



Leader en exploration pétrolière au Québec



**MANAGEMENT DISCUSSION AND
ANALYSIS OF FINANCIAL RESULTS**

**For the third quarter ended
June 30, 2007**



MANAGEMENT DISCUSSION AND ANALYSIS OF FINANCIAL RESULTS FOR THE THIRD QUARTER ENDED JUNE 30, 2007

This interim management discussion and analysis complies with Rule 51-102A of the Canadian Securities Administration regarding continuous disclosure for reporting issuers. It is an addition and supplement to the quarterly financial statements and should be read in conjunction with them and in parallel with the audited financial statements for fiscal years ended September 30, 2006 and 2005, and the annual management report when required. It presents the view of management on current Company activities and financial results, as well as a preview of the activities during the coming months.

1.1 Date

The present management discussion and analysis for the quarter ended June 30, 2007 is prepared as of July 26, 2007.

1.2 Nature of activities and overall performance

The Company is incorporated under Part 1A of the Quebec Companies Act. It has been listed on the TSX Venture Exchange since February 16, 2005. Exploration and development of oil and gas properties are the Company's primary activities. Moreover, to achieve its objectives, the Company has signed various agreements characteristic of the oil and gas industry.

The discovery of the Pétrolia-Haldimand well in March 2006 was a turning point for the Company. Recall that production tests on this well determined a stabilized rate of 34 barrels of light crude per day. When this find was made in only the third hole of a planned six-hole campaign, the Company reorganized its exploration plan to concentrate on developing the Pétrolia-Haldimand oil field.

Pétrolia is currently negotiating a JOA (Joint Operating Agreement) with the operator to undertake development work on the discoveries on the Gaspé and Gastonguay properties. This agreement will establish a framework for putting the Pétrolia-Haldimand field into production, as well as for developing future finds across the Gaspé and Gastonguay properties. Several meetings have taken place on this subject and notable progress has been made at the negotiating table. The exploration of the Gaspé and Gastonguay properties and the development work on the Haldimand oil field will resume as soon as the agreement is signed.

During the coming years, Pétrolia's financial outlays will be directed primarily towards the development of the Pétrolia-Haldimand find. Pétrolia's properties constitute a vast territory to be explored, and the Company is seeking industry partners to develop them.

During the last quarter, the Company continued its efforts to obtain the announced investments and remains confident about securing them. These steps have helped Pétrolia build a significant network of contacts that may prove strategic in the Company's development. These financial resources would ensure, in particular, the development of the Pétrolia-Haldimand oil field and the completion of its other exploration programs through farm-outs.

The Company's current revenue comes from interest income, since the Company is in the exploration and production testing stage with the Pétrolia-Haldimand #1 well. Its funding is therefore provided by issuing shares in its capital stock.

During the quarter, Pétrolia issued 19,500 shares for a total of \$8,005.

During the third quarter, the Company performed exploration work in the amount of \$260,805. The Company incurred a loss of \$390,336 (\$0.0134 per share), compared to \$105,935 (\$0.0047 per share) for the corresponding quarter of the previous year. The differences are due to the granting of stock options during the quarter to administrators and consultants in the amount of \$148,770, and the variation of its fair market value during the quarter, causing a loss of \$150,000.

1.3 Strategy and outlook

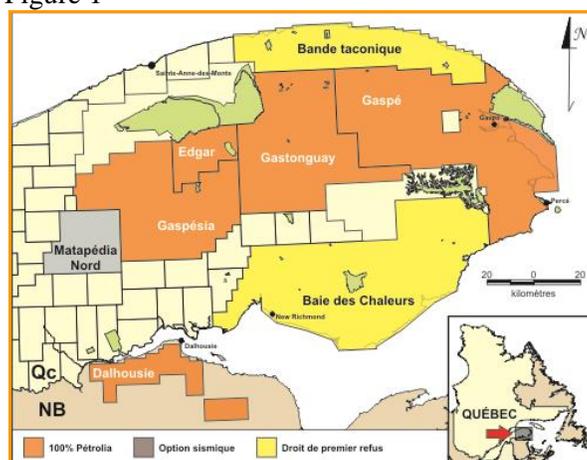
In 2007, Pétrolia is aiming to put the Pétrolia-Haldimand #1 well into production. However, before continuing the work, the Company must finalize a Joint Operating Agreement (JOA) with the operator.

