
As previously stated	\$ (6,486)	\$ (19,052)
Changes in accounting policies (note 2):		
Asset retirement obligations	-	(43)
Exploration costs	-	(590)
As restated	(6,486)	(19,685)
Earnings (loss) for the year	85,218	(9,920)
Realization of equity component of debenture (note 8c)	-	1,140
Reduction of stated capital (note 14e)	-	21,979
Retained earnings (deficit), end of year	\$ 78,732	\$ (6,486)

See accompanying notes to consolidated financial statements.

Consolidated balance sheets

(In thousands of Canadian dollars) December 31, 2005 and 2004

2005

2004

Assets

Current assets

Cash and cash equivalents	\$ 141,660	\$ 64,553
Accounts receivable	44,698	73,210
Inventories (note 4)	116,596	100,282
Prepaid expenses	3,625	3,496
Current portion of fair value of derivatives (note 16c)	4,483	3,418
Future income taxes (note 13)	26,200	12,900
	337,262	257,859
Property, plant and equipment (note 5)	378,207	358,662
Other assets (note 6)	13,284	26,176
	\$ 728,753	\$ 642,697

Liabilities and Shareholders' Equity

Current liabilities

Accounts payable and accrued liabilities	\$ 91,930	\$ 89,749
Interest payable on long-term debt	8,004	563
Current portion of other liabilities (note 7)	28,211	20,595
	128,145	110,907
Long-term debt (note 8)	191,493	223,529
Pension obligation (note 9)	46,743	57,437
Other employee future benefits (note 10)	61,250	57,929
Asset retirement obligations (note 11)	29,219	27,120
Obligations under capital leases (note 12)	9,011	11,719
Future income tax liabilities (note 13)	1,666	1,290
	\$ 467,527	\$ 489,931

Shareholders' equity

Share capital:		
Common shares (note 14a)	143,611	120,138
Warrants (note 14b)	28,931	35,850
Contributed surplus	10,015	3,288
Cumulative translation adjustment	(63)	(24)
Retained earnings (deficit)	78,732	(6,486)
	261,226	152,766
	\$ 728,753	\$ 642,697

Contingencies (note 15), Commitments (note 20), Subsequent events (note 24).
See accompanying notes to consolidated financial statements.

On behalf of the Board: (signed) Allen J. Palmiere

(signed) Peter R. Jones

Allen J. Palmiere
Director

Peter R. Jones
Director

Consolidated statements of cash flows

(In thousands of Canadian dollars) Years ended December 31, 2005 and 2004

2005

2004

Cash provided by (used in):

Operating activities

Earnings (loss) for the year	\$ 85,218	\$ (9,920)
Items not affecting cash:		
Depreciation and amortization	53,100	1,227
Realization of previously unrecorded tax losses	(11,858)	(397)
Unrealized foreign exchange gain	(4,012)	(2,980)
Amortization of deferred financing costs	2,342	216
Accretion expense on asset retirement obligation	2,612	73
Stock-based compensation	2,674	1,193
Unrealized portion of change in fair value of derivative	(562)	(78)
Other	(6,343)	1,165
Change in non-cash working capital (note 21)	21,691	2,273
	144,862	(7,228)

Financing activities

Issuance (repayment) of senior secured notes (note 8a)	(21,953)	214,112
Issuance of common shares, net of costs	20,607	139,484
Repayments of obligations under capital leases	(3,672)	(17)
Repayment of loans payable	(2,000)	-
Deferred financing cost	(350)	(9,600)
Proceeds of exercise of stock options	-	64
Proceeds on exercise of warrants	-	117
Decrease in debenture subscription receivable	-	2,000
Issuance of convertible debenture	-	600
Repayment of convertible debenture	-	(2,860)
Advance from HBMS prior to acquisition	-	540
	(7,368)	344,440

Investing activities

Additions to property, plant and equipment	(70,924)	(5,180)
Decrease (increase) in restricted cash	13,000	(13,000)
Additions (reductions) to environmental deposits	31	(294)
Sale of investments	463	-
Acquisition of HBMS, net of cash acquired (note 3)	-	(255,610)
	(57,430)	(274,084)
Foreign exchange loss on cash held in foreign currency	(2,957)	(689)
Change in cash and cash equivalents	77,107	62,439
Cash and cash equivalents, beginning of year	64,553	2,114
Cash and cash equivalents, end of year	\$ 141,660	\$ 64,553

Supplementary cash flow information

Interest paid	\$ 13,613	\$ 309
Additions to obligations under capital leases	1,451	-
Supplemental disclosure of non-cash financing and investing activities:		
Shares issued in settlement of other indebtedness	-	40
Shares and warrants issued in connection with the acquisition of HBMS	-	13,000

See accompanying notes to consolidated financial statements.

Notes to consolidated financial statements

[Amounts in thousands of Canadian dollars, except share and per share data]

Years ended December 31, 2005 and 2004

1. Nature of business

HudBay Minerals Inc. (the "Company") changed its name from ONTZINC Corporation by way of Articles of Amendment dated December 21, 2004. The Company was formed by amalgamation in 1996 under the Ontario Business Corporations Act and was continued under the Canada Business Act in October 25, 2005. Prior to December 21, 2004, the Company was engaged in the business of evaluation, acquisition and exploration of mineral properties. Substantially all of the efforts of the Company were devoted to these business activities. Prior to that date, the Company had not earned significant revenue and was considered to be in the development stage.

On December 21, 2004, the Company completed a public offering of common shares and warrants raising gross proceeds of \$143,813 and also completed an offering of U.S.\$175,000 Senior Secured Notes. The Company then utilized the proceeds from these financings to complete the acquisition from Anglo American International, S.A. ("Anglo American") of all of the outstanding shares of 152640 Canada Inc., which held all of the outstanding shares of Hudson Bay Mining and Smelting Co., Ltd. ("HBMS").

The Company is now an integrated mining and metals processing company that operates mines and concentrators in northern Manitoba and Saskatchewan, Canada, is re-opening a mine in New York State, and operates a copper and zinc metal production complex in Flin Flon, Manitoba, exercised an option to purchase a copper refinery in Michigan state, and a zinc oxide production facility in Brampton, Ontario.

Also on December 21, 2004, the Company completed a 30 for 1 common share consolidation which has been retroactively reflected as if the common share consolidation had occurred on January 1, 2002. All references to common shares within these consolidated financial statements reflect the consolidation.

2. Significant accounting policies

(a) Basis of presentation

These consolidated financial statements are prepared in accordance with accounting principles generally accepted in Canada ("Canadian GAAP") and are presented in Canadian dollars. These principles conform in all material respects with generally accepted accounting principles in the United States ("U.S. GAAP"), except as described in note 23.

These consolidated financial statements include the financial statements of the Company and its wholly owned subsidiaries. Intercompany accounts and transactions have been eliminated on consolidation.

The financial position of HBMS as at December 31, 2004 and its results of operations and cash flows from the date of acquisition on December 21, 2004 to December 31, 2004 have been included in these consolidated financial statements. As a wholly owned subsidiary for the 2005 fiscal year, the financial position of HBMS as of December 31, 2005 and the results of its operation and cash flows for the entire year have been included in these financial statements. Accordingly, comparative operating results are not considered to be meaningful. The proportionate share of the assets and liabilities of any joint ventures in which HBMS shares joint control has also been included.

(b) Use of estimates

The preparation of financial statements requires the use of management estimates and assumptions that affect the amounts reported in the consolidated financial statements and related notes. Significant areas where management's judgement is applied include ore reserve determinations, in-process inventory quantities, plant and equipment estimated economic lives and salvage values, contingent liabilities, future income tax valuation reserves, asset retirement obligation, pension obligations and other employee future benefits. Actual results could differ from those estimates by material amounts.

(c) Translation of foreign currencies

Monetary assets and liabilities are translated at year-end exchange rates and non-monetary assets and liabilities are translated at historical rates. Gains and losses on translation of monetary assets and monetary liabilities are charged to earnings.

The assets and liabilities of self-sustaining foreign operations are translated at year-end exchange rates, and revenue and expenses are translated at monthly average exchange rates. Differences arising from these foreign currency translations are recorded in shareholders' equity as a cumulative translation adjustment until they are realized by a reduction in the investment.

(d) Revenue recognition

Prior to December 21, 2004, the Company had not earned significant revenue and was considered to be in the development stage.

Sales are recognized and revenue is recorded at market prices when title and the rights and obligations of ownership pass to the customer, collection is reasonably assured and the price is reasonably determinable. A number of the Company's products are sold under pricing arrangements where final prices are determined by quoted market prices in a period subsequent to the date of sale. Subsequent variations in the final determination of metal weights, assay and price are recognized as revenue adjustments as they occur until the price is finalized.

(e) Cash and cash equivalents

Cash and cash equivalents include cash and highly liquid investments with an original maturity of three months or less at the date of acquisition.

(f) Inventories

Inventories consist substantially of in-process inventory (concentrates and metals), metal products and supplies. Concentrates, metals and all other saleable products are valued at the lower of cost and estimated net realizable value. Cost includes material, labour and amortization of all property, plant and equipment directly involved with the mining and production process. In-process inventories represent materials that are currently in the process of being converted to a saleable product. Conversion processes vary depending on the nature of the concentrate or metal. In-process inventory is measured based on assays of the material fed to the processing plants and the projected recoveries of the respective plants and is valued at cost. Cost of finished metal inventory represent the average cost of the in-process inventory incurred prior to the refining and casting process, plus applicable refining and casting costs.

Supplies are valued at the lower of cost, replacement and value in use. Cost is determined on an average basis.

(g) Investments

Investments include marketable securities recorded at the lower of cost and market.

(h) Property, plant and equipment

(i) Mineral properties

(a) Mineral exploration costs are expensed as incurred. When management's evaluation, based on a feasibility study, indicates that the property is capable of economical commercial production, as a result of establishing proven and probable resources, future costs are capitalized as mine development expenditures.

(b) Mineral exploration properties acquired as part of the purchase of HBMS will be carried at initial fair value and be subject to an annual impairment review and evaluation.

(ii) Mine development expenditures

Exploration and development costs for properties deemed capable of economical commercial production are capitalized and amortized using the unit-of-production method. The unit-of-production amortization is based on the related proven and probable tons of ore reserves and associated future development costs. The cost of underground development to provide access to a reserve

Notes to consolidated financial statements

at an operating mine is capitalized where that portion of the development is necessary to access more than one workplace or stope. Capital development includes shafts, ramps, track haulage drifts, ancillary drifts, sumps, electrical substations, refuge stations, ventilation raises, permanent manways, and ore and waste pass raises.

