



CONSOLIDATED FINANCIAL STATEMENTS

THREE AND SIX MONTHS ENDED AUGUST 31, 2009 AND 2008

(Expressed in Canadian Dollars)

(Unaudited)

*These financial statements have not been reviewed by the Company's auditors.*

# ROCKWELL DIAMONDS INC.

## Consolidated Balance Sheets

(Expressed in Canadian Dollars)

	August 31, 2009 (unaudited)	February 28, 2009
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 866,770	\$ 3,997,807
Accounts receivable	881,851	1,131,026
Restricted cash (note 7)	–	2,698,719
Trade receivable from a related party (note 11)	1,451,604	3,490,725
Inventory (note 5)	4,476,508	3,719,919
Prepayments	108,265	61,775
	<u>7,784,998</u>	<u>15,099,971</u>
Property, plant and equipment (note 6)	61,896,713	59,569,186
Mineral property interests (note 7)	34,653,825	28,894,477
Other assets and deposits	236,526	139,140
Reclamation deposits (note 9)	<u>3,083,508</u>	<u>2,659,642</u>
	<u>\$ 107,655,570</u>	<u>\$ 106,362,416</u>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current liabilities</b>		
Bank indebtedness (note 12)	\$ 3,116,898	\$ 3,540,880
Accounts payable and accrued liabilities	5,667,369	4,832,038
Due to related parties (note 11)	772,723	193,655
Income taxes	957,831	456,046
Current portion of capital lease obligations (note 8)	<u>5,454,805</u>	<u>5,440,181</u>
	<u>15,969,626</u>	<u>14,462,800</u>
<b>Long-term liabilities</b>		
Capital lease obligations (note 8)	1,515,732	3,284,596
Due to related parties (note 11)	427,306	383,330
Future income taxes	11,606,000	12,126,000
Reclamation obligation (note 9)	<u>4,257,069</u>	<u>3,802,655</u>
	<u>17,806,107</u>	<u>19,596,581</u>
<b>Non-controlling interest</b>	1,597,817	1,882,009
<b>Shareholders' equity</b>		
Share capital (note 10)	119,954,269	119,952,532
Warrants (note 10(c))	–	1,693,197
Contributed surplus	5,993,759	4,167,304
Accumulated other comprehensive loss	(5,057,807)	(13,409,383)
Deficit	<u>(48,608,201)</u>	<u>(41,982,624)</u>
	<u>72,282,020</u>	<u>70,421,026</u>
Continuance of operations and going concern (note 1)		
Contingencies (note 13)		
	<u>\$ 107,655,570</u>	<u>\$ 106,362,416</u>

The accompanying notes are an integral part of these consolidated financial statements.

Approved by the Board of Directors

/s/ Dr. John Bristow

Dr. John Bristow  
Director, Chief Executive Officer

/s/ Dr. Mark Bristow

Dr. Mark Bristow  
Director

# ROCKWELL DIAMONDS INC.

## Consolidated Statements of Operations and Comprehensive Income (Loss)

(Unaudited - Expressed in Canadian Dollars)

	Three months ended August 31		Six months ended August 31	
	2009	2008	2009	2008
<b>Revenue</b>				
Rough diamonds sales	\$ 5,802,006	\$ 9,912,702	\$ 9,674,805	\$ 17,007,623
Contract diamond sales	–	4,356	–	160,576
Other sales	116,756	250,799	173,130	330,590
	5,918,762	10,167,857	9,847,935	17,498,789
<b>Cost of sales</b>				
Cost of rough diamonds sales	(4,789,630)	(7,650,605)	(9,640,211)	(12,259,173)
Amortization and depletion	(3,139,309)	(2,672,728)	(4,958,389)	(5,246,960)
<b>Operating profit (loss)</b>	<b>(2,010,177)</b>	<b>(155,476)</b>	<b>(4,750,665)</b>	<b>(7,344)</b>
<b>Expenses</b>				
Accretion of reclamation obligation (note 9)	31,885	98,779	17,597	167,402
Exploration	2,305	(32,976)	59,916	271,182
Foreign exchange loss (gain)	2,362	831,009	548,421	624,887
Interest on capital leases	251,548	440,378	594,269	903,195
Interest expense	73,047	162,790	480,349	248,831
Legal, accounting and audit	159,309	639,568	493,009	776,895
Office and administration	800,144	867,755	1,456,613	1,839,810
Shareholder communications	212,170	119,330	331,536	198,975
Stock-based compensation - exploration (note 10(b))	7,807	134,619	37,640	337,243
Stock-based compensation - administration (note 10(b))	10,150	237,883	96,426	720,858
Travel and conferences	41,163	107,806	76,782	319,709
Transfer agent	57,381	34,646	79,554	44,697
	1,649,271	3,641,587	4,272,112	6,453,684
<b>Other items</b>				
Loss on disposal of equipment	11,439	283,785	37,220	304,753
Loss on disposal of mineral property	–	203,338	–	203,338
Interest income	(91,692)	(742,169)	(234,481)	(2,123,452)
Write-down of assets	–	–	657,634	–
	(80,253)	(255,045)	460,373	(1,615,361)
<b>Loss before income taxes</b>	<b>3,579,195</b>	<b>3,542,017</b>	<b>9,483,150</b>	<b>4,845,667</b>
Current income tax expense	–	(110,367)	–	157,629
Future income tax recovery	(719,427)	(592,800)	(2,065,834)	(1,274,808)
<b>Loss before non-controlling interest</b>	<b>2,859,768</b>	<b>2,838,850</b>	<b>7,417,316</b>	<b>3,728,488</b>
Non-controlling interest	(338,122)	(589,003)	(791,739)	(677,288)
<b>Loss for the period</b>	<b>2,521,646</b>	<b>2,249,848</b>	<b>6,625,577</b>	<b>3,051,200</b>
Other comprehensive income	(2,876,659)	–	(8,351,576)	–
<b>Total comprehensive income (loss)</b>	<b>\$ 355,013</b>	<b>\$ (2,249,848)</b>	<b>\$ 1,725,999</b>	<b>\$ (3,051,200)</b>
Basic and diluted loss per common share	\$ 0.01	\$ 0.01	\$ 0.03	\$ 0.01
<b>Weighted average number of common shares outstanding</b>	<b>238,041,651</b>	<b>238,041,569</b>	<b>238,042,360</b>	<b>237,963,291</b>

The accompanying notes are an integral part of these consolidated financial statements.

# ROCKWELL DIAMONDS INC.

## Consolidated Statements of Shareholders' Equity

(Expressed in Canadian Dollars)

	<u>Six months ended August 31</u>		<u>Year ended February 28</u>	
	<u>2009</u>		<u>2009</u>	
	(unaudited)			
<b>Share capital</b>				
	<u>Number of shares</u>		<u>Number of shares</u>	
Balance at beginning of the period	238,041,569	\$ 119,952,532	223,755,854	\$ 112,095,390
Share purchase options exercised at \$0.62 per share	1,500	930	-	-
Consideration for additional interest of operating mines net of issue cost at \$0.55 per share	-	-	14,285,715	7,857,142
Fair value of stock options allocated to shares issued on exercise	-	807	-	-
<b>Balance at end of the period</b>	<b>238,043,069</b>	<b>\$ 119,954,269</b>	<b>238,041,569</b>	<b>\$ 119,952,532</b>
<b>Warrants</b>				
Balance at beginning of the period		\$ 1,693,197		\$ 1,693,197
Expired broker warrants		(1,693,197)		-
<b>Balance at end of the period</b>		<b>\$ -</b>		<b>\$ 1,693,197</b>
<b>Contributed surplus</b>				
Balance at beginning of the period		\$ 4,167,304		\$ 2,332,882
Stock-based compensation (note 10(b))		134,065		1,834,422
Expired broker warrants		1,693,197		-
Fair value of stock options allocated to shares issued on exercise		(807)		-
<b>Balance at end of the period</b>		<b>\$ 5,993,759</b>		<b>\$ 4,167,304</b>
<b>Accumulated other comprehensive loss</b>				
Balance at beginning of the period		\$ (13,409,383)		\$ -
Comprehensive income (loss) on currency translation of previously integrated operations		8,351,576		(13,409,383)
<b>Balance at end of the period</b>		<b>\$ (5,057,807)</b>		<b>\$ (13,409,383)</b>
<b>Deficit</b>				
Balance at beginning of the period		\$ (41,982,624)		\$ (29,006,662)
Loss for the period		(6,625,577)		(12,975,962)
<b>Balance at end of the period</b>		<b>\$ (48,608,201)</b>		<b>\$ (41,982,624)</b>
<b>TOTAL SHAREHOLDERS' EQUITY</b>		<b>\$ 72,282,020</b>		<b>\$ 70,421,026</b>

The accompanying notes are an integral part of these consolidated financial statements.

# ROCKWELL DIAMONDS INC.

Consolidated Statements of Cash Flows  
(Unaudited - Expressed in Canadian Dollars)

Cash provided by (used in):	Three months ended August 31		Six months ended August 31	
	2009	2008	2009	2008
<b>Operating activities</b>				
Loss for the period	\$ (2,521,646)	\$ (2,249,848)	\$ (6,625,577)	\$ (3,051,200)
Items not affecting cash				
Accretion of reclamation obligation	31,885	98,779	17,597	167,402
Amortization and depletion	3,125,915	1,794,224	3,818,835	3,625,611
Amortization of capital lease equipment	13,394	878,504	1,139,554	1,621,349
Write-down of mineral property interests	–	(895,590)	657,634	(470,615)
Stock-based compensation (note 10)	17,957	372,502	134,066	1,058,101
Loss on disposal of equipment	11,439	283,785	37,220	304,753
Future income tax recovery	(719,427)	(592,800)	(2,065,834)	(1,274,808)
Unrealized foreign exchange gain	(93,117)	1,553,769	(409,836)	1,968,720
Non-controlling interest	(338,122)	(589,004)	(791,739)	(677,287)
Changes in non-cash working capital items				
Accounts receivable	466,344	430,708	249,175	(97,687)
Amounts due to and from related parties	724,662	(233,875)	2,662,165	(707,599)
Inventory	(842,453)	743,635	(756,589)	(1,716,400)
Prepayments	(77,011)	2,198,419	(46,490)	(97,918)
Accounts payable and accrued liabilities	514,222	1,874,246	835,331	1,167,006
Income taxes	159,439	66,125	501,785	383,189
Cash provided used in operating activities	473,481	5,733,580	(642,703)	2,202,617
<b>Investing activities</b>				
Acquisition of Saxendrift Mines (Pty) Limited	–	–	–	(12,205,245)
Restricted cash	–	(316,583)	2,698,719	10,244,319
Proceeds on sale of shares in subsidiary	–	2,537,066	–	2,537,066
Purchase of equipment and mineral properties	(455,198)	(7,871,929)	(2,854,924)	(9,617,907)
Proceeds received on disposal of equipment	32,953	76,943	366,415	216,370
Other assets and deposits	(74,527)	(290,912)	(97,386)	373,614
Reclamation deposits	(120,845)	(43,791)	(423,866)	(86,394)
Cash used in investing activities	(617,617)	(5,909,206)	(311,042)	(8,538,177)
<b>Financing activities</b>				
Principal repayments under capital lease obligations	(579,022)	(2,189,963)	(1,754,240)	(4,583,049)
Common shares issued for cash, net of issue costs	–	–	930	–
Addition of capital lease obligations	–	14,213	–	1,033,647
Amounts received to related parties	–	(25,570)	–	7,053
Amounts paid pursuant to property acquisition	–	(94,174)	–	364,901
Drawdown of credit facility	(611,013)	–	(423,982)	–
Cash provided by (used in) financing activities	\$ (1,190,035)	(2,295,494)	\$ (2,177,292)	(3,177,448)
<b>Decrease in cash and cash equivalents during the period</b>	<b>(1,334,171)</b>	<b>(2,471,120)</b>	<b>(3,131,037)</b>	<b>(9,513,008)</b>
Cash and cash equivalents, beginning of period	\$ 2,200,941	12,581,960	\$ 3,997,807	19,623,848
<b>Cash and cash equivalents, end of period</b>	<b>\$ 866,770</b>	<b>\$ 10,110,840</b>	<b>\$ 866,770</b>	<b>\$ 10,110,840</b>
Interest paid on facilities during the period	\$ 73,047	\$ –	\$ 480,349	\$ –
Interest paid on capital leases	251,548	162,790	594,269	248,831
Interest received	91,692	742,169	234,481	2,123,452
Income taxes paid during the period	(159,439)	(66,125)	(501,785)	(383,189)
<b>Supplemental disclosure of non-cash investing and financing activities:</b>				
Issuance of commons shares as consideration for acquisition of property	\$ –	\$ –	\$ –	\$ (7,857,143)
Issuance of common shares as consideration for property finders fees	\$ –	\$ –	\$ –	\$ –
Equipment acquired under capital lease	\$ –	14,214	\$ –	1,033,648

The accompanying notes are an integral part of these consolidated financial statements.

# ROCKWELL DIAMONDS INC.

Notes to the Consolidated Financial Statements

For the three and six months ended August 31, 2009 and 2008

(Unaudited – Expressed in Canadian Dollars unless otherwise stated)

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## 1. CONTINUANCE OF OPERATIONS AND GOING CONCERN

Rockwell Diamonds Inc. (“Rockwell” or the “Company”) is engaged in the business of diamond production and the acquisition and exploration of natural resource properties. The Company’s principal mineral property interests are located in South Africa.

The accompanying interim consolidated financial statements have been prepared on a going concern basis in accordance with Canadian generally accepted accounting principles (“GAAP”). The going concern basis of presentation assumes that Rockwell will continue in operation for the foreseeable future and will be able to realise its assets and discharge its liabilities and commitments in the normal course of business.