After signing the JOA, the steps involved will be an assessment of the deposit's sub-surface extension and definition of the petroleum reservoir's characteristics (flow rate, pressure, and permeability, among others). In order to reach these objectives, a three-dimensional (3-D) seismic survey should be performed, if conditions allow. The data obtained will be interpreted, and the results used to locate at least one confirmation borehole. Regarding the evaluation of the reservoir's characteristics, the Pétrolia-Haldimand #1 well might be re-entered in order to perform additional work. The seismic survey, the re-entry, and the confirmation borehole will enable the confirmation of minimum oil reserves (reserve-certification study) and define the scope of future development work.

Pétrolia is now promoting a new exploration initiative called the Bourque project. This involves reef-type traps, such as those now producing in Alberta, with petroleum targets that are somewhat deeper than at Haldimand (e.g., Leduc Formation).

The schedule for all our oil and gas exploration programs is presented on our website, in the "Press Release" section.

Figure 1





Gaspé Property

Number of permits (block)	23
Pétrolia's interest	100%
Back-in granted to Junex	50% of Pétrolia's interest
Surface area (km ²)	4,186 km ²
Access	Paved roads and good forest roads in mountainous region;
Characteristics	Discovery of light crude in the Pétrolia-Haldimand #1 well; Gaspé is the most-explored region: 7 oil wells drilled since 1999; Sector's oil and gas potential demonstrated; Adequate regional seismic coverage;
Targets	Devonian reefs, limestones, and sandstones, between 600 and 2,500 metres in depth;

Projected work	25 km ² of 3-D seismics (Haldimand project); One confirmation well (Haldimand project); Reserve-certification study (Haldimand project); Seismic (Bourque project); Reprocessing of old seismic profiles.
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The Gaspé exploration permit block is located in the northeastern part of the Gaspé Peninsula, with a total surface area of 4,186 km². Pétrolia holds a 100% interest. The Gaspé - Basin region is where most of the exploration work has been conducted on the peninsula. The presence of oil seeps (60 sites) associated with Devonian sandstones accounts for the attention given to this region by explorers for more than a century, and also by Pétrolia, which has drilled three wells there.

Over the next year, Pétrolia will develop a new project called the "Bourque Project". This project is focused on a new target that is located on the western extension of the Pétrolia-Haldimand geologic structure. The Company recently undertook the interpretation of seismic profiles obtained in the 1980s, based on the reprocessing done in the 1990s. These profiles show reef-type traps, the first to be found in the Gaspé, which is an important step forward in understanding their geometry and formation. The results make it possible to take a fresh look at the property and to identify new targets to explore. However, a detailed seismic campaign is needed before beginning any new drilling.

Once the JOA is signed, the development of the Haldimand oil field, exploration work for the Bourque project, and the reprocessing of seismic profiles will become the Company's priorities.

Gaspésia Property

Number of permits 7
(block)

Pétrolia's interest 100%

Surface area 1,382 km²

Access Forest roads in mountainous region;

Characteristics Low level of regional exploration: first work in 2002;
Poor regional seismic coverage, but calibrated by a borehole;
No borehole on the property, but a few boreholes drilled in the sector, including two on the western edge of the Pétrolia permits;

Targets Sector has oil and gas potential;

Silurian reservoirs to a depth of 3,500 metres;

Work completed Interpretation of the existing seismics;

Completion of a regional seismic survey program over a total length of 126 km in December 2006.

