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**Financial Statements**

**Avalon Ventures Ltd.**

**For the Three Months Ended November 30, 2008**

**Unaudited - See Notice to Reader**

**INDEX**

<b>Balance Sheets</b>	<b>1</b>
<b>Statements of Operations and Deficit</b>	<b>2</b>
<b>Statements of Comprehensive Income (Loss)</b>	<b>3</b>
<b>Cash Flow Statements</b>	<b>4</b>
<b>Notes to the Financial Statements</b>	<b>5 - 12</b>

**NOTICE TO READER**

The accompanying unaudited interim financial statements have been prepared by the Company's management and the Company's independent auditors have not performed a review of these financial statements.

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# Avalon Ventures Ltd.

Balance Sheets

As at November 30, 2008 and August 31, 2008

Unaudited - See Notice to Reader

	November 30, 2008	August 31, 2008
<b>Assets</b>		
<b>Current Assets</b>		
Cash and cash equivalents	\$ 8,309,199	\$ 10,738,700
Receivables	147,303	152,165
Prepaid expenses	111,844	130,226
	<u>8,568,346</u>	<u>11,021,091</u>
<b>Investments Available for Sale</b>	3,943	3,943
<b>Resource Properties</b> (note 4)	14,975,537	13,188,626
<b>Property, Plant and Equipment</b>	<u>158,314</u>	<u>170,930</u>
	<u>\$ 23,706,140</u>	<u>\$ 24,384,590</u>

## Liabilities

### Current Liabilities

Accounts payable	<u>\$ 607,467</u>	<u>\$ 892,806</u>
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## Shareholders' Equity

<b>Share Capital</b> (note 5)	43,408,293	43,273,243
<b>Contributed Surplus</b> (note 6)	54,175	54,175
<b>Deficit</b>	(20,355,595)	(19,827,434)
<b>Accumulated Other Comprehensive Loss</b>	<u>(8,200)</u>	<u>(8,200)</u>
	<u>23,098,673</u>	<u>23,491,784</u>
	<u>\$ 23,706,140</u>	<u>\$ 24,384,590</u>

Approved on behalf of the Board

\_\_\_\_\_, Director  
"Donald S. Bubar"

\_\_\_\_\_, Director  
"Brian MacEachen"

# Avalon Ventures Ltd.

Statements of Operations and Deficit  
For the Three Months Ended November 30, 2008 and 2007  
Unaudited - See Notice to Reader

	2008	2007
<b>Revenue</b>		
Interest income	\$ 44,246	\$ 22,399
<b>Expenses</b>		
Amortization	12,616	5,249
Consulting fees	2,025	1,763
Directors' fees	11,000	9,000
Insurance	12,909	9,788
Interest and financing costs	2,447	7,738
Office and general	5,014	5,858
Professional fees	32,926	28,000
Public and investor relations	117,612	85,521
Rent and utilities	26,102	25,959
Salaries and benefits	161,562	108,600
Shareholders' information	1,283	-
Stock-based compensation	135,050	142,685
Transfer and filing fees	20,677	4,578
Travel	31,184	54,223
	<u>572,407</u>	<u>488,962</u>
<b>Loss before Income Taxes</b>	(528,161)	(466,563)
<b>Future Income Tax Recoveries</b>	<u>-</u>	<u>1,373,500</u>
<b>Net Income (Loss) for the Period</b>	(528,161)	906,937
<b>Deficit - Beginning of Period</b>	<u>(19,827,434)</u>	<u>(18,435,853)</u>
<b>Deficit - End of Period</b>	<u>\$ (20,355,595)</u>	<u>\$ (17,528,916)</u>
<b>Income (Loss) per Share, basic and fully diluted</b>	<u>\$ (0.01)</u>	<u>\$ 0.02</u>
<b>Weighted Average Number of Common Shares Outstanding, basic and fully diluted</b>	<u>64,649,748</u>	<u>53,528,703</u>

# Avalon Ventures Ltd.

Statements of Comprehensive Income (Loss)  
For the Three Months Ended November 30, 2008 and 2007  
Unaudited - See Notice to Reader

