MANAGEMENT'S DISCUSSION AND ANALYSIS
Six Months Ended June 30, 2007

Change in Fiscal Year End

In August, 2006, Fortuna Silver Mines Inc. (the "Company") changed its fiscal year end from September 30th to December 31st. The Company's year end now matches that of its Peruvian subsidiary which owns the Caylloma Mine, resulting in an increase in the efficiency of the Company's accounting operations. A Notice of Change in Fiscal Year End has been filed on sedar.com.

General

This Management's Discussion and Analysis ("MD&A") supplements the unaudited financial statements of the Company for the six months ended June 30, 2007. The following information, prepared as of July 31, 2007, should be read in conjunction with the June 30, 2007 financial statements, which have been prepared in accordance with Canadian generally accepted accounting principles. All amounts are expressed in Canadian dollars unless otherwise indicated.

Business of the Company

Fortuna Silver Mines Inc. is a mining company focused on producing silver and developing silver projects in Latin America. The Company's principal assets are the Caylloma Polymetalic Mine in southern Peru and the San Jose Silver-Gold Project in southern Mexico.

Recent Developments and Highlights

Operations and financial results

For the three month period ending June 30, 2007 Fortuna generated net income of $0.95 million. This result was rooted in a strong operating income of $2.44 million. During the three month period revenues increased 53% in respect of the 1st quarter of the year to $8.8 million and amounted to $14.54 million for the 1st semester of 2007.

As a result of cash surplus at the Caylloma mine, the Company generated positive cash flow from operating activities (before changes in non-cash working capital) of $3.06 million for the three month period and $5.45 million for the semester.

Treated ore at Caylloma increased 21% with respect to the previous quarter with an average throughput rate of 701 tpd for the three months, and a record of 748 tpd for the month of July. Production cash cost was US$46.65 per tonne and unit NSR of treated ore was US$123.65 per tonne for the period.

San Jose Drilling Results

Drilling on the San Jose project continues to deliver consistent results. Twenty-nine drill holes totaling 10,693.50m have been completed this year up until July 23, and the company anticipates drilling a total of at least 25,000 meters with three drill rigs this year. Results have been made public through two news releases dated May 30th and July 16th, 2007 and available on the company's website at www.fortunasilver.com. Highlights of these results include:

- Hole SJO-060 averaging 10.9 g/t Au plus 588 g/t Ag (1,141 g/t Ag equivalent) over 25.1 metres;
- Hole SJO-057 averaging 6.1 g/t Au plus 588 g/t Ag (897 g/t Ag equivalent) over 11.6 metres;
- Hole SJO-055 averaging 11.9 g/t Au plus 1,151 g/t Ag (1,756 g/t Ag equivalent) over 2.5 metres;
- Hole SJO-063 averaging 4.4 g/t Au plus 1,224 g/t Ag (1,450 g/t Ag equivalent) over 2.6 metres;
- Hole SJO-065 averaging 1.4 g/t Au plus 183 g/t Ag (256 g/t Ag equivalent) over 20.9 metres
- Hole SJO-064 averaging 2.48 g/t Au plus 283 g/t Ag (410 g/t Ag equivalent) over 104.8 meters.

Silver equivalency estimates were derived using US$10.30/oz for silver and US$525/oz for gold yielding a Ag:Au ratio of 51:1. Metallurgical recoveries and net smelter returns are assumed to be 100% for purposes of estimating silver equivalency. True width of mineralization ranges from 70% to 90% of interval.

Quarterly Information

The following table provides information for the eight fiscal quarters ended March 31, 2007:

		Quarters Ended							
		30-Jun-07	31-Mar-07	31-Dec-06	30-Sep-06	30-Jun-06	31-Mar-06	31-Dec-05	30-Sep-05
Revenues	**$ 000**	**8,797**	**5,739**	**3,370**	**0**	**0**	**0**	**0**	**0**
Net Income (loss)	**$ 000**	**947**	**(1,756)**	**21**	**(1,745)**	**363**	**(2,371)**	**(616)**	**(202)**
Net Income (loss) per share, basic	**$**	**0.01**	**(0.03)**	**0.00**	**(0.04)**	**0.01**	**(0.09)**	**(0.03)**	**(0.02)**
Net Income (loss) per share, diluted	**$**	**0.01**		**0.00**		**0.01**			

Financial Results

For the three months ended June 30, 2007 the Company recorded net income of $947,139 compared to net income of $362,879 for the corresponding period in 2006. This result is rooted in a strong operating income for the period of $2.44 million. The larger losses in March of 2007, and March and September of 2006, were driven by stock based compensation charges; $2.31 million, 2.13 million, and $1.81 million respectively.