Processing of seismic data acquired in 2006;

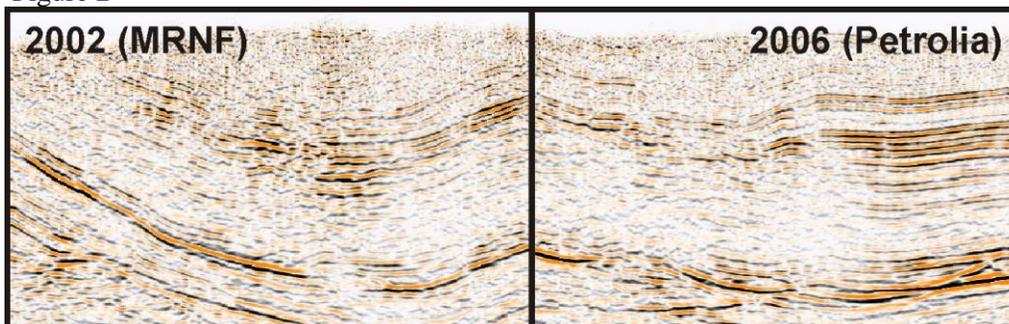
Reprocessing of all the lines acquired previously and completed in June 2007.

Projected work Interpretation incorporating geological, geophysical, and petrophysical data;
Inversion of the potential-field data;
GOCAD 3-D model incorporating all available data.

Following a study by Sproule designed to integrate the seismic and geological data, recommendations were made to Pétrolia to develop the Gaspésia property. The first step, aimed at assessing the hydrocarbon potential, was marked by the execution of a regional seismic survey in December 2006. Processing of the data, completed in June 2007, confirms the excellent quality of the data obtained.

A high-resolution seismic reflection survey was completed in December 2006 and the final results were delivered in June 2007. The objective of the regional seismic program was to identify a hydrocarbon reservoir in an area where conditions are favorable for the discovery of oil. The seismic data acquired prior to 2006 for this region were reprocessed to obtain a uniform seismic image for interpretation.

Figure 2





The seismic data acquired in 2006 with a wide frequency band (6-130 Hz), high fold coverage (90), and high spatial precision (10 m) provide a high-quality seismic image near the surface. The new seismic data were recorded with a large separation between the sources and the receivers (3,600 m), which enables complex structures to be imaged. The effort put into the acquisition and the excellent conditions during the survey (low noise and good receiver coupling) are responsible for one of the best seismic surveys carried out in the Gaspé peninsula (Figure 2).

The seismic interpretation currently underway was facilitated by the identification of contacts in the main formations all the way to the surface, allowing for direct correlation with the geologic maps. The seismic profile acquired in 2005 (PET-05-03) allows the interpretation to be calibrated against the only deep well in the region, the La Verendrye #1 well. A preliminary interpretation identified a series of faults that were not previously known. These faults could represent new possibilities for traps likely to contain hydrocarbons. Additionally, two new exploration concepts were developed, which will have to be verified by detailed studies.

Moreover, an internal evaluation of the Gaspésia permit block was performed based on the regional seismic program and the thermal-maturation study. With this new information available, Pétrolia has decided to focus its exploration program on the area to the north of the Causapscaal fault.

Dalhousie Property

Number of permits 3
(block)

Pétrolia's interest

100%

Surface area

682 km²

Access

Paved secondary roads;
Urban and industrial zone nearby

Characteristics

Very low level of exploration in the region (no boreholes or seismics have been carried out to date);
Sector has oil and gas potential

Targets

Devonian and Silurian;

Work completed

Geological compilation in 2005 by the Geological Survey of Canada;
Work on thermal maturation and evaluation of the hydrocarbon potential in northeastern New Brunswick by the Geological Survey of Canada in 2005

Projected work

Regional geophysical surveys.

In 2005, the Geological Survey of Canada completed an initial study of thermal maturation and hydrocarbon potential in northeastern New Brunswick. The data collected suggest the presence of zones with favourable conditions for preserving liquid and/or gaseous hydrocarbons. These permits were acquired based on the results of this study and essentially cover the areas with the most favourable conditions for oil. The city of Dalhousie is located on the edge of the permits and its thermal power plant and major maritime port represent a potential market.

Last June, Pétrolia carried out a geological field investigation of the Dalhousie property in cooperation with the New Brunswick Ministry of Natural Resources. This geological reconnaissance constitutes the first stage of petroleum exploration.