	2008	2007
<b>Net Income (Loss) for the Period</b>	\$ (528,161)	\$ 906,937
<b>Other Comprehensive Income</b>	<u>-</u>	<u>-</u>
<b>Comprehensive Income (Loss) for the Period</b>	<u>\$ (528,161)</u>	<u>\$ 906,937</u>

# Avalon Ventures Ltd.

## Cash Flow Statements

For the Three Months Ended November 30, 2008 and 2007

Unaudited - See Notice to Reader

	2008	2007
<b>Cash Flows from Operating Activities</b>		
Cash paid to suppliers and employees	\$ (499,721)	\$ (177,800)
Interest received	44,246	22,399
	<u>(455,475)</u>	<u>(155,401)</u>
<b>Cash Flows from Financing Activities</b>		
Share capital - private placement	-	15,527,155
Share capital - exercise of warrants	-	355,869
Share capital - exercise of options	-	96,000
	<u>-</u>	<u>15,979,024</u>
<b>Cash Flows from Investing Activities</b>		
Resource property expenditures	(1,974,026)	(1,047,798)
Purchase of property, plant and equipment	-	(5,849)
	<u>(1,974,026)</u>	<u>(1,053,647)</u>
<b>Change in cash and cash equivalents</b>	(2,429,501)	14,769,976
<b>Cash and cash equivalents - beginning of period</b>	<u>10,738,700</u>	<u>1,562,102</u>
<b>Cash and cash equivalents - end of period</b>	<u>\$ 8,309,199</u>	<u>\$ 16,332,078</u>
<b>Non-Cash Financing and Investing Activities</b>		
Agents' Compensation Options issued for commissions on private placement	<u>\$ -</u>	<u>\$ 425,720</u>

# Avalon Ventures Ltd.

Notes to the Financial Statements

For the Three Months Ended November 30, 2008

Unaudited - See Notice to Reader

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## 1. Accounting Policies

These interim financial statements have been prepared by the Company in accordance with Canadian generally accepted accounting principles. These financial statements are based on accounting principles and practices consistent with those used in the preparation of the Company's annual financial statements except for the changes made to adopt to the new accounting standards as described in the following paragraph. Certain information and note disclosure normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. These interim financial statements should be read together with the audited financial statements and the accompanying notes of the Company for the year ended August 31, 2008.

### **New Accounting Policies**

On September 1, 2008, the Company adopted three new accounting standards issued by the CICA: Handbook Section 1535, "Capital Disclosures", Handbook Section 3862, "Financial Instruments – Disclosures", and Handbook Section 3863, "Financial Instruments – Presentation". The Company has applied these new standards on a prospective basis.

#### Capital Disclosures

Handbook Section 1535 requires disclosure of an entity's objectives, policies and process for managing capital, quantitative data about what the entity regards as capital and whether the entity has complied with any capital requirements and, if it has not complied, the consequences of such non-compliance. The Company has included disclosures recommended by this new Handbook section in note 2.

#### Financial Instruments – Disclosures

Handbook Section 3862 requires an entity to provide disclosures to enable users to evaluate the significance of financial instruments for an entity's financial position and performance, including disclosures about fair value. In addition, disclosure is required of qualitative and quantitative information about the nature and extent of risks arising from financial instruments, including specified minimum disclosures about liquidity risk and market risk. The quantitative disclosures must also include a sensitivity analysis for each type of market risk to which an entity is exposed, showing how net income and other comprehensive income would have been affected by reasonably possible changes in the relevant risk variable. The Company has included disclosures recommended by this new Handbook section in note 3.

#### Financial Instruments – Presentation

Handbook Section 3863 replaces the existing requirements on presentation of financial instruments which have been carried forward unchanged to this new section. The adoption of this standard did not have any impact on the presentation of the Company's financial statements.

# Avalon Ventures Ltd.

Notes to the Financial Statements  
For the Three Months Ended November 30, 2008  
Unaudited - See Notice to Reader

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## 2. Capital Disclosures

The Company includes equity, comprised of share capital, contributed surplus and deficit in the definition of capital.

