

## **SHEAR MINERALS LTD.**

### **MANAGEMENT DISCUSSION AND ANALYSIS**

**May 31, 2006**

#### **GENERAL**

This management discussion and analysis (“MD&A”) supplements, but does not form part of, the unaudited interim consolidated financial statements and notes for the periods ended May 31, 2006. The following information, prepared as of July 25, 2006, should be read in conjunction with those statements, which have been prepared in accordance with Canadian generally accepted accounting principles (“GAAP”). All amounts have been expressed in Canadian dollars unless otherwise indicated. Additional information related to the Company can be found on SEDAR at [www.sedar.com](http://www.sedar.com).

#### **FORWARD-LOOKING INFORMATION**

The following MD&A is management’s assessment of the Company’s operations and financial results, together with future prospects. Certain statements contained in the following MD&A are considered forward-looking statements. Such forward-looking statements involve a number of known and unknown risks, uncertainties and other factors which may cause the performance and actual results of the Company to be materially different from any future results expressed or implied.

#### **DESCRIPTION OF BUSINESS**

Shear Minerals Ltd. (“Shear” or the “Company”) is an exploration stage company focussed on diamond exploration. The Company acquires and explores mineral properties located primarily in the Northwest and Nunavut Territories, Alberta, Saskatchewan and Alaska. The Company is a reporting issuer in Alberta and British Columbia and trades on the TSX Venture Exchange under the symbol SRM.

#### **EXPENSES**

The Company’s administrative costs increased to \$146,344 for the three months ended May 31, 2006 compared to \$140,849 for the three months ended May 31, 2005.

General and administrative expenses totalled \$63,742 for the three months ended May 31, 2006, a decrease of \$415 from the prior year. General and administrative expenses consisted of corporate travel and tradeshow of \$16,701 (2005 - \$19,021), office expenses of \$15,133 (2005 - \$23,764), administrative payroll of \$14,538 (2005 - \$10,587), shareholder communications and promotion of \$9,702 (2005 - \$4,205), regulatory and transfer fees of \$4,875 (2005 - \$3,659), and other expenses of \$2,794 (2005 - \$2,921).

In the three months ended May 31, 2006, the Company also incurred management fees of \$22,500 (2005 - \$21,000), professional fees of \$36,041 (2005 - \$24,809), consulting fees of \$17,400 (2005 - \$27,300), and amortization of \$6,661 (2005 - \$3,583).

The Company’s administrative costs decreased to \$279,269 for the six months ended May 31, 2006 from \$389,874 for the six months ended May 31, 2005. The decrease is primarily due to

share based compensation. \$17,500 in share based compensation was charged to administrative expenses in the six months ended May 31, 2006, compared to \$120,725 in the six months ended May 31, 2005.

General and administrative expenses totalled \$148,202 for the six months ended May 31, 2006, a decrease of \$10,824 from the prior period. General and administrative expenses consisted of corporate travel and tradeshows of \$45,434 (2005 - \$37,842), office expenses of \$40,027 (2005 - \$44,378), administrative payroll of \$32,442 (2005 - \$41,091), shareholder communications and promotion of \$12,238 (2005 - \$23,428), regulatory and transfer fees of \$13,036 (2005 - \$8,663), and other expenses of \$5,025 (2005 - \$3,624).

In the six months ended May 31, 2006, Shear incurred management fees of \$44,500 (2005 - \$143,225), professional fees of \$41,290 (2005 - \$30,464), consulting fees of \$32,400 (2005 - \$49,994), and amortization of \$12,877 (2005 - \$7,165). The decrease in management fees and consulting fees is primarily due to share based compensation of \$102,500 and \$16,325, respectively, in the six months ended May 31, 2005. No share based compensation was charged to these accounts in the six months ended May 31, 2006.

## **NET LOSS**

Shear incurred a net loss of \$75,480 (2005 - \$155,011) for the three months ended May 31, 2006, a reduction of \$79,531 from the prior year. This reduction is primarily due to a recovery of write down of short-term investments of \$11,012 in the current period compared to a write down of short-term investments of \$54,430 in the comparative quarter.

In the six months ended May 31, 2006, Shear incurred a net loss of \$177,466 compared with a net loss of \$340,141 in the comparative period, a decrease of \$162,675. The reduction is primarily due to \$120,725 in share based compensation expense that was recorded in the comparative period versus only \$17,500 in the current period. In addition, a recovery of write down of short-term investments of \$20,104 was recorded in the six months ended May 31, 2006, compared to a write down of short-term investments of \$39,756 in the comparative period.

## SUMMARY OF QUARTERLY RESULTS

The following table sets out selected unaudited quarterly financial information of Shear and is derived from unaudited quarterly financial statements prepared by management. Shear's interim financial statements are prepared in accordance with Canadian generally accepted accounting principles and are expressed in Canadian dollars.