Ongoing repairs, maintenance and development expenditures are charged to operations as incurred. These include ore stope access drifts, footwall and hangingwall drifts in stopes, drawpoints, drill drifts, sublevels, slots, drill raises, stope manway access raises and definition diamond drilling.

No amortization is provided in respect of mine development expenditures until commencement of economical commercial production. Commercial production occurs when an asset or property is substantially complete and ready for its intended use. Any production revenue prior to commercial production, net of related costs, is offset against the development costs.

(iii) Plant and equipment

Expenditures for plant and equipment additions, major replacements and improvements are capitalized at cost, net of applied investment tax credits. Plant and equipment, including assets under capital lease, are depreciated on either unit-of-production or straight-line basis. The unit-of-production method is based on proven and probable tons of ore reserves. The assets using the straight-line method are depreciated over the estimated useful lives of the assets, which range from one to 15 years. The Company also considers future estimated residual values in its determination of depreciation.

(iv) Capitalized interest

Interest on borrowings related to the financing of major capital projects under construction is capitalized during the construction phase as part of the cost of the project.

(v) Impairment of long-lived assets

The Company reviews and evaluates the carrying value of its operating mines and exploration and development properties for impairment when events or circumstances indicate that the carrying amounts of related assets or groups of assets may not be recoverable. If the total estimated future cash flows on an undiscounted basis are less than the carrying amount of the asset, an impairment loss is measured and assets are written down to fair value, which is normally the discounted value of future cash flows. Future cash flows are estimated based on estimated future recoverable mine production, expected sales prices (considering current and historical prices, price trends and related factors), production levels, cash costs of production, capital and reclamation costs, all based on detailed engineering life-of-mine plans. Future recoverable mine production is determined from proven and probable reserves and measured, indicated and inferred mineral resources after taking into account estimated dilution and recoveries during mining, and estimated losses during ore processing and treatment. Estimates of recoverable production from measured, indicated and inferred mineral resources are considered economically mineable and are based on management's confidence in converting such resources to proven and probable reserves. All long-lived assets are considered together for purposes of estimating future cash flows. Assumptions underlying future cash flow estimates are subject to risks and uncertainties. It is possible that changes in estimates could occur which may affect the expected recoverability of the Company's investments in mineral properties.

(i) Pension and other employee future benefits

The Company has non-contributory and contributory defined benefit pension plans for its employees. The benefits are based on years of service and final average salary for the salary plan, and flat dollar amount combined with years of service for the hourly. The Company provides long-term disability income, health benefits and other post-employment benefits to hourly employees and long-term disability health benefits to salaried employees. The Company also provides ongoing health care benefits to certain pensioners.

The Company accrues its obligations under the defined benefit plans as the employees render the services necessary to earn the pension and other retirement benefits. The actuarial determination of the accrued benefit obligations for pensions and other retirement benefits uses the projected benefit method prorated on service (which incorporates management's best estimate of future salary levels, other cost escalation, retirement ages of employees and other actuarial factors). The measurement date of the plan assets and accrued benefit obligation coincides with the Company's fiscal year. The most recent actuarial valuation of the pension plans for funding purposes was as of December 31, 2004.

Actuarial gains (losses) on plan assets arise from the difference between the actual return on plan assets for a period and the expected return on plan assets for that period. For the purpose of calculating the expected return on plan assets, those assets are valued at fair value. Actuarial gains (losses) on the accrued benefit obligation arise from differences between actual and expected experience and from changes in the actuarial assumptions used to determine the accrued benefit obligation. The average remaining service period of the active employees covered by the pension plan is 12 years. The average remaining service period of the active employees covered by the other retirement benefits plan is 13.7 years.

The Company also has defined contribution plans providing pension benefits for its salaried employees. The cost of the defined contribution plans is recognized based on the contributions required to be made during each period.

(j) Financial instruments and commodity contracts

The carrying value of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, current portion of long-term debt and current portion of obligations under capital leases approximate their fair value due to their short-term nature. The fair value of long-term debt has been determined using discounted cash flows at current market rates. Derivative financial instruments have been valued at current fair values using quoted market prices or accepted valuation methodologies.

The Company from time to time employs derivative financial instruments, including forwards and option contracts, to manage risk originating from actual exposures to commodity price risk, foreign exchange risk and interest rate risk.

In management's opinion, although the contracts continue to be effective in mitigating the Company's exposure to commodity risk, the Company's management elected not to designate its commodity risk management activities as accounting hedges under The Canadian Institute of Chartered Accountants' ("CICA") Accounting Guideline 13 ("AcG-13"), Hedging Relationships. Management may evaluate, from time to time, its hedge accounting policies and practices and may elect to designate and document contracts as accounting hedges.

Foreign exchange derivative contracts continue to be effective in mitigating some of the Company's exposure to foreign exchange rate fluctuations. The Company elected to designate these contracts as accounting hedges under AcG-13 and has applied cash flow hedge accounting.

The estimated fair value of all derivative financial instruments is based on quoted market prices or, in their absence, third party market indications and forecasts. Unrealized gains or losses and realized gains or losses are recorded in the statement of earnings.

(k) Stock-based compensation plans

The Company's stock-based compensation plan is described in note 14c. The Company accounts for all stock-based payments using the fair value-based method. Under this method, compensation cost attributable to options granted is measured at fair value at the grant date. Any consideration paid on exercise of stock options or purchase of stock is credited to share capital.

(l) Income taxes

The Company accounts for income and mining taxes under the asset and liability method. Under this method of tax allocation, future income and mining tax assets and liabilities are determined based on differences between the financial statement carrying values and their respective income tax basis (temporary differences). Future income tax assets and liabilities are measured using the substantively enacted tax rates expected to be in effect when the temporary differences are likely to reverse. The effect on future income tax assets and liabilities of a change in tax rates is included in income in the year in which the change is enacted or substantively enacted. The amount of future income tax assets recognized is limited to the amount that is more likely than not to be realized.

(m) Flow-through shares

The Company financed a portion of its exploration and development activities through the issue of flow-through shares. Under the terms of these share issues, the tax attributes of the related expenditures are renounced to subscribers. Share capital is reduced and future income tax liabilities and/or tax recoveries are increased by the estimated income tax benefits renounced by the Company to the subscribers.

Notes to consolidated financial statements

(n) Earnings (loss) per share

Basic earnings (loss) per share is computed by dividing earnings (loss) for the year by the weighted average number of common shares outstanding for the year. Shares held in escrow are included in the weighted average number of common shares when they are released from escrow. Diluted earnings (loss) per share is similar to basic earnings per share, except that the denominator is increased to include the number of additional common shares that would have been outstanding if the dilutive potential common shares had been issued using the treasury stock method.

(o) Asset retirement obligations

The Company accounts for asset retirement obligations in accordance with Section 3110 of the CICA Handbook. Section 3110 applies to legal obligations associated with the retirement of long-lived assets that result from the acquisition, construction, development and/or normal operation of a long-lived asset.

This policy requires that the fair value of a liability for an asset retirement obligation be recorded in the period in which it is incurred. When the liability is initially recorded, the cost is capitalized by increasing the carrying amount of the related long-lived asset. Upon settlement of the liability, a gain or loss is recorded. The Company records asset retirement obligations primarily associated with decommissioning and restoration costs. The Company will make periodic assessments as to the reasonableness of its asset retirement obligation estimates and revise those estimates accordingly. The respective asset and liability balances are adjusted with the corresponding increase or decrease expensed in future periods.

The long-term asset retirement obligation is based on environmental plans, in compliance with the current environmental and regulatory requirements. Accretion expense is charged to the consolidated statements of earnings and deficit based on application of an interest component to the existing liability.

(p) Exploration costs

The Company accounts for exploration expenditures by capitalizing the costs when management's evaluation indicates that the property is capable of economical commercial production.

3. Acquisition of Hudson Bay Mining and Smelting Co., Limited

On December 21, 2004, the Company acquired all of the outstanding common shares of HBMS for total purchase consideration of \$315,790, plus \$4,324 of corporate transaction costs. The total purchase consideration of \$315,790 was satisfied by cash of \$302,790 and by the issuance to Anglo of 5,777,777 common shares and 86,666,667 share purchase warrants, where every 30 share purchase warrants are exercisable for one common share at an exercise price of \$3.15 per common share. The value of the common share consideration of \$11,700 has been determined based on the average of the closing price of the Company's common shares for the two days before and after the date of announcement of the transaction on October 7, 2004. The value of the warrant consideration of \$1,300 has been based on a similar method to the valuation of the warrants issued in the public offering as described in note 14b. The acquisition has been accounted for by the purchase method and the result of operations and cash flows have been included within these consolidated financial statements from December 21, 2004.

The following table summarizes the allocation of the purchase consideration of the fair value of the assets and liabilities acquired on the date of acquisition:

Current assets (including cash of \$51,504)	\$ 229,601
Investments	463
Property, plant and equipment (note 5)	349,629
Intangible assets (note 6)	1,452
Current liabilities	(73,886)
Debt obligations (note 8)	(15,179)
Pensions and post-retirement benefit obligations (notes 9 and 10)	(130,353)
Asset retirement obligations (note 11)	(26,163)
Obligations under capital leases (note 12)	(15,074)
Other non-current liabilities	(376)
	<hr/>
	\$ 320,114

During the fourth quarter of 2005, after receiving the final independent asset and obligation valuations from third parties, the Company finalised its accounting for the HBMS acquisition. The excess of amounts assigned to net assets over the purchase price ("negative goodwill") in the amount of \$299.6 million has been allocated as a pro rata reduction as follows:

	Fair market value	Negative goodwill allocation	Carrying value
Property, plant and equipment	\$ 647,976	\$ 298,347	\$ 349,629
Intangible assets	2,691	1,239	1,452
	\$ 650,667	\$ 299,586	\$ 351,081

4. Inventories

	2005	2004
Work-in-process	\$ 84,456	\$ 72,061
Finished goods	16,635	14,639
Material and supplies	15,505	13,582
	\$ 116,596	\$ 100,282

5. Property, plant and equipment

2005	Cost	Accumulated depreciation and amortization	Net book value
Property, plant and equipment	\$ 279,711	\$ 19,924	\$ 259,787
Mine development	135,826	34,398	101,428
Mineral exploration properties	16,992	-	16,992
	\$ 432,529	\$ 54,322	\$ 378,207

2004	Cost	Accumulated depreciation and amortization	Net book value
Property, plant and equipment	\$ 203,705	\$ 418	\$ 203,287
Mine development	156,189	814	155,375
	\$ 359,894	\$ 1,232	\$ 358,662

The depreciation and amortization recorded for 2004 included HBMS for the 10-day period.

