

DIADEM RESOURCES LTD.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

NOVEMBER 30, 2004

Overview

During the fiscal year ended May 31, 2004, management was successful in funding the Company's re-directed exploration programs and day-to-day operations with over \$1.9 million of fresh capital.

Since year end, Diadem has raised a further \$3,201,200 through the private placement of 34,133,331 Common Shares. These funds have improved working capital and funded the Company's on-going exploration and corporate costs. Management is in discussions to avail the Company of further flow-through placements to finance exploration of its Franklin, Attawapiskat and Otish Mountain Diamond Projects.

Results of Operations

The Company commenced its Otish Mountains exploration program during August 2003 under the direction of Roscoe Postle & Associates Inc. A total of 518 till samples were taken and were processed to determine the presence of kimberlite indicator minerals and diamonds. Through November 30, 2004, the Company had expended \$395,203 to acquire and \$732,671 to explore and assess its Otish Mountains claims.

Effective November 26, 2003, the Company entered into an agreement to form a joint venture ("Franklin Diamond Project") with Darnley Bay Resources Ltd. ("DBR") for diamond exploration in an area near Paulatuk in the Northwest Territories. During March and April 2004, the Company staked 459 claims comprising an area of approximately 1,120,071 acres. During May and June 2004, the Company completed a ground magnetic survey over 22 potential kimberlite targets, as well as one known kimberlite, in the Parry Peninsula kimberlite field. The cost of the land assembly and exploration was \$1,250,958 through May 31, 2004. These costs are considered part of the Company's cost of earn-in on the Franklin Project. A further amount of \$30,490 was expended on exploration during the first half of fiscal 2005.

Subsequent to November 30, 2004, the Company paid \$15,000 to enter into an option agreement to acquire a 51% interest in the entire Attawapiskat diamond property of Vault Minerals Inc. The property consists of 219 contiguous claims (3,403 claim units) covering over 53,000 hectares located from 40 to 70 kms southeast of the Attawapiskat cluster of 19 kimberlite pipes (16 held by De Beers) in the James Bay Lowlands area of Northern Ontario. The largest pipe in the cluster, *Victor*, is undergoing final feasibility studies prior to an anticipated De Beers production decision.

During December 2004, the Company made the decision to proceed with phased exploration of the property. Diadem is required to expend at least \$500,000 by December 1, 2005 (of which \$300,000 is committed to be spent by April 1, 2005) on exploration and related costs with a further \$500,000 to be expended after that date and by December 1, 2006. If Diadem exercises its option on or before December 1, 2006, a 51/49 joint venture will be formed and Diadem will be the operator.

General corporate costs were \$137,891 during the second quarter of fiscal 2005 compared to \$143,370 during the second quarter of fiscal 2004. For six months, general corporate costs were \$252,084 compared to \$218,158 during the corresponding period of fiscal 2004. The increase principally results from renewed financing and acquisition activity. During the second quarter 2005, the Company recognized a \$257,500 non-cash charge to operations in recognition of stock options granted. The cost of financial advisory services rendered to the Company include a \$62,500 non-cash charge resulting from the issuance of 2,500,000 warrants in respect of services provided during the period July 1, 2004 to November 30, 2004. Management compensation approximates 77% (2004-61%) of general corporate costs, excluding the non-cash stock option benefit. Certain management costs have been raised to industry norms as a consequence of increased activity and the need to retain experienced management. Costs associated with the shareholder relations and regulatory compliance function approximate 28% (2004-30%) of general corporate costs.

Interest and debt financing costs totalled \$22,844 during the first half of fiscal 2005 (2004-\$31,596). Interest costs decreased as a consequence of settling the debenture and the long-term debt incurred during 2003 to fund a

security deposit lodged in support of assessment work to be conducted on the Franklin Diamond Project in the Northwest Territories.

As at November 30, 2004, the loan receivable from DBR, aggregating \$66,352, is comprised of recoverable interest and finance fees and DBR's share of joint venture costs. Approximately \$2,265 of interest costs were charged to the loan receivable from DBR.

As a result of its increased activities, the Company recorded a net loss of \$555,885 or \$0.006 per share during the second quarter of fiscal 2005 compared to a net loss of \$91,850 or \$0.002 per share during the second quarter of fiscal 2004. The Company recorded a net loss of \$692,519 or \$0.008 per share during the first half of fiscal 2005 compared to a net loss of \$182,748 or \$0.003 per share during the first half of fiscal 2004.

Capital Resources and Liquidity

The consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles and on the assumption that Diadem will be able to realize the carrying value of its assets and discharge its liabilities in the normal course of business as a going concern.

There is uncertainty about the Company's ability to realize the carrying value of its assets and discharge its liabilities as they come due. The ability of the Company to continue as a going concern is dependent upon, among other things, being able to obtain additional financing and maintain positive cash flows from operations. During the second quarter of 2004, the Company eliminated \$790,000 of debt from its balance sheet and reduced outstanding current claims against the Company. This was accomplished following a successful private placement which netted the Company \$2,068,000.

The Company has reported significant losses for several years and has no mining operations and is considered a development stage company. At November 30, 2004, the Company has working capital of \$86,640 and an accumulated deficit of \$22,948,970. There is no assurance the Company can continue to finance its operations through the capital markets.