<b>Period</b>	<b>Revenues (\$)</b>	<b>Net Loss (\$)</b>	<b>Mineral Property Expenditures (\$)</b>	<b>Basic Loss per Share (\$)</b>
Three months ended May 31, 2006	59,852	75,480	288,061	0.001
Three months ended February 28, 2006	9,351	101,986	523,973	0.002
Three months ended November 30, 2005	32,023	282,884	861,469	0.005
Three months ended August 31, 2005	61,084	88,836	1,456,441	0.002
Three months ended May 31, 2005	40,268	155,011	1,007,141	0.003
Three months ended February 28, 2005	49,221	185,130	769,227	0.003
Three months ended November 30, 2004	57,205	569,431	1,145,903	0.011
Three months ended August 31, 2004	46,850	219,765	1,742,571	0.004

The Company's revenues are derived mainly from interest on deposits and short-term investments and management fees charged to joint venture partners. These items fluctuate from quarter to quarter depending on the amount of property work being done and our outstanding investment balance, but have remained fairly consistent overall during the past two years. The Company is in the exploration stage and has no revenue from mining operations. The large variations in the net loss from quarter to quarter are primarily due to non-cash items such as mineral property write downs net of future income tax recoveries, write-downs and recoveries of short-term investments, and share based compensation.

## RELATED PARTY TRANSACTIONS

During the six months ended May 31, 2006, the Company incurred management fees of \$44,500 (2005 - \$67,100 – including \$26,100 in share based compensation) to Encore Resources Inc., a company in which certain directors and officers of the Company have significant influence. In the opinion of management, these fees are considered to be at market value.

Shear Minerals Ltd. is currently a non-participating partner in a joint venture at the Shulin Lake Property. One of the partners is Shulin Lake Mining, a private company in which a director of Shear Minerals Ltd. has a 50% ownership position.

In contemplation of the acquisition of the Stella Polaris Property ("the Property"), Shear entered into an agreement with LynCorp. International Ltd. ("LynCorp"), a private Alberta company owned by a director of Shear, whereby LynCorp agreed to fund \$250,000 in exploration

expenditures or acquisition costs on the Property within one year to earn an undivided 49% interest in the Property.

## **LIQUIDITY AND SOLVENCY**

The Company has no operating revenue to date and relies upon the proceeds of equity financings to support its mineral property acquisition and exploration projects and to provide working capital. The Company had working capital of \$4,499,198 as at May 31, 2006 as compared with \$1,314,946 as at November 30, 2005.

On December 30, 2005, the Company raised additional funds totalling \$1,449,799 through a non-brokered private placement of 4,832,664 flow-through common shares. In connection with the private placement, the Company issued non-transferable share purchase warrants to acquire an aggregate of 318,441 common shares of Shear. The warrants are exercisable at a price of \$0.30 within one year of issuance and result in share issuance costs of \$25,475.

On May 19, 2006, the Company closed a non-brokered private placement of 1,228,500 units ("Units") at a price of \$0.65 per Unit and 3,073,500 flow-through common shares at a price of \$0.70 per flow-through share for gross proceeds of \$2,949,975. Each Unit consisted of one common share and one-half of a non-transferable share purchase warrant. Each whole warrant entitles the holder to acquire an additional common share at a price of \$0.80 at any time within 18 months of issuance. In connection with the private placement, the Company issued non-transferable share purchase warrants to acquire 284,676 common shares. The warrants are exercisable at a price of \$0.65 at anytime within 18 months of issuance. Related to this, the Company recorded share-based compensation in the amount of \$45,548 as a share issue cost.

Management may raise additional capital through equity financings to continue to meet its corporate and exploration commitments over the next year. The Company also has outstanding share options and warrants that if exercised, would result in additional cash proceeds to support corporate activity. Actual funding requirements may vary from those planned due to a number of factors, including the progress of exploration activity and the viability of equity markets.

## DISCLOSURE OF OUTSTANDING SHARE DATA

On June 2, 2006, 27,825 warrants priced at \$0.30 per warrant were exercised.

On July 5, 2006, 400,000 options priced at \$0.25 per option were exercised.

As at July 25, 2006, Shear had 66,102,193 common shares outstanding. The following table provides a summary of Shear's share options and warrants outstanding at July 25, 2006:

Security	Number	Exercise Price (\$)	Expiry Date
Share options	311,000	0.21	March 6, 2007
Share options	734,000	0.26	February 4, 2008
Share options	1,525,000	0.84	September 8, 2008
Share options	530,000	0.83	February 2, 2009
Share options	50,000	0.75	September 3, 2009
Share options	1,400,000	0.40	February 22, 2010
Share options	50,000	0.41	May 3, 2010
Share options	300,000	0.60	April 12, 2011
Warrants	750,000	1.50	November 9, 2006
Warrants	79,333	0.30	December 30, 2006
Warrants	614,250	0.80	September 20, 2007
Warrants	284,676	0.65	September 20, 2007

## MINERAL PROPERTIES

During the three months ended May 31, 2006, expenditures on exploration of the Company's mineral properties totalled \$593,317 (2005 - \$1,118,843). In the six months ended May 31, 2006 exploration expenditures totalled \$1,058,072 (2005 - \$1,744,824).