The Company incurred losses of \$6,625,577 during the six months ended August 31, 2009 and continues to incur losses subsequent to the end of the second quarter. Although the Company has reduced costs substantially, sales prices of diamonds have also decreased compared to fiscal 2009. The risk that cash and working capital will not be sufficient to fund the continuing losses indicates that a material uncertainty exists which may cast substantial doubt on the ability of the Company to continue as a going concern. The directors believe that the Company will continue as a going concern for the next quarter as well as the fiscal year ending on February 28, 2010.

The cash flow forecasts for the 2010 fiscal year indicate that additional funds of approximately \$4 million will be required to enable the Company to continue as a going concern. The additional funding was calculated on the assumption that volumes remain constant with current production, with the new plant still operating at below 50% capacity, prices remaining at current depressed levels (which are 50% below pre-September 2008 levels) and the South African Rand remains at current levels relative to the United States and Canadian dollar.

The Company is in the advanced stages of raising capital to meet expenditure requirements to ensure the continuation of operations until such time as the international diamond markets recover and sufficient funds for capital expenditure to improve efficiencies at existing operations, expand operations to take advantage of existing resources and reopen operations that have been on care and maintenance.

Working capital will be applied to reducing the short term finance and the payment deferral, which will cause significant reductions in interest expenses. Working capital will also be sufficient to provide financial leeway to hold sales tenders at dates where there is higher market demand due to seasonal events. This will generate larger profit margins and improved cash inflows. The capital expenditure will be applied to reopening operations that were placed on care and maintenance and the commencement of the credit crunch, expand operations to take advantage of existing resources and improve efficiencies at existing plants, which will increase production and thereby reducing operation costs. Under a standby commitment, the minimum amount of capital to be raised will ensure that there is sufficient capital to meet expenditure requirements and generate sufficient funds to apply to capital expenditure to ensure improved efficiencies to return the company to profitability.

Accordingly, the interim financial statements have been prepared on the basis of accounting policies applicable to a going concern. If the going concern basis is not appropriate for these consolidated financial statements, then significant adjustments would be necessary in the carrying value of assets and liabilities, the reported revenues and expenses, and the balance sheet classifications used.

# ROCKWELL DIAMONDS INC.

Notes to the Consolidated Financial Statements

For the three and six months ended August 31, 2009 and 2008

(Unaudited – Expressed in Canadian Dollars unless otherwise stated)

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## 2. BASIS OF PRESENTATION AND PRINCIPLES OF CONSOLIDATION

These consolidated financial statements have been prepared in accordance with Canadian GAAP. These consolidated financial statements include the accounts of the Company, its subsidiaries and its variable interest entities where the Company has been determined to be the primary beneficiary. All significant intercompany balances and transactions have been eliminated upon consolidation.

These interim financial statements do not include all the disclosures required for annual financial statements under generally accepted accounting principles. However, these interim financial statements follow the same accounting policies and methods of application as the Company's most recent audited annual financial statements except for the changes described in note 3 below. These interim consolidated financial statements should be read in conjunction with the Company's audited annual consolidated financial statements for the year ended February 28, 2009, which are filed on [www.sedar.com](http://www.sedar.com).

## 3. CHANGES IN ACCOUNTING POLICIES

Effective March 1, 2009, the Company adopted the following accounting standards issued by the Canadian Institute of Chartered Accountants ("CICA"). These new standards have been adopted on a prospective basis with no restatement to prior period financial statements.

(a) *Section 3064 – Goodwill and Intangibles*

The Canadian Accounting Standards Board ("AcSB") issued CICA Handbook Section 3064 which replaces Section 3062, "Goodwill and Other Intangible Assets", and Section 3450, "Research and Development Costs". This new section establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets. Standards concerning goodwill remain unchanged from the standards included in the previous Section 3062. The Company evaluated the impact of this new standard and concluded that this standard did not have a significant impact on the financial statements.

(b) *EIC 173 – Credit Risk and the Fair value of Financial Assets and Financial Liabilities*

The AcSB issued EIC-173 which requires the Corporation to consider its own credit risk as well as the credit risk of its counterparty when determining the fair value of financial assets and liabilities, including derivative instruments. The standard is effective for the first quarter of fiscal 2010 and is required to be applied retrospectively without restatement of prior periods. The adoption of this standard did not have an impact on the valuation of financial assets or liabilities of the Company.

(c) *EIC 174 – Mining Exploration Costs*

The AcSB issued EIC-174, "Mining Exploration Costs" which provides guidance to mining enterprises related to the measurement of exploration costs and the conditions that a mining enterprise should consider when determining the need to perform an impairment review of such costs. The accounting treatments provided in EIC-174 have been applied in the preparation of these financial statements and did not have an impact on the valuation of the Company's mineral properties.

# ROCKWELL DIAMONDS INC.

Notes to the Consolidated Financial Statements

For the three and six months ended August 31, 2009 and 2008

(Unaudited – Expressed in Canadian Dollars unless otherwise stated)

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(d) *New Accounting Standards Not Yet Adopted:*

i) *International Financial Reporting Standards ("IFRS")*

In 2006, the Canadian Accounting Standards Board ("AcSB") published a new strategic plan that will significantly affect financial reporting requirements for Canadian companies. The AcSB strategic plan outlines the convergence of Canadian GAAP with International Financial Reporting Standards ("IFRS") over an expected five year transitional period. In February 2008, the AcSB announced that 2011 is the changeover date for publicly-listed companies to use IFRS, replacing Canadian GAAP. The date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. The transition date of March 1, 2011 will require the restatement for comparative purposes of amounts reported by the Company for the year ended February 28, 2011. The Company is currently in the process of developing an IFRS conversion plan and evaluating the impact of the transition to IFRS.

ii) *Business Combinations/Consolidated Financial Statements/Non-Controlling Interests*

The AcSB adopted CICA sections 1582, "Business Combinations", 1601, "Consolidated Financial Statements", and 1602, "Non-Controlling Interests" which superseded current sections 1581, "Business Combinations" and 1600 "Consolidated Financial Statements". These new sections replace existing guidance on business combinations and consolidated financial statements to harmonize Canadian accounting for business combinations with IFRS. These Sections will be applied prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011. Earlier adoption is permitted. If an entity applies these Sections before January 1, 2011, it is required to disclose that fact and apply each of the new sections concurrently. The Corporation is currently evaluating the impact of the adoption of these changes on its consolidated financial statements.

## 4. CAPITAL MANAGEMENT AND FINANCIAL INSTRUMENTS

(a) *Capital Management Objectives*

The Company's primary objectives when managing capital are to safeguard the Company's ability to continue as a going concern, so that it can continue to provide returns for shareholders, and to have sufficient funds on hand for business opportunities as they arise.

The Company considers the components of shareholders' equity, as well as its cash and cash equivalents, and bank indebtedness as capital. The Company's investment policy is to invest its cash in highly liquid short-term interest-bearing investments, having maturity dates of three months or less from the date of acquisition, that are readily convertible to known amounts of cash.

The Company manages the capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets. The Company may issue new shares through private placements, issue debt, or return capital to shareholders, in order to maintain or adjust the capital structure.



## ROCKWELL DIAMONDS INC.

Notes to the Consolidated Financial Statements

For the three and six months ended August 31, 2009 and 2008

(Unaudited – Expressed in Canadian Dollars unless otherwise stated)

As at August 31, 2009, the Company is not subject to externally imposed capital requirements other than the overdraft facility (note 12).

In order to facilitate the management of its capital requirements, the Company prepares annual expenditure budgets that are updated as necessary depending on various factors, including successful capital deployment and general industry conditions.

There were no changes to the Company's approach to capital management during the three months ended August 31, 2009 and the Company expects it will be able to raise sufficient capital resources to carry out its plans of operations for fiscal 2010 as disclosed in note 1.

(b) *Carrying Amounts and Fair Values of Financial Instrument*

The carrying value of the Company's cash and cash equivalents, accounts receivable, restricted cash, trade receivable from a related party, reclamation deposits, bank indebtedness, accounts payable and accrued liabilities and due to/from related parties approximate their fair values.

Aside from the financial assets mentioned above, the carrying amounts of the Company's other financial assets approximate their fair values. The following tables show the estimated fair values of the financial assets:

	Estimated fair value as at	
	August 31, 2009	February 28, 2009
Cash and equivalents	\$ 866,770	\$ 3,997,807
Restricted cash	-	2,698,719
Held for trading	\$ 866,770	\$ 6,696,526
Accounts receivable	\$ 881,851	\$ 1,131,026
Trade receivable from a related party	1,451,604	3,490,725
Loans and receivables	\$ 2,333,455	\$ 4,621,751
Reclamation deposits	\$ 3,083,508	\$ 2,659,642
Available for sale financial assets	\$ 3,083,508	\$ 2,659,642
Total financial assets	\$ 6,283,733	\$ 13,977,919

The fair value of reclamation deposits represents the market value of quoted investments.

# ROCKWELL DIAMONDS INC.

## Notes to the Consolidated Financial Statements

For the three and six months ended August 31, 2009 and 2008

(Unaudited – Expressed in Canadian Dollars unless otherwise stated)

The fair values of financial liabilities are as follows:

	Estimated fair value as at	
	August 31, 2009	February 28, 2009
Bank Indebtedness	\$ 3,116,898	\$ 3,540,880
Accounts payable and accrued liabilities	5,667,369	4,832,038
Amounts due to a related party	1,200,029	576,985
Capital lease obligations	6,970,537	8,724,777
Income tax liability	957,831	456,046
	\$ 17,912,664	\$ 18,130,726

## 5. INVENTORY

	As at August 31, 2009	As at February 28, 2009
Rough diamond inventory	\$ 2,357,137	\$ 1,845,986
Mine supplies	2,119,371	1,873,933
Total inventory	\$ 4,476,508	\$ 3,719,919

As at August 31, 2009, rough diamond inventory was valued at net realizable value. This is established using the values of previous tenders less estimated cost of realizing the sale.

## 6. PROPERTY, PLANT AND EQUIPMENT

	As at August 31, 2009		
	Cost	Accumulated Amortization	Net book value
Land and buildings	\$ 6,395,904	\$ –	\$ 6,395,904
Processing plant and equipment	57,624,602	20,018,519	37,606,083
Processing plant and equipment under capital lease obligation	23,827,112	7,429,969	16,397,143
Office equipment	959,460	433,992	525,468
Vehicles and light equipment	1,753,222	781,107	972,115
	\$ 90,560,300	\$ 28,663,587	\$ 61,896,713

  

	As at February 28, 2009		
	Cost	Accumulated Amortization and Impairments	Net book value
Land and buildings	\$ 5,822,677	\$ 228,591	\$ 5,594,086
Processing plant and equipment	52,090,193	15,102,720	36,987,473
Processing plant and equipment under capital lease obligation	21,374,971	5,931,733	15,443,238
Office equipment	859,678	302,618	557,060
Vehicles and light equipment	1,579,592	592,263	987,329
	\$ 81,727,111	\$ 22,157,925	\$ 59,569,186

## ROCKWELL DIAMONDS INC.

Notes to the Consolidated Financial Statements

For the three and six months ended August 31, 2009 and 2008

(Unaudited – Expressed in Canadian Dollars unless otherwise stated)

The Company's bankers have registered two notarial general covering bonds of ZAR 10 million (\$1.4 million) over all loose assets on the property of the farm Holpan, Barkley West, Northern Cape (refer Note 12).

### 7. MINERAL PROPERTY INTERESTS

<b>Acquisition Costs</b>	<b>As at August 31, 2009</b>	<b>As at February 28, 2009</b>
<b>H.C. Van Wyk Diamonds and Klipdam Mining</b>		
Balance, beginning of period	\$ 22,373,984	\$ 25,247,936
Acquisition costs	–	55,746
Foreign exchange and other adjustments	2,235,795	(7,321,972)
Future income tax liability	–	6,390,327
Change in future income tax rate	–	(201,415)
Depletion of mineral properties during the period	(130,188)	(1,796,639)
H.C. Van Wyk and Klipdam, end of period	\$ 24,479,591	\$ 22,373,983
<b>Saxendrift Mine</b>		
Balance, beginning of period	\$ 6,520,494	\$ –
Acquisition costs	1,997,268	5,295,754
Foreign exchange and other adjustments	917,468	(178,144)
Future income tax liability	776,715	1,990,181
Depletion of mineral properties during the period	(37,711)	(587,297)
Saxendrift Mine (Pty) Ltd, end of period	\$ 10,174,234	\$ 6,520,494
<b>Balance, end of period</b>	<b>\$ 34,653,825</b>	<b>\$ 28,894,477</b>

#### *Acquisition of Niewejaarskraal mining rights relating to Saxendrift Mine (Pty) Ltd. acquisition*

As at February 28, 2009, the Company was committed to pay Trans Hex for the acquisition of the remaining Niewejaarskraal mining rights. The Company had placed \$2.7 million in trust toward application of the remaining payment, to be released to Transhex upon the anticipated grant of Ministerial Consent to the cession of each of the Outstanding Mining Rights to the Company and registration of cession of such rights in its name.

On April 11<sup>th</sup>, 2009 all the conditions precedent were met and the Company paid ZAR18.9 million (\$2.6 million) in cash to Trans Hex for the remaining Niewejaarskraal mining rights of which ZAR 16.5 million (\$2.0 million) was capitalized. This action completed the Saxendrift/Remhoogte-Holsloot transaction negotiated during April 2008. The Company has no further commitments in relation to more acquisitions.