Included in property, plant and equipment are the following:

	2005	2004
Property, plant and equipment under construction or development	\$ 8,006	\$ 6,753
Equipment under capital leases:		
Cost	\$ 17,090	\$ 15,521
Less accumulated depreciation	1,738	39
	\$ 15,352	\$ 15,482
Amortization expense related to equipment under capital leases	\$ 1,699	\$ 39

6. Other assets

	2005	2004
Deferred financing costs	\$ 7,610	\$ 9,600
Deferred option premiums	3,647	-
Intangible assets	-	552
Restricted cash	-	13,000
Environmental deposits	1,758	1,789
Fair value of derivatives (note 16c)	269	772
Investments	-	463
	\$ 13,284	\$ 26,176

Upon finalization of the acquisition accounting for HBMS, the fair value of supplier contracts and licensing agreements, prior to the application of negative goodwill, in the amount of \$2,691 was recognized. As part of the recognition of income tax assets during 2005, intangible assets have been reduced to nil. For 2004, intangible assets include zinc process licensing agreements, which were amortized over the estimated life of the zinc plant facility, being 13 years.

Environmental deposits include various amounts with government agencies in the Province of Nova Scotia, Canada and in New York State, United States, in connection with the acquisitions of the Gay's River and Balmat mine properties.

7. Current portion of other liabilities

	2005	2004
Current portion of long-term debt (note 8)	\$ 4,000	\$ 2,000
Current portion of pension obligation (note 9)	18,355	12,650
Current portion of other employee future benefits (note 10)	2,031	2,012
Current portion of obligations under capital leases (note 12)	3,825	3,338
Current portion of fair value of derivatives	-	178
Current portion of non-current liabilities	-	417
	\$ 28,211	\$ 20,595

8. Long-term debt

	2005	2004
Senior Secured Notes (a)	\$ 181,428	\$ 210,350
Province of Manitoba (b)	14,065	15,179
Convertible debentures (c)	-	-
	195,493	225,529
Less current portion of long-term debt	4,000	2,000
	\$ 191,493	\$ 223,529

(a) Senior Secured Notes

On December 21, 2004, a subsidiary of the Company issued U.S. \$175,000 Senior Secured Notes ("Notes") bearing interest at 9.625% per annum with interest payable semi-annually in arrears on January 15 and July 15 of each year, commencing on July 15, 2005. The Notes will mature on January 15, 2012. Subsequent to the issuance of the Notes, the subsidiary which issued the Notes amalgamated with HBMS. Financing costs amounting to \$9,950 were incurred in connection with the issuance of the Notes and are amortized into income on a straight-line basis over the term of the Notes, unless redeemed early.

HBMS may redeem up to 35% of the aggregate principal amount of the Notes at any time prior to January 15, 2008 with the net proceeds from certain equity offerings at a price equal to 109.625% of the principal amount of the Notes plus accrued and unpaid interest. After January 15, 2009, HBMS may redeem some or all of the Notes at the redemption prices of 104.813% in 2009, 102.406% in 2010 and 100% thereafter. In addition, if HBMS undergoes a change of control or if it sells certain of its assets, it may be required to offer to purchase the Notes at specified redemption prices. HBMS also has the right to redeem all of the Notes if at any time Canadian law changes to require it to withhold taxes from payments on the Notes. The Company is not precluded from repurchasing the Notes in the open market at market prices. Before the end of the year, the Company repurchased US\$19,000 of the Notes in the open market reducing the outstanding notional amount of the Notes to US\$156,000. The Company paid a premium for this purchase in the amount of US\$1,284 that was recorded as an expense. In addition, deferred financing costs in the amount of \$927 related to this purchase were also expensed.

The Notes are HBMS's senior obligations and will rank equally in right of payment with all of its existing and future senior indebtedness and rank senior to all of its existing and future subordinated indebtedness. The Notes are guaranteed on a senior basis by the Company's subsidiary, Hudson Bay Exploration and Development Company Limited, and will be guaranteed by any future domestic restricted subsidiaries. Subsequent to December 31, 2004, the Notes are also guaranteed by the Company. The Company's guarantee of the Notes will terminate on the date upon which it owns less than a majority of the voting shares of HBMS. The Notes and the subsidiary guarantee are secured by first priority liens on HBMS's real property, mineral claims and leases in the Provinces of Manitoba and Saskatchewan and second priority liens on HBMS's and the subsidiary guarantor's accounts receivable and inventories, which may be used to secure, on a first-priority basis, HBMS's obligations under any future credit facility.

The Company's interest expense on the Notes and weighted average interest rate is as follows:

	2005	2004
Interest expense	\$ 20,237	\$ 608
Weighted average interest rate	9.625%	9.625%

(b) Loan payable

The interest-free loan from the Province of Manitoba is secured by an irrevocable standby letter of credit issued by a Canadian chartered bank and is due in instalments of \$4 million on June 14, 2006 and 2007 and \$7.5 million on June 14, 2008. As at December 21, the fair value of the loan was determined using the net present value of the interest-free component of the loan, assuming a discount rate of 6%. The discounted loan amount is being accreted to the principal amount through annual accretions with an offsetting charge to interest expense.

(c) Convertible debentures

In December 2003, the Company completed a private placement of \$2,000 principal amount of secured convertible debentures. During 2004, the proceeds were received, and an additional \$600 of secured convertible debentures were issued with costs of \$216 recorded as deferred financing costs. The debentures were repaid in the amount of \$2,860 in December 2004 with the difference from book value of \$761 recorded as debt settlement expense. The equity component of the debentures was \$1,250 and the difference between this and the fair value of the holder conversion option, or \$110, was credited to retained earnings and the carrying value of the equity component has been eliminated. The unamortized amount of deferred financing costs relating to the debentures of \$108 was written off as a component of financing costs for the year.

9. Pension obligation

Prior to December 21, 2004, the Company did not sponsor any pension plans. HBMS maintains several non-contributory and contributory defined benefit pension plans for its employees.

The Company uses a December 31 measurement date for all of its plans. For the Company's significant plans, the most recent actuarial valuations filed for funding purposes were performed as at December 31, 2004. For these plans, the next actuarial valuation required for funding purposes will be performed as at December 31, 2005. Any actuarial gains or losses over 10 per cent of the greater of the obligation and the fair value of assets are amortized over the expected service life of the plan population.

Notes to consolidated financial statements

Information about the Company's non-contributory and contributory defined benefit plan is as follows:

	2005	2004
Obligations and funded status		
Change in pension obligation:		
Obligation, as at January 1	\$ 217,812	\$ -
Obligation, at December 21, 2004	-	217,432
Service cost	7,426	607
Interest cost	12,754	345
Employee contributions	156	-
Actuarial loss	15,823	-
Flex account balance at end of year	1,544	-
Benefits paid	(10,743)	(572)
Obligation, at December 31	244,772	217,812
Change in pension plan assets:		
Fair value of plan assets, at January 1	147,725	-
Fair value of plan assets, at December 21, 2004	-	146,942
Actual return on plan assets	20,712	283
Employer contributions	14,634	1,072
Employee contributions	156	-
Flex account balance at end of year	1,544	-
Benefits paid	(10,743)	(572)
Fair value of plan assets, at December 31	174,028	147,725
Unfunded status of plans at end of year	(70,744)	(70,087)
Unamortized net actuarial loss	5,646	-
Net amount recognized at December 31	\$ (65,098)	\$ (70,087)

As a result of the closure of the Ruttan mine, the Company plans to settle its obligations under the pension plans for the former employees of the Ruttan mine through the purchase of insurance contracts by which the insurer assumes all of the Company's risks and obligations under the plans.

Pension expense includes the following components:

	2005	2004
Service cost	\$ 7,426	\$ 607
Interest cost	12,754	345
Actual asset return (gain)	(20,712)	(283)
Actuarial loss	15,823	-
Costs arising in the period	15,291	669
Difference in costs arising and recognized in period:		
Return on plan assets	10,176	-
Actuarial loss	(15,823)	-
Other employee future benefit expense	9,644	669
Defined contribution pension	227	5
	\$ 9,871	\$ 674

(a) Additional information

The weighted average assumptions used in the determination of the accrued benefit expense and obligations were as follows:

	2005	2004
To determine the net benefit expense for the year:		
Discount rate	5.8%	5.8%
Expected return on plan assets	7.0%	7.0%
Rate of compensation increase	4.7%	4.7%
To determine the accrued benefit obligations at the end of the year:		
Discount rate	5.0%	5.8%
Rate of compensation increase	3.4%	4.7%

The Company's pension cost is materially affected by the discount rate used to measure obligations, the level of plan assets available to fund those obligations and the expected long-term rate of return on plan assets.

The Company reviews the assumptions used to measure pension costs (including the discount rate) on an annual basis. Economic and market conditions at the measurement date impact these assumptions from year to year.

Establishing the expected future rate of return on pension assets is a judgmental matter. The Company considers the following factors in determining this assumption:

- (i) Duration of pension plan liabilities; and
- (ii) Types of investment classes in which the plan assets are invested and the expected compound returns on those investment classes.

(b) Plan assets

The pension plan asset allocations, by asset category, are as follows:

	2005		2004	
	Weighted average	Target	Weighted average	Target
Equity securities	58%	57%	59%	57%
Debt securities	42%	43%	41%	43%
	100%	100%	100%	100%

The Company's primary quantitative investment objective is to maximize the long-term real rate of return, subject to an acceptable degree of investment risk, and the preservation of principal. Risk tolerance is established through consideration of several factors, including past performance, current market conditions and the funded status of the plan.

With the exception of fixed income investments and non-North American equities, the plan assets are actively managed by investment managers, with the goal of attaining returns that are in excess of that which could be realized with passively managed investments. Although the actual composition of the invested funds will vary from the prescribed investment mix, the investment managers have a responsibility to bring items back to the appropriate mix.

(c) Expected cash flows

The employer contributions (or benefit payments in respect of the supplementary plan) for the year ending December 31, 2006 are expected to be \$18,400.