### 1. CHURCHILL DIAMOND, NUNAVUT

The Churchill Diamond Project ("Churchill") is composed of mineral rights to approximately 2.0 million acres near the community of Rankin Inlet in the Kivalliq region of Nunavut. This project is a new and expanding kimberlite district which Shear and its partners discovered in 2003. To date, a total of 41 kimberlites (includes 2 on the Churchill West Diamond Property) have been discovered through drilling. Shear has a 51% interest in the project and is operator. Stornoway Diamond Corp. and BHP Billiton Diamonds Inc. ("BHP Billiton") have 35% and 14% interests respectively.

On March 27, 2006 BHP Billiton informed Shear of their intention not to participate in the 2006 Churchill and Churchill West exploration programs and to allow BHP Billiton's interest in the two projects to dilute accordingly. The property is subject to a 2.0% gross overriding royalty and net smelter royalty in favour of the Hunter Exploration Group ("Hunter") with respect to the commercial production of diamonds. 100% of all non diamond rights are held by Kaminak Gold Corp.

With BHP Billiton not participating in the 2006 exploration program, at the conclusion of the 2006 exploration program the interests are forecast to be Shear with 52.59%, Stornoway Diamond Corp with 36.09%, and BHP Billiton with 11.32%.

On May 30, 2003, the Company entered into an agreement with BHP Billiton whereby BHP Billiton will fund the entire cost to collect, sample and process the initial 200 tonnes of kimberlitic material from the Churchill Property and sign a standstill agreement for a four year period whereby BHP Billiton is prohibited from participating in a takeover bid, merger, or acquisition of more than 10% of the voting securities of Shear.

### Exploration Update

In April of 2006 the Company announced that 3 macro diamonds (defined as greater than or equal to 0.5mm in two dimensions) and 159 micro diamonds have been recovered from 7.9kg of material from sample 05PST003 that was processed through the SRC indicator mineral circuit. The original sample weighed 20kg, however only 7.9kg of the remaining archived fractions was submitted for diamond analysis to the SRC. The majority of the diamonds were described as clear and colourless and were dominated by octahedron shapes.

Sample Number	Sample Weight (kg)	0.075mm Sieve	0.106mm Sieve	0.15mm Sieve	0.212mm Sieve	0.3mm Sieve	0.425mm Sieve	TOTAL
05PST003	7.9	95	26	19	11	4	7 <sup>1</sup>	162

<sup>1</sup> The three largest diamonds measured 0.76 x 0.56 x 0.50 mm; 0.96 x 0.60 x 0.51mm and 0.70 x 0.60 x 0.42 mm.

On July 13, 2006, the Company reported that a bedrock source for the diamondiferous till sample PST003 had been identified during the first phase of drilling at the Churchill Project. A total of 303 diamonds, including four macro diamonds were recovered from a composite 22.8kg sample of kimberlite collected from seven drill holes that tested the PST003 anomaly. Drill testing of a geochemical target located 3.5km north of PST003 also intersected kimberlite and returned 100 diamonds, including one macro diamond from a 5.65kg sample.

At the diamondiferous till location PST003 seven holes were completed (380m) from three different set ups each approximately 50m apart. Nine kimberlite intersections, averaging 0.75m, were drilled. All seven holes were located at the head of a high interest G10 indicator mineral dispersion train measuring 550m wide and 1.2km long within the Sedna Corridor. The kimberlite intersections coincide with a property scale set of 040° trending lineaments which can be traced with geophysical and air photo data sets. The kimberlite trends NE-SW and appears to dip steeply to the east and is open at depth and along strike.

An additional hole (94m) was drilled in the MSC-19 area located to the 3.5km northeast of PST003. At this time it is uncertain whether the 1.48m intersection at MSC-19 is an extension of PST003. Overburden at both drill areas ranged from 0.2m to 4.9m. Shallow hand dug pits at site PST003 have unearthed in situ kimberlite. Samples were collected from the shallow pits and will be submitted for diamond processing. Further test pits will be dug in both areas later in the summer to collect larger samples.