Also for the three months ended June 30, 2007 mine operating income was $4.01 million and cash generated by operating activities before changes in non-cash working capital items was $3.06 million, reflecting the cash surplus of the Company's operating Caylloma mine.

Sales for the second quarter of 2007 were $8.8 million. This is a 53% increase over the previous quarter, which is explained by higher concentrate production and sales. Concentrate tonnage sold increased 31% for zinc and 36% for lead, where unit value of concentrate increased 26% for zinc and 15% for lead due to higher metal content and higher metal prices.

Total **cost of sales** was $4.79 million, of which $1.59 million was depletion, depreciation, and accretion. This corresponds entirely to production and sales from Caylloma.

Selling, general and administrative expenses for the period totalled $1.46 million compared to $0.02 million for the corresponding quarter of 2006. The increase is due to the impact of the beginning of operations in our Peruvian subsidiary and higher total corporate expenses associated with the growth of the Company. It is comprised of $473,683 of selling expenses and mining royalty paid to the Peruvian government on account of our operations at the Caylloma mine, and $986,041 of total corporate administrative expenses. The stock based compensation charge totalled $113,350 for the three month period ended June 30, 2007, compared to nil for the corresponding period in 2006.

Interest and other income and expenses were $335,682 compared to $126,394 for the corresponding quarter of 2006.

Foreign exchange loss recorded for the period was $709,429, compared to a gain of $254,168 for the corresponding quarter of 2006. This has to do with the strong appreciation of the Canadian dollar against the

US currency experienced during the second quarter of 2007, where the functional currency of the company is the US Dollar.

The $1.08 million **Income tax provision** recorded for the period resulted from the taxable income generated in our Peruvian Subsidiary and consisted entirely of future income tax.

Results of Operations

Mexico – San Jose Silver-Gold Project

Drilling on the San Jose project continues to deliver consistent results. Twenty-nine drill holes totaling 10,693.50m have been completed this year up until July 23, and the company anticipates drilling a total of at least 25,000 meters with three drill rigs this year. Results have been made public through two news releases dated May 30th and July 16th, 2007 and available on the company's website at www.fortunasilver.com. Highlights of these results include:

- Hole SJO-060 averaging 10.9 g/t Au plus 588 g/t Ag (1,141 g/t Ag equivalent) over 25.1 metres;
- Hole SJO-057 averaging 6.1 g/t Au plus 588 g/t Ag (897 g/t Ag equivalent) over 11.6 metres;
- Hole SJO-055 averaging 11.9 g/t Au plus 1,151 g/t Ag (1,756 g/t Ag equivalent) over 2.5 metres;
- Hole SJO-063 averaging 4.4 g/t Au plus 1,224 g/t Ag (1,450 g/t Ag equivalent) over 2.6 metres;
- Hole SJO-065 averaging 1.4 g/t Au plus 183 g/t Ag (256 g/t Ag equivalent) over 20.9 metres
- Hole SJO-064 averaging 2.48 g/t Au plus 283 g/t Ag (410 g/t Ag equivalent) over 104.8 meters.

Silver equivalency estimates were derived using US$10.30/oz for silver and US$525/oz for gold yielding a Ag:Au ratio of 51:1. Metallurgical recoveries and net smelter returns are assumed to be 100% for purposes of estimating silver equivalency. True width of mineralization ranges from 70% to 90% of interval.

Additional targets like San Ignacio and the gap zone both located south of the Trinidad shoot along the same structure are expected to be drill tested during the third and fourth quarters of the year.

During the quarter the joint venture acquired a double-boom jumbo for the underground development planned to begin late in August of 2007. The contractor for mine development has been selected and is currently mobilizing to the site.

The joint venture continues its land acquisition program in the project area and components of a scoping study are already taking place; a social base study as well as a hydrological study in the project area have been commissioned.

The re-commissioning of the 350 tpd plant facility acquired on February 2007 has been put on hold to prioritize efforts and resources in favour of the advancement of the definitive design and permitting of the larger plant.