During December 2004, the Company placed 7,554,670 Units at a price of \$0.15 per Unit for gross proceeds of \$1,133,200. Each Unit consisted of one flow-through common share and one-half of one flow-through common share purchase warrant. Each warrant entitles the holder to purchase one additional flow-through common share at a price of \$0.20 per share for a period of nine months after the closing of the private placement. A total of \$46,396 in cash commissions was paid and 309,307 non flow-through broker warrants were issued, exercisable for a period of nine months from the date of closing. The funds will be used to incur Canadian exploration expense on its Franklin, Attawapiskat and Otish Mountain diamond projects, which expense will be renounced to investors.

The Company formed a wholly-owned subsidiary, Diadem Explorations Inc. ("DEI"), to implement the acquisition of an aggregate of 2,064 mining claims in the Otish Mountains region of Quebec. The acquisitions were effected August 29, 2003 by issuing Series B First Preferred Shares of DEI having a value of \$384,248, which was equal to the historical staking costs and work carried out on the claims by the vendors. The Series B First Preferred Shares are exchangeable, at any time after December 31, 2004 and up to December 31, 2006, into 3,256,338 Common Shares of the Company at the option of either the Company or the vendor based on a weighted average trading price of \$0.118 per share during the three month period ended December 31, 2004. During January 2005, two vendors exchanged 23,952 Series B First Preference Shares for 202,985 common shares of the Company.

Exploration Projects

Franklin Diamond Project

In May, 2004 twenty-two airborne targets, including one known kimberlite and three previously surveyed targets that were not GPS referenced, were surveyed by ground magnetometer by JVX Ltd. using the JVX ROVER sled-mounted magnetometer system towed behind a snowmobile. Horizontal control was provided by differential GPS and positioning accurate within 2 meters. A total of 19 grids were established and a total of 487.5 km of line surveyed with readings obtained every 2.5 meters. Of the targets evaluated a total of at least 8 high priority drill targets have been identified including the three targets that had been previously magnetically surveyed but not GPS located. Three of the targets exhibit geophysical characteristics consistent with known kimberlites on the property. Of particular interest are the five remaining targets, of which three exist as circular magnetic lows and

two as circular magnetic highs. The inference of the occurrence of both magnetic lows and highs is there may be potential for kimberlites of differing ages. Survey data continues to be further processed and evaluated. Geophysical modelling of selected priority targets will be completed as a prelude to drill testing targets. Management anticipates funding further exploration of the Franklin Diamond Project primarily through the issuance of flow-through shares.

Attawapiskat Diamond Project

On November 29, 2004 Diadem announced that it had entered into an option agreement to acquire a 51% interest in the entire Attawapiskat diamond property of Vault Minerals Inc. The property consists of 219 contiguous claims (3,403 claim units) covering over 53,000 hectares located from 40 to 70 kms southeast of the Attawapiskat cluster of 19 kimberlite pipes (16 held by De Beers) in the James Bay Lowlands area of Northern Ontario. Diadem is required to expend at least \$500,000 by December 1, 2005 (of which \$300,000 is committed to be spent by April 1, 2005) on exploration and related costs with a further \$500,000 to be expended after that date and by December 1, 2006. Furthermore, option payments of \$100,000 are required during the option period including committed cash payments totalling \$15,000 on or before April 1, 2005. If Diadem exercises its option on or before December 1, 2006, a 51/49 joint venture will be formed and Diadem will be the operator. Subsequent to November 30th Diadem entered into an agreement to complete an airborne geophysical survey over the property which, if successfully completed prior to April 1, 2005, would, along with project support costs and related project expenditures, fulfill Diadem's obligation to expend \$300,000 prior to April 1, 2005.

Otish Diamond Project

Diadem's widespread property package offers an opportunity to assess the prospectivity of the entire Otish region which has established diamond potential. Outside of Ashton Mining's Foxtrot property area, little in the way of intensive exploration work has been carried out. Follow-up work is budgeted for the testing of 10 anomalous targets. This work would initially include detailed airborne magnetometer surveys to identify priority targets for detailed ground work to include ground geophysics and diamond drilling. Management anticipates funding further exploration of the Otish Diamond Project primarily through the issuance of flow-through shares.

Leek Springs Diamond Project

The Company currently has a 43.8% vested interest in and holds an option to acquire up to a 57.9% interest in 125 unpatented mining claims covering approximately 2,500 acres in the Leek Springs area of Eldorado County, California. This option was granted by the Silverstone Prospecting Syndicate ("SPS") which holds the remaining interest in the mining claims.

To earn the final 14.1% interest in the mining claims, the Company needed to incur approximately US\$2,000,000 on further exploration of the Leek Springs claims by December 31, 2004. The Company is in discussions with SPS to restructure ownership of the project.

Risks

There is no assurance that management can continue to finance its operations. The consolidated financial statements do not reflect adjustments to the carrying value of assets and liabilities that would be necessary if the going concern assumption were not appropriate. The Company's assets are subject to the risk of increases in taxes and royalties, renegotiation of contracts and currency exchange fluctuations. Operational risks include finding and developing economic ore reserves. Diadem is subject to various regulatory risks, many of which also are beyond the control of the Company.

Paul A. Carroll
Chairman of the Board and
Chief Executive Officer

David J. Layman
Vice-President, Finance

January 27, 2005