

Form 51-102F1
Interim Management Discussion and Analysis¹
For
Stornoway Diamond Corporation
(“Stornoway” or the “Company”)

Containing Information up to and including September 15, 2011

OVERALL PERFORMANCE

Stornoway engages in the exploration and development of diamond projects in Canada, with a highly prospective pipeline of projects from feasibility-study stage to grass roots exploration. Stornoway’s principal focus is its 100% owned Renard Diamond Project located in north-central Quebec, currently the subject of a feasibility study and with the potential to become Quebec’s first diamond mine. Four additional projects in eastern Nunavut and on the Ontario/Quebec border are classified as being at an “advanced” stage, and Stornoway is also engaged in exploration at several early stage grass roots projects throughout Canada in geologically prospective, underexplored regions. Stornoway’s strategy is to build a growth oriented company that succeeds in the practical business of mining and selling rough diamonds. Stornoway’s long term view of the rough diamond market is positive, with tightening mine supply and growing demand, particularly in developing markets, resulting in real, long term price growth. In this context, Stornoway is well positioned to move Renard towards commercial production, and to add diamond resources from existing internal growth projects or acquisitions as new opportunities are identified. In addition, the Company has a management team with experience at each stage of the diamond pipeline, from exploration through development, mining and marketing.

As of September 15, 2011, the Company holds interests, directly or through joint ventures, in a property portfolio of some 19 properties representing approximately 2.0 million acres that can be roughly subdivided into 135,000 acres of ‘development’ stage projects (the Foxtrot Property, which includes the Renard Diamond Project), 1.27 million acres of ‘advanced’ exploration properties (Aviat, Qilalugaq, Churchill and Timiskaming) and 600,000 acres of ‘early stage’ projects (Hammer Property and others).

Forward-Looking Statements

This document may contain "forward-looking statements" within the meaning of Canadian securities legislation and the United States Private Securities Litigation Reform Act of 1995. These forward-looking statements are made as of the date of this document and the Company does not intend, and does not assume any obligation, to update these forward-looking statements, except as required by law.

These forward-looking statements include, among others, statements with respect to Stornoway's objectives for the ensuing year, our medium and long-term goals, and strategies to achieve those objectives and goals, as well as statements with respect to our beliefs, plans, objectives, expectations, anticipations, estimates and intentions. All forward-looking statements and information are based on Stornoway's current beliefs as well as assumptions made by and information currently available to Stornoway concerning anticipated financial performance, business prospects, strategies, regulatory developments, development plans, exploration, development and mining activities and commitments. Although management considers these assumptions to be reasonable based on information currently available to it, they may prove to be incorrect.

¹ **Note to Reader**

The following management discussion and analysis of the Company’s financial condition and results of operations should be read in conjunction with the audited consolidated financial statements for the years ended April 30, 2011 and 2010 together with the notes thereto (prepared in Canadian funds in accordance with Canadian Generally Accepted Accounting Principles “GAAP”); the condensed interim consolidated financial statements for the three months ended July 31, 2011 and July 31, 2010 have been prepared in Canadian funds in accordance with International Financial Reporting Standards (“IFRS”).

By their very nature, forward-looking statements involve inherent risks and uncertainties, both general and specific, and risks exist that predictions, forecasts, projections and other forward-looking statements will not be achieved. We caution readers not to place undue reliance on these statements as a number of important factors could cause the actual results to differ materially from the beliefs, plans, objectives, expectations, anticipations, estimates and intentions expressed in such forward-looking statements.

Forward-looking statements relate to future events or future performance and reflect current expectations or beliefs regarding future events and include, but are not limited to, statements with respect to: (i) the amount of mineral resources and potential mineral deposits; (ii) the amount of future production over any period; (iii) estimates of net present value and internal rates of return of any proposed mining operations; (iv) estimated capital costs, operating costs and diamond price assumptions and any potential impact on the estimated value of the Renard Diamond Project; (v) mine expansion potential and expected mine life; (vi) expected time frames for completion of permitting and regulatory approvals, completion of a feasibility study and related Environmental and Social Impact Assessment; (vii) that a production decision will be made for the Renard Diamond Project and that the decision will be positive; (viii) anticipated timelines for the commencement of mine production at Renard; (ix) anticipated timelines related to the Route 167 extension and the impact on the development schedule at Renard; (x) anticipated timelines for community consultations and the conclusion of an Impact and Benefits Agreement; (xi) future exploration plans and objectives; and (xii) sources of and anticipated financing requirements. Any statements that express or involve discussions with respect to predictions, expectations, beliefs, plans, projections, objectives, assumptions or future events or performance (often, but not always, using words or phrases such as “expects”, “anticipates”, “plans”, “projects”, “estimates”, “assumes”, “intends”, “strategy”, “goals”, “objectives” or variations thereof or stating that certain actions, events or results “may”, “could”, “would”, “might” or “will” be taken, occur or be achieved, or the negative of any of these terms and similar expressions) are not statements of historical fact and may be forward-looking statements. Many forward-looking statements are made assuming the correctness of other forward looking statements, such as statements of net present value and internal rate of return, which are based on most of the other forward-looking statements and assumptions herein. The cost information is also prepared using current values, but the time for incurring the costs will be in the future and it is assumed costs will remain stable over the relevant period.

Additional risks are described in Stornoway's most recently filed Annual Information Form. Stornoway cautions that the foregoing list of factors that may affect future results is not exhaustive. When relying on our forward-looking statements to make decisions with respect to Stornoway, investors and others should carefully consider the foregoing factors and other uncertainties and potential events. Stornoway does not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by Stornoway or on our behalf, except as required by law.

Highlights for the three months ended July 31, 2011 and the period ended September 15, 2011:

During the three months ended July 31, 2011 and the period ended September 15, 2011, the Company achieved several notable objectives:

Renard Diamond Project

- Announced the results of a diamond valuation exercise undertaken in Antwerp, Belgium in May 2011, which included: a base case modeled diamond price estimate of US\$182 per carat for the diamond samples from the Renard 2 and 3 kimberlite pipes, an increase of 56% over the previous estimate determined in September 2009 ; a base case modeled diamond price estimate of US\$112 per carat for the diamond sample from the Renard 4 kimberlite pipe, an increase of 49% over the previous estimate; and "High" diamond price models of US\$236, US\$205 and US\$185 per carat for the Renard 2, 3 and 4 kimberlite pipes respectively, based on an analysis of diamond price and size distribution upside on the individual valuation samples;
- Continued work on a Feasibility Study for the Renard Diamond Project, with results expected during the Fall of 2011;
- Executed two financing agreements with the Government of Québec by which the Company will contribute to the construction and maintenance costs of the Route 167 Extension, the road development project that will provide year round highway access to the Renard Diamond Project by way of the communities of Mistissini and Chibougamau.

Other Exploration Projects

- Announced the acquisition of 49,350 hectares of new claims in northern Québec, known as the "Aeon Project", where previous exploration work has indicated the potential for undiscovered and potentially diamondiferous kimberlites and completed an airborne geophysical survey and a till sampling program;
- Completed a drill program at the Hammer Property in Nunavut (75% interest); results are pending;
- At the Company's 100% owned Pikoo Property in Saskatchewan, completed an airborne geophysical survey, and initiated an exploration program on the property in September 2011.

Corporate Changes

- On July 20, 2011, the Company announced the appointments of Mme Monique Mercier, M. John LeBoutillier and M. Michel Blouin to the Company's Board of Directors, as designees of Investissement Québec; concurrently with these appointments, M. Jean-Jacques Carrier resigned from the Board of Directors;
- On August 2, 2011, the Company announced the appointment of Mr. Tony Walsh as Chairman of the Board, following the resignation of Ms. Eira Thomas from the Board of Directors.

RESULTS OF OPERATIONS

The Company reports its financial statements in accordance with International Financial Reporting Standards ("IFRS"). The Company's significant accounting policies are set out in Note 2 of the condensed interim consolidated financial statements. Previously the Company reported its interim and annual financial statements in accordance with Canadian Generally Accepted Accounting Principles ("GAAP"). The Company's 2010 comparatives in this MD&A have been presented in accordance with IFRS. As the Company's IFRS transition date was May 1, 2010, the 2009 comparative information in this MD&A has not been restated.

The Company's loss from operations for three months ended July 31, 2011 (the "**Current Period**") was \$9.6 million (a loss of \$0.07 per share) as compared to a loss of \$1.2 million (\$0.02 loss per share) for the three months ended July 31, 2010 (the "**Comparative Period**"). The Company's loss for the Current Period is mainly due to expenses of \$9.6 million (Comparative Period - \$1.4 million), including exploration expenses of \$8.3 million (Comparative Period - \$303,000). Other items which affected the Company's total loss included finance expense (Current Period - \$436,000; Comparative Period - \$Nil) related to the \$100 million credit support agreement with Investissement Québec and a cost recovery from a third party for use of the Company's lab facilities (Current Period - \$132,000;

Comparative Period - \$142,000). Excluding exploration expenses, the Company's expenses increased about 18% during the Current Period. This is a reflection of higher professional fees and regulatory and shareholder communication expense as compared to the three months ended July 31, 2010.

Exploration costs expensed in the Current Period increased significantly from \$1.1 million (offset by \$775,000 of Quebec exploration tax credits received) in the Comparative Period to \$8.3 million in the Current Period. During the Current Period, the Company spent \$6.2 million on exploration in Eastern Canada. The majority of these expenditures related to feasibility level activities at the Renard Diamond Project. In addition, the Company spent \$372,000 on exploration in other Canadian jurisdictions; \$321,000 for generative exploration; and \$1.4 million on exploration related to the Company's Arctic properties. Results from the Company's exploration programs during the Current Period are described below in the "Exploration Update" section.

Overall, the Company's administrative expenditures increased in the Current Period. Professional fees increased significantly (Current Period - \$302,000; Comparative Period- \$91,000) and include consulting fees for financial advisory services, accruals for the annual audit and the quarterly review, and legal expenses related to project financing consultation. Regulatory and shareholder communication expense (Current Period - \$208,000; Comparative Period - \$96,000) also increased primarily due to a higher level of shareholder communications, larger sponsorships, and a one-time fee for a video project. These increases are offset by slight decreases in salaries, benefits and director's fees (Current Period - \$189,000; Comparative Period - \$198,000), rent and facility fees (Current Period - \$117,000; Comparative Period - \$118,000) and office and sundry (Current Period - \$130,000; Comparative Period - \$147,000). Expenses also include a number of non-cash items: accretion (Current Period - \$5,000; Comparative Period- \$2,000), amortization (Current Period - \$211,000; Comparative Period - \$159,000) and share-based payments (Current Period - \$160,000; Comparative Period - \$312,000).