Notes to consolidated financial statements

The expected benefit payments for fiscal year ending:

	Benefits Paid
2006	\$ 9,000
2007	9,200
2008	9,600
2009	10,300
2010	11,200
2011 – 2015	65,000

10. Other employee future benefits

Prior to December 21, 2004, the Company did not sponsor any post-employment benefit plans. HBMS sponsors several such plans and uses a December 31 measurement date. Information about the Company's post-retirement and other post-employment benefits is as follows:

	2005	2004
Obligations and funded status		
Change in other employee future benefits:		
Obligation, at January 1	\$ 59,941	\$ -
Obligation, at December 21, 2004	-	59,870
Service cost	1,593	22
Interest cost	3,506	104
Actuarial losses	11,500	-
Benefits paid	(1,759)	(55)
Obligation, at December 31	\$ 74,781	\$ 59,941
Change in plan assets:		
Fair value of plan, at January 1	\$ -	\$ -
Fair value of plan, at December 21, 2004	-	-
Employer contributions	1,759	55
Benefits paid	(1,759)	(55)
Fair value of plan assets at December 31	\$ -	\$ -
Unfunded status of plans at end of year	\$ (74,781)	\$ (59,941)
Unrecognized net actuarial loss	11,500	-
Net amount recognized at December 31	\$ (63,281)	\$ (59,941)

Other employee future benefits expense includes the following components:

	2005	2004
Service cost	\$ 1,593	\$ 22
Interest cost	3,506	104
Actuarial loss	11,500	-
Costs arising in the period	16,599	126
Unrecognized actuarial loss	(11,500)	-
Other employee future benefits expense	\$ 5,099	\$ 126

(a) Additional information

The weighted average assumptions used in the determination of other employee future benefits expense and obligations are as follows:

	2005	2004
To determine net benefit expense for the year:		
Discount rate	6.0%	6.0%
Weighted average health care trend rate	9.2%	9.2%

	2005	2004
To determine benefit obligation at end of year:		
Discount rate	5.1%	6.0%
Weighted average health care trend rate	8.7%	9.2%

The health care cost trend rate used in measuring other employee future benefits was assumed to begin at 8.7% in 2006, gradually declining to 4.6% by 2015 and remaining at those levels thereafter.

If the health care cost trend rate was increased by one percentage point, the accumulated post-retirement benefit obligation and the aggregate service and interest cost would have increased as follows:

	2005	2004
Accumulated post-retirement benefit obligation	\$ 15,761	\$ 12,558
Aggregate of service and interest cost	1,267	38

If the health care cost trend rate was decreased by one percentage point, the accumulated post-retirement benefit obligation and the aggregate service and interest cost would have decreased as follows:

	2005	2004
Accumulated post-retirement benefit obligation	\$ 12,129	\$ 9,749
Aggregate of service and interest cost	961	28

Any actuarial gains or losses over 10 per cent of the obligation are amortized over the expected service life of the plan population.

(b) Expected cash flow

Expected benefit payments for each of the next five years through 2010 and the aggregate of the five years thereafter are as follows:

	Benefits Paid
2006	\$ 2,000
2007	2,200
2008	2,300
2009	2,500
2010	2,800
2011 – 2015	18,300

11. Asset retirement obligations

The Company has completed an independent review, to the feasibility level of accuracy, of its asset retirement obligations assumed through its acquisition of HBMS as described in note 3.

Notes to consolidated financial statements

The Company's asset retirement obligations relate to the final reclamation and closure of currently operating mines, mines under care and maintenance, closed and abandoned properties.

	2005	2004
Balance, beginning of year	\$ 27,120	\$ 769
Obligations settled during the year	(463)	-
Liability assumed through acquisition of HBMS	(50)	26,213
Accretion expense	2,612	138
Balance, end of year	\$ 29,219	\$ 27,120

Total undiscounted future cash flows required to settle the decommissioning and restoration asset retirement obligations are estimated to be \$55.1 million (2004 - \$53.9 million). A credit adjusted risk-free rate of 9.625% has been utilized to determine the majority of the obligation recorded in the consolidated balance sheet. Management anticipates that such obligations will substantially be settled at or near the closure of the mining and processing facilities. The current mine plan based on known reserves and resources extends to 2018.

In view of the uncertainties concerning environmental remediation, the ultimate cost of asset retirement obligations could differ materially from the estimated amounts provided. The estimate of the total liability for asset retirement obligation costs is subject to change based on amendments to laws and regulations and as new information concerning the Company's operations becomes available. Future changes, if any, to the estimated total liability as a result of amended requirements, laws, regulations and operating assumptions may be significant and would be recognized prospectively as a change in accounting estimate, when applicable. Environmental laws and regulations are continually evolving in all regions in which the Company operates. The Company is not able to determine the impact, if any, of environmental laws and regulations that may be enacted in the future on its results of operations or financial position due to the uncertainty surrounding the ultimate form that such future laws and regulations may take.

12. Obligations under capital leases

The Company has entered into capital lease obligations for equipment.

	2005	2004
Lease obligations	\$ 12,836	\$ 15,057
Less current portion of obligations	3,825	3,338
	\$ 9,011	\$ 11,719

The following represents the minimum lease payments for equipment used in operations for the next five years:

	2005
2006	\$ 4,436
2007	4,428
2008	3,554
2009	1,523
2010	102
	14,043
Less imputed interest	1,207
	\$ 12,836

The capital lease average interest rate was 5.2% and is fixed for the term of the leases that expire 2007 to 2010.

13. Income Taxes

(a) Income tax recovery

Income tax expense (recovery) differs from the amount that would be computed by applying the statutory income tax rates to income before income taxes. A reconciliation of income taxes calculated at the statutory rates to the actual tax provision is as follows:

	2005	2004
Statutory tax rate	42%	38%
Tax expense (benefit) at statutory rate	\$ 31,557	\$ (3,921)
Effect of:		
Resource and depletion allowance, net of resource tax recovery	(20,569)	(18)
Temporary differences not recognized	28,946	405
Tax losses (benefit realized) not recognized	(40,674)	3,205
Other permanent differences	1,798	329
Recognition of prior years' temporary differences	(11,858)	(473)
Income tax recovery	\$ (10,800)	\$ (473)
Income tax provision applicable to:		
Current taxes	678	(473)
Future taxes	(11,478)	-
Income tax recovery	\$ (10,800)	\$ (473)

(b) Tax effect of temporary differences

The tax effects of temporary differences that give rise to significant portions of the future tax assets or future tax liabilities at December 31, 2005 and 2004 are presented below:

	2005	2004
Future income tax assets:		
Property, plant and equipment	\$ 218,394	\$ 265,675
Pension obligation	23,839	26,016
Other employee future benefits	23,238	22,405
Asset retirement obligations	10,689	9,184
Non-capital losses (see (c) below)	73,560	58,252
Share issue costs	3,140	3,744
Other	440	-
	353,300	385,276
Less valuation allowance	327,100	372,376
Net future tax asset	\$ 26,200	\$ 12,900
Future income tax liability:		
Derivatives and other timing differences	\$ (1,666)	\$ (1,290)

The valuation allowance represents management's best estimate of the allowance necessary to reflect the future income tax assets at an amount that the company considers is more likely than not to be realized. Since HBMS had many years of ever increasing timing differences with 2005 the first year of a reduction, the tax asset has been based on only one future year of earnings. This is deemed appropriate due to uncertainties of future metal prices, exchange rates and the magnitude of prior losses, but will continue to be reviewed as circumstances change.

Notes to consolidated financial statements

(c) Non-capital losses

At December 31, 2005, the Company has cumulative non-capital losses of \$189,678 in Canada and net operating losses of \$11,998 in the U.S.

The non-capital losses expire as follows:

2006	\$ 506
2007	355
2008	350
2009	8,691
2010	50,194
2013	61,252
2014	48,267
2015	12,003
2016	8,060
2024	1,042
2025	3,492
2026	7,464

14. Share capital

(a) Common shares

Authorized

Unlimited common shares

Issued

	2005		2004	
	Common shares	Amount	Common shares	Amount
Balance, beginning of year	77,450,628	\$ 120,138	5,661,592	\$ 21,379
Issued for debt	-	-	5,334	40
Issued on private placements, net	-	-	2,382,466	7,817
Issued pursuant to public offering	-	-	69,694,778	156,813
Cancellation of repurchase shares	-	-	(340,000)	(336)
Exercise of warrants	4,047,032	12,941	28,030	160
Exercise of options	310,340	1,130	19,334	64
Issued flow through shares	2,999,452	10,000	-	-
Value attributed to warrants issued	-	-	-	(29,465)
Tax effect of flow-through shares	-	-	-	(397)
Share issue costs	-	(598)	-	(13,958)
Elimination of fractional shares	-	-	(906)	-
Stated capital reduction	-	-	-	(21,979)
Balance, end of year	84,807,452	\$ 143,611	77,450,628	\$ 120,138

On June 22, 2005, the Company completed a private placement of 2,193,000 flow-through common shares at a price of \$3.42 per share for aggregate gross proceeds of approximately \$7,500. Commission and fees related to the offering was paid to the underwriters resulting in net proceeds of \$7,078. The gross proceeds are being used to incur Canadian exploration expenses that will be renounced in favour of the holders for the 2006 taxation year.

On February 22, 2005, the Company completed a private placement of 806,452 flow-through common shares at a price of \$3.10 per share for aggregate gross proceeds of approximately \$2,500. Commission related to the offering was paid to the underwriters resulting in net proceeds of \$2,323. The proceeds are being used to incur Canadian exploration expenses that will be renounced in favour of the holders for the 2006 taxation year.

On December 21, 2004, the Company completed an offering of 63,917,000 subscription receipts at a price of \$2.25 per subscription receipt pursuant to a final prospectus dated December 14, 2004, for gross proceeds of \$143,813. Net proceeds of the issuance were approximately \$133,005. Each subscription receipt entitled the holder to receive one common share and 15 common share purchase warrants. Every 30 common share purchase warrants entitles the holder thereof to acquire one common share for a period of 5 years from the date of issuance, exercisable at a price of \$3.15 per share. The gross proceeds of \$2.25 per subscription receipt was allocated on the basis of \$2.025 as to each common share and \$0.225 as to each one-half of one share purchase warrant.

In connection with the offering, the agents for the offering were issued broker warrants to acquire 3,835,020 common shares at a price equal to 115% of the offering price of the subscription receipts, or \$2.589 per warrant, for a period of 24 months to December 21, 2006.

Broker warrants issued in connection with the Company's offering of subscription receipts on December 21, 2004 were exercised during the year ended December 31, 2005 aggregating the following amounts: 89,028,543 warrants to purchase 2,967,618 common shares for proceeds of \$7,679.

Under the terms of the agreement for the acquisition of HBMS from Anglo American on December 21, 2004, the Company issued to Anglo American 5,777,778 common shares and 86,666,667 warrants for consideration of \$13,000.

On December 21, 2004, the Company completed a 30 for 1 common share consolidation which has been retroactively reflected as if the share consolidation had occurred on January 1, 2002 and is reflected in the following disclosures. The warrants outstanding at the time of the share consolidation were not consolidated.