The Company's objectives when managing capital are as follows:

- (i) to safeguard the Company's ability to continue as a going concern;
- (ii) to raise sufficient capital to finance its exploration and development activities on its Thor Lake Project;
- (iii) to raise sufficient capital to meet its general and administrative expenditures, and to explore and develop its other resource properties;

The Company manages its capital structure and makes adjustments to it, based on the general economic conditions, the Company's short term working capital requirements, and its planned exploration and development program expenditure requirements. The Company does not have any externally imposed capital requirements.

## 3. Financial Instruments

The Company has classified its financial instruments as follows:

<u>Financial Instrument</u>	<u>Classification</u>	<u>Accounting Treatment</u>
Cash and cash equivalents	Held for trading	Fair market value
Receivables	Loans and receivables	Amortized cost
Investments available for sale	Available-for-sale	Fair market value
Accounts payable	Other liabilities	Amortized cost

Cash and cash equivalents include bank deposits and highly liquid short term money market investments such as bankers acceptance notes, treasury bills and guaranteed investment certificates.

Investments available for sale ("Investments") consist of shares received as consideration for resource property interest. All Investments are in publicly traded companies.

The Company's risk exposures and the impact on the Company's financial instruments are summarized below:

### **Credit risk**

The Company is not exposed to any significant credit risk as at November 30, 2008. The Company's cash and cash equivalents are either on deposit with a highly rated banking group in Canada or invested in bankers acceptance notes or guaranteed investment certificates issued by two highly rated Canadian banking groups.

### **Liquidity risk**

The Company has sufficient funds to cover its short term working capital requirements.

# Avalon Ventures Ltd.

Notes to the Financial Statements  
For the Three Months Ended November 30, 2008  
Unaudited - See Notice to Reader

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## 3. Financial Instruments (continued)

### Market risk

#### (i) Interest rate risk

The Company has significant cash and cash equivalents balances and it has no interest-bearing debt. The Company's current policy is to invest its excess cash in highly liquid money market investments such as bankers acceptance notes, treasury bills and guaranteed investment certificates. These short term money market investments are subject to interest rate fluctuations.

#### (ii) Foreign currency risk

The Company's functional currency is primarily the Canadian dollar. The majority of the Company's purchases are transacted in Canadian dollars. As at November 30, 2008, the Company had US\$24,749 in cash.

#### (iii) Price risk

The prices of metals fluctuate widely and are affected by many factors outside of the Company's control. The prices of metals and future expectation of such prices have a significant impact on the market sentiment for investment in mining and mineral exploration companies. This in turn may impact the Company's ability to raise equity financing for its long term working capital requirements.

In addition, the values of the Company's Investments are subject market price fluctuations.

### Sensitivity analysis

Based on management's knowledge and experiences of the financial markets, the Company's management believes the following movements are "reasonably possible" over a three month period.

As at November 30, 2008, approximately 50% of the Company's cash and cash equivalents are at fixed interest rates within the next three months. Sensitivity to a plus or minus 25 basis points change in rates would decrease or increase the Company's net loss by approximately \$6,200 over a three month period.

The Company had US\$24,749 in cash as at November 30, 2008 and its quarterly average expenditures transacted in US dollars is approximately US\$50,000. If the Canadian Dollar weakens or strengthens 10% against the United States Dollar with other variables held constant, the Company's net loss would increase or decrease by approximately \$3,000 over a three month period.

A plus or minus 10% change in the market price of the Company's Investments would not have any significant effect on the Company's net loss.

# Avalon Ventures Ltd.

Notes to the Financial Statements

For the Three Months Ended November 30, 2008

Unaudited - See Notice to Reader

## 4. Resource Properties

	November 30, 2008					
	Separation Rapids Lithium- Tantalum Project	Warren Township Anorthosite Project	Thor Lake Rare Metals Project	Red Hill Copper- Zinc-Silver Project	East Kemptville Rare Metals Project	Total
Acquisition costs	\$ -	\$ -	\$ 590	\$ -	\$ -	\$ 590
Community consultation	-	-	25,054	-	-	25,054
Diamond drilling	-	-	704,096	-	-	704,096
Environmental studies/permitting	36,525	-	509,267	-	-	545,792
Feasibility/engineering studies	1,657	67	90,192	-	-	91,916
Geochemical	-	-	-	-	19,269	19,269
Geology	-	-	83,357	295	76,474	160,126
Geophysical	-	-	6,623	-	-	6,623
Metallurgical/market studies	25,806	2,750	204,889	-	-	233,445
Current expenditures	63,988	2,817	1,624,068	295	95,743	1,786,911
Balance - August 31, 2008	3,713,949	1,185,805	7,281,767	598,264	408,841	13,188,626
Balance – November 30, 2008	\$ 3,777,937	\$ 1,188,622	\$ 8,905,835	\$ 598,559	\$ 504,584	\$ 14,975,537