The Company's interest income was \$105,000 in the Current Period as compared to interest income of \$14,000 in the Comparative Period, due to higher cash and cash equivalents balance available for investment. The Company's finance expense was \$436,000 in the Current Period (Comparative Period - \$Nil) and relates to the commitment fee payment equal to 1.75% per annum for a \$100 million credit support agreement with Investissement Québec. During the Current Period, the Company recorded a deferred income tax recovery of \$243,000 (Comparative Period – deferred income tax expense of \$6,000), which decreased the Company's net loss after taxes to \$9.6 million (Comparative Period - \$1.2 million). The deferred income tax recovery for the Current Period arose as a result of the premium paid for flow through shares in excess of the market value of the shares. For accounting purposes, the proceeds from issuance of these shares are allocated between the offering 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 the investor pays for the shares. A liability is recognized in other liabilities for this difference. The liability is reduced and the reduction of premium liability is recorded in deferred tax recovery on a pro-rata basis as eligible expenditures are incurred.

As at July 31, 2011, total assets decreased to \$247.3 million from \$257.4 million at the April 30, 2011 year-end. Exploration and evaluation assets decreased slightly to \$214.50 million from \$214.54 million at April 30, 2010, because the Company wrote-off the exploration and evaluation assets related to capitalized acquisition costs of \$49,000 where no future exploration programs were planned for the foreseeable future.

The Company's cash, cash equivalents and short-term deposit amounts decreased during the Current Period, from \$34.5 million as of April 30, 2011 to \$25.0 million as of July 31, 2011. The decrease in the Company's cash balance is primarily a result of increased exploration expenditures. The Company's total liabilities, consisting primarily of trade accounts payable, accrued liabilities and provisions (\$4.4 million as at July 31, 2011 versus \$4.8 million at April 30, 2011) and an asset retirement obligation of \$1.4 million, decreased to \$5.8 million as at July 31, 2011 from \$6.5 million as at April 30, 2011. Shareholders' equity decreased to \$241.5 million as at July 31, 2011 from \$250.9 million as at April 30, 2011 and consists of share capital, non-voting convertible shares, contributed surplus, accumulated other comprehensive loss and deficit.

SIGNIFICANT SHAREHOLDER – DIAQUEM INC.

On April 1, 2011 the Company and DIAQUEM Inc. ("Diaquem") closed the agreement, previously announced December 14, 2010, to acquire Diaquem's 50% interest in the Renard Diamond Project (the "Acquisition"). Under the terms of the Acquisition, Diaquem became a significant shareholder of the Company, and retained a direct royalty interest on future diamond production. Diaquem is a wholly-owned subsidiary of SOQUEM INC., itself a wholly-owned subsidiary of Investissement Québec (formerly Société générale de financement du Québec), the Québec government's main industrial and financial holding company. In conjunction with the Acquisition,

Investissement Québec (“IQ”) entered into a credit support agreement with the Company with respect to future project debt financing of a minimum of \$100 million. The Company’s shareholders approved the Acquisition at a special meeting held on February 10, 2011.

On July 20, 2011, the Company appointed Mme Monique Mercier, M. John LeBoutillier and M. Michel Blouin to the Company's Board of Directors. The new appointments were made pursuant to the April 1, 2011 acquisition by Stornoway of the 50% interest in Renard Diamond Project previously held by Diaquem. As provided under the terms of the acquisition and permitted under the Articles of Stornoway, the new directors have been designated by IQ and appointed by the Board of Directors.

Concurrently to the appointment of Mme Mercier and Messrs. Blouin and LeBoutillier, effective July 20th, 2011, M. Jean-Jacques Carrier, Senior Vice-President and Chief Financial and Risk Officer of IQ, stepped down as Diaquem's designated director on Stornoway’s Board, a position he has held since April 1, 2011.

EXPLORATION UPDATE

Stornoway's material mineral property is the Renard Diamond Project, part of the larger Foxtrot Property in the Otish Mountains located in Québec, Canada. The following discussion is an update to disclosure in documentation filed with regulatory agencies and is available for viewing under Stornoway's profile on the SEDAR website at www.sedar.com. The exploration programs described below were conducted under the direction of Robin Hopkins, P.Geol. (NT/NU), the Company’s Vice President, Exploration, and a Qualified Person under National Instrument (“NI”) 43-101. Mr. Hopkins has reviewed the summaries below.

FOXTROT PROPERTY – RENARD KIMBERLITE BODIES, QUEBEC

Stornoway’s wholly owned subsidiary Les Diamants Stornoway (Canada) inc. (“Les Diamants Stornoway”) has a 100% interest in the Foxtrot Property, which contains the Renard cluster of kimberlite bodies. Until April 1, 2011, this interest was held as a 50/50 joint venture between Les Diamants Stornoway and SOQUEM Inc.’s (“SOQUEM”) wholly owned subsidiary, Diaquem. Diaquem retains a 2% gross revenue royalty on life of mine production from Renard.

Since 1996, an area of more than 400,000 square kilometres of the eastern Archean Superior craton has been evaluated. Exploration conducted by the joint venture prior to April 1, 2011 resulted in the discovery of a field of kimberlite intrusions on the Foxtrot property, notably the Renard cluster of kimberlite bodies, and the nearby “Lynx-Hibou” system of kimberlite dykes.

Preliminary Economic Assessment – March 2010

In March 2010, Stornoway announced the results of a Preliminary Economic Assessment (“PEA”), subsequently published in May 2010, wherein the Renard Diamond Project was estimated to have the potential to produce approximately 30 million carats of diamonds over a 25 year mine life, with a pre-tax Net Present Value of C\$885 million (at an 8% discount rate) and an Internal Rate of Return of 24.8%. Total capital investment was estimated at C\$511 million. The 2010 PEA was based upon an NI 43-101 compliant Mineral Resource initially published in December 2009 (the “2009 Mineral Resource”) of 23.0 million carats of Indicated Mineral Resource and 13.3 million carats of Inferred Mineral Resource, utilizing a diamond valuation for the Renard kimberlite pipes determined by WWW International Diamond Consultants Ltd. (“WWW”) in September 2009. At this time, a further 12 to 26 million carats was classified as a non-resource Potential Mineral Deposit (“PMD”).

Work undertaken since the announcement of the PEA has resulted in updates to the Mineral Resources, as more fully described in the Company’s Annual MD&A dated June 28, 2011 (available on Sedar at: www.sedar.com). In addition, the Company conducted a diamond valuation exercise in Antwerp, Belgium in May 2011 (see “*Diamond Valuation Updated*” below).

Feasibility Study – July 2010 to Present

Stornoway announced the formal commencement of the Renard feasibility study (the “Feasibility Study”) and related programs of work in July 2010. The total cost of the Feasibility Study, covering a two year period from January 2010 to December 2011, was initially estimated to be \$28.3 million, including all studies, associated exploration work, program support, operator management fees and contingencies. In April 2011, a supplementary budget for out-of-scope items totaling \$4.2 million was approved, increasing the total Feasibility Study budget to \$32.5 million.

The Feasibility Study is designed to build upon the PEA published in May 2010 as summarized above, and includes the following elements:

- A mine Feasibility Study incorporating both open pit and underground mining scenarios, with examination of an increased processing capacity of up to 7,000 tonnes per day;
- An Environmental and Social Impact Assessment (“ESIA”);
- Mine permitting, community consultation, and the negotiation of an Impact and Benefits Agreement (“IBA”);
- Establishment of a Québec based owner’s team for mine development; and
- A separate Feasibility Study and Environmental Assessment for a power line to connect the project to the Hydro-Québec James Bay hydroelectric network.

The commencement of a Feasibility Study at Renard is a significant milestone for the Company towards building Québec’s first diamond mine. An important element of the work program is a separate and distinct Feasibility Study and Environmental Assessment for a power line to the project, which is being conducted under the auspices of Hydro-Québec but financed by the Company. The power line has the potential to greatly reduce the project’s operating costs, reduce its overall environmental footprint, and to insulate the project from future fuel cost escalation. In support of the Feasibility Study, beginning in May 2010 the Company established a Québec based mining team. The Company’s objective at Renard is to define a robust, low-risk project with high margins and a substantial mine life, which is readily financeable.

The Feasibility Study is expected to be completed during the Fall of 2011.

Diamond Valuation Updated

On June 13, 2011, the Company announced results of a revised diamond valuation exercise undertaken May 9th-13th in Antwerp, Belgium, under the supervision of WWW International Diamond Consultants Ltd. (“WWW”). In addition to WWW, four other diamond companies also provided price estimates, and the average of the five valuations was used by WWW to construct a diamond price model with "High" and "Minimum" sensitivities.

Consistent with prior valuations, WWW created a single diamond price model for the Renard 2 and Renard 3 valuation samples given the similarity of the diamonds in terms of diamond qualities and size distribution. This base case price model is US\$182/carat, a 56% increase compared to the price model of US\$117/carat established in September 2009. Also consistent with past practice, a separate diamond price model has been adopted for the Renard 4 valuation sample given its apparently finer distribution of diamond sizes. The Renard 4 base case price model is US\$112/carat, a 49% increase compared to the previously established price model of \$75/carat. Model price sensitivities are US\$163 to US\$236/carat for Renard 2, US\$153 to US\$205/carat for Renard 3 and US\$105 to US\$185/carat for Renard 4. Diamond price models represent the diamond price that might reasonably be expected based on commercial-scale recoveries of all diamond size classes. WWW’s sensitivity limits are set such that it is highly unlikely that an actual diamond price achieved for each kimberlite body would fall below the "Minimum" sensitivity, but it is possible that the actual diamond price achieved may be higher than the "High" sensitivity number, which is not a maximum price.

As recommended by WWW, Stornoway will utilize a base case diamond price model of US\$182/carat for the Renard 2 and 3 kimberlite pipes in the financial model of the Renard Feasibility Study. In the case of Renard 4, prior analysis has suggested that the apparently finer size distribution of diamonds in the Renard 4 valuation sample, which accounts for that sample’s lower base price model of US\$112/carat, is attributable to increased diamond breakage and poor plant performance during recovery. On this basis, and taking into account alternate interpretations of diamond quality and size distribution, the Renard 2 and Renard 3 diamond price was adopted for Renard 4 during the recent declaration of the project’s NI 43-101 compliant Mineral Resource (Stornoway press release dated

January 24, 2011). It is expected that a similar approach will be taken in the determination of an applicable diamond price for Renard 4 in the upcoming Feasibility Study.