(i) In addition, the Company completed the following private placements during 2004:

(a) In September 2004, 1,105,666 units at a price of \$1.50 per unit for gross proceeds of \$1,726. Each unit consists of one common share and 15 common share purchase warrants. Each 30 common share purchase warrants entitles the holder thereof to acquire one common share for a period of two years from the date of issuance, exercisable at a price of \$1.80 per share.

In addition, the broker was issued 3,452,000 broker warrants, with each 30 broker warrants exercisable for one common share at a price of \$1.50 per share and a one-half of a share purchase warrant for a period of two years from the closing date and paid a commission of \$117. Each whole share purchase warrant entitles the holder to acquire a share at an exercise price of \$0.06 per share for a period of two years following the date of issuance. An over-allotment option was provided to the broker to purchase up to 15% of the number of broker units issued at closing at the issue price of \$2.70 at any time prior to November 30, 2004. On November 30, 2004, the broker exercised its over-allotment option and purchased an additional 172,600 units at a price of \$2.70 per unit. Upon exercise of the over-allotment option, the broker was issued an additional 517,800 broker warrants, with each 30 broker warrants exercisable at a price of \$2.70 per unit. Each broker unit is comprised of one common share and 15 broker common share purchase warrants. Every 30 broker common share purchase warrants is exercisable for one common share at an exercise price of \$3.60 and one-half of a share purchase warrant for a period of two years from the date of issue. Each whole share purchase warrant entitles the holder to acquire a share at an exercise price of \$0.12 per share for a period of two years following the date of issuance.

The former Chairman and Chief Executive Officer of the Company and the former Corporate Secretary purchased 333,333 and 6,667 of these units, respectively. Subsequent to September 30, 2004, the Company and these officers agreed to unwind these transactions, so that the securities comprising the units have been returned to the Company and the Company has returned the purchase price paid for the units.

(b) In June 2004, 1,036,920 units at a price of \$5.40 per unit for gross proceeds of \$5,599. Each unit consists of one common share and 15 common share purchase warrants. Every 30 warrants entitled the holder thereof to acquire one common share for a period of two years from the date of issuance, exercisable at a price of \$6.00 per share. Certain former officers and directors of the Company purchased an aggregate of 795,986 of these units.

Notes to consolidated financial statements

(b) Warrants

	Number	Amount
Warrants outstanding, December 31, 2003	74,894,424	\$ 4,433
Issued on private placements	40,140,997	2,380
Issued pursuant to public offering	1,045,421,667	27,181
Issued to agents for public offering	115,050,600	2,078
Warrants repurchased	(5,100,000)	(173)
Exercised	(840,909)	(43)
Cancelled	(88,456)	(6)
Warrants outstanding, December 31, 2004	1,269,478,323	\$ 35,850
Issued on private placements	1,727,258	44
Exercised	(121,411,064)	(2,590)
Cancelled	(73,712,059)	(4,373)
Warrants outstanding, December 31, 2005	1,076,082,458	\$ 28,931

Warrants outstanding to acquire common shares (30 warrants required to acquire one common share) of the Company at December 31, 2005 are as follows:

Warrants outstanding	Exercise price	Expiry date
768,400	\$ 0.12	January 13, 2006
15,553,797	0.20	March 31, 2006
2,566,785	0.06	September 28, 2006
263,330	0.05	September 28, 2006
2,721,923	0.12	November 30, 2006
251,955	0.09	November 30, 2006
26,022,057	0.086	December 21, 2006
1,027,934,211	0.105	December 21, 2009
1,076,082,458		

For purposes of valuation, the fair value of warrants issued prior to December 21, 2004 was estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions: dividend yield of 0%; expected volatility of 100% for the year ended December 31, 2003 and 125% for the year ended December 31, 2004; risk-free interest rate of 4.5%; and an expected life of two years.

The fair value of the listed warrants and the broker warrants issued on December 21, 2004 was estimated on the date of issuance using the Black-Scholes option model with the following assumptions: dividend yield of 0%; expected volatility of 40%; risk-free interest rate of 4.25%; and an expected life of five and two years, respectively.

(c) Stock option plan

Under the Company's stock option plan (the "Plan") approved in June 2005, the Company may grant options up to 10% of the issued and outstanding common shares of the Company to employees, officers, and directors of the Company for a maximum term of ten years. Of the common shares covered by the stock option plan, the first 33 1/3% are exercisable immediately, the next 33 1/3% are exercisable after one year, and the last 33 1/3% exercisable after two years. Shares in respect of which options are not exercised as well as shares in respect of which options are exercised, shall become available for the grant of subsequent options. Except in specified circumstances, options are not assignable and terminate upon the optionee ceasing to be employed by or associated with the Company. The terms of the Plan further provide that the price at which shares may be issued under the Plan cannot be less than the market price of the shares when the relevant options are granted. Certain restrictions apply on the issuance of options pursuant to the Plan.

The fair value of the options granted during 2005 has been estimated at the date of grant using a Black-Scholes option pricing model with the following assumptions: risk-free interest rate of 3.2%; dividend yield of 0%; volatility factor of the expected market price of the Company's common stock of 42%; and a weighted average expected life of these options of 4 years.

	2005		2004	
	Number of shares	Weighted average exercise price	Number of shares	Weighted average exercise price
Balance, beginning of year	663,167	\$ 3.60	550,000	\$ 5.08
Cancelled	(718,999)	3.71	(334,167)	4.80
Granted	3,865,000	2.63	466,667	3.60
Exercised	(310,340)	2.61	(19,333)	3.30
Outstanding, end of year	3,498,828	\$ 2.66	663,167	\$ 3.60

On July 5, 2004, the Company repriced an aggregate of 85,833 previously granted options to \$3.00. The options were previously exercisable at prices ranging from \$3.30 to \$7.20 per share with expiry dates from June 13, 2006 to November 27, 2008.

The following table summarizes the options outstanding at December 31, 2005:

Number of options outstanding	Exercise price	Weighted average remaining contractual life (years)	Number of options exercisable	Weighted average remaining contractual life (years)
3,229,661	\$ 2.59	9.4	916,205	9.4
27,500	3.00	2.9	27,500	2.9
225,000	3.35	9.4	75,000	9.4
5,000	4.50	0.4	5,000	0.4
11,667	7.50	1.7	11,667	1.7
3,498,828	\$ 2.66		1,035,372	

The fair value of the options granted during 2004 has been estimated at the date of grant using a Black-Scholes option pricing model with the following assumptions: risk-free interest rate of 4.50%; dividend yield of 0%; volatility factor of the expected market price of the Company's common stock of 100% for the year ended December 31, 2003 and 125% for the year ended December 31, 2004; and a weighted average expected life of these options of 4.0 years.

Stock-based compensation amounted to \$2,674 and \$1,193 for the years ended December 31, 2005 and 2004, respectively and is included in general and administrative expense.

(d) Earnings (loss) per share

For 2004, the conversion of stock options and warrants in the calculation of fully diluted resulted in the same earnings per share as basic earnings per share.

(e) Stated capital reduction

On December 8, 2004, a special resolution was passed by the Company's shareholders to eliminate the deficit of the Company at June 30, 2004 by reducing the stated capital by \$21,979. This deficit was accumulated in connection with the Company's historical operations and does not relate to the Company's current business mandate.

15. Contingencies

The Company and its subsidiaries are involved in various claims and litigation arising in the ordinary course and conduct of their business. Since the outcome is uncertain, no amount has been recorded in these consolidated financial statements.

The significant claims and litigation matters are as follows:

- (a) Statements of claim were filed against Saskatchewan Power Corporation ("SaskPower"), the Company and Churchill River Power Company Limited ("CRP") on February 10, 1995, seeking an aggregate of \$1 billion in compensatory damages and in excess of \$100 million in punitive damages. These claims were filed in connection with the use and operation of the Whitesand Dam and the Island Falls Hydro Electric Station in Saskatchewan which were transferred by CRP, formerly a wholly owned subsidiary of the Company, to SaskPower in 1981. Based on the current knowledge of management, in management's opinion, the ultimate resolution of the claims will not be material to the consolidated financial position.
- (b) On December 20, 2004, a Statement of Claim was filed by the Peter Ballantyne Cree Nation against SaskPower, The Government of Canada and The Province of Saskatchewan. The action claims damages alleged as a result of the operation and use of the Whitesand Dam and Island Falls Hydro-Electric Station. HBMS and CRP have not been named as parties in the action. It has recently come to our attention that CRP, a former subsidiary of HBMS, which was dissolved, has been revived by SaskPower for the purpose of taking legal action against CRP for alleged breaches by CRP of its obligations under a certain Purchase and Sale Agreement made in 1981. At present, the resolution of any claim that will be advanced against CRP or HBMS is not reasonably determinable.
- (c) In May 2004, a number of plaintiffs initiated an action, in the State of North Carolina, against Zochem, Consider Metal Marketing Inc. ("CMM") and a number of other defendants seeking damages in an unspecified amount and alleging that they had been injured as a result of an explosion that occurred at a pharmaceutical plant. The plaintiffs have alleged that Zochem and/or CMM designed, manufactured, sold and supplied chemicals used in the manufacture of a rubber compound that were dangerous, defective and susceptible to causing explosions. HBMS has retained legal counsel in North Carolina and cannot currently assess its potential liability in relation to this claim.
- (d) On April 21, 2004, Novawest Resources Inc. issued a claim in the British Columbia Supreme Court seeking unspecified damages against certain defendants, including Hudson Bay Exploration and Development Company Limited, a subsidiary of the Company. The claim alleges a breach of confidence and claims damages as a result of such breach. The defendants have retained counsel to defend the claim and liability is denied. The likelihood of success of the claim cannot be determined at this time. Based on the current knowledge of management, in management's opinion, the ultimate resolution of the claim will not be material to the consolidated financial position.

16. Risk management using financial instruments

(a) Foreign currency risk management

The Company uses forward exchange or currency collar contracts to limit the effects of movements in exchange rates on foreign currency-denominated assets and liabilities and future anticipated transactions. Hedge accounting is applied to the following contracts.

In 2004, the Company paid U.S. \$1.2 million to purchase an option giving it the right, but not the obligation, to pay an additional U.S. \$2.9 million to purchase U.S. dollar put options. The put options secure the right, but not the obligation, to sell U.S. \$4.375 million per quarter at \$1.20482 starting in April 2005 and continuing to January 2009. The fair value at December 31, 2005 is estimated to be US\$3.5 million; the fair value at December 31, 2004 approximates its carrying value as a result of the December 21, 2004 acquisition.