# Avalon Ventures Ltd.

Notes to the Financial Statements  
For the Three Months Ended November 30, 2008  
Unaudited - See Notice to Reader

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## 5. Share Capital

### a) Issued and Outstanding:

	<u>Number</u>	<u>Amount</u>
<b>Common Shares</b>		
Balance - August 31, 2008 and November 30, 2008	<u>64,649,748</u>	<u>\$ 40,032,502</u>
<b>Warrants</b>		
Balance - August 31, 2008 and November 30, 2008	<u>3,805,000</u>	<u>\$ 1,461,881</u>
<b>Stock Options</b>		
Balance - August 31, 2008	4,327,500	\$ 1,353,140
Granted	32,000	746
Fair value of options recognized relating to previous option grants	<u>-</u>	<u>134,304</u>
Balance - November 30, 2008	<u>4,359,500</u>	<u>\$ 1,488,190</u>
<b>Agents' Compensation Options</b>		
Balance - August 31, 2008 and November 30, 2008	<u>725,000</u>	<u>\$ 425,720</u>
		<u>\$ 43,408,293</u>

### b) Common and Preferred Shares

The Company is presently authorized to issue an unlimited number of common shares without par value. The Company is also authorized to issue up to 25,000,000 preferred shares without par value, of which none have been issued.

### c) Warrants

As at November 30, 2008, the Company had 3,805,000 non-flow-through warrants outstanding. Each warrant entitles the holder to purchase one common share at \$2.00 per share and expires on May 22, 2009.

During the three months ended November 30, 2008, no share purchase warrants were issued, exercised or expired/cancelled:

	<u>Number of Warrants</u>	<u>Weighted Average Exercise Price</u>
Balance - August 31, 2008 and November 30, 2008	<u>3,805,000</u>	<u>\$ 2.00</u>

# Avalon Ventures Ltd.

Notes to the Financial Statements  
For the Three Months Ended November 30, 2008  
Unaudited - See Notice to Reader

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## 5. Share Capital (continued)

### d) Stock Option Plan

The shareholders have approved a Stock Option Plan (the "Plan") that provides for the issue of up to 10% of the number of issued and outstanding common shares of the Company to eligible employees, directors and service providers of the Company.

The Plan authorizes the granting of options to purchase shares of the Company's common stock at an option price equal to or greater than the closing price of the shares for either the trading day prior to the grant or the day of the grant. The options generally vest over a period of one to four years, and generally have a term of two to five years (but can have a maximum term 10 years).

During the three months ended November 30, 2008, stock options were granted, exercised and expired/cancelled as follows:

	<b>Number of Options</b>	<b>Weighted Average Exercise Price</b>
Balance - August 31, 2008	4,327,500	\$ 1.13
Granted	<u>32,000</u>	<u>1.86</u>
Balance – November 30, 2008	<u>4,359,500</u>	<u>\$ 1.13</u>
Vested options included in outstanding options above - November 30, 2008	<u>2,252,500</u>	<u>\$ 0.91</u>

During the three months ended November 30, 2008, the Company granted 32,000 stock options to a consultant of the Company. Each option entitles the holder to purchase one common share of the Company at a price of \$1.86 per share until September 1, 2010. These options vest at the rate of 25% every three months following September 1, 2008. As at November 30, 2008, 8,000 options had been earned. The estimated fair value of these options totalled \$746, and this amount had been recorded as stock-based compensation expense.

During the three months ended November 30, 2008, the Company also recorded stock-based compensation expense of \$134,304 related to stock options with graded vesting schedules which were earned during the quarter.