Peru – Caylloma Mine

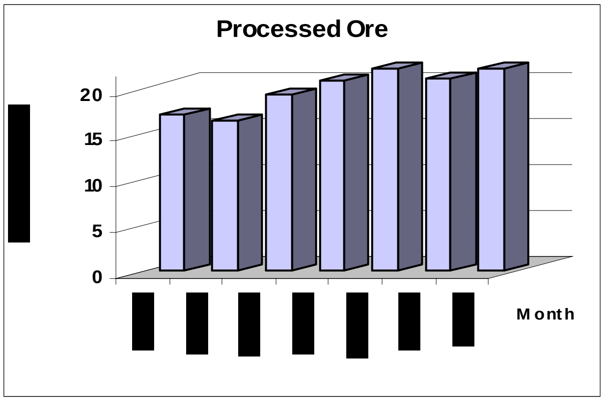
Caylloma Mine	Quarters ended	
	31-Mar-07	**31-Jun-07**
Tonnes milled	52,687	63,806
Grade per tonne		
Silver (oz)	2.23	2.29
Lead (%)	1.38	1.67
Zinc (%)	2.66	2.92
Recoveries		
Silver (%)	71.39	73.28
Lead (%)	88.59	89.22
Zinc (%)	84.16	86.22
Production (metal contained)		
Silver (oz)	95,473	119,110
Lead (tonnes)	646	952
Zinc (tonnes)	1,178	1,605
Unit cash production cost (US$/tonne)	42.62	46.65
Unit Net Smelter Return (US$/tonne)	90.26	123.65

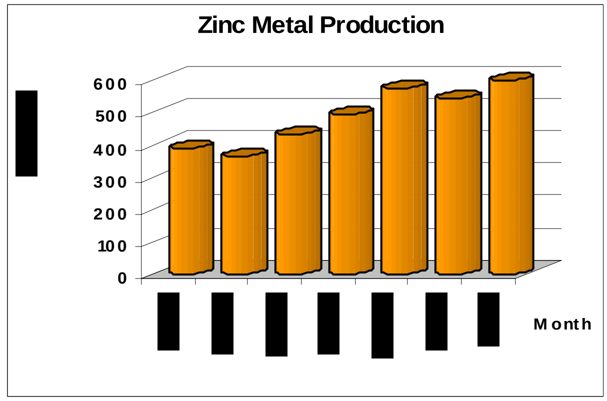
The Caylloma mine is out of the balancing phase typical of any start-up operation and has achieved its design parameters. The mine production is unhedged and the company continues to benefit from historic high prices, particularly for lead and zinc which combined accounted for 75 per cent of revenue for the quarter. In order to continue capitalizing on this base metal bonanza triggered by prices the company will continue, in the short and medium term, to direct the mine development and operations to the base metal rich portions of the deposit.

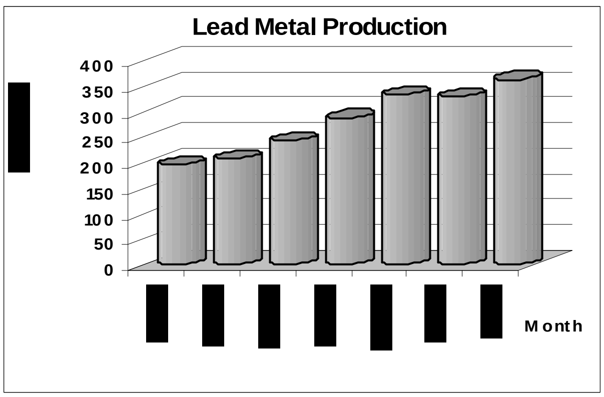
Total ore milled for the quarter was 63,806 tonnes, yielding an average daily throughput of 701 tpd. Throughput rate is expected to stabilize around 730 tpd until completion of mine development and other investments necessary to achieve permitted capacity of 1,100 tpd.

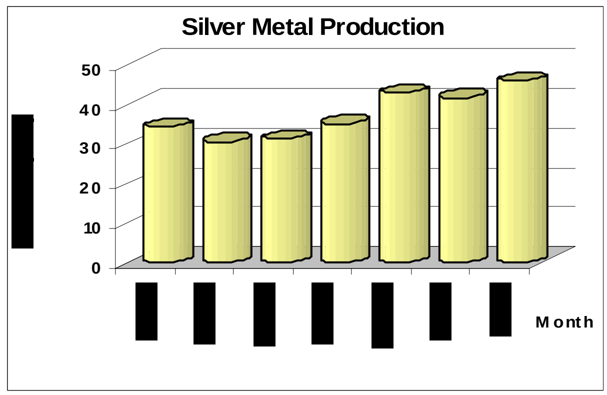
Cash cost per tonne of ore milled during the second quarter of 2007 was US$46.65/tonne. The increase in production cost for this quarter has to do with temporary accumulation of ore in the stopes due to the mining method being used as well as an adjustment to unit costs granted to mining contractors during the period.