Selected samples of the kimberlite drilled at PST003 have been examined petrographically by Mineral Services Canada Inc. The samples all have similar characteristics and are described as being of magmatic origin and containing abundant olivine macrocrysts (up to 10mm in diameter), abundant olivine phenocrysts, phlogopite, and common mantle derived garnets (often with alteration to kelyphite) within a matrix of olivine microphenocrysts, opaques, perovskite and

carbonate. Some samples show evidence of flow differentiation and secondary veining of carbonate, magnetite and serpentine. Based on the samples examined, the kimberlite drilled is interpreted to have a high diamond carrying capacity, and is similar in character to the kimberlite fragments recovered in till sample 05PST003 and float sample 05FWR006 from the Josephine River Corridor.

Samples were submitted for diamond analysis to the Saskatchewan Research Council Geoanalytical Laboratories accredited to the ISO/IEC 17025 standard by the Standards Council of Canada as a testing laboratory for diamond analysis using caustic fusion. The majority of the diamonds were described as clear and colourless and were dominated by octahedron shapes. Diamonds were recovered as follows:

Target ID	Sample Weight (kg)	0.075mm Sieve	0.106mm Sieve	0.15mm Sieve	0.212mm Sieve	0.3mm Sieve	0.425mm Sieve	0.6 mm Sieve	Total
PST003 <sup>1</sup>	22.8	135	92	34	28	10	3	1	303
MSC-19 <sup>2</sup>	5.65	43	38	8	6	3	2	0	100

<sup>1</sup> The three largest diamonds measured 0.84x0.70x0.54 mm (white clear octahedroid); 1.10x0.62x0.18mm (yellow broken octahedroid); 0.96x0.52x0.48mm (white included octahedron).

<sup>2</sup> The three largest diamonds measured 0.72x0.50x0.50mm (colourless octahedron); 0.64x0.48x0.48mm(colourless); 0.60x0.30x0.28mm (white octahedron, broken).

Below is a table with details of the drill intercepts:

Drill Hole ID	Target ID	Dip	Azimuth	End of Hole (m)	Overburden (m)	Kimberlite Intercepts (m)	Total Kimberlite (m)
06PST03-01	PST003 (Set up 1)	-50°	135°	53.0	0.7	33.45-34.33	0.88
06PST03-02	PST003 (Set up 1)	-70°	135°	74.0	0.9	52.36-53.88	1.52
06PST03-03	PST003 (Set up 2)	-50°	135°	41.0	2.0	23.00-23.90	0.9
06PST03-04	PST003 (Set up 2)	-75°	135°	65.0	2.3	43.3-44.50	1.20
06PST03-05	PST003 (Set up 3)	-55°	135°	29.0	5.6	22.6-23.00	0.4
06PST03-06	PST003 (Set up 3)	-75°	135°	68.0	3.8	36.5-37.5, 48.7-49.0, 49.4-49.7	1.60
06PST03-07	PST003 (Set up 3)	-45°	135°	50.0	6.2	20.0-20.15	0.15
06KD-08	MSC-19	-50°	290°	94.0	4.2	48.75-50.23	1.48

## Future Plans

A total budget of \$4.6 million has been proposed for 2006 (Shear's share - \$2,728,000) which includes an exploration program to follow up regions of high interest mineral chemistry. For example, in the area of sample 05PST003, further drilling is planned for the summer of 2006 and an on-site indicator mineral processing facility has been commissioned to fast track the 2006 sample results.

## 2. CHURCHILL WEST, NUNAVUT

The Company is currently exploring the Churchill West project with International Samuel Exploration Corp. ("Samuel"), Stornoway and BHP Billiton where the Company holds a 26.45% interest, and Samuel, Stornoway and BHP Billiton have interests of 48.14%, 18.15% and 7.26%, respectively in the diamond rights to the property. On March 27, 2006 BHP Billiton informed Shear of their intention not to participate in the 2006 Churchill and Churchill West exploration programs and to allow BHP Billiton's interest in the two projects to dilute accordingly. The

property is subject to a 2.0% gross overriding royalty and net smelter royalty in favour of Hunter with respect to the commercial production of diamonds. 100% of all non diamond rights are held by Kaminak Gold Corp.

The Churchill West project encompasses 397,705 acres located near the community of Rankin Inlet in the Kivalliq region of Nunavut, contiguous to the Churchill Diamond Project. In 2003 two kimberlites were discovered on the Churchill West property.

In 2005 the Company and its partners completed a \$300,000 high resolution airborne geophysical survey at the Churchill West Diamond Property. The 3,658 line km magnetic-electromagnetic airborne geophysical survey was intended to follow up indicator mineral chemistry of interest in the southeastern region of the property and was flown at 100 meter line spacing.

With BHP Billiton not participating, at the conclusion of the 2006 exploration program Samuel's ownership is projected to be 48.74% and Shear, Stornoway and BHP Billiton will have a 26.76%, 18.36% and 6.14% interest respectively. Shear has assumed operatorship of the Churchill West Diamond Joint Venture.

### **Future Plans**

A budget of \$400,000 has been proposed for 2006 (Shear's share - \$114,000) which will include the interpretation of the 2005 geophysical data and ground follow up of targets of interest.

