



INDUSTRIAS PEÑOLES, S.A.B. DE C.V.

ONE HUNDRED TWENTY FIFTH ANNIVERSARY

Industrias Peñoles, S.A.B. de C.V. ANNUAL REPORT OF THE BOARD OF DIRECTORS TO THE SHAREHOLDERS' MEETING, CORRESPONDING TO FISCAL YEAR 2012.

Dear shareholders:

As Chairman of the Board of Directors of Industrias Peñoles, S.A.B. de C.V., and on behalf of the Board, it is my honor to present to you this report based on an analysis of the information provided by the Chief Executive Officer in his Annual Report on the Company's performance, the financial and operating results obtained in the 2012 fiscal year, and key developments from the period, as well as a report on the main activities of the Board of Directors.

In 2012 the Company faced a challenging macroeconomic environment, mainly due to the prolonged debt crisis in the euro zone, the uncertain fiscal policy of the United States, and weak economic growth in various world economies. With the exception of gold, whose average price rose over 2011, lower metal prices affected our 2012 financial results compared with the year before. Nonetheless, Peñoles remains a solid and financially stable company. As has been the case throughout our history, our commitment to Mexico and to prudent and organic long-term growth remains strong.

The Company celebrated its 125th anniversary in 2012, a milestone of permanence that reflects the strategy of organic and profitable growth as well as the Company's commitment to the country. Of course this also demonstrates the positive impact we have had on the economic, industrial and social development of Mexico. We take great pride in

being a Mexican company, which since its founding in 1887 has made important contributions to the country. As Mexico has grown and transformed, so too has the Company: from a small group of three mines located in the town of Peñoles in the Durango mountains – from where we took our name – to a world-class mining company with integrated businesses in smelting and refining non-ferrous metals and producing value-added chemicals.

These achievements are the result of a clear and unflagging focus on profitability and continuous investment to replenish reserves, identify new geological resources, develop new productive mines, and transform the mineral wealth beneath the soil into useful products for the global market. All this, combined with a focus on sustainable development, respect for the environment and support for the communities where we operate. Our vision has helped drive the industrialization and development of Mexico.

Moreover, at Peñoles we have provided countless benefits and created value for generations of stakeholders. Our effective management of shareholders' equity is considerable when measured in terms of profitability and growth. We have also created many direct and indirect jobs in remote areas. Our contribution to the service and supply chain and the comprehensive solutions we offer our clients, as well as the support provided for infrastructure development in the communities across every region where we operate have also been a priority. All this reaffirms our commitment to our shareholders and the sustainability of our operations.

Furthermore, our focus on organic growth, based on prudence and making rational investment decisions, is a hallmark that differs from what has happened in the industry, where the growth of leading global companies has been based on costly acquisitions that eventually undermine profitability.

In Mexico, the last three governments have maintained the financial stability of the country and improved the competitive conditions of the economy. The new government bodes well to consolidate and improve the economic conditions of the country. We remain enthusiastic about the promising future of Mexico, as this is reflected in our investment decisions.

A strategic and competitive differentiator for Peñoles is investment across economic and metal cycles. As a company with a 125 year history, we keenly understand the cyclical nature of metals prices and the prudence with which we must conduct ourselves in changing and risky environments.

As such, in 2012 and for the third consecutive year, we set a new record of investment both in capital expenditures and exploration, of USD\$1,179.4 million, 23.1% higher than in 2011 and more than three times the capital invested just five years ago. Our investments have allowed us to construct and commence operations at three new mining units in the past two years, expand capacity, improve the productivity of our operations and enhance the efficiency of our processes. Furthermore, we have tripled the value of our fixed assets in the past ten years.

This year, the exploration group conducted an extensive program with more than 760,000 meters drilled at 45 projects in Mexico and South America. Progress is particularly notable at Humos (in Sonora, copper), and at our Fresnillo plc subsidiary's advanced projects: Centauro Deep, Orisyvo and Juanicipio. Other projects have also shown promising results in terms of identified mineral resources.

In 2012 our community investments totaled USD\$10.2 million, in line with our commitment to actively support the economic development and self-sufficiency of the regions where we operate. Our efforts over the years have included the building of new roads and schools as well as the installation of electric service and water lines. Today, we also focus on reforestation and conservation projects, job training programs and small business development as part of our community self-development initiative. Our goal is to promote the prosperity of these communities.

Looking at our performance in 2012, our mining operations once again set records in milling and processing mineral, but lower ore grades in certain deposits did not allow us to increase the production of most metal contents. Production of gold, however, reached a new record with the start-up of the new Noche Buena mine in Sonora. Silver volumes remained nearly stable, the result, on one hand, of lower

expected ore grades at the Fresnillo mine, and on the other, greater contributions from other mines, especially from Ciénega in Durango, and Saucito in the Fresnillo district. The production of lead contents grew thanks to higher volumes processed at Naica, while zinc and copper were at similar levels to the previous year.

In the metallurgical operations, increased production of refined gold reflected the treatment of higher volumes of concentrates and rich materials from our own mines, as well as third party purchases. Refined silver production was lower following the strategic decision to reduce third party purchases of direct materials, while zinc and lead productions were slightly lower than in 2011.

In the chemical operations, sodium sulfate volumes reached a new production record, while commercial efforts increased sales and our customer base. The performance of our other chemical products was favorable, despite difficult market conditions for some of them. These products continue to strengthen our vertical integration and diversify our markets.