The net-smelter-return (NSR) value per tonne of ore milled during the quarter was US$123.65/tonne. The increase with respect to the previous quarter is explained by higher metal prices, as well as improved head grades and metallurgical recoveries. The composition of sales per metal for the first six months of 2007 was; zinc 57%, silver 20%, lead 18%, gold 5%.









Exploration at Caylloma for 2007 is targeting the immediate mine area as well as the greater surrounding land package of 12,000 hectares.

Acquisitions

Fortuna is constantly evaluating new mining opportunities in order to meet our corporate objective of building significant silver inventory and cash flow, by acquiring advanced projects or operating mines from private parties in Latin America.

Cash cost per tonne (Non-GAAP measures)

Cash cost per tonne is a key performance measure that management uses to monitor performance. These performance measures have no meaning within Canadian Generally Accepted Accounting Principles (GAAP), and, therefore, amounts presented may not be comparable to similar data presented by other mining companies.

The following table presents a reconciliation of cash production costs per tonne of processed ore to the cost of sales from the consolidated statement of operations for the tree months ended June 30, 2007:

	CAD$	US$ @ 0.9088
Cost of sales	**4,785,310**	**4,349,056**
Change in inventory (ore and concentrate stock piles)	**36,000**	**32,718**
Depletion, depreciation, and accretion	**(1,545,883)**	**(1,404,952)**
Total cash production cost	**3,275,427**	**2,976,822**
Total processed ore (tonnes)		**63,806**
Cash production cost per tonne of processed ore (US$)		**46.65**

Liquidity and Capital Resources

The Company's cash resources and working capital at the end of the period were $35.28 million and $39.14 million respectively, compared to $13.42 million and $15.31 million for the corresponding period of 2006.

As a result of positive cash flow coming from our Peruvian operations net cash provided by operating activities was $1.49 million for the three month period and $3.32 million for the first six months of the year.

During 2006 the Company incurred total investment expenditures of $5.85 million in its mineral properties and plant and equipment. Management expects Caylloma to address ongoing and expansion capital needs for 2007 from cash generated internally by the operation. With regards to San Jose, for this stage of the project a US$12 million investment plan is currently underway of which Fortuna's cost share is 76% and which the Company is well funded to execute.

During the three month period net proceeds from issuance of common shares amounted to $4.77 million. This was comprised of $571,177 from the exercise of stock options and $4.2 million from the exercise of warrants. Total net cash provided by financing activities was $4.76 million.

Management believes the Company's financial position after the closing of its January financing as well as a result of its ongoing operation in Caylloma are sufficient to support the Company's operating and capital requirements on an ongoing basis. Actual funding requirements may vary from those planned due to further acquisition opportunities. Management believes it will be able to raise equity capital as required in both the short and long term, but recognizes the uncertainty attached thereto.

Related Party Transactions

The Company incurred charges with directors, officers, and companies having a common director or officer as follows:

	6 months ended June 30, 2007	6 months ended June 30, 2006
Mineral property costs – geological fees	$ 45,072	$ 78,250
Consulting fees	49,534	37,693
Salaries and wages	39,753	2,672
Management fees	115,343	40,521

These charges were measured at the exchange amount, which is the amount agreed upon by the transacting parties.

At June 30, 2007, accounts payable and accrued liabilities included $1,382 (December 31, 2006 - $395) to an officer of the Company.

At June 30, 2007, due to related parties consists of $26,491 (December 31, 2006 - $41,147) owing to an officer and to companies with a common director. These amounts were incurred as a result of shared administrative costs. These amounts are unsecured, non-interest bearing and payable in the normal course of business.

At June 30, 2007, due from related parties consists of $82 (December 31, 2006 - $13,869) owed from companies with a common director which were incurred as a result of shared administrative costs. This amount is unsecured, non-interest bearing and will be collected in the normal course of business.

Critical Accounting Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the consolidated financial statements and the reported amounts of revenue and expenses during the years. Significant items subject to such estimates and assumptions include the carrying amount of mineral property, plant and equipment, revenue recognition, inventories and future income taxes, provisions for asset retirement obligation and reclamation, and stock based compensation.

Change in Accounting Policy

On January 1, 2007, the Company adopted the provisions of CICA Sections 1530 “Comprehensive Income”, 3251 “Equity”, 3855 “Financial Instruments – Recognition and Measurement”, 3861 “Financial Instruments – Presentation and Disclosure”, and 3865 “Hedges”. These sections address the classification, recognition and measurement of financial instruments and hedges in the financial statements and inclusion of other comprehensive income.

Comprehensive income is the change in the net assets of a company arising from transactions, events and circumstances not related to shareholders. It consists of net income and other comprehensive income, which includes items that would not normally be included in net income such as unrealized gains and losses on available-for-sale securities.