### **3. HECLA, NUNAVUT**

The Hecla Diamond Project is composed of 465,000 acres of federal prospecting permits located on Melville Island in the NWT. Shear has 100% of this project.

The project was acquired based on a conceptual idea and as a result of the identification from air photos and satellite imagery of more than 15 features in two locales suggestive of kimberlitic intrusives. There are more than 15 features that are circular in shape and range in diameter up to 200m. The host rocks are Paleozoic flat lying sediments that make these features prominent, similar to the known kimberlites on both Somerset Island and the Brodeur Peninsula.

Shear has agreed to issue an aggregate of 200,000 common shares as a finder's fee upon the following milestones being achieved: 25,000 shares upon the successful acquisition of the land (completed); 75,000 shares upon the discovery of a kimberlite; and 100,000 shares upon the discovery of one or more diamonds per kilogram in any 25 kilogram sample of kimberlite.

In addition, Shear has granted a 2% gross overriding royalty fee, of which 1% can be purchased by Shear for \$1.5 million.

In July 2005 the Company mobilized a five person crew to Resolute in order to initiate fieldwork on the Hecla Diamond Project located on Melville Island in the Northwest Territories. The 8 day field program included prospecting sites of interest, sampling and mapping. No indicator minerals were recovered from the samples collected. Many areas were not able to be evaluated due to snow cover.

## **Future Plans**

A preliminary budget of \$75,000 has been set for the property in 2006. Any future field visits will be subject to weather conditions due to the northern location of this property.

## **4. AYLMEER LAKE WEST, NORTHWEST TERRITORIES**

This project operates under a joint venture agreement with Diamondex Resources Ltd. Shear currently holds 61.9% of the project. Shear is obligated to pay a 3.5% gross underlying royalty on production from the property. The property is comprised of two mineral leases (5,165 acres) located 50 km east of the Diavik Diamond Mine and the established diamond district of Lac de Gras and approximately 320 km northeast of Yellowknife, Northwest Territories. There are two known kimberlites on the property: the Nicholas Bay and Nic2 kimberlites. No work was completed in 2005.

## **Future Plans**

Budgetary meetings for the 2006 field program are currently underway and joint venture agreements are being finalized. The 2006 program may include the re-interpretation of the known kimberlites to determine whether further sampling of the kimberlites is warranted.

## **5. XYZ, NORTHWEST TERRITORIES**

This project operates under a joint venture agreement with Hunter. Shear holds an 80% interest in the project. Hunter retains a 2.0% net smelter royalty on non-diamond production as well as a 2.0% gross overriding royalty on diamond production from the property. Shear is required to pay Hunter a \$10,000 annual advance royalty payment which increases to \$25,000 annually commencing June 30, 2008.

The XYZ Project is composed of more than 19,000 acres of mineral claims located along the northwest boundary of the Ekati™ Diamond Mine property and 225 km northeast of Yellowknife, NWT. The project was acquired in 2001 after a high concentration of G10 garnets (a 5 kg un-concentrated sample yielded 15,500 pyrope garnets, 29% of which were G10's, 10,000 microilmenites and 1,000 olivines) and three diamonds (the largest measuring 0.44x0.42x0.212 mm) were identified in a 194 kg beach sand sample from the property. Since that time, Shear has completed airborne geophysics, sampling and ground geophysics and drilling (no kimberlite was intersected).

The source to the indicator minerals being found on surface still remains unknown but Shear believes the source to be local. In 2005 the Company completed a 3 day sampling program and collected 79 till surface samples for kimberlite indicator mineral processing. Results will be incorporated into future planning. The purpose of the sampling is to better rank the geophysical anomalies for follow up drill testing. Shear plans to continue to interpret the data and to follow up on the remaining 10 geophysical targets.

## **Future Plans**

Budgetary meetings for the 2006 field program are currently underway. The 2006 program will include the interpretation of the 2005 sample results in conjunction with the geophysical data, followed by ground follow up that could include drill testing of priority targets.

## **6. AFRIDI LAKE, NORTHWEST TERRITORIES**

This project operates under a joint venture agreement with International Samuel Exploration Corporation (“Samuel”), New World Resource Corp. (“New World” - formerly Dasher Energy Corp.) and Mantle Resources Inc. (“Mantle”). Shear currently holds 56% interest in the property and Samuel, New World and Mantle have 25.4%, 8.2% and 8.2%, respectively.

The Company is obligated to issue 100,000 of its common shares to Mantle for each diamondiferous kimberlite discovered on the property, to a maximum of three kimberlites. The Company is also obligated to pay a 5% gross overriding royalty and net smelter fee on production of the property.