## ROCKWELL DIAMONDS INC.

Notes to the Consolidated Financial Statements

For the three and six months ended August 31, 2009 and 2008

(Unaudited – Expressed in Canadian Dollars unless otherwise stated)

### 8. CAPITAL LEASE OBLIGATIONS

Included in property, plant and equipment are mining equipment that the Company acquired pursuant to three to four year capital lease agreements.

The Company's capital lease obligations are with the following financial institutions:

	<b>As at August 31, 2009</b>	<b>As at February 28, 2009</b>
Stannic	\$ 250,710	\$ 883,409
Wesbank	71,167	81,779
Nedbank	-	178,092
Komatfin	6,648,660	7,581,497
	<b>\$ 6,970,537</b>	<b>\$ 8,724,777</b>

Capital lease obligations as detailed above are secured over plant and equipment and are repayable, on average, in 36 monthly installments. Interest is charged at rates of between 12.00% to 12.75% per annum linked to the prevailing prime rate of the relative financial institution mentioned above.

Future minimum lease payments are as follows:

	<b>As at August 31, 2009</b>	<b>As at February 28, 2009</b>
2010	\$ 6,008,067	\$ 6,570,081
2011	1,435,121	2,860,859
2012	-	106,122
Total minimum lease payments	7,443,188	9,537,062
Less: interest portion	(472,651)	(812,285)
Present value of capital lease obligations	6,970,537	8,724,777
Current portion	5,454,805	5,440,181
Non-current portion	\$ 1,515,732	\$ 3,284,596

Commencing July 2009, the Company successfully negotiated a payment deferral of the capital portion of the lease payments on its Komatsu equipment with Komatfin. This enabled the group to defer its cash commitments by ZAR 4 million (\$ 554,000) per month for the months of July 2009 to October 2009.

## ROCKWELL DIAMONDS INC.

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### 9. RECLAMATION OBLIGATION

The continuity of the provision for reclamation costs related to the Holpan, Wouterspan, Klipdam and Saxendrift mines, are as follows:

	As at August 31, 2009	As at February 28, 2009
<b>Holpan, Wouterspan and Klipdam</b>		
Balance, beginning of period	\$ 2,690,335	\$ 1,755,820
Changes during the period:		
Reclamation obligation recognized (expenditure incurred)	(500,718)	(10,274)
Foreign exchange on reclamation	303,592	–
Accretion expense	346,402	944,789
Balance, end of period	\$ 2,839,611	\$ 2,690,335
<b>Saxendrift</b>		
Balance, beginning of period	\$ 1,112,320	\$ –
Changes during the period:		
Reclamation obligation recognized	–	984,720
Foreign exchange on reclamation	133,225	–
Accretion expense	171,913	127,600
Balance, end of period	\$ 1,417,458	\$ 1,112,320
<b>Total reclamation obligation, end of period</b>	<b>\$ 4,257,069</b>	<b>\$ 3,802,655</b>

The rehabilitation provision is based on an independent professional surveyor's measurement of those mined areas which need to be rehabilitated at year-end.

These measurements determine the volume of material needed to reclaim the mined areas. The liability is calculated by applying a cost of ZAR4.00 (\$0.51) for each cubic meter measured, and has been determined with reference to plant, fuel and labour usage and has been found acceptable by the Department of Mineral and Energy Affairs.

As required by regulatory authorities, at August 31, 2009, the Company had cash reclamation deposits totaling \$3,083,508 (2008 – \$3,167,790). These investments have been ceded as security in favour of the guarantees the bank issued on behalf of the group.

# ROCKWELL DIAMONDS INC.

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## 10. SHARE CAPITAL

### (a) Authorized share capital

The Company's authorized share capital consists of an unlimited number of common shares, without par value, and an unlimited number of preferred shares without par value, of which no preferred shares have been issued.

### (b) Share purchase options

The continuity of share purchase options for three months ended August 31, 2009 is as follows:

Expiry date	Exercise price	Feb 28 2009	Granted	Exercised	Expired/ cancelled	August 31 2009
September 24, 2012	\$ 0.62	5,901,334	–	1,500	3,334	5,896,500
November 14, 2012	\$ 0.63	1,104,834	–	–	3,334	1,101,500
June 20, 2011	\$ 0.45	950,000	–	–	–	950,000
		<b>7,956,168</b>	–	1,500	6,668	<b>7,948,000</b>
Weighted average exercise price		\$ 0.60	\$ 0.00	\$ 0.62	\$ 0.63	\$ 0.60
Weighted average fair value of options granted during the period						\$ 0.00

As at August 31, 2009, 7,318,000 of the options outstanding with a weighted average exercise price of \$0.60 per share have vested with grantees.

Using a Black-Scholes option pricing model with the assumptions noted below, the fair values of stock options granted have been reflected in the statement of operations as follows:

	Three months ended August 31		Six months ended August 31	
	2009	2008	2009	2008
Exploration and engineering	\$ 7,807	\$ 134,619	\$ 37,640	\$ 337,243
Operations and administration	10,150	237,883	96,426	720,858
<b>Total compensation cost expensed to operations, with the offset credited to contributed surplus</b>	<b>\$ 17,957</b>	<b>\$ 372,502</b>	<b>\$ 134,066</b>	<b>\$1,058,101</b>

The weighted-average assumptions used to estimate the fair value of options granted are as follows:

	Three months ended August 31		Six months ended August 31	
	2009	2008	2009	2008
Risk free interest rate	nil	4%	nil	4%
Weighted average expected life	nil	4.8 years	nil	4.8 years
Weighted average expected volatility	nil	114%	nil	114%
Expected dividends	nil	nil	nil	nil

# ROCKWELL DIAMONDS INC.

Notes to the Consolidated Financial Statements

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## c) *Share purchase warrants*

The continuity of share purchase warrants (each warrant exercisable into one common share) for the period ended August 31, 2009 is as follows:

Expiry date	November 22, 2009 <sup>(i)</sup>	May 09, 2009 <sup>(ii)</sup>	May 09, 2009 <sup>(iii)</sup>
<b>Balance, February 28, 2009</b>	<b>39,600,000</b>	<b>116,007,154</b>	<b>5,772,000</b>
Issued	–	–	–
Exercised	–	–	–
Expired	–	116,007,154	5,772,000
<b>Balance, August 31, 2009</b>	<b>39,600,000</b>	<b>–</b>	<b>–</b>

- (i) The share purchase warrants are exercisable over three years with the option to exercise at \$0.60 expiring on November 22, 2007, the option to exercise at \$0.80 expiring on November 22, 2008 and the option to exercise at \$1.00 expiring on November 22, 2009.
- (ii) In May 2007, Rockwell completed a \$60 million private placement financing of 116,007,154 million equity Units at \$0.52 each with each Unit consisting of one common share and one share purchase warrant exercisable over two years at \$0.70. These warrants expired unexercised on May 9, 2009.
- (iii) In May 2007, the Company issued 5,772,000 broker warrants exercisable over two years at \$0.70 expiring on May 9, 2009. Using a Black-Scholes option pricing model, the fair value of the 5,772,000 broker warrants granted in the amount of \$1,693,197 (2008 \$1,693,197) have been reflected in the consolidated balance sheet. The weighted-average assumptions used to estimate the fair value of warrants granted were an expected volatility of 97%, expected dividends of nil, expected life of 2 years and risk free rate of 4%. These warrants expired unexercised on May 9, 2009.

## 11. RELATED PARTY BALANCES AND TRANSACTIONS

Balances payable	As at August 31, 2009	As at February 28, 2009
Jeffrey Brenner	\$ –	\$ 7,890
Jakes Tyres (g)	21,660	5,498
Hunter Dickinson Services Inc. (a)	740,711	180,267
Seven Bridges Trading (c)	10,352	–
<b>Current balances payable</b>	<b>\$ 772,723</b>	<b>\$ 193,655</b>
Liberty Lane (i)	427,306	383,330
<b>Long-term balances payable</b>	<b>\$ 1,200,029</b>	<b>\$ 383,330</b>
Balances receivable		
Flawless Diamonds Trading House (e)	\$ 1,395,997	\$ 3,441,510
Banzi Trade 26 (Pty) Ltd (f)	23,482	19,547
Diacor CC (h)	32,125	29,668
	<b>\$ 1,451,604</b>	<b>\$ 3,490,725</b>

# ROCKWELL DIAMONDS INC.

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Transactions	Three months ended Aug 31		Six months ended Aug 31	
	2009	2008	2009	2008
Services rendered and expenses reimbursed:				
Hunter Dickinson Services Inc. (a)	\$ 173,616	\$ 249,346	\$ 536,627	\$ 380,708
CEC Engineering (b)	–	14,289	–	14,289
Seven Bridges Trading (c)	57,396	37,128	73,135	67,992
Cashmere Trading (d)	–	9,483	–	–
Banzi Trade 26 (Pty) Ltd (f)	6,666	4,927	7,578	12,573
Jakes Tyres (g)	38,815	148,644	43,845	348,037
Diacor CC (h)	–	32,696	–	36,314
Sales rendered to:				
Flawless Diamonds Trading House (e)	\$ 5,802,006	\$ 9,912,702	\$ 9,674,805	\$ 17,007,623
Banzi Trade 26 (Pty) Ltd (f)	\$ 861	\$ –	\$ 1,438	\$ 884

- (a) Hunter Dickinson Services Inc. (“HDSI”) is a private company with a director in common with the Company. HDSI provides geological, technical, corporate development, administrative and management services to, and incurs third party costs on behalf of, the Company on a full cost recovery market related basis pursuant to an agreement dated November 21, 2008.
- (b) CEC Engineering Ltd. is a private company owned by David Copeland, Chairman and a director of the Company, which provides engineering and project management services at market rates.
- (c) Seven Bridges Trading is a wholly owned subsidiary of Randgold Resources, a public company where Mark Bristow, a director of the Company, serves in an executive capacity. Seven Bridges Trading provides office, conferencing, information technology, and other administrative and management services at market rates to the Company’s South African subsidiaries.
- (d) Cashmere Trading is a private company owned by Hennie Van Wyk, a former officer of the Company, which provides helicopter services for the movement of product on an ad-hoc basis at competitive market rates thereby providing benefits to the company and its employees in respect of secure transport of high value product and reduced insurance premiums.
- (e) Flawless Diamonds Trading House (“Flawless”) is a private company where certain directors, former directors and officers of the Company, namely, Messr. Brenner, J W and D M Bristow and Van Wyk, are shareholders of. Flawless is a registered diamond broker which provides specialist diamond valuation, marketing and tender sales services to the Company for a fixed fee of 1% of turnover which is below the market rate charged by similar tender houses.
- (f) Banzi Trade 26 (Pty) Ltd (“Banzi”) is 49% owned by HC van Wyk Diamonds Ltd and 51% by Bokomoso Trust. Banzi is an empowered private company established to provide self sustaining job creation programs to local communities as part of the company’s Social and Labour Plan which is required in terms of the Minerals and Petroleum Resources Development Act “MPRDA”). Banzi provides the Company with buildings materials at market rates.
- (g) Jakes Tyres is a private company with former directors and officers (H C van Wyk) in common with the Company that provides tyres, tyre repair services and consumables at market rates to Rockwell’s remote Middle Orange River operations.



# ROCKWELL DIAMONDS INC.

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- (h) Diacor CC is a private company of which H C van Wyk, a former director and officer of the Company, is a director from which the Company has purchased consumable materials at market rates.
- (i) Liberty Lane is the BEE partner of the Saxendrift property and has certain directors in common with the Company.

## 12. BANK INDEBTEDNESS

The Company has an overdraft facility in the amount of ZAR28 million (\$3.9 million) available for its operations, of which \$3.1 million has been utilized. Current operating income is being used to service this facility. This facility has an interest cost of Prime (currently 11% per annum) plus 0.6% and has a notarial bond over assets of ZAR10 million (\$1.4 million).

HC van Wyk Diamonds Ltd holds guarantees by the bank towards Eskom (Electricity Provider) of ZAR1,225,300 (\$172,646) and the Department of Minerals and Energy (DME) of ZAR 21,884,273(\$3,083,508) towards rehabilitation expenses.

## 13. CONTINGENCIES

In connection with the acquisition of Saxendrift, one of the assets purchased from Trans Hex, with a carrying value of \$6,459 is the subject of a dispute between Trans Hex and a third party, which claims ownership in a certain plant. Although the Company is not subject to this dispute and cannot determine the likelihood of the outcome, the Company has a warranty claim with Trans Hex should the third party be successful with its claim against Trans Hex.

During the first quarter of fiscal 2008, pursuant to an amending agreement to the Midamines Agreement, the Company paid consideration of \$600,000 to Midamines in order to increase the size of the concession (Permit 331). As part of such amending agreement, Midamines waived its right to payment of US\$1,200,000 in royalty payment on December 31, 2007. Subsequently, and pursuant to Midamines' persistent breach of material provisions of the Midamines Agreement (coupled with its failure to remedy such instances of breach notwithstanding notice to do so), Durnpike cancelled the Midamines Agreement and claimed damages.

Midamines has subsequently disputed Durnpike's entitlement to cancel the Midamines Agreement and has demanded payment of US\$1,200,000 as well as other amounts which have not yet been particularised. Midamines has threatened to refer the dispute to arbitration and to join Rockwell as party thereto, but no formal referral to arbitration has as yet been forthcoming.

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## **1.1 Date**

This Management Discussion and Analysis ("MD&A") should be read in conjunction with the unaudited consolidated financial statements of Rockwell Diamonds Inc. ("Rockwell", or the "Company") for the three and six months ended August 31, 2009, and the audited consolidated financial statements for the year ended February 28, 2009, prepared in accordance with Canadian generally accepted accounting principles, and publicly available on SEDAR at [www.sedar.com](http://www.sedar.com).