(b) Credit risk

The Company provides credit to its customers in the normal course of its operations. It carries out, on a continuing basis, credit checks on its customers and maintains provisions for contingent credit losses. Substantially all of the Company's accounts receivable are with CMM, a joint venture.

The Company is exposed to credit risk in the event of non-performance by counterparties in connection with its derivative contracts. The Company does not obtain collateral or other security to support financial instruments subject to credit risk but mitigates this risk by dealing only with financially sound counterparties and, accordingly, does not anticipate loss for non-performance.

(c) Commodity price risk management

From time to time, the Company maintains price protection programs and conducts commodity price risk management through the use of forward sales contracts, spot deferred contracts, option contracts and commodity collar contracts.

Through its joint venture interest in CMM, the Company manages the risk associated with forward physical sales where it receives a fixed price regarding zinc and zinc oxide and, accordingly, enters into forward zinc purchase contracts to convert the fixed price to a floating price arrangement. At December 31, 2005, the joint venture had outstanding forward contracts to purchase 11,322 tonnes of zinc at prices ranging from U.S. \$834 to U.S. \$1879 per tonne with settlement dates in the next three years. The fair value at December 31, 2005 and 2004 approximates its carrying value.

17. Fair value of financial instruments

The carrying value for cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, current portion of long-term debt and current portion of obligations under capital lease approximate their fair value due to their short-term nature.

The fair value of the senior secured debt using discounted cash flows at current market rates is approximately \$202,940 (2004 – \$223,529).

Derivative financial instruments have been valued at current fair values using quoted market prices or accepted valuation methodologies.

18. Related party information

- (a) During the year ended December 31, 2004, the Company paid \$2,317 to two law firms which were associated with two individuals who were former directors of the Company at the time. The payments in 2004 were substantially in respect of services in connection with the acquisition of HBMS and the related financings.
- (b) In June 2004, certain individuals who were former officers and directors of the Company at the time purchased an aggregate of 795,986 units in connection with a private placement completed by the Company (note 14a(i)(b)).
- (c) In September 2004, the former Chairman of the Company acquired 333,333 units and the then corporate secretary acquired 6,667 units in connection with a private placement completed by the Company (note 14a(i)(a)). In December 2004, these transactions were reversed.

19. Investment in joint ventures

Considar Metal Marketing SA ("CMMSA"), an entity incorporated under the laws of the Grand Duchy of Luxembourg, is a joint venture in which the Company holds a 50% interest. The joint venture, together with its wholly owned subsidiary, CMM, carries on the business of providing metal marketing to customers in various metal-related industries.

The following is a summary of the Company's 50% pro rata share of the book value of the assets, liabilities, revenue and expenses of the CMMSA joint venture. Up to the end of 2005, substantially all of the Company's sales were transacted with the joint venture. Effective January 1, 2006, the Company has changed its sales agreement with CMM to an agency agreement for copper and precious metal products, and plans to make a similar change for the zinc and zinc oxide products during the first half of 2006.

Such information is presented prior to intercompany eliminations.

Notes to consolidated financial statements

	2005	2004
Assets		
Current assets	\$ 33,783	\$ 52,535
Unrealized fair value derivative	269	772
Property, plant and equipment	93	112
Liabilities		
Current liabilities	\$ 29,177	\$ 49,264
Future income taxes payable	1,665	1,290
Sales		
	\$ 352,528	\$ 6,898
Costs and expenses:		
Operating, general and administrative	356,867	7,053
Depreciation and amortization	31	2
Gain on derivative instruments	(5,319)	(78)
	351,579	6,977
Earnings (loss) before income taxes	\$ 949	\$ (79)
Cash flows:		
Operating activities	\$ (1,207)	\$ 106
Investing activities	(12)	(5)

20. Commitments

(a) Operating lease commitments

The Company has entered into various lease commitments for facilities and equipment. The leases expire in periods ranging from one to four years. The aggregate remaining minimum annual lease payments required for the next four years are as follows:

2006	\$ 2,413
2007	609
2008	241
2009	106

Through its joint venture interest in CMMSA, as at December 31, 2005, the Company has various lease commitments for facilities and equipment which expire in periods ranging from one to eight years. The aggregate remaining minimum annual lease payments, representing 100% of CMMSA's commitment, required for the next five years are as follows:

2006	\$ 204
2007	218
2008	216
2009	218
2010 and thereafter	285

The Company has recorded operating lease expense of \$3,746, including \$106 for the 50% share of the CMM leases.

(b) Buy-sell commitments

The Company has a commitment to purchase copper concentrate based on a schedule of payments rather than actual physical delivery. The contract requires delivery of 72,000 dry metric tonnes annually from 2006 to 2008.

The Company also has a long-term agreement for the purchase of 10% of another mine's concentrate, or approximately 13,000 dry metric tonnes in 2006, and 20% of annual production or approximately 26,000 dry metric tonnes each year thereafter. The term of this agreement is from 2006 to 2015 and is subject to certain termination rights effective after December 31, 2008.

Payment for both the above-mentioned purchased concentrates is based on the market price of contained metal during a quotational period following delivery of the concentrate, less a fixed treatment and refining credit. If the Company cannot process the deemed tonnage in a timely manner, management believes the Company will be able to negotiate alternate arrangements for the sale or diversion of the tonnage.

The Company relies partly on processing purchased concentrates to achieve a portion of profits. The continued availability of such concentrates at economic terms beyond the expiry of current existing contracts cannot be determined at this time.

(c) Other commitments and agreements

- (i) On January 1, 2006 the Company entered into an agency agreement with CMM for the Company's copper and precious metals products. As a result of this agreement, the Company retains title to the copper and precious metals until they are ultimately sold to the customers. In order to facilitate this agreement, the Company, in effect, on December 31, 2005 acquired the inventory of CMM. This purchase resulted in a reversal of the originating sales transactions associated with these products. Therefore the net result was the removal of any associated profit margin and inclusion of the associated inventories in the financial statements of the Company.
- (ii) On the majority of the Callinan/777 mine, the Company is subject to a royalty payment of \$0.25 per ton of ore milled and a net profits interest of 6-2/3% of the net proceeds of production if aggregate cash flow for the year and cumulative cashflow are positive. To date, the cumulative cash flow has been negative.
- (iii) HBMS has a profit-sharing plan, whereby 10% of the Company's after-tax earnings (excluding provisions or recoveries for future income tax) calculated in accordance with Canadian generally accepted accounting principles for any given fiscal year will be distributed to all employees in the Flin Flon/Snow Lake operations, with the exception of executive officers and key management personnel. This expense has been accrued in these financial statements.
- (iv) The Company entered into a security agreement dated March 31, 1999 in favour of the Province of Saskatchewan in respect of its reclamation undertakings in Saskatchewan. As security for the implementation of decommissioning plans in respect of its undertakings in Saskatchewan, the Company has granted to the Province of Saskatchewan a first priority security interest in its mining equipment, buildings and fixtures and a first charge on all proceeds derived from any dealings with such mining equipment, buildings and fixtures. In addition, the Company has a security agreement dated May 7, 2004 in favour of the Province of Manitoba in respect of its reclamation undertakings in Manitoba. As security for the implementation of a decommissioning plan in respect of its undertakings in Manitoba, the Company has granted to the Province of Manitoba a first priority security interest in its mining equipment, buildings and fixtures owned by the Company and located on the lands and a first charge on all proceeds derived from any dealings with such mining equipment, buildings and fixtures. The security interests granted to the Provinces of Saskatchewan and Manitoba rank *pari passu*.

The Company has completed a study of reclamation costs (see note 11). The Company believes the existing security provided is adequate and sufficient. However, the Company has provided additional security to the provinces in the form of a letter of credit in the amount of \$13 million. For 2005, the reports have been submitted to the provinces, and upon completion of their review the appropriate security may be reassessed.

- (v) In the normal course of operations, the Company provides indemnifications that are often standard contractual terms to counterparties in transactions, such as purchase and sale contracts, service agreements and leasing transactions. These indemnification agreements may require the Company to compensate the counterparties for costs incurred as a result of various events, including environmental liabilities, changes in (or in the interpretation of) laws and regulations, or as a result of litigation claims or statutory sanctions that may be suffered by the counterparty as a consequence of the transaction. The terms of these indemnification agreements will vary based upon the contract, the nature of which prevents the Company from making a reasonable estimate of the maximum potential amount that could be required to pay to counterparties. Historically, the Company has not made any significant payments under such indemnifications. Management estimates that there are no significant liabilities with respect to these indemnification guarantees.
- (vi) The Company has outstanding letters of credit in the amount of \$35.2 million (including the above-mentioned amount for environmental reclamation).

Notes to consolidated financial statements

- (vii) In 2003, the Company established a wholly-owned subsidiary, St. Lawrence Zinc Company LLC ("St. Lawrence"). St. Lawrence was incorporated in the State of New York for the purposes of acquiring the Balmat zinc mine ("Balmat"). On September 24, 2003, St. Lawrence purchased the Balmat zinc mine and related assets located in upper New York State. Total consideration paid consisted of a cash deposit of U.S. \$1 million required to assume an environmental bond. In addition, contingent consideration, consisting of US \$20 million, was provided for in connection with the acquisition. The contingent consideration will be accounted for as additional purchase price as the contingencies are resolved and the amounts payable become fixed and/or determinable. The contingent consideration is payable out of 30% of the net future cash flow from operations after allowing for reasonable capital and exploration expenditures. A further \$5 million is payable if the monthly average special high grade settlement price of zinc, as quoted by The London Metal Exchange, averages \$0.70 or greater during any consecutive 24-month period after the closing date and prior to the fifth anniversary of the date on which the seller receives payment of the \$20 million.
- (viii) Pursuant to a Purchase Agreement dated February 2002, the Company acquired from Regal Mines Limited certain properties and other assets located in Nova Scotia, including lead and zinc mining and milling operations (collectively the "Gays River"). A component of the purchase price was a 2% of net smelter return payable based on operations. The Company has entered into a letter of intent to sell its holding in Scozinc Limited to Acadian Gold Corporation for \$7.5 million. The potential sales transaction with Acadian Gold Corporation of Halifax is subject to the satisfaction of certain conditions, including the provision of certain cash deposits, board approvals, the purchaser completing satisfactory financing agreements, due diligence, the entering into of a definitive sale and purchase agreement and receipt of all necessary regulatory approvals.

21. Change in non-cash working capital

	2005	2004
Accounts receivable	\$ 28,512	\$ (8,285)
Inventories	(16,314)	(11,843)
Accounts payable and accrued liabilities	2,181	17,565
Prepaid expenses	(129)	4,328
Interest payable	7,441	508
	\$ 21,691	\$ 2,273

22. Segmented information

The Company is an integrated base metals producer and operates in a single reportable operating segment.