In addition to their valuation work on the Renard 2, Renard 3 and Renard 4 diamond samples, WWW also provided an updated valuation for the Lynx and Hibou diamond samples. WWW has recommended a base case modeled price of US\$119/carat be adopted for the Lynx diamond sample with sensitivities of US\$99 to US\$144/carat, and a base case modeled price of US\$118/carat be adopted for the Hibou diamond sample with sensitivities of US\$88 to US\$136/carat. The proposed mine plan for Renard presently does not include a plan to mine the Lynx and Hibou dykes.

Route 167 Extension – Financing Agreements

In August 2011, the Company entered into two financing agreements with the Government of Québec by which the Company will contribute to the construction and maintenance costs of the Route 167 Extension, the road development project that will provide year round highway access to the Renard Diamond Project by way of the communities of Mistissini and Chibougamau. The agreements represent an important example of financial partnership between industry and government in full accord with the recently announced “Plan Nord”, the Québec Government’s initiative to maximize, notably, the natural resource potential of northern Québec.

Under the auspices of the Plan Nord, \$1.2 billion will be committed over five years to fund infrastructure development in the region of Québec north of the 49th parallel. Included in this amount will be \$331.6 million to facilitate the construction of the Route 167 Extension. In two separate agreements executed on August 1, 2011 with the ministère des Ressources naturelles et de la Faune and the ministère des Transports (the “MTQ”), the Company has agreed to contribute \$44 million to the development of the new road, to be paid in annual installments over a ten year period starting in July 2015. The Company’s contribution will be financed by Québec at 6.3% and will be conditional upon, amongst other things, the completion of the road on schedule, the receipt of all regulatory approvals for the construction of the Renard Diamond Project and the successful completion of project financing for the project. In addition, the Company has agreed to contribute a maximum of \$5,000 per kilometer, or \$1.215 million per year, to the maintenance of the road during operation. Other partners may also be called upon to contribute to the financing of this infrastructure.

The two financing agreements executed on August 1, 2011 are consistent with the Company’s previously stated commitment to provide financial assistance for the development of the Route 167 Extension, the key catalyst for the successful and timely development of the Renard Diamond Project. The two financing agreements are beneficial to the Company because no up-front capital investment is required. Instead, the agreements are established on the basis of long term cost recovery tied to the successful development of the project.

The Route 167 Extension will be constructed as a 243 km-long, 70 km/hour two lane gravel-top highway under the supervision of the MTQ. The road will be designated as a multi-service provincial highway connecting Renard to the end of the current Route 167 at Lac Albanel (Temiscamie), and will provide access to a number of other prospective mining projects as well as the new Albanel-Temiscamie-Otish Park. Construction is expected to commence in the Fall of 2011; however there will be no financial impact on the Company until 2015.

OTHER PROPERTY INTERESTS

Stornoway's diamond exploration programs are conducted under the direction of Robin Hopkins, P.Geol. (NT/NU), Vice President, Exploration, a Qualified Person under NI 43-101. Mr. Hopkins has reviewed the disclosure contained in this Interim MD&A.

The Company maintains interests in four advanced exploration stage properties, those being the Aviat, Qilalugaq and Churchill Properties in Nunavut, and the Timiskaming Property in Ontario. The advanced projects have demonstrated the potential for significant tonnages and high diamond contents on a non-resource basis, and now merit either additional delineation drilling or bulk sampling. The Company considers the Aviat, Qilalugaq and Timiskaming projects to be credible "pipeline" projects, providing the Company with significant exposure to long term diamond price growth, however, the Company’s interest in the Churchill Property is a historical interest and the Company has no plans to participate in future exploration or development programs on this property for the foreseeable future.

During the Spring of 2011, the Company initiated exploration activities on several earlier-stage projects where previous work identified the potential for new kimberlite discoveries. It is management’s intention to continue to

advance the Company's pipeline of projects, with particular emphasis on discovery and the establishment of new resources. In the near to medium term, the immediate focus of the Company's non-Renard exploration efforts will be on discovery oriented activities, both within the existing property portfolio and in new generative programs. The Company is the operator or participant in a number of other minor or early stage grassroots projects, including landholdings in Nunavut, Northwest Territories, Alberta, Saskatchewan, Ontario and Quebec, Canada.

The Company and its wholly owned subsidiaries also hold varying interests in approximately 0.6 million acres in about 14 properties, representing a series of early stage or grass-roots projects which either host, or have the potential to host, kimberlite bodies. Some of the known kimberlites have been adequately tested by drilling and micro/macro diamond techniques, while others require additional work to be fully evaluated. Certain properties have logistical or other considerations that may limit or prevent access at the present time. Other properties have promising indicator mineral trains and/or geophysical targets that would warrant drill testing if sufficient funds were available.

The Company maintains regional geological, geochemical and geophysical databases, and undertook generative exploration programs throughout Canada during 2008. This work investigated geologically prospective terrains, un-sourced indicator mineral anomalies derived from public, quasi-public and proprietary databases and unexplained geophysical targets from both ground and airborne surveys. Till and heavy mineral sampling, airborne and ground geophysical surveys and prospecting programs were completed in 2008. Rock samples were collected for both caustic fusion and DMS processing. However, in late 2008, the Company suspended activities on all grassroots generative programs in response to the deepening international credit crisis and the accompanying contraction of the Canadian venture capital market. In September 2010, the Company announced that exploration activities in high priority locations had been restarted, including the processing of samples collected during the 2008 field work. Partial results available to date from the 2008 generative exploration programs have been, and will continue to be, used to identify and acquire targeted landholdings thought to have the potential to host diamondiferous kimberlites. Results for additional work are pending and Stornoway anticipates continued property acquisition.

In April 2011, the Company announced an exploration budget of \$5.6 million for exploration programs during 2011 outside of the Renard Diamond Project. As at July 31, 2011 the Company had incurred exploration expenses of approximately \$2.5 million pursuant to its 2011 exploration programs.

Aeon Claims (Northern Quebec)

In July 2011, the Company announced the acquisition of 49,350 hectares of new claims in northern Québec where previous exploration work has indicated the potential for undiscovered and potentially diamondiferous kimberlites. The new claims, wholly owned by Stornoway and designated the "Aeon Project", are situated 300 kilometers north of the Company's Renard Diamond Project and approximately 100 kilometers north of the network of Hydro-Québec power stations located along the all-season Trans-Taiga Highway.

The Aeon area of interest was first identified by a regional geochemical sampling program designed to test the potential for diamondiferous kimberlites over a broad region of northern Québec. Subsequent follow-up sampling has now confirmed the potential for multiple kimberlites or kimberlite clusters localized within two 10 km by 10 km source areas. Kimberlite indicator mineral grain counts in anomalous samples are comparable to those associated with the discovery of the Renard Diamond Project to the south, and the chemistry of the indicator minerals is suggestive of a diamondiferous source. Renard represents the nearest known kimberlite cluster to the Aeon Project, although other kimberlites have been identified in the Wemindji area some 490km to the west and in the Torngat area approximately 530km to the northeast.

Stornoway initially applied for the Aeon claims in April 2011, and claim certificates were officially issued by the ministère des Ressources naturelles et de la Faune in July 2011. During 2011, the Company undertook a high-resolution airborne geophysical survey, and conducted detailed till sampling and follow-up prospecting on high-priority targets with the goal of preparing for discovery drilling in 2012.

The Aeon Project is located within the region of northern Quebec governed by the James Bay and Northern Québec Agreement (1975, as amended; the "JBNQA"), a land claims agreement executed by the Government of Québec, the Government of Canada, Hydro-Québec, the Grand Council of the Crees (Eeyou Istchee) and the Northern Québec Inuit Association, amongst others. Within the context of the administrative regions of the JBNQA, the project is situated north of the 55th parallel.

The 2011 Aeon exploration program represents about \$1.1 million within the Company's larger \$5.6 million budget for exploration.

Hammer (Nunavut)

In July of 2009, the Company reported discovery, by surface prospecting, of the Hammer kimberlite in the Coronation Gulf/North Slave Diamond District of Nunavut. The project is a 75%-25% joint venture between the Company and North Arrow Minerals Inc. respectively. The Hammer Property is located approximately 500km north of Yellowknife, Northwest Territories, within the Coronation Gulf/North Slave Diamond District. Permafrost conditions and equipment constraints prevented the collection of fresh kimberlite for representative microdiamond analysis, but caustic fusion of a 6.6kg sample returned a diamond on the 0.106mm square mesh screen, confirming that the body is diamondiferous. Some 17 kimberlites were previously known to exist in the general area, with the Company holding variable interests in ten of them. The diamond contents of individual bodies range from barren to highly diamondiferous. No development work on any kimberlite has taken place to date, although large tonnage sampling programs have been undertaken by De Beers and Rio Tinto (through Kennecott Canada Inc.) at the Knife and Anuri kimberlites respectively.

During the summer of 2011, the Company conducted a drill program to determine the Hammer kimberlite's size and shape, to test for multiple phases of kimberlite, and to collect sufficient samples to permit an estimate of diamond content. Results from this recently completed drill program will be reported when received.

Pikoo Project (Saskatchewan)

On April 26, 2011, the Company announced the acquisition of 33,374 hectares of contiguous claims at the "Pikoo Project" located in central Saskatchewan. The Pikoo claims are owned 100% by the Company, and are located 140 km east of La Ronge Saskatchewan and 100 km west of Flin Flon Manitoba. An all-season road to the community of Deschambault Lake comes to within 6km of the property's southern boundary.

The Company commenced acquisition of the Pikoo claims in February and March 2011, and claim certificates have been issued by Saskatchewan Ministry of Energy and Resources. During the summer of 2011, the Company has undertaken an airborne geophysical survey, and is in the process of conducting detailed till sampling and follow-up prospecting on high-priority targets in preparation for potential drilling later in 2011 or in 2012. The area of interest was first identified in 2006 following a regional geochemical sampling program designed to test the diamond potential of the northern portion of the Sask Craton, which hosts the Fort a la Corne cluster of kimberlite pipes approximately 220 km to the southwest. Subsequent follow-up sampling confirmed the potential for multiple kimberlites or kimberlite clusters localized within a 15km by 20km source area. No kimberlites are currently known in the vicinity of the Pikoo Project, and their identification would represent a significant new discovery in Canadian diamond exploration.