This MD&A is prepared as of October 7, 2009. All dollar figures stated herein are expressed in Canadian dollars, unless otherwise specified.

This discussion includes certain statements that may be deemed "forward-looking statements". All statements in this discussion, other than statements of historical facts, that address future production, reserve potential, exploration drilling, exploitation activities and events or developments that the Company expects are forward-looking statements. Although the Company believes the expectations expressed in such forward-looking statements are based on reasonable assumptions, such statements are not guarantees of future performance and actual results or developments may differ materially from those in the forward-looking statements. Factors that could cause actual results to differ materially from those in forward-looking statements include market prices, exploitation and exploration successes, continued availability of capital and financing and general economic, market or business conditions. Investors are cautioned that any such statements are not guarantees of future performance and that actual results or developments may differ materially from those projected in the forward-looking statements.

### *Information Concerning Estimates of Indicated and Inferred Resources*

This management discussion also uses the terms 'indicated resources' and 'inferred resources'. Rockwell Diamonds Inc advises investors that although these terms are recognized and required by Canadian regulations (under National Instrument 43-101 Standards of Disclosure for Mineral Projects), the U.S. Securities and Exchange Commission does not recognize them. Investors are cautioned not to assume that any part or all of the mineral deposits in these categories will ever be converted into reserves. In addition, 'inferred resources' have a great amount of uncertainty as to their existence, and economic and legal feasibility. It cannot be assumed that all or any part of an Inferred Mineral Resource will ever be upgraded to a higher category. Under Canadian rules, estimates of Inferred Mineral Resources may not form the basis of feasibility or pre-feasibility studies, or economic studies except for Preliminary Assessment as defined under 43-101. Investors are cautioned not to assume that part or all of an inferred resource exists, or is economically or legally mineable.

## **1.2 Overview**

Rockwell Diamonds Inc. ("Rockwell" or the "Company") is engaged in the business of alluvial diamond production. The Company has also investigated other potential diamond acquisitions which would provide accretive value to Rockwell. In the light of current financial and diamond market conditions the Company is unlikely to progress acquisition opportunities until such time as these conditions improve.

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### **1.2.1 Summary**

#### *Operations*

In the 2009 fiscal year, the diamond market was significantly impacted by the world financial crisis. Rough diamond prices are slowly recovering; the average price received over the quarter increased to US\$855 per carat, 54% up from US\$555 per carat obtained in the first quarter.

The Company sold parcels of diamonds in March, May, June, July and late in August 2009. The average price per carat received was US\$531.43 in March, US\$584.69 in May, US\$699.75 in June, US\$807.20 in early July, US\$1,090.55 on July 27 and US\$862.36 in the August/September tenders. The latter decrease was not due to a decline in price, but rather due to a lower grade mix of stones being offered on tender in August.

In fiscal 2010, Rockwell has operated three alluvial diamond mines: Holpan, Klipdam and Saxendrift. The Wouterspan operation remains on care and maintenance.

Wouterspan has been responsible for many of the Company's higher value stones; however, the decision to suspend operations was due to the relatively high operation costs and the collapse in the demand for high value stones.

The Company is currently in the process of raising capital to strengthen its balance sheet, settle short term liabilities and a payment deferral on equipment leases negotiated with Komatfin, undertake further plant improvement and optimization at existing operations, and initiate low cost modernization of the Wouterspan processing plant for potential re-commissioning subject to further improvements in diamond prices and this will enable the Company to upgrade the plant at Wouterspan mine to a higher volume and therefore more economical operation. This, coupled with operational improvements, reduction in operating costs, and improved prices and demand for diamonds will ensure that the Company returns to profit.

In the three month period ended August 31, 2009:

- 7,935.94 carats were produced at the Holpan/Klipdam and Saxendrift operations, with a small number of carats (8.78 carats) being recovered through the Wouterspan final recovery plant during auditing and reprocessing of concentrate material.
- 6,119.7 carats were sold at an average price of US\$854.86 per carat.
- Revenues from sales of \$5.8 million together with other sales of \$0.1 million resulted in \$5.9 million in revenue.
- Cost of sales of totalled \$4.8 million; and amortization totalled \$3.1 million, resulting in an operating loss of \$2.0 million for the period.

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- Net general and administrative expenses amounted to \$1.3 million, interest expenses of \$0.2 million offset by a net tax recovery of \$0.7 million, resulted in a loss of \$2.5 million or 0.01 cents per share.

In the six months ended August 31, 2009:

- 11,957.16 carats were produced from operations at Holpan/Klipdam, Wouterspan and Saxendrift.
- 11,235.99 carats were sold at an average price of US\$718.22 per carat.
- Revenues from sales of \$9.67 million and other sales of \$0.17 million resulted in \$9.8 million in revenue.
- Cost of sales of \$9.6 million and amortization totalled \$5.0 million, resulting in an operating loss of \$4.8 million for the period.
- Net general and administrative expenses amounted to \$3.2 million, interest expenses of \$0.8 million offset by a net tax recovery of \$2.0 million, resulted in a loss of \$6.6 million or \$0.03 per share.

Diamonds in inventory at August 31, 2009 totalled 4,247.49 carats.

#### *Corporate*

On April 29, 2009, Pala Investments Holdings Limited (“Pala”) called a special shareholders’ meeting of the Company. The meeting was called to remove certain directors of the Company, to appoint and elect certain new directors and to amend and terminate the Company’s shareholders’ rights plan. The special shareholders meeting was held on June 17, 2009 and the proposed resolutions to reconstitute the Board and amend and terminate the shareholders’ rights plan were not approved by the shareholders.

As a result of this, two directors and Audit Committee members, Messers G. Radke and T. Janes resigned from the Board of Directors. Subsequent to the quarter ended August 31, 2009, Messer’s W. Jacobs and R. Linnell have been appointed to the Board of Directors. The new directors have joined Mr. W. Fisher to form the current Audit Committee.

#### **1.2.2 Financing**

During the quarter, the Company invoked a four month payment deferral (capital portion of Hire Purchase lease payments) from Komatfin, the financial institution that finances the Mobile Production Vehicles (yellow fleet). As at the end of the quarter, capital lease obligations were \$6.97 million of a leased fleet which originally cost \$23.8 million. Total plant and equipment at a cost of \$81.4 and a net book value of \$54 million make up the operations plant and yellow fleet.

The payment deferral, which commenced in July and will run until November 1, 2009, will provide short term financing of \$2.2 million. The period of the Komatfin Hire Purchase finance agreements will not be increased and subsequent payments will be adjusted to address the loan amount.

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Rockwell is in the process of securing equity purchase commitments to raise \$7 to \$10 million at prevailing share prices, less allowable discounts, in order to strengthen the Company's balance sheet, settle short term debt including the payment deferral negotiated with Komatfin in respect of equipment leases and to undertake further production improvements and cost saving measures at existing operations. If funds permit, the Company will also initiate the modernization of the Wouterspan processing plant with a view to re-commission this operation subject to further improvements in diamond prices. The fund-raising is expected to be achieved through a combination rights offering and private placement although there can be no certainty of its success at the present time.

### **1.2.3 Agreements**

#### ***Black Economic Empowerment Holdings ("BEE") in Rockwell Properties***

During the year ended May 31, 2007, Africa Vanguard Resources (Pty) Limited ("AVR"), the holding Company of Richtrau No 136 (Pty) Limited ("Richtrau"), purchased through Richtrau a 15% interest in Van Wyk Diamond Group ("VWDG") from the Van Wyk Trust for an amount of ZAR22 million (C\$3.4 million). The holdings of the VWDG comprised the mining projects known as Holpan, Klipdam, and Wouterspan purchased by Rockwell through its wholly owned South African subsidiary Rockwell Resources RSA (Pty) Limited ("Rockwell RSA") from H C Van Wyk Diamonds Limited. Subsequently on November 30, 2008, AVR indicated its commitment to increase its shareholding in the VWDG to 26% by subscribing for an additional 11% of the shares in each of the entities comprising VWDG. The additional 11% stake was acquired by another subsidiary of AVR, Georgia Avenue Investments (Pty) Limited ("Georgia"), at a subscription price of ZAR17.5 million. The AVR group was also contractually committed to inject ZAR10.5 million in working capital into the VWDG.

Due to the world wide credit contraction and economic recession, depressed market conditions and decline in diamond prices, the AVR group indicated to the Board of Directors of Rockwell RSA (the holding company of the entities in VWDG) during the fourth quarter of fiscal 2009 that it was unable to make outstanding payments to complete its financial obligations, and that it was pursuing other funding mechanisms to meet its obligations. As at February 28, 2009, AVR owed Rockwell approximately ZAR19 million to conclude the Georgia transactions; this amount is outstanding. The contractually committed ZAR10.5 million due to VWDG has also not been received from AVR at this point in time.

Rockwell RSA has, in conjunction with AVR, endeavoured to identify alternate sources of funding to assist AVR complete its investment in the VWDG projects, and currently negotiations are being progressed with the Industrial Development Corporation ("IDC") of South Africa. Rockwell RSA is in on-going discussions with AVR, and has also engaged with the Department of Minerals and Energy with the assistance of its legal counsel to address the completion of the BEE participation in the share capital of the entities comprising VWDG. The shares for the outstanding equity purchases are held in trust by legal firm Tabacks pending conclusion of the transaction.

Effective October 2, 2008, AVR via Liberty Lane Investments (Pty) Limited, acquired a shareholding of an effective 26% in the Saxendrift project by subscribing for shares in Saxendrift Mines (Pty) Limited. This transaction was also conducted in respect of the Minerals and Petroleum Resources Development Act and has been structured via a loan structure underwritten by Rockwell Resources RSA (Pty) Limited. AVR has paid an initial deposit of ZAR3 million in respect of this transaction which is structured over a

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two year period. Rockwell is also in discussion with AVR regarding the funding for the outstanding amount of this transaction.

**1.2.4 Production Properties**

*Production and Sales – Quarter Comparison*

The following is a comparison of the current quarter (ended August 31, 2009) with the quarter ended August 31, 2008.

<b>PRODUCTION</b>						
<b>Operation</b>	<b>3 months ended August 31, 2009</b>			<b>3 months ended August 31, 2008</b>		
	<b>Volume (cubic meters)</b>	<b>Carats</b>	<b>Average grade (carats per 100 cubic meters)</b>	<b>Volume (cubic meters)</b>	<b>Carats</b>	<b>Average grade (carats per 100 cubic meters)</b>
Holpan	237,492	2,159.67	0.91	150,285	774.01	0.52
Klipdam	276,260	3,661.07	1.33	210,759	1,622.13	0.77
Wouterspan	-	8.78*	-	120,829	708.12	0.59
Saxendrift	271,427	2,106.42	0.78	84,883	1,161.99	1.37
<b>Total</b>	<b>785,179</b>	<b>7,935.94</b>	<b>1.01</b>	<b>566,756</b>	<b>4,266.25</b>	<b>0.75</b>

\*from reprocessed concentrate

<b>SALES, REVENUE AND INVENTORY</b>								
<b>Operation</b>	<b>3 months ended August 31, 2009</b>				<b>3 months ended August 31, 2008</b>			
	<b>Sales (carats)</b>	<b>Value of Sales (US\$)</b>	<b>Average value (US\$ per carat)</b>	<b>Inventory (carats)</b>	<b>Sales (carats)</b>	<b>Value of Sales (US\$)</b>	<b>Average value (US\$ per carat)</b>	<b>Inventory (carats)</b>
Holpan	1,566.03	1,122,021	716.47	1,276.65	1,015.39	842,285	829.52	267.65
Klipdam	2,634.37	1,210,408	459.47	1,904.31	1,898.91	5,294,781	2,788.33	679.31
Wouterspan	-	-	-	22.49	1,093.56	1,700,432	1,554.95	272.88
Makoensklouf	-	-	-	-	-	-	-	0.38
Saxendrift	1,919.30	2,899,053	1,510.47	1,044.04	1,016.48	1,967,072	1,935.18	420.56
<b>Total</b>	<b>6,119.70</b>	<b>5,231,482</b>	<b>854.86</b>	<b>4,247.49</b>	<b>5,024.34</b>	<b>9,804,570</b>	<b>1,951.41</b>	<b>1,640.78</b>

<b>INVENTORY (carats)</b>				
<b>Operation</b>	<b>Rough Diamond Inventory June 1, 2009</b>	<b>Production</b>	<b>Rough Diamond Sales</b>	<b>Rough Diamond Inventory August 31, 2009</b>
Holpan	683.01	2,159.67	1,566.03	1,276.65
Klipdam	877.61	3,661.07	2,634.37	1,904.31
Wouterspan	13.71	8.78	-	22.49
Saxendrift	856.92	2,106.42	1,919.30	1,044.04
<b>Total</b>	<b>2,431.25</b>	<b>7,935.94</b>	<b>6,119.70</b>	<b>4,247.49</b>

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***Production and Sales –Six Month Comparison***

The following is a comparison of the first six months of fiscal 2010 (ended August 31, 2009) with the six months ended August 31, 2008.