The Company's revenue by significant product types:

	2005	2004
Revenues		
Copper ⁽¹⁾	\$ 351,756	\$ 8,277
Zinc	142,690	2,386
Zinc oxide	75,032	1,243
Gold	50,354	1,249
Silver	11,208	309
Other	20,988	(137)
	\$ 652,028	\$ 13,327

(1) Includes purchased copper of approximately \$144,000.

23. Reconciliation of Canadian and United States generally accepted accounting principles

The consolidated financial statements of the Company have been prepared in accordance with Canadian GAAP which differ in certain material respects from U.S. GAAP.

If U.S. GAAP were employed, the net earnings (loss) for the years would be adjusted as follows:

	2005	2004
Earnings (loss) for the year based on Canadian GAAP	\$ 85,218	\$ (9,920)
Impact on loss of U.S. GAAP adjustments:		
Depreciation and amortization (a)	(4,111)	(142)
Accretion of convertible debentures (b)	-	632
Debt settlement expense (b)	-	508
Earnings (loss) for the year under U.S. GAAP	\$ 81,107	\$ (8,922)
Basic and diluted income (loss) per share under U.S. GAAP	\$ 0.99	\$ (1.00)
Basic and diluted income (loss) per share under U.S. GAAP	\$ 0.67	\$ (1.00)
Weighted average number of common shares outstanding		
Basic	82,008,190	8,894,235
Diluted (note 14d)	121,116,832	8,894,235

The following summarizes the Company's adjusted consolidated balance sheet captions conforming to U.S. GAAP:

	2005	2004
Assets		
Financial derivative asset	\$ 4,085	\$ -
Property, plant and equipment (a)	373,954	358,520
Liabilities		
Pension obligation (e)	\$ 75,683	\$ 70,087
Future income tax liability (c)	3,217	1,290
Shareholders' equity		
Common shares (d)	\$ 164,039	\$ 142,117
Retained earnings (deficit) (d)	52,500	(28,607)
Currency translation adjustment	-	-
Accumulated other comprehensive income (loss)	(6,563)	(24)

(a) Depreciation and amortization

Under Canadian GAAP, amortization of mine development costs using the units of production method is calculated using historical costs plus estimated future underground development costs required to access proven and probable reserves. For U.S. GAAP purposes, amortization of mine development costs is calculated using historical capitalized costs incurred. Mine development costs which benefit the entire mine life are amortized over proven and probable reserves and the remainder of the mine development costs are amortized over the currently accessible proven and probable reserves to which these costs relate.

(b) Convertible debentures

Under Canadian GAAP, the Company accounts for the convertible debentures in accordance with their substance and, as such, they are presented in the consolidated financial statements in their liability and equity component parts. The debt component is accreted over the life of the debt by way of a charge to interest expense. Under U.S. GAAP, the entire face value of the convertible debentures is treated as debt and interest is based on the coupon rate of 12%.

Notes to consolidated financial statements

Under Canadian GAAP, the premium on redemption is calculated by reference to the carrying value of the debt component only and the residual equity component is credited to shareholders' equity. Under U.S. GAAP, the premium on redemption is calculated by reference to the entire face value of the debentures. These debentures were fully redeemed in 2004.

(c) Flow-through shares

Under U.S. GAAP, when flow-through shares are issued, the proceeds are allocated between the issue of shares and the sale of tax benefits. The allocation is made based on the difference between the quoted price of the existing shares and the amount that the investor pays for the shares. The shareholders' equity is reduced and a liability is recognized for this difference.

(d) Stated capital reduction

Canadian GAAP allows for the reduction of the stated capital of outstanding common shares with a corresponding offset to deficit. This reclassification, which the Company made in 2004, is not permitted by U.S. GAAP and would result in an increase in both share capital and deficit of \$21,979 at December 31, 2004.

(e) Pension

For defined benefit pension plans US GAAP reporting requires the recognition of a minimum of additional pension liability in the amount of the excess of the unfunded accumulated benefit obligation over the recorded pension obligation, with any unrecognized prior service costs as an offsetting intangible pension asset. This difference is recorded as a reduction to the accumulated other comprehensive income. At December 31, 2005 the minimum additional liability was \$10,585, thus reducing the accumulated other comprehensive income by \$10,585. At December 31, 2004 there was no minimum additional liability to recognize as pensions were fair valued upon the acquisition of HBMS.

Information for pension plans with an accumulated benefit obligation in excess of plan assets:

	2005	2004
Projected benefit obligation	\$ 242,773	\$ 216,167
Accumulated benefits obligation	233,875	203,415
Fair value of plan assets	171,992	146,014
Accumulated benefits obligations (all defined benefit plans)	\$ 235,790	\$ 204,964

(f) Comprehensive income

Comprehensive income is recognized and measured under U.S. GAAP pursuant to Statements of Financial Accounting Standards (SFAS) 130, Reporting Comprehensive Income. This standard defines comprehensive income as all changes in equity other than those resulting from investments by owners and distributions to owners. Comprehensive income is comprised of two components, net income and OCI. OCI refers to amounts that are recorded as an element of shareholders' equity but are excluded from net income because these transactions or events were attributed to changes from non-owner sources. The following is a summary of the Company's comprehensive income as measured under SFAS 130:

	2005	2004
Income (loss) under U.S. GAAP	\$ 81,107	\$ (8,922)
Other comprehensive income (loss):		
Change in cumulative translation adjustments	(39)	(24)
Additional minimum pension liability	(10,585)	-
Effective portion of foreign currency hedge	4,085	-
Comprehensive income (loss) based on U.S. GAAP	\$ 74,568	\$ (8,946)

(g) Joint ventures

U.S. GAAP requires investments in joint ventures to be accounted for under the equity method, while under Canadian GAAP, the accounts in joint ventures are proportionately consolidated. However, under rules promulgated by the Securities and Exchange Commission, a foreign registrant may, subject to the provision of additional information, continue to follow proportionate consolidation for the purposes of registration and other filings notwithstanding the departure from U.S. GAAP. Consequently, the consolidated balance sheet has not been adjusted to restate the accounting for joint venture under U.S. GAAP. Additional information concerning the Company's interests in joint ventures is presented in note 19.

(h) Stock-based compensation plans

The Company's stock-based compensation plan is described in note 14c. The Company accounts for all stock-based payments using the fair value-based method under SFAS 123. Under this method, compensation cost attributable to options granted is measured at fair value at the grant date. Any consideration paid on exercise of stock options or purchase of stock is credited to share capital.

(i) Derivative instruments and hedging activities

Under Canadian GAAP, effective January 1, 2004, derivatives used for non-trading purposes that do not qualify for hedge accounting are carried at fair value on the consolidated balance sheet, with changes in fair value reflected in earnings. Derivatives embedded within hybrid instruments are generally not separately accounted for except for those related to equity-linked deposit contracts, which are not applicable to the Company. Gains and losses on derivative instruments held within an effective hedge relationship are recognized in earnings on the same basis and in the same period as the underlying hedged items. There is no difference in accounting between Canadian and US GAAP in respect of derivatives that do not qualify for hedge accounting. Unlike Canadian GAAP, however, the Company recognizes all of its derivative instruments (whether designed in hedging relationships or not, or embedded within hybrid instruments) at fair value on the consolidated balance sheet for US GAAP purposes. Under US GAAP the accounting for changes in the fair value (i.e. gains or losses) of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship. For strategies designated as fair value hedges, the effective portion of the change in the fair value of the derivative is offset in income against the change in fair value, attributed to the risk being hedged, of the underlying hedged asset, liability or firm commitment. For cash flow hedges, the effective portion of the changes in the fair value of the derivative is accumulated in OCI until the variability in cash flows being hedged is recognized in earnings in future accounting periods. For both fair value and cash flow hedges, if a derivative instrument is designated as a hedge and meets the criteria for hedge effectiveness, earnings offset is available, but only to the extent that the hedge is effective. Ineffective portions of fair value or cash flow hedges are recorded in earnings in the current period.

(j) Income taxes

Accounting for income taxes under Canadian and US GAAP is similar, except that income tax rates of enacted or substantively enacted tax law must be used to calculate future income tax assets and liabilities under Canadian GAAP, whereas only income tax rates of enacted tax law can be used under US GAAP. In the periods presented there was no difference in tax rates. The Company has accumulated losses for income tax purposes, and as such, no recognition of the tax implications have been recorded on the US GAAP earnings as income tax expense would be offset by a similar amount of income tax recovery and is considered to be immaterial.

(k) Recent US accounting pronouncements

- (i) In March 2005, the Financial Accounting Standards Board (FASB) issued Financial Interpretation 47, Accounting for Conditional Asset Retirement Obligations (FIN 47). FIN 47 clarifies that the term conditional asset retirement obligation as used in FASB Statement No. 143, Accounting for Asset Retirement Obligations, refers to a legal obligation to perform an asset retirement activity in which the timing and (or) method of settlement are conditional on a future event that may or may not be within the control of the entity. The obligation to perform the asset retirement activity is unconditional even though uncertainty exists about the timing and/or method of settlement. Thus, the timing and/or method of settlement may be conditional on a future event. Accordingly, an entity is required to recognize a liability for the fair value of a conditional asset retirement obligation if the fair value of the liability can be reasonably estimated. FIN 47 also clarifies when an entity would have sufficient information

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to reasonably estimate the fair value of an asset retirement obligation. FIN 47 is effective no later than the end of fiscal years ending after December 15, 2005. The adoption of this statement has not had a material impact on our results of operations or financial position.