Exploration and Evaluation Asset Write-offs

During the period ended July 31, 2011, the Company wrote-off the exploration and evaluation assets related to capitalized acquisition costs of \$49,000 where no future exploration programs were planned for the foreseeable future (July 31, 2010 – \$Nil).

RISKS AND UNCERTAINTIES

The Company's securities should be considered a highly speculative investment and investors should carefully consider all of the information disclosed in the Company's Canadian regulatory filings prior to making an investment in the Company, including the risk factors discussed under the heading "Risk Factors" in the Company's Annual Information Form ("AIF") dated July 21, 2011 available on SEDAR at www.sedar.com.

The Company's financial condition and future prospects are significantly affected by overall economic conditions. The Company has no source of operating revenue and relies on equity financings and, in prior years, the sale of non-core assets to finance its operations and in particular, to further exploration on its properties. Additional financings are dilutive to existing shareholders. Failure to secure additional financing, as required, could result in the postponement of exploration programs, or delays in the development of the Renard Diamond Project. The Company's investments (common shares in other publicly-traded exploration companies) can fluctuate significantly in value, and it could be difficult for the Company to realize funds quickly from the sale of these investments without causing further downward pressure on the share price of the investment companies.

The majority of the Company's expenses at the present time are denominated in Canadian Dollars so its exposure to foreign exchange risk is limited.

The Company has no exposure to asset-backed commercial paper through its short-term investments, which are invested in chartered bank-issued high-interest savings accounts, Bankers' Acceptance ("BAs") or Bankers' Deposit Notes ("BDNs") or Guaranteed Investment Certificates ("GICs") to minimize, to the extent possible, the Company's credit risk. The majority of the Company's receivables consist of sales tax receivables due from the federal government, receivables from a related party for the reimbursement of administrative and technical time and its share of exploration expenses on a property, and receivables from a company that previously used the Company's facilities and personnel on a cost recovery basis. The maximum amount of the Company's exposure to credit risk with respect to its receivables is the carrying value of those receivables as at the balance sheet date.

The Company's liquidity risk, the risk that the Company won't be able to meet its obligations as they come due, has been mitigated as compared to the prior comparative period because the Company was able to complete a significant equity financing in January 2011 and was also able to raise "flow-through" funds for grass-roots exploration in Canada during the year ended April 30, 2011 (see "*Previous Financings*" below for a description of the Company's financing activities). The Company is required to spend approximately \$146,000 on Canadian Exploration Expense ("CEE") by December 2011. Although there has been a significant improvement in the equity market in Canada since 2009, overall market conditions remain uncertain and subject to volatility. The Company's material mineral properties are all in good standing and the Company has sufficient financial resources to keep those properties in good standing through 2012. The Company regularly reviews its landholdings with a view to reducing or consolidating those landholdings to focus on specific areas of interest and exploration potential.

As of the report date, the Company has positive working capital which will be used to fund the Company's Feasibility Study at the Renard Diamond Project, conduct exploration programs at several of the Company's exploration properties and for general working capital over the next year. The Company has minimum commitments under its operating leases totaling \$970,000, and is committed to pay \$1.75 million annually pursuant to the terms of the Credit Support Agreement with IQ. Please see the "*Commitments*" schedule and related descriptions below for more information.

The Company will need to secure some form of additional financing to further develop the Renard Diamond Project, assuming receipt of a positive bankable feasibility study during 2011, a production decision by the Company's Board of Directors, and receipt of the required regulatory approvals and permits for mine construction during 2012. The Company's management will continue to consider various alternatives for future financing requirements, within the context of existing market conditions. There can be no guarantee that the Company's management will be successful in these endeavours. Failure to obtain additional financing could result in the delay or indefinite postponement of further exploration and development of the Company's properties and ultimately in the loss of its properties.

SUMMARY OF QUARTERLY RESULTS

The following table sets out selected unaudited consolidated quarterly financial information of Stornoway and is derived from the unaudited quarterly consolidated financial statements prepared by management. Stornoway's condensed interim consolidated financial statements are prepared in accordance with International Financial Reporting Standards (unless otherwise indicated) and are expressed in thousands of Canadian dollars (except for per share amounts).

Period	Loss or (Income) from Continued Operation and Net Loss (Income)	Basic Loss (Earnings) per share ⁽¹⁾ from Continued Operation and Net Loss (Income) ⁽²⁾	Fully Diluted Loss (Income) per share ⁽¹⁾ - from Continued Operation and Net Loss (Income) ⁽²⁾	Exploration Expenses
Three months ended July 31, 2011	\$9,619	\$0.07	\$0.07	\$8,290
Three months ended April 30, 2011	7,841	0.10	0.10	3,801
Three months ended January 31, 2011	2,874	0.04	0.04	2,039
Three months ended October 31, 2010	4,300	0.06	0.06	2,352
Three months ended July 31, 2010	1,175	0.02	0.02	303
Three months ended April 30, 2010 ⁽³⁾	14,063	0.21	0.21	991
Three months ended January 31, 2010 ⁽³⁾	1,320	0.02	0.02	628
Three months ended October 31, 2009 ⁽³⁾	5,891	0.09	0.09	1,304

⁽¹⁾ Based on the treasury share method for calculating diluted earnings.

⁽²⁾ On February 22, 2011, the Company's common shares were consolidated on 1-new-for-4-old basis. All basic and fully diluted loss per share information has been adjusted to reflect this share consolidation for all periods presented.

⁽³⁾ Fiscal 2009 financial information is presented in accordance with previous Canadian GAAP and may not be appropriate as a comparative basis.

Quarterly results will vary in accordance with the Company's exploration and financing activities. Exploration expenses and exploration and evaluation asset write-offs typically have the most significant impact on the Company's quarterly results, followed by share-based payments expense and general and administrative expenses. Exploration and evaluation assets write-offs typically vary in accordance with exploration results and changes to the Company's land position and can rarely be predicted in advance. Exploration expenses will change based on the type of exploration work completed in any given quarter. The Company's cash flow is affected by the seasonality of the exploration business, and fluctuations in general and administrative expenses are typically seasonal as well.

In a typical quarter, the Company's professional fees will increase when property option and joint venture agreements are in development and negotiation, and investor relations activities increase in proportion to shareholder inquiries, communications and as a result of the Company's periodic "roadshows". Share-based payments expense varies, and is dependent upon the size, timing, the vesting schedules and estimated fair value of the stock options granted (see "*Critical Accounting Estimates*" below for details on the key assumptions used). The Company typically grants stock options at least annually and usually following the Company's Annual General Meeting, which is usually held in the fall.

The Company's activities in the Current Period were focused on the continuation of the Feasibility Study at Renard and grass-roots exploration throughout Canada. Loss from continued operations presented in the table above includes the Company's quarterly exploration expenditures.

LIQUIDITY

The Company's cash and cash equivalents decreased from \$22.7 million at April 30, 2011 to \$13.2 million at July 31, 2011. In addition, as at July 31, 2011 the Company has a further \$11.8 million classified as short-term deposits, of which \$328,000 is held as collateral security for the Company's credit cards and \$8,000 is held as a line of credit to satisfy exploration bonding requirements. A GIC equivalent to the utilization of the line of credit is provided as collateral security. The remainder of \$11.8 million classified as a short-term deposit is held in a GIC and a term deposit that is cashable any time after 30 days from the investment date. As at July 31, 2011, the Company had working capital (current assets minus current liabilities) of \$22.5 million (April 30, 2011 - \$31.9 million).

PREVIOUS FINANCINGS

Flow-through Financing – June 2010

In June 2010, the Company completed a "flow-through" financing which consisted of 2,193,750 "flow-through" common shares of the Company for gross proceeds of \$5.0 million. The "flow-through" common shares were issued at a price of \$2.28 per share. The Company paid a 6.5% cash commission on certain subscriptions received and issued 131,625 compensation options to the agents. Gross proceeds from this financing must be used on CEE as defined in the Tax Act. Flow-through common shares provide for the Company's CEE to be transferred to the purchasers of the flow-through common shares and, as a result, the tax basis for these expenditures is not available to the Company (*expressed in thousands of Canadian Dollars*).

Flow-through commitment at June 29, 2010	\$	5,002
Qualifying expenditures to July 31, 2011		<u>(4,856)</u>
Flow-through funds on hand at July 31, 2011	\$	<u>146</u>

As at July 31, 2011, the Company had spent approximately 97% of the proceeds from this offering on exploration programs at a number of its properties across Canada, including approximately \$1.1 million for exploratory drilling at the Company's Renard Diamond Project, and including a generative program in Québec, in accordance with the previously announced use of proceeds of this financing. The Company expects to spend all remaining flow-through funds prior to December 31, 2011.

Short Form Offering – January 6, 2011

On January 6, 2011, the Company completed a prospectus offering and issued 14,350,000 common shares at \$2.44 for gross proceeds of \$35.0 million. The transaction was completed by a syndicate of underwriters led by RBC Capital Markets and including Desjardins Securities, BMO Capital Markets and Canaccord Genuity (the "Underwriters"). The Underwriters received a cash fee equal to 6% of the gross proceeds from the sale of the common shares. The Company is using the net proceeds from the Offering to complete a Feasibility Study at the Renard Diamond Project and for general working capital purposes.

The Company expects to apply the net proceeds as follows:

Description of Expenditure	Anticipated Use	Actual Use*
	\$000s	\$000s
<i>Renard Diamond Project</i>		
Mine, plant and surface infrastructure design	7,000	5,534
Environmental and socio-economic studies	2,200	1,216
Project management and support costs	2,400	1,844
Other work related to the feasibility study	2,800	465
Estimated cost to complete	<u>-</u>	<u>7,600</u>
	<u>14,400</u>	<u>16,659</u>
Annual commitment fee payable for Credit Support Agreement	1,750	436
Estimated costs related to the Transaction	2,050	2,715
General working capital, administrative expenses and salary expenses (including technical)	<u>14,363</u>	<u>12,753</u>
	<u>18,163</u>	<u>15,904</u>
	<u>32,563</u>	<u>32,563</u>

*from February 1 to July 31, 2011

Stornoway is using the net proceeds from the Offering to complete a bankable Feasibility Study on the Renard Diamond Project during 2011, with a goal of making a production decision by the end of 2011, and for general working capital and administrative expenses in 2011 and 2012. In order to complete the bankable Feasibility Study, Stornoway must submit a “project description” to the Quebec government and obtain all required permits, finish resource and reserve estimate work, including geotechnical drilling at site, complete a revised economic assessment, finalize the mine, plant and surface infrastructure design as well as complete environmental and socio-economic impact studies. Stornoway expects to complete the bankable Feasibility Study during the Fall of 2011, but receipt of the required permits and other approvals is not expected until mid-2012.