<b>PRODUCTION</b>						
<b>Operation</b>	<b>6 months ended August 31, 2009</b>			<b>6 months ended August 31, 2008</b>		
	<b>Volume (cubic meters)</b>	<b>Carats</b>	<b>Average grade (carats per 100 cubic meters)</b>	<b>Volume (cubic meters)</b>	<b>Carats</b>	<b>Average grade (carats per 100 cubic meters)</b>
Holpan	428,152	3,146.09	0.73	356,751	2,579.36	0.72
Klipdam	486,970	5,268.91	1.08	429,429	4,232.01	0.99
Wouterspan	-	8.78	-	363,069	2,328.42	0.64
Saxendrift	508,390	3,533.38	0.7	89,484	1,437.04	1.58
<b>Total</b>	<b>1,423,512</b>	<b>11,957.16</b>	<b>0.84</b>	<b>1,238,733</b>	<b>10,576.83</b>	<b>0.85</b>

<b>SALES, REVENUE AND INVENTORY</b>								
<b>Operation</b>	<b>6 months ended August 31, 2009</b>				<b>6 months ended August 31, 2008</b>			
	<b>Sales (carats)</b>	<b>Value of Sales (US\$)</b>	<b>Average value (US\$ per carat)</b>	<b>Inventory (carats)</b>	<b>Sales (carats)</b>	<b>Value of Sales (US\$)</b>	<b>Average value (US\$ per carat)</b>	<b>Inventory (carats)</b>
Holpan	2,710.52	1,438,365	530.66	1,276.65	2,589.96	3,471,620	1,340.41	267.65
Klipdam	5,107.23	2,393,682	468.69	1,904.31*	3,912.71	7,744,322	1,979.27	679.31
Wouterspan	561.69	269,088	479.07	22.49	2,360.46	3,704,334	1,569.33	272.88
Makoenskloof	-	-	-	-	-	-	-	0.38
Saxendrift	2,856.55	3,968,797	1,389.37	1,044.04	1,016.48	1,967,072	1,935.18	420.56
<b>Total</b>	<b>11,235.99</b>	<b>8,069,931</b>	<b>718.22</b>	<b>4,247.49</b>	<b>9,879.61</b>	<b>16,887,348</b>	<b>1,709.31</b>	<b>1,640.78</b>

<b>INVENTORY (carats)</b>				
<b>Operation</b>	<b>Rough Diamond Inventory Beginning of Period</b>	<b>Production</b>	<b>Rough Diamond Sales</b>	<b>Rough Diamond Inventory End of Period</b>
Holpan	841.08	3,146.09	2,710.52	1,276.65
Klipdam	1,742.63	5,268.91	5,107.23	1,904.31*
Wouterspan	575.40	8.78	561.69	22.49
Saxendrift	367.21	3,533.38	2,856.55	1,044.04
<b>Total</b>	<b>3,526.32</b>	<b>11,957.16</b>	<b>11,235.99</b>	<b>4,247.49</b>

\*Included in the Klipdam inventory are 199.89 carats from Windsorton, a prospecting right

***Holpan/Klipdam***

The Holpan/Klipdam Property is located 45 km from Kimberley, South Africa. It consists of the contiguous Holpan 161 farm and Klipdam 157 farm, covering an area of 3,836 hectares. The production from Holpan and Klipdam is accounted for separately because they are separate operating entities.



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Quarter ended August 31, 2009

Production at Holpan in the quarter was 2,159.67 carats from 237,492 cubic meters (439,360 tonnes) of gravels processed, compared with 774.01 carats from 150,285 cubic meters (300,570 tonnes) of gravels processed in the quarter ended August 31, 2008.

Sales from Holpan were 1,566.03 carats at an average value of US\$716.47 per carat, an increase in carats and a decrease in value from the 1,015.39 carats at an average value per carat of US\$829.52 sold in the quarter ended August 31, 2008.

Production at Klipdam was 3,661.07 carats from 276,260 cubic meters (511,081 tonnes) of gravels, compared to 1,622.13 carats from 210,759 cubic meters (421,518 tonnes) of gravels produced in the quarter ended August 31, 2008.

Sales from Klipdam were 2,634.37 carats at an average value of US\$459.47 per carat, an increase in carats and decrease in value compared to 1,898.91 carats at an average value per carat of US\$2,788.33 in the quarter ended August 31, 2008. The decrease in carat value was, in part, the result of a lower grade/quality mix of stones offered for tender in August.

Six months ended August 31, 2009

Production at Holpan over the six months was 3,146.09 carats from 428,152 cubic meters (792,081 tonnes) of gravels processed, compared with 2,579.36 carats from 356,751 cubic meters (713,502 tonnes) of gravels processed in the six months ended August 31, 2008.

Sales from Holpan were 2,710.52 carats at an average value of US\$530.66 per carat, an increase in carat sales and decrease in value per carat sold from 2,589.96 carats at an average value of US\$1,340.41 per carat in the quarter ended August 31, 2008.

The inventory at Holpan is 1,276.65 carats.

In the first half of the 2010 fiscal year, production at Klipdam was 5,268.91 carats from 486,970 cubic meters (900,894 tonnes) of gravels, compared to 4,232.01 carats from 429,429 cubic meters (858,858 tonnes) of gravels produced in the quarter ended August 31, 2008.

Sales from Klipdam were 5,107.23 carats at an average value of US\$468.69 per carat, an increase in carats sold but a decrease in value per carat sold from 3,912.71 carats at an average value of US\$1,979.27 per carat in the quarter ended August 31, 2008.

There is an inventory of 1,904.31 carats for Klipdam.

***Wouterspan***

The Wouterspan Property is located near Douglas, South Africa. It comprises portions, totalling 969.4 hectares, of the Lanyon Vale 376 farm. Operations are taking place on two portions of the property called the Farhom and Okapi farms, exploiting the Rooikoppie and Primary gravel units.

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Quarter ended August 31, 2009

During the quarter, 8.78 carats were recovered from reprocessing of stockpiled concentrate. This is a decrease from 708.12 carats produced from 120,829 cubic meters (241,658 tonnes) of gravels processed in the quarter ended August 31, 2008.

Six months ended August 31, 2009

During the first half of the fiscal 2010 year, 8.78 carats were recovered from reprocessing of stockpiled concentrate. This is a decrease from 2,328.42 carats produced from 363,069 cubic meters (726,138 tonnes) of gravels processed in the six months ended August 31, 2008.

Sales from Wouterspan were 561.69 carats from inventory which received an average price of US\$479.07 per carat. This is a decrease in carats and value per carat sold from 2,360.46 carats at an average value of US\$1,569.33 per carat in the six months ended August 31, 2008.

The inventory at Wouterspan is 22.49 carats.

***Saxendrift Property***

The Saxendrift property is located on the south bank of the Middle Orange River and adjacent to the Wouterspan diamond operation. The Company acquired and re-commissioned the property in the first quarter of fiscal 2009.

Quarter ended August 31, 2009

During the quarter, the property produced 2,106.42 carats from 271,427 cubic meters (569,997 tonnes) of gravels, an increase from 1,161.99 carats produced and 84,883 cubic meters (169,766 tonnes) of gravels processed in the six months ended August 31, 2008.

Sales from Saxendrift during the three months ended August 31, 2009 were 1,919.30 carats at an average price of US\$1,510.47 per carat. In the quarter ended August 31, 2008, 1,016.48 carats were sold at an average price of US\$1,935.18 per carat.

During the first half of the fiscal 2010 year, the property produced 3,533.38 carats from 508,390 cubic meters (1,067,619 tonnes) of gravels, an increase from 1,437.04 carats produced and 89,484 cubic meters (178,968 tonnes) of gravels processed in the six months ended August 31, 2008.

Sales from Saxendrift were 2,856.55 carats at an average price of US\$1,389.37 per carat, an increase in carats and a decrease value per carat sold from 1,016.48 carats at an average value of US\$1,935.18 per carat in the six months ended August 31, 2008.

The inventory at Saxendrift is 1,044.04 carats.

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### **Production Costs**

Production at the three operations steadily increased from an average of 413,386 tonnes in the first quarter to an average of 506,812 in the second quarter. The increase has been significantly influenced by the expanded capacity of the Saxendrift plant.

The average operating cost over six months was US\$2.72 per tonne, an decrease from US\$4.77 per tonne in the six months ended August 31, 2008, which is below the US\$3.00 - 3.50 per tonne range that was forecasted.

These operating costs are the cash costs of operations, consisting predominantly of fuel and oil, power, maintenance and replacement costs, operations salaries and direct mine operating costs.

The Company's drive to cut costs and optimize its operations continues to yield results. Costs for each operation were: Holpan US\$2.72 per tonne; Klipdam US\$2.64 per tonne and Saxendrift US\$2.59 per tonne.

The average cost for all the operations including rehabilitation, lease payments and royalties was US\$4 per tonne. These operations reflect six months of which four months were good seasonal conditions.

### **1.2.5 Exploration and Development Properties**

#### *Niewejaarskraal Project*

The Niewejaarskraal Project, located on the Middle Orange River area of South Africa, was a past producer of alluvial diamonds.

In terms of the Sale of Shares and Claims Agreement entered into between, among others, Rockwell Resources RSA (Proprietary) Limited ("Rockwell") and Trans Hex Operations (Proprietary) Limited ("Trans Hex") on March 3, 2007, Rockwell indirectly acquired the mining and prospecting rights to, among other areas, Portion 6 of the Farm Niewejaarskraal 40 in the magisterial district of Prieska ("Niewejaarskraal"). In terms of the same agreement, Rockwell also indirectly acquired, among other things, certain mining equipment situated on Niewejaarskraal, including a dense media separation plant previously erected and operated by Trans Hex.

As at February 28, 2009, the Company was committed to pay Trans Hex for the acquisition of the remaining Niewejaarskraal mining rights. The Company had placed \$2.7 million in trust toward application of the remaining payment, to be released to Trans Hex upon the anticipated grant of Ministerial Consent to the cession of each of the Outstanding Mining Rights to the Company and registration of cession of such rights in its name. Cession of the Niewejaarskraal mining right occurred on March 4, 2009.

On April 11, 2009 all the conditions precedent were met and the Company paid ZAR18.9 million (\$2.6 million) in cash to Trans Hex for the remaining Niewejaarskraal mining rights of which ZAR 16.5 million (\$2.0 million) was capitalized. This action completed the Saxendrift transaction negotiated during April 2008. The Company has no further commitments in relation to more acquisitions.

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During the course of 2008 and prior to the prospecting and mining rights having been transferred from Trans Hex to Rockwell, a representative of the land owner of Niewejaarskraal asserted a claim of ownership over the equipment located on Niewejaarskraal. This claim was ostensibly based on a surface rights agreement entered into between Trans Hex and the owner of Niewejaarskraal and an allegation that Trans Hex had abandoned the mining equipment concerned. This Contract expired prior to Rockwell receiving the Niewejaarskraal mining rights. Since the transfer of the prospecting and mining rights associated with and the mining equipment located on Niewejaarskraal to Rockwell, it has not received any formal approach from the land owner of Niewejaarskraal to progress this claim. Discussions with the landowner have indicated that he would be happy to enter into amenable and workable landowner agreements with Rockwell, subject to appropriate land use agreements being entered into between the Parties. In addition, Rockwell has had sight of the legal advice provided by external legal counsel to Trans Hex to the effect that the merits of this claim are limited. In the event that a claim were to be made by the owner of Niewejaarskraal against Rockwell in respect of this mining equipment, Rockwell will vigorously defend its ownership of that equipment and will also seek to rely on certain protective warranties and indemnities that were given to it by Trans Hex in the Sale of Shares and Claims Agreement.

***Kwango River Project, DRC***

Durnpike's interest in the Kwango River Project was constituted by an agreement ("Midamines Agreement") concluded during 2006 with Midamines SPRL ("Midamines"), the holder of the exploration permit on the Kwango River Project, to act as contractor on behalf of Midamines to manage and carry out exploration and mining. Durnpike was entitled to an 80% share of the net revenue from the sale of any diamonds produced from the contract area.

Under the Midamines Agreement, Durnpike agreed to certain minimum royalty payments being made to Midamines, and Midamines undertook several obligations in favour of Durnpike including that of procuring and facilitating Durnpike's access to the Kwango River Project site. The royalties took the form of a series of recurring annual minimum royalty payments of US\$1,200,000 per annum (commencing on December 31, 2007). During the first quarter of 2008, pursuant to an amending agreement to the Midamines Agreement, the Company paid consideration of \$600,000 to Midamines in order to increase the size of the concession (Permit 331). As part of such amending agreement Midamines waived its right to payment of the abovementioned US\$1,200,000 royalty payment on December 31, 2007. Subsequently, and pursuant to Midamines' persistent breach of material provisions of the Midamines Agreement (coupled with its failure to remedy such instances of breach notwithstanding notice to do so), Durnpike cancelled the Midamines Agreement and claimed damages.

Midamines has subsequently disputed Durnpike's entitlement to cancel the Midamines Agreement and has demanded payment of US\$1.2 million as well as other amounts which have not yet been determined. Midamines has threatened to refer the dispute to arbitration and to joint Rockwell as party thereto, but no formal referral to arbitration has as yet been forthcoming.

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*Other*

Rockwell has adopted a policy that includes insurance cover for all equipment that is purchased on an instalment plan (called Hire Purchase in South Africa) or leases but it does not carry full coverage for other equipment that is paid off or which has been acquired in respect of its acquisitions of Trans Hex mineral rights and equipment. The Company also has coverage on small vehicles, busses, road trucks, Flow-sort X-ray equipment and some of its fixed properties and assets.

### **1.2.6 Diamond Market Trends**

*The Diamond Market Update*

Prices continued on an upswing during the second quarter of the 2010 fiscal year, and also stabilized towards the end of the quarter.