The Afridi Lake Property is comprised of 24 mineral claims and three mineral leases (68,600 acres) located approximately 40km east of the Diavik Diamond Mine and the established diamond district of Lac de Gras and approximately 320 km northeast of Yellowknife, Northwest Territories. There are five known kimberlites on the properties (DA-1, DA-2, DA-3, DA-2SW and the Jordan kimberlites) and more than 100 geophysical targets, some of which have been covered by ground geophysics and are drill-ready.

In 2005 the Company completed a 3 day sampling program and collected 31 surface till samples for kimberlite indicator mineral processing. Results will be incorporated into future planning. The purpose of the sampling is to better rank the geophysical anomalies for follow up drill testing.

### **Future Plans**

Budgetary meetings for the 2006 field program are currently underway. The 2006 program will include interpreting the 2005 sample results in conjunction with the geophysical data and possible ground follow up that could include drill testing of priority targets.

## **7. SHULIN LAKE PROJECT, ALASKA**

During 2003 and 2004, the Company allowed its vested interest in the Shulin Lake project to become diluted to 12%, then 9.2% by not participating in the fall 2003 and fall 2004 exploration programs. However, due to positive exploration results, the Company did participate in the winter 2004 drilling program, maintaining its interest at 9.2%.

If the Company decides not to participate in future exploration costs, this interest will be diluted on a pro-rata basis to a minimum 4% profit interest.

On July 18, 2005, the Company announced that it has been informed by joint venture operator Golconda Resources Ltd. that one white transparent diamond fragment (0.46x0.26x0.14mm) was recovered from 2,400kg of tuffaceous material from a total of 9 samples. These samples were collected from the drilling of three separate magnetic anomalies and were processed at the SGS Lakefield lab in Lakefield, Ontario. Golconda is currently devising a program to determine the origin of the tuffaceous phase that contains the diamonds that the partnership has recovered over the past three years.

## **Future Plans**

The Company has decided not to participate further in the current \$300,000 exploration drilling program and will dilute down from its current 9.2% to 8.2%. Upon receiving the result of the current program, Shear will be re-evaluating its position with respect to future expenditures.

## **8. PICHE, ALBERTA**

On November 16, 2005, the Company acquired an option on the Piche Lake Property in north central Alberta. Under the terms of the agreement Shear can earn into an initial 51% by incurring a total of \$500,000 of exploration expenditures over two years inclusive of \$100,000 in exploration within the first year. In addition, Shear has the ability to earn an additional 24% in the property by spending an additional \$1 million in exploration expenditures over two years after earning 51%.

The Piche Lake Property is road accessible and is composed of two blocks collectively totaling 380,000 acres and is located 170km northeast of Edmonton, Alberta. Previous exploration by Marmac Mines Ltd. has outlined one prominent pipe like discontinuity on seismic data that is suggestive of a kimberlite pipe. The Piche Lake Property is located within the regional Vegreville kimberlite indicator mineral trend as outlined by the Alberta Geological Survey and is also in located along the projected trend of the Snowbird Tectonic Zone, a crustal structure potentially favorable for kimberlite emplacement.

On May 3, 2006 the Company completed an airborne geophysical survey which covered 19 townships at 150m spacings in order to follow up eight high priority seismic pipe-like targets suggestive of kimberlite at both the Piche Lake and Liege Properties. The survey, conducted by Firefly Aviation, provides high resolution data that can assist Shear to more accurately locate and rank the targets and identify any new targets suggestive of kimberlite.

As part of this exploration program, Shear has mobilized a field crew to Northern Alberta to initiate ground geophysical surveys on the Piche Lake Property. A total of 60 initial targets have been chosen from the airborne geophysics for ground checking and then possible ground geophysical surveying. This program is part of a more comprehensive ground follow up program for 2006 that will be carried out on both projects. The interpretation is underway on the Liege Property and several geophysical anomalies suggestive of kimberlite have been picked. Possible drill targets will be finalized once groundwork has been completed.

## **Future Plans**

The Company will evaluate the data from the airborne geophysical survey and decide whether to proceed with further ground geophysical surveys and possible drill testing of high interest targets. A budget of \$125,000 has been approved for the property in 2006.

## **9. LIEGE, ALBERTA**

On November 30, 2005, the Company acquired a farm-out agreement on a significant land position in north central Alberta for diamond exploration. The property, known as the Liege Diamond Project, was acquired from a Canadian oil and natural gas exploration, development and production company. Under the terms of the agreement, Shear can earn into an initial 51% interest by incurring a total of \$1,000,000 of exploration expenditures over three years inclusive

of \$325,000 in exploration within the first year. A \$10,000 cash finder's fee was paid by Shear under the terms of the agreement.

Seven prominent pipe-like targets have been identified from seismic surveys and are suggestive of kimberlites. They were generated during exploration for oil and gas. The Liege Diamond Project consists of 155,000 acres and is located 360km north of Edmonton, Alberta. The project area lies 80km immediately east of the Buffalo Head Hills kimberlite cluster and is located along the projected trend of the Peace River Arch, a crustal structure potentially favorable for kimberlite emplacement.