Over the course of the next year, Pétrolia is planning to perform geophysical work in order to complete the regional study of the geology of northeastern New Brunswick. This study will enable better targeting of prospective zones, possibly leading to a detailed seismic survey.

1.4 Effectiveness of Disclosure Procedures and Controls

The President and Chief Executive Officer and the Vice President of Finance have designed or supervised the design of disclosure controls and procedures in order to provide reasonable assurance that material information relating to the Company is made known to them, particularly during the period in which the annual filings are being prepared. They have also designed or supervised the design of internal controls over financial reporting in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian Generally Accepted Accounting Principles.

The assessment of the effectiveness of disclosure procedures and controls was conducted as of September 30, 2006, by the Company's officers, specifically the President and Chief Executive Officer and the Vice President of Finance, and under their supervision. Based on this assessment, these officers concluded that the Company's disclosure controls and procedures are effective in reasonably ensuring that the material information relating to the Company is made known to them by other members of the Company's staff on a timely basis.

1.5 Operating Results and Cash Position

For the quarter, the Company's revenues were limited to interest income of \$1,366 from short-term investments, compared to \$11,596 for the same quarter in 2006. The decrease in investment income is a result of decreased temporary investments.

As of June 30, 2007, the Company had cash and cash equivalents of \$368,317, a decrease of \$284,484 for the quarter. Disbursements related to deferred operating expenses and taxes on properties totaling \$246,368 explain much of the change in cash and cash equivalents.

As of June 30, 2007, working capital was \$290,658. As of the same date, the Company had met its commitments to its flow-through share subscribers by performing all of the exploration work which it had abandoned.

In accordance with research permits granted by the Quebec Ministry of Natural Resources and Wildlife, the Company agreed to pay fees in the amount of \$200,018 by 2010. The minimum payments of \$74,111 have already been paid for the current fiscal year and \$68,340 for the next three fiscal years. In addition, the Company must perform work on its properties located in Quebec with minimum costs that vary according to the age of the permits. These costs correspond to \$0.50 per hectare for the permit's first year and increase annually by \$0.50, reaching \$2.50 per hectare starting with the fifth year.

The minimum payments due are \$150,000 for fiscal year 2008, \$790,000 in 2009, \$880,545 in 2010, and \$125,025 in 2011.

1.6 Analysis of General and Administrative Expenses

General and administrative expenses for the quarter totaled \$273,544, compared to \$160,630 in 2006. The variance of \$112,914 between this quarter in 2007 and this quarter in 2006 was caused by recorded stock-based compensation in the amount of \$148,770 in 2007, compared to \$31,500 in 2006.

1.7 Summary of quarterly results

	<u>2007</u>		<u>2006</u>				<u>2005</u>	
	<u>June</u>	<u>March</u>	<u>December</u>	<u>September</u>	<u>June</u>	<u>March</u>	<u>December</u>	<u>September</u>
	\$	\$	\$	\$	\$	\$	\$	\$
Revenue	1,366	12,212	22,338	12,233	11,596	22,595	9,929	103,687
Net earnings (Net loss)	(390,336)	315,253	(21,008)	(122,458)	(105,935)	(195,831)	(53,701)	56,319
Net earnings (Net loss) per share and diluted per share	(0.0134)	0.109	(0.0007)	(0.0049)	(0.0047)	(0.0098)	(0.0030)	0.049

The revenue consists of grants and interest earned for each of the quarters. General and administrative expenses have been relatively stable from one quarter to another in 2007. The changes in losses or quarterly profits are explained as follows:

- 2005 – September: Recorded \$99,905 from disposal of well rights and \$28,651 for future income taxes;
- 2006 – March: Recorded stock-based compensation in the amount of \$130,065;
- 2007 – March: Gain in the amount of \$400,000 resulting from an investment recorded at fair value.
- 2007 – June: Recorded an investment at fair value causing a loss of \$150,000 and stock-based compensation of \$148,770.

1.8 Related-Party Transactions

During the quarter, a company (Géominex Inc.) in which one of Pétrolia's directors holds a minority interest, billed for deferred exploration expenses for a total of \$70,000 (2006 - \$48,200) and rent of \$600 (2006 - \$3,120). As of June 30, 2007, \$35,340 is due (2006 - \$8,455).