Demand for polished stones was predominantly in the bridal size ranges. Retailers have experienced 25-30% drop in sales compared to this period in fiscal 2009 (calendar 2008). Overall, stocks have been reduced at retail level and subsequent reordering and purchasing of polished diamonds has occurred, albeit not at levels seen in 2009. There is a tendency for jewellers to create more affordable jewellery whether it includes silver ranges and diamond solitaires, set in gold, with comparatively smaller and lesser coloured stones included

In the rough diamond market, demand continued for 2-10 carat rough diamonds, colors D-L, with good shapes and cleaner purity. Buyers were focusing on diamonds that involved less labor at manufacturing level. Spotted diamonds in all size ranges were in limited demand.

Larger diamonds (plus 10 carats) showed an increase in demand although there is still resistance to paying anywhere near 2009 prices. Buyers of Specials are still limited because of cash flow restrictions and offers received are opportunistic and sometimes successful depending on the financial state of the producer.

De Beers had three Sights during this period. The quantities of diamonds purchased were far in excess of 1<sup>st</sup> quarter Sights. The average value was \$400 million to \$500 million per Sight. De Beers resisted low prices offered for larger goods and withheld stones at these sizes, mostly selling diamonds that could be used in Bridal Collections i.e. 2-10 carat cleaner stones with better shapes and colours, and which relates to the increased prices offered on the open market for these ranges.

Diamond Centres have experienced buying activity in both rough and polished diamonds, and the mood is, overall, more positive. There is still resistance to offer credit and centers like Mumbai have reverted to cash sales as opposed to the normal 45 days credit that was offered in the past.

Investors have been showing interest, particularly in larger diamonds, with the intention of holding diamonds for extended periods as a store of wealth. With a decline in production levels expected over the next few years as a result of existing older sources of diamonds becoming more difficult and too expensive to mine and the difficulty in getting new deposits to productive levels, diamonds as an investment will become a reality.

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Rockwell has continued improving its production levels while reducing and maintaining a low cash cost per tonne. Rockwell had three sales during this second quarter. Prices achieved were encouraging. Rockwell continues to develop different forms of sales and increase beneficiation criteria of its niche market Special Diamonds incorporating an increased amount of larger stones for beneficiation.

Many companies are back in production and some producers have cancelled their intended December shutdowns. As a consequence, production levels of rough diamonds are expected to increase and be maintained.

Expectation for the third quarter is a slight reduction in demand of rough diamonds but price levels will remain as they presently are. September is time for the Hong Kong Show, results from which are an indicator of where the industry stands with regards to prices and demand of polished diamonds.

*Background*

Diamond clarity is rated using the following scale:

GIA diamond clarity grading scale											
Category	Flawless	Internally Flawless	Very Very Slightly Included		Very Slightly Included		Slightly Included		Included		
Grade	<b>FL</b>	<b>IF</b>	<b>VVS<sub>1</sub></b>	<b>VVS<sub>2</sub></b>	<b>VS<sub>1</sub></b>	<b>VS<sub>2</sub></b>	<b>SI<sub>1</sub></b>	<b>SI<sub>2</sub></b>	<b>I<sub>1</sub></b>	<b>I<sub>2</sub></b>	<b>I<sub>3</sub></b>

- Diamonds with clarity of VS2 or better have experienced the greatest increase in prices increases.
- Diamonds with a grade of less than VS2 have achieved relatively smaller increases in price.

There have been price increases for the full range of coloured diamonds, but the major price increases are for those in the D-K colour range and, predominantly, for the D to F colours. The greatest price increase was for D-coloured stones; however, an overall percentage for the increase in price is hard to determine because of the scarcity and extreme demand for these stone. Similar increases have been experienced for fancy coloured diamonds, i.e. pink, blue or yellow stones. All coloured and rare D-colour diamonds are regarded as investment pieces, comparable to art from a known artist.

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**1.3 Selected Annual Information**

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles, and are expressed in Canadian dollars except common shares outstanding.

<i><b>Balance Sheet</b></i>	<b>As at February 28, 2009</b>	<b>As at February 29, 2008</b>	<b>As at May 31, 2007</b>
Current assets	15,099,971	38,596,562	56,142,572
Mineral properties	28,894,477	25,247,937	24,121,855
Other assets	62,367,968	69,848,625	49,341,956
<b>Total assets</b>	<b>106,362,416</b>	<b>133,693,124</b>	<b>129,606,383</b>
Current liabilities	14,462,800	12,502,301	29,399,774
Other liabilities	21,478,590	34,076,016	28,613,767
Shareholders' equity (deficiency)	70,421,026	87,114,807	71,592,842
<b>Total liabilities and shareholders' equity</b>	<b>106,362,416</b>	<b>133,693,124</b>	<b>129,606,383</b>
	<b>Year ended February 28, 2009</b>	<b>Nine months ended February 29, 2008</b>	<b>Year ended May 31, 2007</b>
<b>Statement of Operations</b>			
Revenue	34,633,477	36,149,308	10,103,328
Mine site operating costs	(25,113,363)	(22,730,271)	(8,974,742)
Amortization and depletion	(11,287,197)	(6,533,941)	(2,074,415)
<b>Operating profit (loss)</b>	<b>(1,767,083)</b>	<b>6,885,096</b>	<b>(945,829)</b>
<b>Expenses</b>			
Accretion of reclamation obligation	1,072,389	464,316	55,471
Exploration	498,739	604,169	1,371,351
Foreign exchange loss (gain)	(350,485)	(751,318)	(3,580,364)
Legal, accounting and audit	1,863,261	790,725	691,759
Office and administration	3,489,460	2,697,077	2,993,453
Shareholder communications	453,489	198,985	200,574
Stock-based compensation	1,834,422	1,826,317	79,623
Travel and conference	605,812	654,705	666,194
Transfer agent filings	250,878	544,232	176,530
<b>Subtotal</b>	<b>9,717,965</b>	<b>7,029,208</b>	<b>2,654,591</b>
Loss on disposal of equipment	364,918	402,411	94,621
Loss on disposal of mineral properties	203,339	-	-
Interest (income)	(2,672,021)	(1,118,396)	(372,149)
Interest on capital leases	1,592,001	1,289,385	433,125
Convertible note accretion and interest expense	3,009,680	270,976	2,466,839
Loss on early extinguishment convertible promissory notes	-	-	137,957
Write down of assets	2,590,958	-	-
Write-off of amounts receivable	291,063	18,360	224,942
Write-down of marketable securities	-	-	1
<b>Subtotal</b>	<b>5,379,938</b>	<b>862,736</b>	<b>2,985,336</b>
<b>Loss before income taxes</b>	<b>16,864,986</b>	<b>1,006,848</b>	<b>6,585,756</b>
Income tax expense	7,000	179,290	-
Future income tax (recovery) expense	(3,347,000)	2,261,110	(635,773)
<b>Loss before non-controlling interest</b>	<b>13,524,986</b>	<b>3,447,248</b>	<b>5,949,983</b>
Non-controlling interest	(549,024)	5,955,779	415,159
<b>Loss for the period</b>	<b>12,975,962</b>	<b>9,403,027</b>	<b>6,365,142</b>
Other comprehensive loss	13,409,383	-	-
<b>Total comprehensive loss</b>	<b>26,385,345</b>	<b>9,403,027</b>	<b>6,365,142</b>
Basic and diluted loss per common share	0.05	0.05	0.11
Weighted average number of common shares outstanding	237,924,152	196,428,551	55,418,242

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**1.4 Summary of Quarterly Results**

Expressed in thousands of Canadian dollars (000), except per-share amounts. Minor differences are due to rounding.

<b>Balance Sheet</b>	<b>Aug 31 2009</b>	<b>May 31 2009</b>	<b>Feb 28 2009</b>	<b>Nov 30 2008</b>	<b>Aug 31 2008</b>	<b>May 31 2008</b>	<b>Feb 29 2008</b>	<b>Nov 30 2007</b>
Current assets	7,785	8,986	15,100	22,830	21,757	27,190	38,597	36,823
Mineral properties	34,654	34,219	28,894	36,831	37,386	36,592	25,248	24,928
Other assets	65,217	65,100	62,368	85,330	80,146	74,621	69,848	66,544
<b>Total assets</b>	<b>107,656</b>	<b>108,305</b>	<b>106,362</b>	<b>144,991</b>	<b>139,289</b>	<b>138,403</b>	<b>133,693</b>	<b>128,295</b>
Current liabilities	15,970	15,623	14,463	14,814	17,369	15,353	12,502	17,173
Other liabilities	19,404	20,773	19,597	32,171	28,941	28,194	34,076	30,395
Shareholders' equity (deficiency)	72,282	71,909	72,303	98,006	92,979	94,856	87,115	80,727
<b>Total liabilities and shareholders' equity</b>	<b>107,656</b>	<b>108,305</b>	<b>106,362</b>	<b>144,991</b>	<b>139,289</b>	<b>138,403</b>	<b>133,693</b>	<b>128,295</b>
Working capital (deficit)	(8,185)	(6,637)	637	8,016	4,388	11,837	26,095	19,650
<b>Statement of Operations</b>	<b>Aug 31 2009</b>	<b>May 31 2009</b>	<b>Feb 28 2009</b>	<b>Nov 30 2008</b>	<b>Aug 31 2008</b>	<b>May 31 2008</b>	<b>Feb 29 2008</b>	<b>Nov 30 2007</b>
Revenue	5,919	3,929	1,008	16,126	10,168	7,331	9,802	12,125
Mine site operating costs	(4,790)	(4,851)	(9,143)	(3,710)	(7,651)	(4,609)	(7,350)	(9,571)
Amortization and depletion	(3,139)	(1,819)	(3,177)	(2,864)	(2,673)	(2,574)	(2,418)	(2,141)
<b>Operating profit (loss)</b>	<b>(2,010)</b>	<b>(2,740)</b>	<b>(11,312)</b>	<b>9,552</b>	<b>(156)</b>	<b>148</b>	<b>34</b>	<b>413</b>
<b>Expenses</b>								
Accretion of reclamation obligation	32	(14)	809	95	99	69	378	28
Exploration	2	58	132	96	(33)	304	174	127
Foreign exchange loss (gain)	2	546	(72)	(903)	831	(206)	16	(126)
Legal, accounting and audit	160	334	408	678	640	137	472	253
Office and administration	800	656	960	689	868	972	1,147	(850)
Shareholder communications	212	119	81	173	119	80	65	64
Stock-based compensation	18	116	276	499	373	686	1,177	617
Travel and conference	41	36	147	139	108	212	382	147
Transfer agent	58	22	178	28	35	10	439	98
<b>Subtotal</b>	<b>1,325</b>	<b>1,873</b>	<b>2,919</b>	<b>1,494</b>	<b>3,040</b>	<b>2,264</b>	<b>4,250</b>	<b>2,058</b>
Write-off of amounts receivable	–	–	291	–	–	–	18	–
Loss (gain) on disposal of equipment	11	26	66	(6)	284	21	424	3
Loss on disposal of mineral properties	–	–	203	–	–	–	–	–
Interest income	(92)	(143)	(191)	(357)	(743)	(1,381)	(447)	(186)
Interest on capital leases	252	343	354	335	440	463	391	427
Accretion and interest expense	73	407	2,309	452	163	86	84	102
Write down of assets	–	658	2,591	–	–	–	–	–
<b>Profit (loss) before income taxes</b>	<b>(3,579)</b>	<b>(5,904)</b>	<b>(19,854)</b>	<b>7,634</b>	<b>(3,340)</b>	<b>(1,305)</b>	<b>(4,686)</b>	<b>(1,991)</b>
Future income tax recovery (expense)	719	1,346	2,089	(134)	703	414	(698)	25
<b>Profit (loss) before non-controlling interest</b>	<b>(2,860)</b>	<b>(4,558)</b>	<b>(17,765)</b>	<b>7,768</b>	<b>(2,637)</b>	<b>(891)</b>	<b>(5,384)</b>	<b>(1,966)</b>
Non-controlling interest	(338)	(454)	2,015	(3,241)	589	88	3,322	(837)
<b>Profit (loss) for the period</b>	<b>(2,522)</b>	<b>(4,104)</b>	<b>(19,780)</b>	<b>11,009</b>	<b>(3,226)</b>	<b>(979)</b>	<b>(8,706)</b>	<b>(1,129)</b>
Basic and diluted profit (loss) per share	(0.01)	(0.02)	(0.08)	0.05	(0.01)	(0.00)	(0.04)	(0.00)
Weighted average number of common shares outstanding (thousands)	238,042	238,042	237,924	238,537	238,537	237,731	223,891	187,817



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## **1.5 Results of Operations**

The Company realized a loss of \$6.6 million for the six month period ended August 31, 2009 compared to a net loss of \$3.1 million for the comparable period in the prior year. The loss was due to the collapse in the diamond market and precipitous decline in diamond prices that commenced in the fourth quarter of fiscal 2009 due to the ongoing global credit crisis and economic recession. This resulted in on going weakness of diamond prices through the first two quarters of fiscal 2010. Though prices remained weak during this period there has been an overall improvement in prices of about 15% to 20% from the initial sharp fall in prices of about 50% in the last quarter of fiscal 2009. Operations at the Wouterspan Mine are still in care and maintenance in order to preserve the Company's cash reserves, and will be reopened in line with improvements in diamond prices.

During the six months ended August 31, 2009, the Company realized rough diamond sales of \$9.7 million compared to \$17.0 million for the comparable period in the prior year. Sales in March were at US\$531.43 per carat, 35% of the pre-October 2008 average sales prices achieved of about US\$1,800 per carat. Prices have gradually recovered, climbing to US\$1,090.55 per carat in July and US\$862.36 per carat in August/September tenders. The latter decrease was not due to a decline in price, but rather due to a lower grade mix of stones being offered on tender in August.