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### **Future Plans**

The Company will evaluate the data from the airborne geophysical survey and decide whether to proceed with further ground geophysical surveys and possible drill testing of high interest targets. A budget of \$125,000 has been approved for the property in 2006.

## **10. STELLA POLARIS, SASKATCHEWAN**

On April 21, 2006, the Company acquired a significant land position in southern Saskatchewan for diamond exploration. The Stella Polaris Diamond Project (the "Property") is comprised of 235 mineral claims totaling approximately 300,000 hectares (741,000 acres) located approximately 150 km southwest of Regina, SK along the border to the US and is road accessible throughout the year. Shear acquired the Property by staking based on data acquired by Shear from two arm's length parties (the "Vendors").

Pursuant to an agreement dated January 30, 2006 ("the Agreement") between Shear and the Vendors, Shear must:

- (a) within 10 days of receipt of regulatory approval, pay to the Vendors \$25,000 and issue to the Vendors an aggregate of 200,000 common shares of Shear ("Common Shares");
- (b) pay \$25,000 to the Vendors before January 30, 2007;
- (c) pay \$35,000 to the Vendors and issue to the Vendors an aggregate of 100,000 Common Shares before January 30, 2008;
- (d) pay \$50,000 to the Vendors and issue to the Vendors an aggregate of 100,000 Common Shares before January 30, 2009; and

- (e) pay \$75,000 to the Vendors and issue to the Vendors an aggregate of 200,000 Common Shares before January 30, 2010.

(collectively, the “Consideration”). Until the Consideration is fully paid, Shear and the Vendors are subject to an area of mutual interest and will jointly review decisions regarding the Property, including proposed work programs. Shear can elect to accelerate payment of the Consideration, in which case the Vendors will have no further interest in the Property except for a 3% gross overriding royalty (“GORR”) on diamonds, metals and minerals produced from the Property. Shear shall be entitled to purchase 1% of the 3% GORR for \$2 million cash at any time. Shear can be relieved of its obligations pursuant to the Agreement, including the payment of the balance of the Consideration following the initial payment and share issuance, by relinquishing all rights in the Property to the Vendors.

In contemplation of the acquisition of the Property, Shear entered into an agreement with LynCorp. International Ltd. (“LynCorp”), a private Alberta company owned by a director of Shear, whereby LynCorp agreed to fund \$250,000 in exploration expenditures or acquisition costs on the Property within one year to earn an undivided 49% interest in the Property. Once the earn-in is complete, a formal joint venture will be formed whereby each party is responsible for their pro rata share of exploration expenditures and property payments consisting of both cash and shares (or cash equivalent). Shear has a right of first refusal on LynCorp’s interest. Shear will be the operator of the Property.

### **Future Plans**

A review of all existing information is currently being undertaken and further detailed sampling will commence in August of 2006. A budget of \$250,000 has been allocated for the initial program including a limited drill program.

### **11. OTHER**

In 2005 the Company conducted one regional diamond indicator mineral sampling program based on conceptual ideas. Based on sample results, the Company will determine whether or not to acquire mineral rights in the area.

## ANALYSIS OF ACQUISITION AND EXPLORATION COSTS

	For the Three Months Ended May 31, 2006			For the Three Months Ended May 31, 2005
	Acquisition Costs	Exploration Costs	Total	Total
<b>Churchill Diamond Project</b>				
Land tenure	\$ (271,282)	\$ -	\$ (271,282)	\$ (106,940)
General exploration	-	128,644	<b>128,644</b>	583,501
Project consulting	-	78,474	<b>78,474</b>	68,350
Environment	-	10,030	<b>10,030</b>	16,853
Field travel	-	12,899	<b>12,899</b>	10,715
Field supplies	-	2,196	<b>2,196</b>	27
Drilling services	-	111,214	<b>111,214</b>	427,121
Sampling	-	433,003	<b>433,003</b>	220,762
Ground geophysics	-	43,026	<b>43,026</b>	141,968
Airborne geophysics	-	9,514	<b>9,514</b>	125,072
Community consultations	-	11,319	<b>11,319</b>	17,319
Expenses recovered from partners	(490)	(354,831)	<b>(355,321)</b>	(729,487)
	<u>(271,772)</u>	<u>485,488</u>	<u><b>213,716</b></u>	<u>775,261</u>
<b>Churchill West Project</b>				
Land tenure	560	-	<b>560</b>	26,069
General exploration	-	168	<b>168</b>	383
Project consulting	-	2,450	<b>2,450</b>	2,462
Sampling	-	-	-	22,528
Analytical	-	-	-	1,024
Community consultations	-	75	<b>75</b>	-
Expenses recovered from partners	-	-	-	(32,559)
	<u>560</u>	<u>2,693</u>	<u><b>3,253</b></u>	<u>19,907</u>
<b>Hecla Project</b>				
Land tenure	-	-	-	980
Option costs – shares	-	-	-	13,250
General exploration	-	-	-	37
Project consulting	-	-	-	75
	<u>-</u>	<u>-</u>	<u>-</u>	<u>14,342</u>
<b>Aylmer Lake West</b>				
General exploration	-	444	<b>444</b>	8,841
Project consulting	-	37	<b>37</b>	-
	<u>-</u>	<u>481</u>	<u><b>481</b></u>	<u>8,841</u>
<b>XYZ</b>				
General exploration	-	897	<b>897</b>	298
Sampling	-	275	<b>275</b>	-
	<u>-</u>	<u>1,172</u>	<u><b>1,172</b></u>	<u>298</u>