WORKING CAPITAL

The Company’s working capital as at July 31, 2011 was \$22.5 million (April 30, 2011 - \$31.9 million). During the Current Period, the Company’s cash position decreased by \$9.5 million to \$13.2 million in cash and cash equivalents at July 31, 2011 as compared to the Comparative Period, where the Company’s cash position increased by \$3.2 million to \$12.5 million in cash and cash equivalents. A decrease in trade accounts payable, accrued liabilities and provisions (Current Period - \$416,000; Comparative Period - \$885,000), share-based payments expense (Current Period - \$160,000; Comparative Period - \$312,000), amortization (Current Period - \$211,000; Comparative Period - \$159,000), deferred income tax recovery (Current Period - \$243,000; Comparative Period - deferred income tax expense of \$6,000), a decrease in prepaid expenses (Current Period - \$511,000; Comparative Period - \$8,000) and an increase in other receivables (Current Period - \$165,000; Comparative Period - a decrease of \$409,000) represent the largest reconciling items from the condensed interim consolidated statements of loss to the condensed consolidated statements of cash flows - operating activities, for the period ended July 31, 2011.

The Company’s primary operating activity is the acquisition and exploration of its exploration and evaluation assets. During the Current Period, the Company expensed \$8.3 million (Comparative Period- \$1.1 million, offset by \$775,000 of Quebec exploration tax credits received), with the most significant expenditures on the Renard Diamond Project in Quebec. Exploration expenses relate to the initial search for deposits with economic potential and to detailed assessments of deposits or other projects that have been identified as having economic potential. The Company’s most significant operating expenses during the Current Period included \$302,000 (Comparative Period - \$91,000) for professional fees, \$208,000 (Comparative Period - \$96,000) for regulatory and shareholder communication expense, \$436,000 (Comparative Period - \$Nil) for finance expense, and \$189,000 (Comparative Period - \$198,000) for salaries, benefits and director’s fees. The Company’s loss for the Current Period of \$9.6 million (Comparative Period - \$1.2 million) was reduced by cost recoveries of \$132,000 (Comparative Period - \$142,000) for a third party’s use of the Company’s North Vancouver laboratory facilities, and by interest income of \$105,000 (Comparative Period - \$14,000).

The Company's ability to generate cash is very much affected by the current market conditions, its share price and third party interest in its assets. The Company is very reliant on equity financings, which are dilutive to existing shareholders, to fund ongoing exploration and development activities, and for general corporate purposes. In previous years, the Company was able to sell non-core assets as one means to finance its operations and to further exploration on its material mineral property interests. The Company's ability to sell non-core assets in the future is dependent on interest in the Company's assets from third parties. In addition, the Company is eligible for investment tax credits with respect to its exploration activities in certain provinces, which may help the Company finance its operations to some extent; however, the timing and amounts of those tax credits cannot be reliably estimated. The funds that the Company does have which aren't allocated for short-term cash requirements are invested in tranches for up to 90 days in BAs or BDNs issued by various Canadian chartered banks or held in high interest savings accounts at the same institutions. Some excess cash is also invested in GICs and term deposits, cashable after 30 days, which typically pay a higher interest rate than BAs or BDNs. The Company has no exposure to asset-backed commercial paper.

CREDIT FACILITY

The Company has no credit facilities that could be used for ongoing operations or general working capital requirements because it has no operating cash flow.

During the year ended April 30, 2011, as part of the Acquisition agreement described under "*Significant Shareholder – Diaquem Inc.*" above, the Company and IQ entered into a credit support agreement (the "Credit Support Agreement"), pursuant to which IQ committed to provide financing in favour of Stornoway in a minimum amount of \$100 million to fund a portion of the construction and development costs of the Renard Diamond Project (the "IQ Commitment").

The following description of certain material provisions of the Credit Support Agreement is a summary only, is not comprehensive and is qualified in its entirety by reference to the full text of the Credit Support Agreement, which was filed on SEDAR in April 2011 and is available at www.sedar.com.

The IQ Commitment will be senior and first ranking, *pari passu* with the other debt of Stornoway that may be provided by a lending syndicate formed to fund a portion of the construction costs of the Renard Diamond Project. The IQ Commitment may either form part of the commitments made available by the lending syndicate or, absent a concurrent facility by a lending syndicate, be made available separately by IQ on terms no less favourable than prevailing commercially reasonable market terms. In addition, IQ shall be entitled to receive the same benefits, on a pro rata basis, as the lending syndicate. In respect of the lending syndicate, IQ will have the right to be lead or co-lead lender and manager or co-manager.

The obligations of IQ under the Credit Support Agreement will terminate on the earlier to occur of: (a) the date on which Stornoway notifies IQ in writing that the Credit Support Agreement is terminated; (b) the date of the initial borrowing under the IQ Commitment; and (c) the date which is the 4-year anniversary of the closing of the Acquisition (closing occurred on April 1, 2011).

As consideration for the IQ Commitment, Stornoway has agreed to pay IQ, for the period from and including the date of the Credit Support Agreement up to the date the Credit Support Agreement is terminated, a non-refundable commitment fee equal to 1.75% per annum computed daily on the amount of \$100 million, payable quarterly in arrears on the first business day of the following quarter.

The IQ Commitment shall be conditional upon: (i) the decision of the Board of Directors of Stornoway, following receipt and consideration of a bankable feasibility study relating to the Renard Diamond Project and any other factors as it deems relevant, to proceed with the construction and development of the Renard Diamond Project; (ii) the closing conditions of the lending syndicate (if any); and (iii) in the absence of a concurrent lending syndicate, the IQ Commitment shall be subject to customary closing conditions in favour of IQ as a lender, including satisfactory due diligence investigations and satisfactory settlement of definitive loan and security documentation (but, for greater certainty, it shall not be a condition of closing that Stornoway shall have entered into any marketing off-take or analogous agreement with any third party).

CAPITAL REQUIREMENTS

The Company's most significant fixed costs relate to its leases for office space and then the costs associated with maintaining a TSX listing. The Company's minimum commitment for its premises for the five year period between

2012 and 2016 is \$970,000. The Company is able to reduce some of this liability through the sub-lease of excess space. In addition, the Company is committed to minimum future financial capital contributions for the construction and maintenance of the Route 167 segment. The Company has agreed, subject to certain key milestones being achieved, to contribute \$44 million to the development of the Route 167 extension, to be paid over a ten year period starting in July 2015 and financed by the Province of Quebec at a rate of 6.3%. The Company also has a \$100 million credit support agreement with IQ to fund a portion of future construction and development costs at the Renard Diamond Project, under which commitment fee payments equal to 1.75% per annum are payable by the Company. (See "Commitments" for more details).

The Company has sufficient financial resources to keep its material landholdings and the majority of its non-material landholdings in good standing into 2012 and beyond. The Company has also incurred sufficient exploration expenditures on these properties to keep them in good standing with the respective provincial and territorial governments through 2011 as well. The Company's management actively manages its landholdings in an effort to keep those landholdings with the greatest exploration potential in good standing for as long as possible. The Company's management regularly reviews its cash position against future plans and makes decisions regarding these plans accordingly. Exploration work in 2010 was primarily focused on the Company's Renard Diamond Project, directed to a resource expansion and optimization program, with additional drilling and diamond sampling. Funds from the short-form prospectus offering, which closed in January 2011, are being used towards the completion of a bankable Feasibility Study at Renard and for general working capital purposes. Funds from the flow-through financing, which closed in June 2010, were used to fund Stornoway's exploration drill program at the Renard Diamond Project during 2010, as well as grass-roots exploration work at several of the Company's other Canadian exploration properties between 2010 and 2011. In addition, the Company is conducting in-depth reviews, compilation and analysis of its exploration data acquired over several years of fieldwork to refine specific targets of interest on its current mineral properties and to identify new areas with exploration potential.

The Company has no history of profitable operations and its present business is at the exploration/pre-development stage. The Company has no source of operating cash flow and no assurance that additional funding will be available to it for further exploration and development of its projects when required. As such, the Company is subject to many risks common to such enterprises, including under-capitalization, cash shortages and limitations with respect to personnel, financial and other resources and the lack of revenues. Although the Company has been successful in the past in obtaining financing through the sale of equity securities or joint ventures, there can be no assurance that the Company will be able to obtain adequate financing in the future or that the terms of such financing will be favorable. Such means of financing typically result in dilution of a shareholder's interest, either directly as a result of issuing equity securities or indirectly through dilution of an interest in one of the Company's projects. Failure to obtain additional financing could result in the delay or indefinite postponement of further exploration and development of its properties and ultimately in the loss of its properties.

CAPITAL RESOURCES

The Company has no operations that generate cash flow and its long-term financial success is dependent on management's ability to discover economically viable diamond deposits. The diamond exploration process can take many years and is subject to factors that are beyond the Company's control. Many factors influence the Company's ability to raise funds, including the health of the resource market, the climate for diamond exploration investment, the Company's track record and the experience and caliber of its management.

Several factors will influence the Company's cash requirements in the near future. These factors include: the receipt of a positive Feasibility Study and the required permits to construct a diamond mine at Renard, as well as a decision to proceed with further development. The Company's exploration plans for 2011 and 2012 will also affect its cash requirements, and are subject to change. The Company's actual funding requirements may vary from those planned due to a number of factors, including the progress of exploration activity and results.

The Company has historically financed its exploration programs through the issuance of equity capital, and through the use of a convertible debenture (issued in March 2007 and extinguished in July 2008) while at the same time trying to reduce shareholder dilution by securing joint venture partners where appropriate and in prior years, by the monetization of non-core assets. Between 2009 and mid-2011, Canadian equity capital markets have seen significant improvements as compared to late 2008 and early 2009. Interest in the diamond sector has also improved recently. The Company's management intends to continue to seek out the best opportunities to maximize

shareholder value by furthering exploration programs on its most promising projects and by generating new discoveries.