As noted above the sharp decrease in diamond prices was a result of the credit crunch and ensuing recession which resulted in prices falling sharply in late calendar 2008. Sales prices achieved in the first quarter were below the cost of production; however, prices achieved in the second quarter have covered the cost of production, but have not been sufficient to cover fixed overheads in full and lease payments. As the Company was required to maintain liquidity, sales have been made below production cost. In July and August cash inflows from sales have exceeded outflows from operating expenses, though overall inflows have not been sufficient to cover the full costs of the lease payments on a limited amount of earth moving equipment. For this reason the Company has invoked the payment deferral with Komatfin.

Mining costs for the six months ended August 31, 2009 amounted to \$9.6 million (six months ended August 31, 2008 - \$12.3 million), which excludes amortization and depletion charges of \$5 million (six months ended August 31, 2008 – \$5.2 million).

Exploration expenses (excluding stock-based compensation) decreased to \$59,916 for the six months ended August 31, 2009 compared to \$271,182 for the same period in the prior year. This decrease is due to less engineering activities and property assessment fees performed during the six month period ended August 31, 2009 on South African diamond properties.

Administrative costs for the six months ended August 31, 2009 decreased to \$1.5 million in comparison to \$1.8 million incurred for the same period in the prior year, primarily due to controlling costs and reducing overheads. Travel and conference expenses amounted to \$76,782 for the six months ended August 31, 2009 compared to \$319,709 for the same period in the previous year. Legal, accounting and audit expenses for the six months ended August 31, 2009 amounted to \$493,009 compared to \$776,895 incurred for the same period in the prior year, even though the Company experienced significant legal costs due to the unsolicited bid by Pala.

Stock-based compensation decreased to \$134,066 for the six months ending August 31, 2009 in comparison to \$1,058,101 for the same period in the previous year.

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Interest expenses increased to \$480,349 for the six months ended August 31, 2009, compared to \$248,831 for the six months ended August 31, 2008, mainly due to the the use of the credit facility to maintain working capital.

Please refer to section 1.2 for additional discussion on the Company's results of operations.

## **1.6 Liquidity**

### *Liquidity Risk*

At August 31, 2009, the Company had cash and equivalents of \$0.9 million and bank indebtedness of \$3.1 million, for a net indebtedness of \$2.2 million. The Company also had a working capital deficit of \$8.2 million, as compared to cash and equivalents of \$4 million and bank indebtedness of \$3.5 million, for a net indebtedness of \$0.5 million, and working capital of \$0.6 million at February 28, 2009. The Company had no long-term debt at August 31, 2009, other than asset retirement obligations relating to its Klipdam, Holpan, Wouterspan mines and Saxendrift operations, and capital lease obligations relating to mining equipment with three to four year lease agreements. The Company's capital lease obligations are denominated in South African Rand ("ZAR"). Capital lease obligations have been presented at an exchange rate of 1 Canadian dollar = ZAR 7.097, the closing rate in effect on August 31, 2009. Since then, the South African Rand has marginally strengthened to 1 Canadian dollar = ZAR 7.013 as of July 13, 2009.

To meet short term liquidity requirements the Company has invoked a payment deferral over its lease obligations on a limited number of earth moving vehicles. This will enable the group to reduce its cash commitments by approximately ZAR4 million (\$546,000) per month from July to the end of October 2009.

The cash burn rate in the first quarter of fiscal 2010 was \$2 million, which reduced to \$1.8 million in the second quarter, being a \$0.7 million reduction in cash resources and \$1.1 million utilized from the Komatfin payment deferral. Improved diamond prices and the reduced cash outflow from the payment deferral on its lease obligations has resulted in positive cash flow from operations, however still insufficient to fully cover corporate overheads. The strengthening of the rand by 7% in the current quarter and 28% in the fiscal year to date, has had a significant negative effect on cash inflows from sales, which are realized in US Dollars.

The Company has implemented the necessary plans to ensure sufficient financial liquidity in the near term. The Company's ability to repay or refinance its financial liabilities to their contractual maturities depends on a number of factors such as an improvement in diamond demand and prices and unfreezing of credit and capital markets, some of which are beyond the Company's control. There is no assurance that our expected cash flows from operations in combination with other steps being taken will allow the Company to meet these obligations as they become due.

To ensure the continuation of operations, and develop existing and new opportunities, the Board of Directors of Rockwell has initiated a financing to strengthen the Company's balance sheet through a rights offering and this process is expected to be completed by the end of the third quarter of fiscal 2010.

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*Contractual Obligations and Commitments*

The Company has the following payment commitments: (a) minimum lease payments of \$6.9 million, with \$5.4 million payable in the next 12 months, with instalments up to the year 2012 to various financial institutions for plant and equipment.

The following are the contractual maturities of contractual obligations:

	Payments due by period				
	Total	Less than one	1 to 3 years	3-5 years	More than 5
Contractual obligation	Nil	Nil	Nil	Nil	Nil
Long term debt obligations	6.9m	5.4m	1.5m	Nil	Nil
Operating lease obligations	Nil	Nil	Nil	Nil	Nil
Purchase obligations	Nil	Nil	Nil	Nil	Nil
Other	Nil	Nil	Nil	Nil	Nil
Total	6.9m	5.4m	1.5m	Nil	Nil

Other than described above and in the notes of the financial statements for the six months ended August 31, 2009, the Company has no "Purchase Obligations" defined as any agreement to purchase goods or services that is enforceable and legally binding on the Company that specifies all significant terms, including: fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction.

The payment deferral to the Company's equipment lessors will not change the period of the contracts, as subsequent payments will be increased to catch up the capital portion of the payments deferred. The interest position as well as the additional interest calculated on the capital not paid, has been paid in the current period.

## **1.7 Capital Resources**

The Company's sources of capital are primarily equity investment and debt.

Historically, the Company's sources of funding have been cash flow from operations and the issuance of equity securities for cash, primarily through private placements to sophisticated investors and institutions. The Company has issued common share capital in each of the past few years, pursuant to private placement financings and the exercise of warrants and options. The Company's access to financing, when the financing is not transaction specific, is always uncertain. There can be no assurance of continued access to significant equity funding.

The Company's access to capital sources is dependent upon general financial market conditions, especially those that pertain to venture capital situations such as mineral exploration and development.

Recent market events and conditions, including disruptions in the international credit markets and other financial systems and the deterioration of global economic conditions have had a significant material adverse impact on a number of financial institutions forcing them into bankruptcy or requiring

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government authorities to rescue them. These events and a general flight from risk have limited access to capital and credit for many companies. The unprecedented disruptions in the current credit and financial markets, could, among other things, impede access to capital or increase the cost of capital, which would have an adverse effect on the Company's ability to obtain, or increase its cost of obtaining, capital and financing, if required, for its operations. The Company's access to additional capital may not be available on terms acceptable to the Company or at all.

Furthermore, in recent months, worldwide securities markets have experienced a high level of price and volume volatility, and the market price of securities of many companies have experienced unprecedented declines in price which have not necessarily been related to the operating performance, underlying asset values or prospects of such companies. In addition, significantly higher redemptions by holders of mutual and hedge funds has forced many of such funds (including those holding the Company's securities) to sell such securities at any price. Therefore, there can be no assurance that significant fluctuations in the trading price of the Company's common shares will not occur, or that such fluctuations will not materially adversely affect the Company's ability to raise equity funding without significant dilution to its existing shareholders, or at all.

During the six months ended August 31, 2009, the Company did not complete any debt financings, other than the payment deferral on its capital lease obligations. The Company anticipates that it has sufficient funding facilities and funds available (Refer to Section 1.6 above) to meet its working capital requirements, provided that the diamond market recovers and sales achieve over US\$917 per carat in the near future and the exchange rate remains constant. At an exchange rate of ZAR8.00 to US\$1 and current volumes and grade being achieved, breakeven point is anticipated to be reached when the Sales price per carat recovers to the US\$1,100 – US\$1,200 per carat range.

The Company is in the advanced stages of the process of raising capital to meet the expenditure requirements to ensure the continuation of operations until such time as the international diamond markets recover and sufficient funds for capital expenditure to improve efficiencies at existing operations, expand operations to take advantage of existing resources and reopen operations that have been on care and maintenance in line with future market improvement.

Financial resources will be applied to reducing the short term finance and the Komatfin payment deferral, which will cause significant reductions in interest expenses. Working capital will also be sufficient to provide financial leeway to hold sales tenders at dates where there is higher market demand due to seasonal events. This will generate larger profit margins and improved cash inflows.

The capital expenditure will be applied to further optimisation of existing operations and reopening operations that were placed on care and maintenance at the commencement of the Credit Crunch.

Other than already described above, the Company had no other lines of credit or other sources of financing which have been arranged but as yet unused as at August 31, 2009.

## **1.8 Off-Balance Sheet Arrangements**

None.

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**1.9 Transactions with Related Parties**

<b>Balances payable</b>	<b>As at August 31, 2009</b>	<b>As at February 28, 2009</b>
Jeffrey Brenner	\$ -	\$ 7,890
Jakes Tyres (g)	21,660	5,498
Hunter Dickinson Services Inc. (a)	740,711	180,267
Seven Bridges Trading (c)	10,352	-
<b>Current balances payable</b>	<b>\$ 772,723</b>	<b>\$ 193,655</b>
Liberty Lane (i)	427,306	383,330
<b>Long-term balances payable</b>	<b>\$ 1,200,029</b>	<b>\$ 383,330</b>

  

<b>Balances receivable</b>		
Flawless Diamonds Trading House (e)	\$ 1,395,997	\$ 3,441,510
Banzi Trade 26 (Pty) Ltd (f)	23,482	19,547
Diacor CC (h)	32,125	29,668
	<b>\$ 1,451,604</b>	<b>\$ 3,490,725</b>

<b>Transactions</b>	<b>Three months ended Aug 31</b>		<b>Six months ended Aug 31</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
Services rendered and expenses reimbursed:				
Hunter Dickinson Services Inc. (a)	\$ 173,616	\$ 249,346	\$ 536,627	\$ 380,708
CEC Engineering (b)	-	14,289	-	14,289
Seven Bridges Trading (c)	57,396	37,128	73,135	67,992
Cashmere Trading (d)	-	9,483	-	-
Banzi Trade 26 (Pty) Ltd (f)	6,666	4,927	7,578	12,573
Jakes Tyres (g)	38,815	148,644	43,845	348,037
Diacor CC (h)	-	32,696	-	36,314
Sales rendered to:				
Flawless Diamonds Trading House (e)	\$ 5,802,006	\$ 9,912,702	\$ 9,674,805	\$ 17,007,623
Banzi Trade 26 (Pty) Ltd (f)	\$ 861	\$ -	\$ 1,438	\$ 884

Related Party transactions are explained below. These arrangements and transactions have typically been established to provide professional and cost effective services and resources to Rockwell. In particular these services relate to the remote areas in which some of Rockwell's operations are located and have also been established to address security and social responsibility requirements. In remote areas it is difficult to obtain key services and make purchases of certain supplies on an as needed basis. Likewise security consideration is paramount given the high value product produced by the Company.

- (a) Hunter Dickinson Services Inc. ("HDSI") is a private company with a director in common with the Company. HDSI provides geological, technical, corporate development, administrative and management services to, and incurs third party costs on behalf of, the

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Company on a full cost recovery market related basis pursuant to an agreement dated November 21, 2008.

- (b) CEC Engineering Ltd. is a private company owned by David Copeland, Chairman and a director of the Company, which provides engineering and project management services at market rates.
- (c) Seven Bridges Trading is a wholly owned subsidiary of Randgold Resources, a public company where Mark Bristow, a director of the Company, serves in an executive capacity. Seven Bridges Trading provides office, conferencing, information technology, and other administrative and management services at market rates to the Company's South African subsidiaries.
- (d) Cashmere Trading is a private company owned by Hennie Van Wyk, a former officer of the Company, which provides helicopter services for the movement of product on an ad-hoc basis at competitive market rates thereby providing benefits to the company and its employees in respect of secure transport of high value product and reduced insurance premiums.
- (e) Flawless Diamonds Trading House ("Flawless") is a private company where certain directors, former directors and officers of the Company, namely, Messr. Brenner, J W and D M Bristow and Van Wyk, are shareholders of. Flawless is a registered diamond broker which provides specialist diamond valuation, marketing and tender sales services to the Company for a fixed fee of 1% of turnover which is below the market rate charged by similar tender houses.
- (f) Banzi Trade 26 (Pty) Ltd ("Banzi") is 49% owned by HC van Wyk Diamonds Ltd and 51% by Bokomoso Trust. Banzi is an empowered private company established to provide self sustaining job creation programs to local communities as part of the company's Social and Labour Plan which is required in terms of the Minerals and Petroleum Resources Development Act "MPRDA"). Banzi provides the Company with buildings materials at market rates.
- (g) Jakes Tyres is a private company with former directors and officers (H C van Wyk) in common with the Company that provides tyres, tyre repair services and consumables at market rates to Rockwell's remote Middle Orange River operations.
- (h) Diacor CC is a private company of which H C van Wyk, a former director and officer of the Company, is a director from which the Company has purchased consumable materials at market rates.
- (i) Liberty Lane is the BEE partner of the Saxendrift property and has certain directors in common with the Company.

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**1.10 Fourth Quarter**

None.

**1.11 Proposed Transactions**

None.