The fair value of stock options to employees and directors was estimated at the grant date and the options to service providers were estimated at the service completion date based on the Black-Scholes pricing model, using the following weighted average assumptions:

Expected dividend yield	Nil
Risk-free interest rate	2.10%
Expected life	1.57 years
Expected volatility	86%

# Avalon Ventures Ltd.

Notes to the Financial Statements

For the Three Months Ended November 30, 2008

Unaudited - See Notice to Reader

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## 5. Share Capital (continued)

Option pricing models require the input of highly subjective assumptions including the expected price volatility. Changes in the subjective input assumptions can materially affect the fair value estimate and, therefore, the existing models do not necessarily provide a reliable measure of the fair value of the Company's stock options.

As at November 30, 2008, the following options were vested and outstanding:

Option Price	Number of Options		Weighted Average Remaining Contractual Life
	Unvested	Vested	
\$ 1.86	32,000	-	1.8 years
\$ 1.82	168,750	56,250	4.0 years
\$ 1.80	225,000	75,000	3.4 years
\$ 1.61	393,750	381,250	2.6 years
\$ 1.30	-	100,000	0.2 years
\$ 1.24	200,000	-	4.4 years
\$ 1.20	787,500	162,500	3.4 years
\$ 1.08	-	150,000	2.6 years
\$ 0.98	300,000	100,000	3.1 years
\$ 0.80	-	300,000	2.9 years
\$ 0.69	-	200,000	2.3 years
\$ 0.48	-	225,000	2.0 years
\$ 0.25	-	502,500	0.2 years
	<u>2,107,000</u>	<u>2,252,500</u>	

### e) Agents' Compensation Options

As at November 30, 2008, the Company had 725,000 Agents' Compensation Options issued and outstanding. Each Agent's Compensation Option entitles the agent holder to purchase one Unit at a price of \$1.55 per Unit, exercisable until November 22, 2009. Each Unit will consist of one common share and one-half of one common share purchase warrant. Each whole warrant entitles the holder to purchase one common share at an exercise price of \$2.00 per share until May 22, 2009. No warrants will be issued upon any exercise of the Agents' Compensation Options after May 22, 2009.

## 6. Contributed Surplus

Contributed surplus consists of expired warrants and options. There were no changes in contributed surplus during the three months ended November 30, 2008.

Balance - August 31, 2008 and November 30, 2008

\$ 54,175

# Avalon Ventures Ltd.

Notes to the Financial Statements  
For the Three Months Ended November 30, 2008  
Unaudited - See Notice to Reader

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## 7. Related Party Transactions

During the three months ended November 30, 2008, the Company:

- a) incurred accounting fees of \$18,000 with an accounting firm in which an officer is the principal. As at November 30, 2008, accounts payable included \$11,000 accrued to this accounting firm; and
- b) incurred consulting fees of \$38,500 with a company owned by an officer of the Company, which were deferred as resource property costs. As at November 30, 2008, accounts payable included \$11,393 payable to this company.

## 8. Recent Accounting Pronouncements

Recent accounting pronouncements issued and not yet effective:

International Financial Reporting Standards (“IFRS”)

The CICA plans to incorporate IFRS into the CICA Handbook as a replacement for current Canadian Generally Accepted Accounting Principles for most publicly accountable enterprises effectively for fiscal years beginning on or after January 1, 2011. The transition date of September 1, 2011 for the Company will require restatement for comparative purposes of amounts reported by the Company for the year ended August 31, 2010. While the Company has begun assessing the adoption of IFRS for 2011, the financial reporting impact of the transition to IFRS has not been determined at this time.

## 9. Subsequent Events

Subsequent to the three months ended November 30, 2008, the Company:

- a) completed a private placement for 3,000,000 flow-through common shares at a price of \$0.50 per share for gross proceeds of \$1,500,000.

In connection with this private placement, the Company paid finders’ fees of \$99,375 and granted 198,750 non-transferable finders’ warrants to the finders. Each warrant entitles the holder to purchase one non-flow-through common share at a price of \$0.50 per share, exercisable until November 15, 2010; and

- b) granted 200,000 stock options to a consultant. Each option entitles the holder to purchase one common share of the Company at a price of \$0.50 per share until December 31, 2010. These options vest at the rate of 25% every three months following December 31, 2008.