The Company has a number of stock options and warrants outstanding which, if exercised, would increase the Company's available cash. A summary of the stock options and warrants currently outstanding is included under "Outstanding Share Capital" below.

ADDITIONAL DISCLOSURE

Additional disclosure concerning Stornoway's general and administrative expenses and exploration expenses is provided in the Company's consolidated statements of loss and deficit and the consolidated schedule of resource property costs contained in its audited consolidated financial statements for April 30, 2011 and April 30, 2010 (prepared under Canadian GAAP) and in its condensed interim consolidated financial statements for three months ended July 31, 2011 and 2010 (prepared under IFRS). The Company has also filed an AIF, dated July 21, 2011, which provides detailed information about the Company and its properties. These documents are available on Stornoway's website at www.stornowaydiamonds.com or on its SEDAR Page Site accessed through www.sedar.com.

COMMITMENTS

The Company is committed to minimum future operating lease payments for its office premises and to minimum future financial capital contributions for the construction and maintenance of the Route 167 segment for a maximum of ten years from year 2015 as follows (expressed in thousands of Canadian dollars):

	Operating lease payments	Commitment fee	Route 167		Total
Fiscal year ending April 30, 2013	\$ 454	\$ 1,750	\$ -	\$ -	2,204
Fiscal year ending April 30, 2014	380	1,750	-	-	2,130
Fiscal year ending April 30, 2015	117	1,750	-	-	1,867
Fiscal year ending April 30, 2016	19	-	4,042	-	4,061
Fiscal year ending April 30, 2017	-	-	7,275	-	7,275
Thereafter	-	-	61,430	-	61,430
	\$ 970	\$ 5,250	\$ 72,747	\$ -	78,967

In August 2011, the Company entered into two financing agreements with the Government of Québec by which the Company will contribute to the construction and maintenance costs of the Route 167 extension, the road development project that will provide year round highway access to the Renard Diamond Project by way of the communities of Mistissini and Chibougamau. In two separate agreements executed with the ministère des Ressources naturelles et de la Faune and the ministère des Transports, the Company has agreed to contribute \$44 million to the development of the Route 167 extension, to be amortized over a ten year period and starting in July 2015. The Company's contribution will be financed by Québec at 6.3% and will be conditional upon, amongst other things, the completion of the road on schedule, the receipt of all regulatory approvals for the construction of the Renard Diamond Project and the successful completion of project financing for the Renard Diamond Project. In addition, the Company has agreed to contribute a maximum of \$5,000 per kilometer, or \$1.215 million per year, to the maintenance of the road starting July 1, 2015. It is management's assumption that these conditions will be met, and therefore these commitments have been disclosed.

The Company has a \$100 million credit support agreement with IQ (see "Credit Facility" above) to fund a portion of future construction and development costs at the Renard Diamond Project, under which commitment fee payments equal to 1.75% per annum are payable by the Company. The obligations of IQ will terminate on the earlier to occur of: (a) the date on which the Company notifies IQ in writing that the credit support agreement is terminated; (b) the date of the initial borrowing under the IQ commitment; and (c) April 1, 2015.

In addition, the Company has GICs in the amount of \$328,000 as collateral security for its corporate credit cards and a line of credit of \$8,000 to satisfy exploration bonding requirements. A GIC equivalent to the utilization of the line of credit is provided as collateral security.

OUTSTANDING SHARE CAPITAL

Stornoway's authorized capital is an unlimited number of common shares and an unlimited number of non-voting convertible shares without par value.

As at September 15, 2011, there were 118,619,740 common shares and 22,543,918 non-voting convertible shares issued and outstanding. The non-voting convertible shares have no expiry date and no restrictions except that Diaquem cannot hold more than 25% of Stornoway's voting, common shares.

As at September 15, 2011, the following stock options are outstanding:

Range of Exercise Prices	Number of Options Outstanding	Weighted Average Exercise Price	Year of Expiry	Weighted Average Remaining Contractual Life
\$ 4.08	27,750	\$ 4.08	2011	0.27 years
\$ 2.52 ~ \$ 27.76	1,248,495	\$ 4.68	2012	0.84 years
\$ 0.40 ~ \$ 29.68	980,301	\$ 2.03	2013	2.18 years
\$ 0.40 ~ \$ 19.44	671,025	\$ 1.18	2014	3.07 years
\$ 2.24 ~ \$ 5.36	1,167,600	\$ 2.40	2015	3.91 years
\$ 2.08 ~ \$ 2.50	125,000	\$ 2.50	2016	4.73 years
	<u>4,220,171</u>			

As at September 15, 2011, the following warrants are outstanding:

Number of Warrants	Exercise Price	Expiry Date
26,325	\$ 2.28	December 29, 2011
338,042	\$ 2.00	February 23, 2012
<u>364,367</u>		

TRANSACTIONS WITH RELATED PARTIES

Related party transactions (See Note 11 of the condensed interim consolidated financial statements for the three months ended July 31, 2011 and 2010) are as follows:

a) Key Management Personnel Remuneration

Key management includes the Company's directors and officers. Compensation awarded to key management includes (*expressed in thousands of Canadian dollars*):

	Three Months Ended	
	July 31, 2011	July 31, 2010
Salaries and other short-term employee benefits	\$ 285	\$ 295
Director's fees	12	23
Share-based payments	103	419
	<u>\$ 400</u>	<u>\$ 737</u>

b) Transactions with related parties

The Company entered into the following transactions with related parties not disclosed elsewhere in the Company's condensed interim consolidated financial statements for the three months ended July 31, 2011 and July 31, 2010:

- i) During the period ended July 31, 2011, the Company paid \$8,500 (July 31, 2010 - \$13,500), charged \$8,300 (July 31, 2010 - \$9,700) and included \$1,200 in receivables (April 30, 2011 - accrued as payable \$1,000) for the reimbursement of administrative and technical time to Strongbow Exploration Inc., a company with an officer in common.
- ii) During the period ended July 31, 2011, the Company charged \$4,600 (July 31, 2010 - \$8,300) and included \$15,000 (April 30, 2011 - \$12,000) in receivables for the reimbursement of administrative

and technical time to North Arrow Minerals Inc., (“North Arrow”) a company with an officer in common. In addition, the Company has recorded a receivable of \$125,000 from North Arrow for North Arrow’s share of exploration expenses incurred as at July 31, 2011 on the Hammer property, which is a 75%-25% option agreement between the Company and North Arrow, respectively.

These amounts are non-interest bearing, unsecured and are due on demand. All transactions with related parties have occurred in the normal course of the Company’s operations and are based on agreed upon amounts between the parties.

CRITICAL ACCOUNTING ESTIMATES

The preparation of the Company’s condensed interim consolidated financial statements under IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of expenses during the reporting period. Actual outcomes could differ from these estimates. The condensed interim consolidated financial statements include estimates which, by their nature, are uncertain. The impacts of such estimates are pervasive throughout the condensed interim consolidated financial statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and the revision affects both current and future periods.

Significant assumptions about the future and other sources of estimation uncertainty that management has made at the balance sheet date, that could result in a material adjustment to the carrying amounts of assets and liabilities, in the event that actual results differ from assumptions made, but are not limited to, the following:

- the estimated useful lives of property, plant and equipment which are included in the condensed interim consolidated balance sheets, the componentization of property, plant and equipment and the related amortization included in the condensed interim consolidated statements of loss;
- the inputs used in accounting for share-based payments (warrants and options) in the condensed interim consolidated statements of loss;
- the provision for income taxes which is included in the condensed interim consolidated statements of loss and the composition of deferred income tax liabilities included in the condensed interim consolidated balance sheet at July 31, 2011;
- the inputs used in determining the recoverable amounts of exploration and evaluation assets, if an impairment trigger exists;
- the inputs used in determining asset retirement obligations included in the condensed interim consolidated balance sheets;
- the inputs used in determining the various commitments and contingencies accrued in the condensed interim consolidated balance sheets; and
- the going concern assumption.

Please refer to Note 2 of the condensed interim consolidated financial statements of the Company for the three months ended July 31, 2011 and 2010 for a description of all significant accounting policies.

Impairment of long-lived assets

The Company’s management reviews the carrying value of the Company’s long-lived assets when there are events or circumstances that may indicate impairment. IAS 36 *Impairment of Assets* uses a one-step approach for both identifying and measuring impairments, which is based on comparing the carrying value to the recoverable amount. The recoverable amount is the higher of fair value less selling costs and value in use, which is based on discounted cash flows.

In making an assessment of the potential impairment of the Company’s long-lived assets, management has used estimates of future mineral prices, mineral resource quantities, and operating, capital and reclamation costs, as well as making judgments on the potential of certain projects based on the available information at the balance sheet date. These estimates are subject to certain risks and uncertainties that may affect the determination of the recoverability of the Company’s long-lived assets. Although management has made its best estimates of potential impairment, the

interpretation of these factors is subjective and will not necessarily result in precise determinations. Should an underlying assumption change, the resulting estimates could change by a material amount.

Exploration and evaluation assets mainly include capitalized acquisition costs and are the Company's most significant long-lived asset. The Company's exploration and evaluation assets are at three different stages:

- a) development (Renard);
- b) advanced exploration (Aviat, Churchill, Qilalugaq and Timiskaming); and
- c) grass-roots exploration.

The Company expenses exploration costs but uses the guidance set out in IFRS 6, Exploration for and evaluation of mineral resources, as the basis for determining whether its grass-roots properties should be written off. Paragraph 20 sets out factors that may indicate the need for a write-down:

- a) the period for which the entity has the right to explore in the specific area has expired during the period or will expire in the near future, and is not expected to be renewed.
- b) substantive expenditure on further exploration for and evaluation of mineral resources in the specific area is neither budgeted nor planned.
- c) exploration for and evaluation of mineral resources in the specific area have not led to the discovery of commercially viable quantities of mineral resources and the entity has decided to discontinue such activities in the specific area.
- d) sufficient data exist to indicate that, although a development in the specific area is likely to proceed, the carrying amount of the exploration and evaluation asset is unlikely to be recovered in full from successful development or by sale.

Using these conditions as a guideline for estimating whether an impairment exists on its grass-roots properties, and based on the Company's plans to further evaluate and advance these properties by analyzing results received to-date, management has determined that certain non-material amounts related to the Company's grass-roots exploration and evaluation assets as of July 31, 2011 and as of the report date should be written-off, as no future exploration work is planned for the foreseeable future and limited exploration work has been carried out on the properties during the last three years. During the period ended July 31, 2011, the Company wrote-off exploration and evaluation assets of \$49,000 where no future exploration programs were planned for the foreseeable future (July 31, 2010 – \$Nil).