During 2012 we made significant advances in the execution of our growth projects. Among these, of particular note was the successful start-up of the Noche Buena mine in Sonora, which contributed to our record production levels of gold contents; also fundamental was the construction of the Velardeña zinc mine in Durango, where testing of the plant began at year-end 2012 and operations are expected to commence in the first quarter of 2013. Velardeña will enhance the vertical integration with our metallurgical business, and its location, near the smelter, strengthens its competitiveness.

In addition, investments were approved for the construction of the San Julián silver-gold project (Fresnillo plc), with commercial production expected in the second half of 2014, and for the Rey de Plata polymetallic mine, where production of zinc, copper, silver, lead and gold is expected to begin in 2015. The expansion of the Química del Rey sodium sulfate plant to 780,000 tons per year was also approved, to be completed in 2015. Combined, these projects represent investments of more than USD\$800 million over the next three years.

Also of note is the start-up of Phase II of the project Fuerza Eólica del Istmo, a renewable energy plant located in La Ventosa region of the state of Oaxaca, which adds 30 megawatts (MW) of installed capacity to Phase I, bringing the total to 80 MW. This project once again demonstrates our commitment to sustainability and the environment, and improves our energy self-sufficiency.

These advances reflect the permanent emphasis on seeking operating efficiency and maintaining control of costs, as well as the development and application of new technologies and the disciplined execution of growth projects.

Peñoles' current financial position is very solid. While 2012 earnings were lower than in the previous year, the Company continued to generate attractive cash flow and maintain a sound and conservative balance sheet.

Gross sales for 2012, excluding hedging results, totaled \$98,063.4 million (+1.6%) compared to 2011; this was primarily due to greater volumes of gold and the higher exchange rate of the peso against the dollar. Gross profit was \$28,570.7 million (-14.6%), EBITDA totaled \$25,928.1 million and operating income was \$20,311.8 million (18.2% and 26.2% lower, respectively). Net income was \$9,857.3 million (-22.7%) and \$7,985.3 million in dividends were declared during 2012. Our debt to EBITDA ratio was 0.4 times at year-end, and we have sufficient liquidity to cover operating and financial needs for the medium term.

The financial markets demonstrated their confidence in our Company. In June 2012, we successfully placed USD\$200 million of 10-year exchange traded bonds in the domestic market, our second issuance in three years. We also obtained an important upgrade to our credit rating from Standard & Poor's, from "AA+" to "AAA".

We remain very cautious and vigilant about development in the global economy and the potential impact that financial uncertainty may have on external factors that will affect our results for the years to come, particularly metal prices, input costs, inflation and exchange rates. At the same time, we remain committed to prudent management practices

and adopting timely and effective actions to mitigate any adverse effects. The continuous rise in the cost of certain inputs concerns us.

In Peñoles we are also firmly committed to our employees and view them as valued stakeholders, thus we aim to provide opportunities for development, respect and recognition in a safe work environment. Our priority continues to be watching over their health and physical integrity. As such, we are significantly increasing our efforts to enhance safety training programs and workshops for our employees and contractors, further fostering a safety culture in the Organization through extensive inspections and detailed analysis.

The Company's internationalization effort is notable for the listing of the Fresnillo plc subsidiary on the London market almost five years ago. It has been one of the most successful companies in this market. In addition, our corporate practices undoubtedly comply with the highest international standards. They have also been instrumental our exploration efforts in Chile and Peru.

During the course of this year, the Board of Directors has adhered to solid corporate governance practices. To carry out its functions, the Board has the support of the Committees recommended by the Code of Best Corporate Practices. The Board met five times during the 2012 fiscal year. The items discussed and approved at those meetings include:

- The reinforcement of safety programs
- Issuance of long-term exchange traded bonds
- Labor-management relations
- The metals hedging program
- Approval of the Rey de Plata project
- The capacity expansion at Química del Rey
- Basis of the 2013 budget

In compliance with the Securities Market Law, the Audit and Corporate Governance Committee has submitted its Annual Report, which is presented to this Shareholders' Meeting.

The financial statements from which the previous comments are derived, as well as the main accounting policies and criteria used in the

preparation of the financial information, were audited by the external auditors and included in the Annual Report. As of January 1st, 2011 the Company adopted International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB), and there were no significant changes to the accounting standards in the current year being reported.

It is also submitted for consideration of this Shareholders' Meeting the report on the main accounting policies and criteria used for the preparation of the financial statements that comprise, among others: basis for reporting and consolidating, significant accounting policies and newly issued accounting standards, that were audited by external auditors.

In the opinion of the Board of Directors, the report presented to this Shareholders' Meeting by the Chief Executive Officer reasonably reflects the financial position and results of the Company, as well as the key highlights and developments of the business in 2012.

In accordance with policy, the performance of senior executives is evaluated annually. Each increase of salary and benefits must be authorized by the Nomination, Evaluation and Compensation Committee. Salary increases are made annually and bonuses are determined based on the results of performance evaluations. The remuneration package of senior executives is comprised of a base salary, legal and other benefits.

I would like to thank the members on the Board of Directors for their dedication, commitment and valuable contributions. I would also like to thank our employees for their dedication and effort. Thank you also to you our shareholders, for your continued confidence in us. As we reflect on the past 125 years of Industrias Peñoles, we recognize that our achievements would not be possible without your support. We remain confident in the future growth and are committed to continued value creation.

Alberto Baillères
Chairman of the Board of Directors