- (ii) In March 2005, the FASB ratified the consensus reached by the Emerging Issues Task Force ("EITF") on Issue No. 04-6, "Accounting for Stripping Costs Incurred During Production in the Mining Industry," that stripping costs incurred during production are variable inventory costs that should be attributed to ore produced in that period as a component of inventory and recognized in cost of sales in the same period as related revenue. The consensus will be effective for the Company in 2006. The Company is reviewing the guidance to determine the potential impact, if any, on its consolidated financial statements. The EIC in Canada has reached a tentative conclusion on this issue that differs from the EITF consensus. Specifically, it has suggested that the activity of removing overburden and other mine waste minerals in the production phase represents either a component of inventory or a betterment to the mineral property, depending on the benefit received by the entity. The Company is monitoring the developments and will determine the potential impact, if any, on its consolidated financial statements if and when related Canadian guidance is released.
- (iii) In June 2005, the FASB issued Statement 154, Accounting Changes and Error Corrections which replaces APB Opinion 20 and FASB Statement 3. Statement 154 changes the requirements for the accounting and reporting of a change in accounting principle. Opinion 20 previously required that most voluntary changes in accounting principles be recognized by including the cumulative effect of the new accounting principle in net income of the period of the change. In the absence of explicit transition provisions provided for in new or existing accounting pronouncements, Statement 154 now requires retrospective application of changes in accounting principle to prior period financial statements, unless it is impracticable to do so. The Statement is effective for fiscal years beginning after December 15, 2005, and is not expected to have a material impact on the Company's consolidated financial statements.
- (iv) In December 2004, the FASB issued SFAS 123 (Revised 2004), "Share-Based Payment," which requires all share-based payments to employees, including grants of employee stock options, to be recognized as compensation expense in the consolidated financial statements based on their fair values. In 2005, the FASB released several related Staff Positions ("FSPs") to help clarify and interpret this new guidance. The new rules modify certain measurement and expense recognition provisions of SFAS No. 123, "Accounting for Stock-Based Compensation," including the requirement to estimate employee forfeitures each period when recognizing compensation expense and requiring that the initial and subsequent measurement of the cost of liability-based awards each period be based on the fair value (instead of the intrinsic value) of the award. SFAS No. 123(R) also requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow as required under current literature. This requirement will reduce net operating cash flows and increase net financing cash flows in the periods after adoption. The Company previously elected to expense employee stock-based compensation using the fair value method prospectively for all awards granted or modified on or after January 1, 2003. The new standard is effective January 1, 2006. The Company is assessing the impact of adoption on its consolidated financial position and results of operation, but does not expect it to be material.
- (v) SFAS 153, Exchanges of Non-monetary Assets, was issued in December 2004 as an amendment to Accounting Principles Board (APB) Opinion No. 29. SFAS 153 provides guidance on the measurement of exchanges of non-monetary assets, with exceptions for exchanges that do not have commercial substance. Under SFAS 153, a non-monetary exchange has commercial substance if, as a result of the exchange, the future cash flows of an entity are expected to change significantly. Under SFAS 153, a non-monetary exchange is measured based on the fair values of the assets exchanged. If fair value is not determinable, the exchange lacks commercial substance or the exchange is to facilitate sales to customers, a non-monetary exchange is measured based on the recorded amount of the non-monetary asset relinquished. SFAS 153 will be effective for non-monetary exchanges that occur in fiscal periods beginning after June 15, 2005, and is not expected to have a material impact on the Company's consolidated financial statements.
- (vi) In November 2005, the FASB issued FSP FAS 115-1 and FAS 124-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments," which nullified 2004 guidance issued by the EITF on determining whether an impairment is other-than-temporary, and effectively reverted back to previous guidance in this area. The FSP generally encompasses guidance for determining when an investment is impaired, how to measure the impairment loss and what disclosures should be made regarding impaired securities. This FSP is effective for the first quarter of 2006 and is not expected to have a material impact on the Company's consolidated financial statements.

- (vii) In March 2005, the FASB issued FSP FIN 46(R)-5, "Implicit Variable Interests under FASB Interpretation No. 46(R), Consolidation of Variable Interest Entities," to address whether a company has an implicit variable interest in a VIE or potential VIE when specific conditions exist. The guidance describes an implicit variable interest as an implied financial interest in an entity that changes with changes in the fair value of the entity's net assets exclusive of variable interests. An implicit variable interest acts the same as an explicit variable interest except that it involves the absorbing and/or receiving of variability indirectly from the entity (rather than directly). The guidance did not have a material impact on the Company's consolidated financial statements.
- (viii) In September 2005, the EITF reached a consensus on Issue No. 04-13, Accounting for Purchases and Sales of Inventory with the Same Counterparty. This issue addresses the question of when it is appropriate to measure purchase and sales of inventory at fair value and record them in cost of sales and revenues and when they should be recorded as exchanges measured at the book value of the item sold. The EITF concluded that purchases and sales of inventory with the same counterparty that are entered into in contemplation of one another should be combined and recorded as exchanges measured at the book value of the item sold. The consensus should be applied to new arrangements entered into, and modifications or renewals of existing agreements, beginning with the second quarter of 2006. We do not expect the adoption of this statement will have a material impact on our results of operations or financial position.
- (ix) SFAS 151, Inventory Costs, was issued in November 2004 as an amendment to Accounting Research Bulletin (ARB) No. 43. SFAS 151 specifies the general principles applicable to the pricing and allocation of certain costs to inventory. Under SFAS 151, abnormal amounts of idle facility expense, freight, handling costs and wasted materials are recognized as current period charges rather than capitalized to inventory. SFAS 151 also requires that the allocation of fixed production overhead to the cost of inventory be based on the normal capacity of production facilities. SFAS 151 will be effective for inventory costs incurred beginning in the Company's 2006 fiscal year. The Company is presently evaluating the impact of SFAS 151 on the Company's consolidated financial statements.

(l) Recent Canadian accounting pronouncements

- (i) In January the Canadian Institute of Chartered Accountants ("CICA") issued Section 1530, "Comprehensive Income," Section 3251, "Equity," Section 3855, "Financial Instruments – Recognition and Measurement" and Section 3865, "Hedges." The new standards increase harmonization with US GAAP and will require the following: 1) Financial assets will be classified as either held-to-maturity, held-for-trading or available-for-sale. Held-to-maturity classification will be restricted to fixed maturity instruments that the Company intends and is able to hold to maturity and will be accounted for at amortized cost. Held-for-trading instruments will be recorded at fair value with realized and unrealized gains and losses reported in net income. The remaining financial assets will be classified as available-for-sale. These will be recorded at fair value with unrealized gains and losses reported in a new category of the consolidated balance sheet under shareholders' equity called other comprehensive income ("OCI"); and 2) Derivatives will be classified as held-for-trading unless designated as hedging instruments. All derivatives, including embedded derivatives that must be separately accounted for, will be recorded at fair value on the consolidated balance sheet. For derivatives that hedge the changes in fair value of an asset or liability, changes in the derivatives' fair value will be reported in net income and be substantially offset by changes in the fair value of the hedged asset or liability attributable to the risk being hedged. For derivatives that hedge variability in cash flows, the effective portion of the changes in the derivatives' fair value will be initially recognized in OCI and the ineffective portion will be recorded in net income. The amounts temporarily recorded in OCI will subsequently be reclassified to net income in the periods when net income is affected by the variability in the cash flows of the hedged item.

The above guidance will apply for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2006. Earlier adoption will be permitted only as of the beginning of a fiscal year. The impact of implementing these new standards is not yet determinable as it is highly dependent on fair values, outstanding positions and hedging strategies at the time of adoption.

- (ii) In October 2005, the Emerging Issues Committee of the CICA (the "EIC") issued Abstract No. 157, "Implicit Variable Interests Under AcG-15" ("EIC-157"), to address whether a company has an implicit variable interest in a VIE or potential VIE when specific conditions exist. An implicit variable interest acts the same as an explicit variable interest except that it involves the absorbing and/or receiving of variability indirectly from the entity (rather than directly). The identification of an implicit variable interest is a matter of judgment that depends on the relevant facts and circumstances. EIC-157 will be effective in the first quarter of 2006. The implementation of this EIC is not expected to have a material impact on the Company's consolidated financial statements.

(iii) In November 2005, the EIC issued Abstract No. 159, "Conditional Asset Retirement Obligations," to clarify the accounting treatment for a legal obligation to perform an asset retirement activity in which the timing and/or method of settlement are conditional on a future event that may or may not be within the control of the entity. Under this EIC, an entity is required to recognize a liability for the fair value of a conditional asset retirement obligation if the fair value of the liability can be reasonably estimated. The guidance is effective for the second quarter of 2006 and is to be applied retroactively, with restatement of prior periods. The implementation of this EIC is not expected to have a material impact on the Company's consolidated financial statements.

24. Subsequent events

(a) Credit Facility

On February 9, 2006, the Company announced completion of a \$25 million credit facility with The Bank of Nova Scotia (Scotia Capital). The facility, subject to customary conditions, is secured by inventory and receivables. The Bank of Nova Scotia may consent to increasing the facility to \$50 million if certain conditions are met.

(b) Acquisition of White Pine Copper Refinery Inc.

On January 1, 2006, the Company, through HBMS, acquired all of the outstanding common shares of White Pine Copper Refinery Inc. (WPCR) for total purchase consideration of \$17.6 million. The acquisition will be accounted for by the purchase method and the result of operations and cash flows will be included during 2006.

The following table summarizes the preliminary allocation of the purchase consideration based on management's current best estimate of the fair value of the assets and liabilities acquired on the date of acquisition:

Current assets (including cash of \$873)	\$	2,718
Property, plant and equipment		16,258
Current liabilities		(1,344)
	\$	17,632

Management expects to obtain additional information that may require additional adjustments to amounts shown above for property, plant and equipment, intangible assets and asset retirement obligations, and these potential adjustments may be material.

25. Hudson Bay Mining and Smelting Co., Limited

A summary of the annual comparative financial information for Hudson Bay Mining and Smelting Co., Limited is as follows:

	2005	2004
Total revenues	\$ 652,013	\$ 538,433
Net earnings	104,860	50,132
Long-term financial debt (excluding current portion)	200,504	238,586
Total assets	700,579	803,803

26. Comparative figures

Certain figures, previously reported for 2004, have been reclassified to conform with the basis of presentation adopted in the current year.

Corporate officers

Peter R. Jones, P.Eng.

President and Chief Executive Officer

**H. Russell Rood, B.Sc. (Civil Engineering),
B.Sc. (Mining Engineering)**

President, Mining Division

Tom A. Goodman

Vice President, Technical Services and
Human Resources

Brian D. Gordon, LLB

Vice President and General Counsel

Alan T. C. Hair, B.Sc. (Hons)

Vice President, Metallurgy,
Safety, Health & Environment

Jeff A. Swinoga, CA, MBA

Vice-President and
Chief Financial Officer

Corporate & shareholders' information

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Website: www.hudbayminerals.com

Listing**Toronto Stock Exchange**

Trading symbols: HBM; HBM.WT

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Auditors**Deloitte & Touche LLP**

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Appointment of auditors

In connection with the purchase of HBMS by the Company, the board of directors determined that the Company and its subsidiaries would best be served by having a single firm of auditors. Accordingly, in May 2005, Deloitte & Touche LLP, who had served as auditors of HBMS for more than 10 years, were appointed as auditors of the Company and its subsidiaries.

Annual general meeting

June 1, 2006
10:00 am EDT
Gallery Room
TSX Conference Centre
130 King Street West
Toronto, Ontario

www.hudbayminerals.com

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MINERALS INC