**1.12 Critical Accounting Estimates**

The Company's accounting policies are presented in note 3 of the audited consolidated financial statements for the year ended February 28, 2009 and note 3 of the interim consolidated financial statements for the six months ended August 31, 2009, which have been publicly filed on SEDAR at [www.sedar.com](http://www.sedar.com) and as presented in changes in accounting policies item 1.13. The preparation of consolidated financial statements in accordance with generally accepted accounting principles requires management to select accounting policies and make estimates. Such estimates may have a significant impact on the financial statements. These estimates include:

- mineral resources and reserves,
- the carrying values of diamond and supplies inventories,
- the carrying values of mineral properties,
- the carrying values of property, plant and equipment,
- rates of amortization of property, plant and equipment
- the carrying values of the reclamation liability,
- the assumptions used in determining the reclamation obligation,
- the valuation allowances for future income taxes,
- the valuation of stock-based compensation expense.

Actual amounts could differ from the estimates used and, accordingly, affect the results of operation.

**Mineral resources and reserves, and the carrying values of property, plant and equipment**

Mineral resources and reserves are estimated by professional geologists and engineers in accordance with recognized industry, professional and regulatory standards. These estimates require inputs such as future metal prices, future operating costs, and various technical geological, engineering, and construction parameters. Changes in any of these inputs could cause a significant change in the estimated resources and reserves which, in turn, could have a material effect on the carrying value of property, plant and equipment.

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The carrying value of mineral properties is also dependant on the valuation used for the common shares and warrants of the Company issued for the acquisition of mineral properties. The value of the common shares issued is the price of the common shares of the Company at the date of issuance to effect the acquisition. The Company uses the Black-Scholes pricing model to estimate a value for the warrants issued upon the acquisition of a property. This model, and other models which are used to value options and warrants, require inputs such as expected volatility, expected life to exercise, and interest rates. Changes in any of these inputs could cause a significant change in the carrying value initially recorded for mineral properties.

Long-lived assets, including mineral properties and equipment, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed, if any, are presented separately on the balance sheet and reported at the lower of the carrying amount and the fair value less costs to sell, and are no longer amortized.

The Company's estimates of mineral prices, recoverable reserves, and operating, capital and reclamation costs used in impairment tests are subject to certain risks and uncertainties that may affect the recoverability of mineral property costs. Although the Company has made its best estimate of these factors, it is possible that changes could occur in the future that could adversely affect management's estimate of the net cash flow from its assets.

#### **Site restoration costs**

Upon the completion of any mining activities, the Company will ordinarily be required to undertake environmental reclamation activities in accordance with local and/or industry standards. The estimated costs of these reclamation activities are dependent on labour costs, the environmental impacts of the Company's operations, the effectiveness of the chosen reclamation techniques, and applicable government environmental standards. Changes in any of these factors could cause a significant change in the reclamation expense charged in a period.

#### **Stock-based compensation expense**

From time to time, the Company may grant share purchase options to employees, directors, and service providers. The Company uses the Black-Scholes option pricing model to estimate a value for these options. This model, and other models which are used to value options, require inputs such as expected volatility, expected life to exercise, and interest rates. Changes in any of these inputs could cause a significant change in the stock-based compensation expense charged in a period.

### **1.13 Changes in Accounting Policies including Initial Adoption**

- (a) The following accounting policies were adopted during the period ended August 31, 2009:



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(i) *Goodwill and Intangibles (Section 3064)*

The AcSB issued CICA Handbook Section 3064, which replaces Section 3062, “*Goodwill and Other Intangible Assets*”, and Section 3450, “*Research and Development Costs*”. This new section establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets. Standards concerning goodwill remain unchanged from the standards included in the previous Section 3062. The section applies to interim and annual financial statements relating to fiscal years beginning on or after October 1, 2008. The Company evaluated the impact of this new standard and concluded that this standard did not have a significant impact on the financial statements.

(ii) *EIC 173 – Credit Risk and the Fair value of Financial Assets and Financial Liabilities*

The AcSB issued EIC-173 which requires the Company to consider its own credit risk as well as the credit risk of its counterparty when determining the fair value of financial assets and liabilities, including derivative instruments. The standard is effective for the first quarter of fiscal 2010 and is required to be applied retrospectively without restatement of prior periods. The Company evaluated the impact of this new standard and concluded that this standard did not have a significant impact on the financial statements.

(iii) *EIC 174 – Mining Exploration Costs*

The AcSB issued EIC-174, “*Mining Exploration Costs*” which provides guidance to mining enterprises related to the measurement of exploration costs and the conditions that a mining enterprise should consider when determining the need to perform an impairment review of such costs. The standard is effective for the first quarter of fiscal 2010 and is required to be applied retrospectively without restatement of prior periods. The Company evaluated the impact of this new standard and concluded that this standard did not have a significant impact on the financial statements.

(b) Accounting Policies Not Yet Adopted

(i) *International Financial Reporting Standards (“IFRS”)*

The Accounting Standards Board (“AcSB”) confirmed in February 2008 that International Financial Reporting Standards (“IFRS”) will replace Canadian GAAP (“GAAP”) for publicly accountable enterprises for financial periods beginning on and after January 1, 2011. Accordingly, the Company will convert over to IFRS on March 1, 2011 and prepare its first financial statements in accordance with IFRS for the three month period ended May 31, 2011, with comparative information also prepared under IFRS.

Management of IFRS Convergence Project

The Company is currently in the process of preparing its transition plan. This process will involve the establishment of a Steering Committee to manage the IFRS transition process, the allocation of internal resources, the engagement of external expert consultants, assessing the impact of the conversion on the consolidated financial statements and disclosure, considering the impact of conversion on the Company’s information technology systems, internal controls over financial

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reporting and business activities that may be influenced by GAAP measurements, and assessing the readiness of the Company's staff, Board of Directors and auditors.

The IFRS convergence project instituted consists of three primary phases, which in certain cases will be in process concurrently as IFRS is applied to specific areas:

- Initial Scoping and Impact Assessment Analysis: to isolate key areas that will be impacted by the transition to IFRS.
- Evaluation and Design: to identify specific changes required to existing accounting policies, information systems and business processes, together with an analysis of policy alternatives allowed under IFRS and development of draft IFRS financial statements.
- Implementation and Review: to execute the changes to information systems and business processes, completing formal authorization processes to approve recommended accounting policy changes and training programs across the company's finance and other staff, as necessary. It will culminate in the collection of financial information necessary to compile IFRS-compliant financial statements, embedding IFRS principles in business processes, and Audit Committee approval of IFRS financial statements.

A detailed timetable is currently being prepared to manage the transition and the Company is currently on schedule. The Company cannot at this time reasonably estimate the impact of adopting IFRS on its consolidated financial statements.

*(ii) Business Combinations/Consolidated Financial Statements/Non-Controlling Interests*

The AcSB adopted CICA sections 1582, "Business Combinations", 1601, "Consolidated Financial Statements", and 1602, "Non-Controlling Interests" which superseded current sections 1581, "Business Combinations" and 1600 "Consolidated Financial Statements". These new sections replace existing guidance on business combinations and consolidated financial statements to harmonize Canadian accounting for business combinations with IFRS. These Sections will be applied prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011. Earlier adoption is permitted. If an entity applies these Sections before January 1, 2011, it is required to disclose that fact and apply each of the new sections concurrently. The Corporation is currently evaluating the impact of the adoption of these changes on its consolidated financial statements.

#### **1.14 Financial Instruments and Risks and Uncertainties**

The carrying value of the Company's cash and equivalents, amounts receivable, restricted cash, trade receivable from a related party, reclamation deposits accounts payable and accrued liabilities, due to/from related parties and capital lease obligations approximate their fair values.

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Financial Instrument Risk Exposure and Risk Management

The Company is exposed in varying degrees to a variety of financial market and financial instrument related risk, including credit risk, liquidity risk, foreign exchange risk, interest risk and commodity price risk. It is also exposed to the diamond market.

*Credit Risk*

Credit risk is the risk of potential loss to the Company if a counterparty to a financial instrument fails to meet its contractual obligations. The Company's credit risk is primarily attributable to its liquid financial assets including cash and equivalents, accounts receivable and trade receivable from a related party. The Company limits exposure to credit risk on liquid financial assets through maintaining its cash and equivalents with high-credit quality financial institutions. The Company's minimize its credit risk by settling the receivables on its diamond sales in the month following the sale. The carrying value of the Company's cash and cash equivalents, accounts receivable and trade receivable from a related party represent the maximum exposure to credit risk. The Company does not have financial assets that are invested in asset backed commercial paper.

*Liquidity Risk*

Liquidity risk is the risk that the company will not be able to meet its financial obligations as they fall due. The Company ensures that there is sufficient capital and facilities in place in order to meet short term business requirements, after taking into account cash flows from operations and the Company's holdings of cash and cash equivalents. The Company believes that these sources will be sufficient to cover the likely requirements for the foreseeable future. The Company's cash and equivalents are invested in business accounts which are available on demand for the Company's programs, and which are not invested in any asset backed deposits/investments.

The Company operates in South Africa. Like other foreign entities operating there, the Company is subject to currency exchange controls administered by the South African Reserve Bank, that country's central bank. A significant portion of the Company's funding structure for its South African operations consists of advancing loans to its South Africa incorporated subsidiaries and it is possible the Company may not be able to acceptably repatriate such funds once those subsidiaries are able to repay the loans or repatriate other funds such as operating profits should any develop. The repatriation of cash held in South Africa is permitted upon the approval of the South African Reserve Bank. Cash balances in South Africa are the Rand balances disclosed below.

*Foreign Exchange Risk*

In the normal course of business, the Company enters into transactions for the purchase of supplies and services denominated in South African Rand ("ZAR"). In addition, the Company has cash and certain liabilities denominated in South African Rand. As a result, the Company is subject to foreign exchange risk from fluctuations in foreign exchange rates. The Company has not entered into any derivative or other financial instruments to mitigate this foreign exchange risk.

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*Capital Market Risk*

The Company is operating in an uncertain and volatile capital market environment which presents risks in respect of the Company being able to raise equity or debt to finance existing or new projects, or pursue growth opportunities through acquisition

*Diamond Market Risk*

During the latter part (October, November and December) of 2008 and the early part (January and February) of 2009 the international diamond market softened considerably as a consequence of the credit crunch and the volatility and uncertainty in the banking and financial market sector. In the six months ended August 31, 2009, the diamond markets continue to experience the carryover effects from reduced diamond demand and lower pricing. Diamond demand and prices fluctuate and are affected by numerous factors beyond the control of the Company, including worldwide economic trends, worldwide levels of diamond discovery and production and the level of demand for, and discretionary spending on, luxury goods such as diamonds and jewellery. Low or negative growth in the worldwide economy, prolonged credit market disruptions or activities creating disruptions in economic growth could result in decreased demand for diamonds, thereby negatively affecting the price of diamonds. Similarly, a substantial increase in the worldwide level of diamond production could also negatively affect the price of diamonds. In each case, such developments could materially adversely affect the Company's results of operations.

**1.15 Other MD&A Requirements**

Additional information relating to the Company is available on SEDAR at [www.sedar.com](http://www.sedar.com).

**1.15.1 Additional Disclosure for Venture Issuers Without Significant Revenue**

Not applicable. The Company is not a venture issuer.

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**1.15.2 Disclosure of Outstanding Share Data**

The following details the share capital structure as of the date of this MD&A. These figures may be subject to minor accounting adjustments prior to presentation in future consolidated financial statements.

	Expiry date	Exercise price	Number	Total
Common shares				238,043,069
Share purchase options				
	September 24, 2012	\$ 0.62	5,896,500	
	November 14, 2012	\$ 0.63	1,101,500	
	June 20, 2011	\$ 0.45	950,000	7,948,000
Warrants	November 22, 2009	\$ 1.00	39,600,000	39,600,000

**1.15.3 Internal Controls over Financial Reporting Procedures**

The Company's management is responsible for establishing and maintaining adequate internal controls over financial reporting. Any system of internal controls over financial reporting, no matter how well designed, has inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

During management's evaluation of the effectiveness of internal controls over financial reporting for the year ended February 28, 2009, management identified significant deficiencies in the Company's internal controls over financial reporting. The significant deficiencies identified include insufficient supervision and review by key accounting personnel over routine, non-routine and complex accounting transactions, inconsistent application of documented financial reporting procedures by accounting personnel, and the ineffective review of certain accounting transactions by accounting personnel. Management continued to remediate the material weakness that existed as at February 28, 2009, during the period ended August 31, 2009 by implementing the following remediation plans:

- Recruitment of qualified and experienced members to the accounting team. The Company has also contracted the services of an accountant with experience in the diamond industry to assist in the rigorous review of procedures and to assist with addressing backlogs and changes in reporting.
- Enhance controls around the timing and level of review of accounting schedules and calculations that support significant financial statement accounts. The CFO, Group Financial Manager and Rockwell staff has implemented a review of the financial reporting procedures and will continue to implement further improvements to ensure sufficient, appropriate and timely review of the financial information to mitigate any potential future delays. Processes will be thoroughly planned and re-engineered to meet the Company's financially reporting and continuous disclosure obligations.
- Provide appropriate training to accounting personnel regarding the Company's period end financial reporting process and procedures.

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These programs, as enhanced, are designed to reduce, although they may not eliminate, the risk of a material misstatement to a reasonable level.

Other than has already been disclosed there have been no significant changes in internal controls over financial reporting during the period ended August 31, 2009 that could have materially affected or are reasonably likely to materially affect the Company's internal controls over financial reporting.

**1.15.4 Disclosure Controls and Procedures**

The Company has disclosure controls and procedures in place to provide reasonable assurance that any information required to be disclosed by the Company under securities legislation is recorded, processed, summarized and reported within the applicable time periods and to ensure that required information is gathered and communicated to the Company's management so that decisions can be made about timely disclosure of that information.

There have been no significant changes in the Company's disclosure controls and procedures during the period ended August 31, 2009 that could significantly affect disclosure controls and procedures subsequent to the date the Company carried out its evaluation.