**Afridi Lake**

Land tenure	39,354	-	<b>39,354</b>	50
General exploration	-	6,949	<b>6,949</b>	22,420
Project consulting	-	275	<b>275</b>	157
Sampling	-	-	-	10,834
	<u>39,354</u>	<u>7,224</u>	<u><b>46,578</b></u>	<u>33,461</u>

**Back River Gold**

General exploration	-	-	-	20,596
Project consulting	-	-	-	33,870
Field travel	-	-	-	906
Sampling	-	-	-	2,216
	<u>-</u>	<u>-</u>	<u>-</u>	<u>57,588</u>

**Shulin Lake**

Land tenure	-	-	-	3,054
Analytical	-	200	<b>200</b>	-
General exploration	-	-	-	68,137
	<u>-</u>	<u>200</u>	<u><b>200</b></u>	<u>71,191</u>

**Piche**

Land tenure	336	-	<b>336</b>	-
General exploration	-	14,844	<b>14,844</b>	-
Field travel	-	3,368	<b>3,368</b>	-
Ground geophysics	-	6,770	<b>6,770</b>	-
Airborne geophysics	-	33,175	<b>33,175</b>	-
Community consultations	-	1,007	<b>1,007</b>	-
	<u>336</u>	<u>59,164</u>	<u><b>59,500</b></u>	<u>-</u>

**Liege**

General exploration	-	1,882	<b>1,882</b>	-
Project consulting	-	275	<b>275</b>	-
Airborne geophysics	-	29,656	<b>29,656</b>	-
Community consultations	-	325	<b>325</b>	-
	<u>-</u>	<u>32,138</u>	<u><b>32,138</b></u>	<u>-</u>

**Stella Polaris**

Land tenure	4,888	-	<b>4,888</b>	-
Option costs – shares	114,000	-	<b>114,000</b>	-
Option costs – cash	25,000	-	<b>25,000</b>	-
General exploration	-	9,975	<b>9,975</b>	-
Project consulting	-	5,000	<b>5,000</b>	-
Ground geophysics	-	860	<b>860</b>	-
Airborne geophysics	-	200	<b>200</b>	-
Expenses recovered from partners	(103,622)	(15,653)	<b>(119,275)</b>	-
	<u>40,266</u>	<u>382</u>	<u><b>40,648</b></u>	<u>-</u>

<b>Other</b>				
Project consulting	-	4,375	<b>4,375</b>	-
Sampling	-	-	-	39,502
	-	4,375	<b>4,375</b>	39,502
	<b>\$ (191,256)</b>	<b>\$ 593,317</b>	<b>\$ 402,061</b>	<b>\$ 1,020,391</b>

## Risks and Uncertainties

The success of Shear's business is subject to a number of factors, including but not limited to those risks normally encountered by junior resource exploration companies, such as exploration uncertainty, operating hazards, increasing environmental regulation, competition with companies having greater resources, and lack of operating cash flow. In addition, there is no quoted market price for diamonds and the market price for rough diamonds is dependent on an efficient market management system. Shear's on-going ability to finance exploration beyond those programs budgeted to date will depend on, amongst other things, the viability of equity markets.

## Critical Accounting Estimates

The most significant accounting estimate for the Company relates to the carrying value of its mineral property assets. At the end of each quarter, exploration and acquisition expenditures are reviewed and if the expenditures are deemed to have added value to the property, the expenditures are capitalized. Historical exploration and acquisition expenditures are also reviewed each quarter and if a property is inactive for a period of over three years and there are no current plans for further exploration on the property, the property costs are written off. The Company may choose to retain the mineral rights to a property after it is written off if management believes there may be an opportunity to vend or explore the property in the future.

Another significant accounting estimate used by the Company relates to the accounting for share-based compensation. The Black-Scholes Option Pricing Model is used to determine the fair value of the option and utilizes subjective assumptions such as expected price volatility and expected life of the option. Discrepancies in these input assumptions can significantly affect the fair value estimate.