Asset retirement obligations

Asset retirement obligations are an obligation to incur restoration, rehabilitation and environmental costs that arise when environmental disturbance is caused by the exploration, development or ongoing production of a mineral property interest. Such costs arising for the decommissioning of plant and other site preparation work, discounted to their net present value, are provided for and capitalized at the start of each project to the carrying value of the asset, as soon as the obligation to incur such costs arises. Discount rates using a pre-tax market based discount rate that reflects the time value of money are used to calculate the net present value. The related liability is adjusted for each period for the unwinding of the discount rate and for changes to the pre-tax market based discount rate and amount or timing of the underlying cash flows needed to settle the obligation. The Company's asset retirement obligation relates to activities at its Renard Project in Quebec.

The Company has recorded an asset retirement obligation, which reflects the present value of the estimated amount of undiscounted cash flow required to satisfy the asset retirement obligation in respect of the Renard Diamond Project in Quebec. The primary component of this obligation is the removal of equipment currently used at the site. If the Company decides not to go into production on the property, or is unable to further develop the Renard Diamond Project for any reason, it is assumed that the asset retirement obligation will be incurred in 2011. Should the Company decide to proceed with a production decision on the Renard Diamond Project, the obligation will be realized further into the future. The pre-tax market-based discount rate at which the estimated cash flows have been discounted to arrive at the obligation is 1.39%. The discounted amount of inflation-adjusted estimated future cash flows is \$1,443,000.

Diamond Inventory

The fair value of the Company's diamond inventory has been estimated and recorded using a base case diamond model price resulting from a diamond valuation exercise in May 2011 in Antwerp. As no quoted market prices for rough diamonds are readily available, the base case model price used to estimate fair value at the time of acquisition

could vary significantly from the actual sales price achieved. At the present time, the Company has no plans to dispose of its rough diamond inventory and has classified it as a long-term asset.

Share-based payments

The Company's current stock price and the volatility of the Company's stock price will affect the estimates made for share-based payments. The volatility of the Company's stock price and the stock price at the grant date have the most significant impact on the estimate of fair value of share-based payments. The Company expenses share-based payments for its corporate, administrative, exploration and technical staff.

Share-based payments are accounted for using the fair value based method. Under the fair value based method, compensation cost is measured at fair value of the options at the date of grant and is expensed over the vesting period of the award. The Company estimates the fair value using the Black- Scholes option-pricing model. The key assumptions used during the Current Period were: a risk-free interest rate of 2.0%, a dividend yield of 0%, an expected volatility of 83% and expected term of stock options of 5 years. The key assumptions used during the year ended April 30, 2011 were: a risk-free interest rate of 1.7% ~ 2.7%, a dividend yield of 0%, an expected volatility of 84% ~ 94% and expected term of stock options of 3 ~ 5 years. Option pricing models require the input of highly subjective assumptions including the expected price volatility. Changes in the subjective input assumptions can materially affect the fair value estimate, and therefore the existing models do not necessarily provide a reliable single measure of the fair value of the Company's stock options.

During the Current Period, the Company recorded a share-based payments expense of \$160,000 (Comparative Period - \$312,000). The Company granted 75,000 stock options to directors during the Current Period. The options have an exercise price of \$2.08 and expire five years from the grant date. The Company used the Black-Scholes Option Pricing Model to estimate a fair value of \$103,000 for this grant. During the year ended April 30, 2011, the Company granted options to purchase up to 1,195,000 shares of the Company's stock to directors, officers, employees and non-employees at an exercise price range of \$2.24 – 2.60. The Company used the Black-Scholes Option Pricing Model to estimate a fair value of \$1.8 million for these grants.

CHANGES IN ACCOUNTING POLICIES

International financial reporting standards

Effective the first quarter of 2012, the Company began preparing its financial statements in accordance with IFRS. Reconciliations, descriptions and explanations of how the transition to IFRS has affected the reported balance sheet, financial performance and cash flows of the Company are provided in Note 16, "First Time Adoption of IFRS" to the condensed interim consolidated financial statements for the three months ended July 31, 2011. This note also includes reconciliations of equity and comprehensive income (loss) for comparative periods reported under Canadian GAAP with amounts reported for those periods under IFRS.

The Company has changed certain accounting policies to be consistent with IFRS as it is expected to be effective or available on April 30, 2012, the Company's first annual IFRS reporting date. The changes to its accounting policies have resulted in certain changes to the recognition and measurement of assets, liabilities, equity, and expenses within its financial statements.

The following summarizes the significant changes to the Company's accounting policies on adoption of IFRS.

Accounting Policy Area	Description
(i) Property, plant and equipment (IAS 16)	<p>The Company will continue to record its property, plant and equipment assets at cost, less accumulated amortization.</p> <p>IFRS requires that part of an item of PPE with a cost that is significant in relation to the total cost of the asset shall be depreciated separately. Management has reviewed the Company's assets and has identified those assets where the cost of one or more of the components is significant in relation to the total cost of the</p>

	asset. Management has estimated a revised depreciation expense accordingly.
(ii) Income taxes (IAS 12)	Under Canadian GAAP, the Company recognized a future income tax liability on temporary differences arising on the initial recognition of mineral property interests (where the fair value of the asset acquired exceeded its tax basis) in a transaction which was not a business combination and affected neither accounting profit or loss nor taxable profit or loss. IAS 12, "Income Taxes" does not permit the recognition of deferred taxes on such transactions. As of May 1, 2010, the Company has derecognized the impacts of all future income tax liabilities which had previously been recognized on the initial acquisition of the mineral property interests through transactions deemed not to be business combinations and affecting neither accounting profit or loss nor taxable profit or loss.
(iii) Decommissioning liabilities (IAS 37)	At May 1, 2010, the Company did an analysis of the discount rate used to present value its ARO liability. Under Canadian GAAP, a change in the discount rate alone did not result in a re-measurement of the ARO liability. Under IFRS, IAS 37, "Provisions, Contingent Liabilities and Contingent Assets" a change in the discount rate will result in a change in the measurement of the provision. As a result, the ARO liability recorded in 2010 has been re-measured using the pre-tax market based discount rate in effect at year end and an adjustment has been recorded to the corresponding asset.
(iv) Share-based payments (IFRS 2)	Under Canadian GAAP, the Company used the straight-line method of calculating vested options. The fair value of share-based awards with graded vesting was calculated as one grant and the resulting fair value was recognized on a straight-line basis over the vesting period. Also, forfeitures of awards were recognized as they occurred. Under IFRS, each tranche of an award with different vesting dates is considered a separate grant for the calculation of fair value, and the resulting fair value is recognized using the graded-vesting method. Also, forfeiture estimates are recognized on the grant date and revised for actual experiences in subsequent periods.
(v) Asset impairment (IAS 36)	The Company's exploration and evaluation assets are its most significant long-lived asset and must be reviewed for impairment when circumstances suggest that the carrying values may be impaired. There was no impact on the condensed interim consolidated financial statements.
(vi) Flow-through shares	Flow-through shares are a unique Canadian tax incentive which is the subject of specific guidance under Canadian GAAP, however there is no equivalent IFRS guidance. Therefore, the Company intends to adopt a policy whereby the premium paid for flow through shares in excess of the market value of the shares without the flow through features at the time of issue is credited to other liabilities and included in income as a deferred income tax recovery at the time the qualifying expenditures are made.

First-Time Adoption of IFRS

"First-Time Adoption of International Financial Reporting Standards" ("IFRS 1"), provides entities adopting IFRSs for the first time with a number of optional exemptions and mandatory exceptions, in certain areas, to the general requirement for full retrospective application of IFRSs. The most significant IFRS 1 exemptions that applied to the Company upon adoption are summarized as follows:

1. Use the mandatory IFRS 1 election for estimates. An entity's estimates under IFRS at the date of transition to IFRS must be consistent with estimates made for the same date under previous GAAP, unless there is objective evidence that those estimates were in error;
2. Choose the IFRS 1 election for IFRS 2 – Share-Based Payments, which allows an exemption from retroactive restatement of equity instruments granted after November 2, 2002, but vested prior to transition;
3. Choose not to use the IFRS 1 election for IAS 16 – Property, Plant and Equipment, which allows an entity to measure an item of PPE at its fair value at the date of transition and use that fair value as its deemed cost;

4. Choose to use the IFRS 1 election for IFRIC 1 – Changes in Existing Decommissioning, Restoration and Similar Liabilities, which alleviates an entity from re-measuring provisions at every reporting date from the inception of the provision to the IFRS transition date;
5. Choose to use the IFRS 1 election for IFRS 3R – Business Combinations, which allows a first-time adopter of IFRS to not apply IFRS 3R retrospectively to past business combinations;
6. Choose to use the IFRS 1 election for IAS 32 – Borrowing Costs, which allows a first-time adopter to elect to apply this standard prospectively to qualifying assets, either on the date of transition or at any date prior to transition.

Impact of Adopting IFRS on the Company's Business

The adoption of IFRS has resulted in some changes to the Company's accounting systems and business processes. For all changes to policies and procedures that were identified, the effectiveness of internal controls over financial reporting and disclosure controls and procedures was assessed and changes were implemented as appropriate. The Company applied its existing control framework to the IFRS changeover process and no significant changes were identified. The Company has not identified any contractual arrangements that are significantly impacted by the adoption of IFRS.

The Company's staff and advisers involved in the preparation of financial statements have been appropriately trained on the relevant aspects of IFRS and the changes to accounting policies.

The Board of Directors and Audit Committee have been regularly updated throughout the Company's IFRS transition process, and are aware of the key aspects of IFRS affecting the Company. The Audit Committee reviewed and approved the elections taken by the Company upon transition to IFRS, as well as the accounting policies adopted by the Company.

The review phase of the Company's transition to IFRS involves continuous monitoring of changes in IFRS. IFRS accounting standards, and the interpretation thereof, are constantly evolving. As a result, the Company will continue to monitor and evaluate IFRS accounting developments. The review phase will continue through the Company's fiscal year ended April 30, 2012 and beyond.