In addition, the Company shares administrative expenses with Ressources Appalaches, a company that has the same chief executive officer. It billed the Company for the following expenses:

	2007	2006
	\$	\$
Salaries and fringe benefits	49,948	32,046
Office supplies	900	2,250
Telecommunications	1,089	1,175

The balance owed to this company as of June 30, 2007, is \$15,619 (2006 – \$30,617).

The Company rented premises from one of its directors for \$4,350. No balance is due as of June 30, 2007.

These operations occurred in the normal course of business and were recorded at the fair exchange value, which is the amount of the established consideration accepted by the related parties.

1.9 New accounting standards

Accounting modifications

The Canadian Institute of Chartered Accountants (CICA) modified section 1506 entitled "Accounting modifications", which now stipulates that a) an entity should only change accounting methods voluntarily if the change results in financial statements that provide reliable and more relevant information, b) accounting method changes must be accompanied by information regarding the figures of the previous periods and the reason for the change, c) in the case of estimation changes, information on the nature of the change and the amount must be provided. On October 1, 2006, the Company adopted these new recommendations, which had no effect on its interim financial statements.

Financial instruments

The CICA issued new accounting standards related to financial instruments: a) section 1530 "Comprehensive Income", which introduces a new requirement regarding the temporary exclusion of certain types of gains and losses of net earnings, b) section 3855 "Financial Instruments - Recognition and Measurement", which stipulates when an entity must record a financial asset, a financial liability, or a non-financial derivative instrument in its balance sheet and whether the recording of included amounts must be based on the fair value or the costs and also specifies how to present the gains and losses on financial instruments, c) section 3865 "Hedges", which describes when and how hedge accounting can be used. On October 1, 2006, the Company adopted these new recommendations and now considers its temporary investments as financial assets held for trading and records them at the fair value that corresponds to their cost, given their short-term maturity. The Company also considers the long-term investment a financial asset held for trading and records it at the fair value.

1.10 Risk and Uncertainty

The risks that are associated with the Company's activities are the same as those disclosed in the annual management report. Economic and sectoral factors remain mostly unchanged. There was no significant change in the Company's third quarter.

1.11 Additional Information

a) Supplemental information

Certain supplemental information, including prior interim management reports and press releases are available online at www.sedar.com in the documents section or on Pétrolia's Web site at: www.petroliagaz.com.

b) Rule 51-102A section 5.3

Details of deferred exploration expenses for the three and nine months ended June 30, 2007, are presented in the statement of deferred exploration expenses within the Company's interim financial statements as of the same date.

c) Rule 51-102A-section 5.4

Information on shares issued, warrants, and stock options as at July 26, 2007:

Common shares: 29,208,252 common shares were issued, including 1,929,289 shares that have been escrowed, thus leaving 27,278,963 shares outstanding.

Warrants: 2,622,869 warrants can be exercised as follows:

- 1,611,870 shares at a price of \$0.55 per share until September 30, 2007;
- 1,010,999 shares at a price of \$0.75 per share until November 30, 2007.

Broker warrants: 202,603 broker warrants can be exercised at a price of \$0.38 per share until December 30, 2007.

Stock options: The stock options granted to its directors, members of senior management, employees, and service providers are the following:

- 270,000 stock options exercisable at a price of \$0.40 per share until 15 Mar 2010;
- 1,100,000 stock options exercisable at a price of \$0.40 per share until February 3, 2011;
- 150,000 stock options exercisable at a price of \$0.58 per share until May 10, 2011;
- 1,125,000 stock options exercisable at a price of \$0.40 per share until June 21, 2012.



1.12 Management's Responsibility for Financial Information

The financial statements for the periods ended June 30, 2007, have been prepared by management in accordance with Canadian Generally Accepted Accounting Principles and approved by the audit committee. The fairness and objectivity of these financial statements are the responsibility of management.

Rimouski, July 26, 2007

On behalf of the Board

(signed) *André Proulx*

André Proulx
President