As a result of adopting these new standards at January 1, 2007, the Company recorded an unrealized gain of $518,875 for the change in accounting for financial assets classified as "available-for-sale" and measured at fair value instead of cost. This increase is reported as a one-time cumulative effect to other comprehensive income.

Additional detail relating to changes in accounting policy on financial instruments can be found in Note 3 of the unaudited consolidated financial statements for the six months ended June 30, 2007.

Financial Instruments

Cash and cash equivalents, accounts receivable and prepaid expenses, due from related parties, and accounts payable and accrued liabilities have been classified as "held-for-trading". The fair values of these financial instruments approximate their carrying values due to their short-term nature or capacity of prompt liquidation. Unless otherwise noted, it is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from these financial instruments.

Interest rate risk

The Company holds cash and cash equivalents which earn interest at variable rates as determined by financial institutions.

Credit risk

The Company only places its cash with institutions of high credit worthiness.

Foreign exchange risk

The Company holds cash balances and incurs payables that are denominated in multiple foreign currencies, including Peruvian Nuevo Sol, Mexican Pesos and United States Dollars. These balances are subject to changes in the exchange rate between these currencies and the Canadian Dollar, which would result in a currency gain or loss to the Company.

Other Data

Additional information related to the Company is available for viewing at www.sedar.com.

Share Position and Outstanding Warrants and Options

The Company's outstanding share position at July 31, 2007 is 71,192,015 common shares. In addition, a total of 32,426,423 share purchase warrants and incentive stock options are currently outstanding as follows:

Type of Security	Number	Exercise Price	Expiry Date
Warrants	593,356	$1.85	September 23, 2007
	6,570,000	$1.25	September 26, 2007
	270,085	$0.80	September 26, 2007
	1,076,833	$1.25	October 6, 2007
	67,056	$0.80	October 6, 2007
	4,863,046	$1.85	March 23, 2008
	10,093,192	$2.30	July 11, 2008
	862,117	$0.345	June 27, 2010
	1,613,238	$0.345	November 17, 2010
	26,008,923		
Options	12,500	$3.09	August 9, 2007
	39,000	$0.37	December 2, 2009
	30,000	$0.80	July 24, 2010
	345,000	$1.35	February 5, 2016
	451,000	$2.29	March 30, 2016
	90,000	$1.75	May 8, 2016
	200,000	$1.75	May 22, 2016
	315,000	$1.55	July 5, 2016
	860,000	$1.66	July 10, 2016
	225,000	$1.61	September 13, 2016
	50,000	$1.90	November 20, 2016
	50,000	$1.96	November 23, 2016
	1,480,000	$2.22	January 11, 2017
	80,000	$2.75	February 6, 2017
	15,000	$3.09	April 22, 2017
	50,000	$3.10	May 31, 2017
	50,000	$3.10	June 17, 2017
	50,000	$3.05	June 27, 2017
	2,025,000	$3.22	July 2, 2017
	6,417,500		

Forward Looking Information

Certain statements contained in this MD&A and elsewhere constitute forward-looking statements. Such forward-looking statements involve a number of known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the company to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date the statements were made, and readers are advised to consider such forward-looking statements in light of the risks set forth below.

Risks and Uncertainties

The business of mineral exploration and extraction involves a high degree of risk. Few properties that are in the exploration stage ultimately become producing mines. The Company's mineral properties are located in emerging nations and consequently may be subject to a higher level of risk compared to developed countries. Operations, the status of mineral property rights, title to the properties and the recoverability of amounts shown for mineral properties in emerging nations can be affected by changing economic, regulatory, and political situations.

The most significant risk affecting the profitability and viability of the Company's mining operations is the fluctuation of metal prices, as the Company's earnings and cash flow are highly sensitive to changes in these metal prices. Low metal prices will affect the Company's liquidity, and if they persist for an extended period of time, the Company may have to look for other sources of cash flow to maintain liquidity until metal prices recover. Volatility in the metal prices is influenced by factors such as exchange rates, inflation, political circumstances and the world's supply and demand fundamentals, which are beyond the control of the Company.

Other risks facing the Company include environmental risks, share price volatility, and uncertainty of additional financing.

Internal Disclosure Controls and Procedures

Internal control is defined as a process designed to provide reasonable assurance regarding the reliability of financial reporting. In its annual MD&A for the year 2006 the Company disclosed weaknesses in the design of internal control. Management is currently engaged in addressing these issues by increasing the human and financial resources allocated to accounting activities and financial reporting.