New accounting standards and interpretations

In May 2011, the IASB issued the following standards which have not yet been adopted by the Company: IFRS 9, Financial Instruments (IFRS 9), IFRS 10, Consolidated Financial Statements (IFRS 10), IFRS 11, Joint Arrangements (IFRS 11), IFRS 12, Disclosure of Interests in Other Entities (IFRS 12), IAS 27, Separate Financial Statements (IAS 27), IFRS 13, Fair Value Measurement (IFRS 13) and amended IAS 28, Investments in Associates and Joint Ventures (IAS 28). Also in June 2011, the IASB amended IAS 19, Employee Benefits (IAS 19) and IAS 1, Presentation of Financial Statements (IAS 1), which has not yet been adopted by the Company. Each of the new standards is effective for annual periods beginning on or after January 1, 2013 with early adoption permitted. The Company has not yet begun the process of assessing the impact that the new and amended standards will have on its financial statements or whether to early adopt any of the new requirements. The following is a brief summary of the new standards:

IAS 1 – Presentation of Financial Statements

This standard requires companies preparing financial statements under IFRS to group items within Other Comprehensive Income ("OCI") that may be reclassified to the profit or loss. The amendments also reaffirm existing requirements that items in OCI and profit or loss should be presented as either a single statement or two consecutive statements. The amendments to IAS 1 are set out in Presentation of Items of Other Comprehensive Income and are effective for fiscal years beginning on or after January 1, 2013.

IAS 19 - Post-Employment Benefits

In June 2011, the IASB issued an amended version of IAS 19, Employee Benefits ("IAS 19"). The amendments to IAS 19 are meant to improve the quality, transparency and comparability of information presented for postemployment benefits. For defined benefit plans, the amendments eliminate the option to defer actuarial gains and losses on the balance sheet through the "corridor method". The amendments also require any remeasurement

gains or losses, including actuarial gains and losses, to be recognized immediately and presented in other comprehensive income, eliminating the option to recognize and present these through the income statement. Additional disclosures will also be required to present better information about the characteristics, amounts recognized, and risks related to defined benefit plans. The amendments to IAS 19 are effective for financial years beginning on or after January 1, 2013 with earlier adoption permitted. The Company does not have post-employment benefits thus this policy will not have an impact on the Company's financial statements.

IFRS 9 – Financial Instruments – classification and measurement

This is the first part of a new standard on classification and measurement of financial assets that will replace IAS 39, Financial Instruments: Recognition and Measurement. IFRS 9 has two measurement categories: amortized cost and fair value. All equity instruments are measured at fair value. A debt instrument is recorded at amortized cost only if the entity is holding the instrument to collect contractual cash flows and the cash flows represent principal and interest. Otherwise it is recorded at fair value through profit or loss.

IFRS 10 – Consolidation

IFRS 10 requires an entity to consolidate an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Under existing IFRS, consolidation is required when an entity has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. IFRS 10 replaces SIC-12 Consolidation—Special Purpose Entities and parts of IAS 27 Consolidated and Separate Financial Statements.

IFRS 11 - Joint Arrangements

IFRS 11 requires a venturer to classify its interest in a joint arrangement as a joint venture or joint operation. Joint ventures will be accounted for using the equity method of accounting whereas for a joint operation the venturer will recognize its share of the assets, liabilities, revenue and expenses of the joint operation. Under existing IFRS, entities have the choice to proportionately consolidate or equity account for interests in joint ventures. IFRS 11 supersedes IAS 31, Interests in Joint Ventures, and SIC-13, Jointly Controlled Entities—Non-monetary Contributions by Venturers.

IFRS 12 – Disclosure of Interests in Other Entities

IFRS 12 establishes disclosure requirements for interests in other entities, such as joint arrangements, associates, special purpose vehicles and off balance sheet vehicles. The standard carries forward existing disclosures and also introduces significant additional disclosure requirements that address the nature of, and risks associated with, an entity's interests in other entities.

IFRS 13 - Fair Value Measurement

IFRS 13 is a comprehensive standard for fair value measurement and disclosure requirements for use across all IFRS standards. The new standard clarifies that fair value is the price that would be received to sell an asset, or paid to transfer a liability in an orderly transaction between market participants, at the measurement date. It also establishes disclosures about fair value measurement. Under existing IFRS, guidance on measuring and disclosing fair value is dispersed among the specific standards requiring fair value measurements and in many cases does not reflect a clear measurement basis or consistent disclosures.

Amendments to Other Standards

In addition, there have been amendments to existing standards, including IAS 27, Separate Financial Statements (IAS 27), and IAS 28, Investments in Associates and Joint Ventures (IAS 28). IAS 27 addresses accounting for subsidiaries, jointly controlled entities and associates in non-consolidated financial statements. IAS 28 has been amended to include joint ventures in its scope and to address the changes in IFRS 10 – 13.

FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The Company's financial instruments consist of cash and cash equivalents, short-term deposits, other receivables, investments, trade accounts payable, accrued liabilities and provisions and amounts due to related parties. The carrying value of cash and cash equivalents, short-term deposits, other receivables, trade accounts payable, accrued

liabilities and provisions and amounts due to related parties approximate their fair values due to their immediate or short-term maturity. Investments are recorded at fair value based on the quoted market prices in active markets at the balance sheet date, which is consistent with Level 1 of the fair value hierarchy. Short-term deposits are recorded consistent with Level 2 of the hierarchy.

The fair values of financial instruments at July 31, 2011 and April 30, 2011 are summarized as follows (*expressed in thousands of Canadian dollars*):

	July 31, 2011		April 30, 2011	
	Carrying amount	Fair value	Carrying amount	Fair value
Financial Assets	\$	\$	\$	\$
<i>Held-for-trading</i>				
Short-term deposits	11,816	11,816	11,777	11,777
<i>Loans and Receivables</i>				
Cash and cash equivalents	13,208	13,208	22,745	22,745
Other receivables	1,120	1,120	955	955
<i>Available for sale</i>				
Investments	202	202	242	242
Financial Liabilities				
Trade accounts payable, accrued liabilities, provisions and due to related parties	4,374	4,374	4,790	4,790

Unless otherwise noted, it is management's opinion that the Company is not exposed to significant interest, foreign currency or credit risks arising from these financial instruments.

The Company is exposed to a variety of financial risks by virtue of its activities, including credit risk, interest rate risk and liquidity risk. The Company has limited exposure to foreign currency risk as greater than 99% of its assets and liabilities are denominated in Canadian dollars. The Company's objective with respect to risk management is to minimize potential adverse effects on the Company's financial performance. The Company's Board of Directors provides direction and guidance to management with respect to risk management. Management is responsible for establishing controls and procedures to ensure that financial risks are mitigated to acceptable levels.

Credit risk

Credit risk is the risk of financial loss to the Company if a counter-party to a financial instrument fails to meet its contractual obligations. The Company manages credit risk by investing its excess cash in short-term investments with an investment grade rating of "AAA" (R-1 high for money market securities) or better, issued by a Canadian chartered bank. The Company is exposed to credit risk by virtue of its receivables from companies with which it has exploration agreements or options (11% of receivables). Other miscellaneous receivables total approximately 3% of the Company's receivables, while the remainder of the Company's receivables at the balance sheet date (86% of receivables totalling \$959,300 as at July 31, 2011) consist of federal and provincial sales tax refunds where management believes the risk of loss to be remote. The maximum exposure to credit risk at the reporting date is the carrying value of the Company's financial assets.

Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in market interest rates. Financial assets and liabilities with variable interest rates expose the Company to interest rate risk with respect to its cash flow. The risk that the Company will realize a loss as a result of a decline in the fair value of any short-term investment included in cash and cash equivalents is limited because these investments, although readily convertible into cash, are generally held-to-maturity. As of July 31, 2011, management estimates that if interest rates had changed by 1% for those funds invested in GICs, and 0.2% for the other cash equivalents assuming all other variables remained constant, the impact on the Company's loss for the three months ended July 31, 2011 would have been approximately \$43,000.

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its obligations as they become due. The Company's ability to continue as a going concern is dependent on management's ability to raise the funds required through future equity financings, asset sales or exploration option agreements, or a combination thereof.

The Company has no regular cash flow from its operating activities. The Company manages its liquidity risk by forecasting cash flow requirements for its planned exploration and corporate activities and anticipating investing and financing activities. Failure to realize additional funding, as required, could result in the delay or indefinite postponement of further exploration and development of the Company's properties. As at July 31, 2011, the Company had cash and cash equivalents and short-term deposits of \$25.0 million (April 30, 2011 - \$34.5 million), as well as other receivables of \$1.1 million (April 30, 2011 - \$955,000) to settle current liabilities of \$4.4 million (April 30, 2011 - \$4.8 million).

DISCLOSURE CONTROLS

The Company's Chief Executive Officer and Chief Financial Officer (the "Certifying Officers") are responsible for establishing and maintaining disclosure controls and procedures ("the Procedures") which provide reasonable assurance that information required to be disclosed by the Company under provincial or territorial securities legislation (the "Required Filings") is reported within the time periods specified. Without limitation, the Procedures are designed to ensure that material information relating to the Company is accumulated and communicated to management, including its Certifying Officers, as appropriate to allow for timely decisions regarding the Required Filings.

The Certifying Officers evaluated the effectiveness of the Procedures for the period ended July 31, 2011 and have concluded that the Procedures in place as of the end of the fiscal period covered by the Required Filings are effective in providing reasonable assurance that material information relating to the Company is accumulated and communicated to management and reported within the time periods specified.

INTERNAL CONTROLS OVER FINANCIAL REPORTING

The Certifying Officers are responsible for designing a system of internal controls over financial reporting, as defined under National Instrument 52-109, which provides reasonable assurance regarding the reliability of the Company's financial reporting and the preparation of its condensed interim consolidated financial statements in accordance with IFRS.

The Certifying Officers have evaluated, or caused to be evaluated under their supervision, the effectiveness of the Company's internal controls over financial reporting as of July 31, 2011 and have concluded that the Company's internal controls over financial reporting are effective, and are sufficiently designed to provide reasonable assurance regarding the reliability of the Company's financial reporting and the preparation of its consolidated financial statements for external purposes in accordance with IFRS. This evaluation was completed using the framework and criteria established in the Internal Control – Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). There have been no changes in internal control over financial reporting during the period ended July 31, 2011 that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

APPROVAL

The Board of Directors of Stornoway has approved the disclosure contained in this Interim MD&A. A copy of this Interim MD&A will be provided to anyone who requests it.

ADDITIONAL INFORMATION

Additional information relating to Stornoway is on SEDAR at www.sedar.com.