



ProspEx Resources Ltd. - 2009 Second Quarter Results

July 30, 2009

(All amounts are in Canadian dollars, unless stated otherwise)

ProspEx Resources Ltd. ("ProspEx" or the "Company") announces its financial and operating results for the three and six months ended June 30, 2009.

HIGHLIGHTS

- In the second quarter, ProspEx closed the disposition of assets in the Medallion area for proceeds of \$28.0 million, prior to closing adjustments. The Medallion disposition significantly strengthened the Company's balance sheet, reducing net debt at June 30, 2009 to \$23.0 million, compared to \$49.3 million at March 31, 2009. The proceeds of the Medallion disposition provide the Company with financial flexibility in the current environment of lower commodity prices.
- Capital expenditures for exploration and development (before acquisitions and dispositions) were \$1.6 million during the second quarter of 2009, slightly less than cash flow for that period.
- Cash flow before changes in non-cash working capital items for the quarter was \$2.5 million, a decrease of 83% compared to the second quarter of the prior year due to a 28% decrease in production and a 58% decrease in commodity prices.
- During the quarter, ProspEx renegotiated its credit facility and now has a committed facility with a \$40 million limit. The Company's current net debt of \$23.0 million equates to 58% utilization of this facility.
- Production for the second quarter decreased to 3,089 barrels of oil equivalent ("boe") per day, compared to 3,807 boe per day in the first quarter of 2009 due to the Medallion disposition, a scheduled shut down at Ricinus for maintenance, and natural declines.
- ProspEx intends to temporarily curtail approximately 500 boe per day of production due to the low natural gas price environment. The production to be curtailed typically earns a lower netback due to higher unit operating costs and/or lower associated natural gas liquids production.

MESSAGE TO SHAREHOLDERS

In the Company's release of its first quarter results in May of this year, ProspEx characterized the business environment as one of unprecedented uncertainty and distress in equity, credit and commodity markets, and anticipated that natural gas prices would stay low for the balance of 2009, and potentially longer. The Company continues to hold these views.

ProspEx has two key objectives in the current environment: firstly, to strengthen its finances in order to provide financial flexibility during the current downturn in natural gas prices; and secondly to enhance the Company's prospect inventory with projects that offer repeatable opportunities with economies of scale, and thereby position the Company for profitable growth when the business environment improves.

In order to strengthen its finances, ProspEx disposed of its Medallion area assets on June 1, 2009 for proceeds of \$28 million (prior to closing adjustments) reducing its net debt to \$23.0 million. Concurrent with the Medallion disposition ProspEx negotiated a new credit facility, and now has a committed facility with a \$40 million limit. The next scheduled credit facility review date is May 31, 2010. These measures provide the Company with financial

flexibility to carry out its objective of enhancing the Company's prospect inventory. The Company has also entered into certain hedging arrangements to protect cash flow for the remainder of the summer season.

ProspEx's capital spending priorities continue to focus on capturing and proving up new opportunities that are anticipated to generate repeatable prospect inventory with economies of scale. The Company believes that the current business environment offers opportunities to acquire assets of this nature at lower prices than those observed over the past several years. During the second quarter, ProspEx acquired approximately 5,700 net acres of land through asset acquisitions and Crown land purchases. These new assets are seen as offering the opportunity to drill multiple horizontal wells in each section, and represent a material addition to the Company's prospect inventory.

In addition to the acquisition of new assets, ProspEx is also working to prove up repeatable drilling prospects on its existing land base. The first horizontal well in the Kakwa area is expected to commence drilling in early August, and will serve as a pilot test of multi-frac completion technology in horizontal wells. This pilot test is expected to validate an inventory of horizontal development locations across the Company's Kakwa land base.

OPERATIONAL REVIEW

Capital Program

Capital expenditures for exploration and development (before acquisitions and dispositions) were \$1.6 million during the second quarter of 2009. ProspEx did not participate in the drilling of any new wells in the second quarter, due to the combined effects of the traditional "spring break up" period impairing surface access to drilling locations, and a reduced capital program due to the current business environment.

Capital activity in the second quarter was largely focused on land acquisition, as well as asset acquisitions and dispositions. As previously disclosed, the Company closed the disposition of certain properties in the Medallion area on June 1, 2009 for proceeds of \$28.0 million, prior to closing adjustments. These properties consist of 179 (115 net) producing wells, with net production of approximately 750 boe per day (as of the January 1, 2009 effective date), along with associated gas gathering and field compression facilities. The reserves associated with the Medallion disposition were evaluated on behalf of ProspEx by GLJ Petroleum Consultants Ltd. ("GLJ") effective December 31, 2008. These reserves were estimated to be 2,348 mboe on a Total Proved basis, and 3,541 mboe on a Total Proved plus Probable basis.

ProspEx invested \$3 million in the second quarter on asset acquisitions and purchases at Crown land sales. This activity included the purchase of approximately 5,700 net acres of land and 30 boe per day of production on trends that the Company considers to be analogous to its existing Kakwa assets.

In Kakwa in the Deep Basin, the Company expects to commence drilling its first horizontal well in early August. This well is intended to pilot test the use of horizontal drilling with multi-stage fracturing techniques in the Kakwa area, with the objective of confirming the commerciality of a repeatable inventory of horizontal drilling locations at Kakwa.

Production

Production (boe/d)	Q2 2009	Q1 2009	Q4 2008	Q3 2008	Q2 2008
West Central Alberta	1,635	2,099	1,914	1,847	1,904
Deep Basin	944	985	924	1,150	1,362
Southern Alberta	503	713	743	847	1,009
Other	7	10	6	6	10
Total	3,089	3,807	3,587	3,850	4,285

The second quarter production averaged 3,089 boe per day, compared to first quarter of 2009 production of 3,807 boe per day. This decrease was due to the disposition of the Company's Medallion assets as of June 1, 2009 (approximately 240 boe per day impact on average quarterly production), the previously announced shut down of the Ricinus plant for scheduled maintenance (approximately 160 boe per day impact on average quarterly production), as well as natural declines in the Company's production base.

ProspEx intends to temporarily curtail approximately 500 boe per day of production due to the low natural gas price environment. This curtailment represents approximately 20% of ProspEx's current net production capacity of 2,600 boe per day. ProspEx intends to maintain production in its core operating areas of Kakwa in the Deep Basin and Ricinus and Harmattan in West Central Alberta, with the majority of its production outside of these areas curtailed until natural gas prices improve.

The production to be curtailed typically earns a lower netback due to higher unit operating costs and/or lower natural gas liquids production, or shows higher than corporate average production decline rates. The Company believes that curtailing this production until prices improve will maximize shareholder value.

The cash flow impact of this production curtailment is anticipated to be modest. ProspEx estimates that curtailment of this 500 boe per day of production for a three month period ending November 1, 2009 would result in a reduction of cash flow of \$0.4 million, assuming current forward prices. Please be advised that guidance regarding the anticipated reduction in cash flow may constitute a "financial outlook" as contemplated by National Instrument 51-102 of the Canadian Securities Administrators entitled *Disclosure Obligations* ("NI 51-102"). The purpose of such financial outlooks is to forecast the anticipated reduction in cash flow resulting from the planned production curtailment described above. Please be advised that the information may not be appropriate for other purposes.

Financial

The Company has taken steps to strengthen its balance sheet in the face of the relatively low natural gas prices of the current environment. With the recent disposition of the Medallion assets net debt at June 30, 2009 stands at \$23.0 million. This net debt is equivalent to 2.3 years debt to trailing annualized quarterly cash flow, and 58% of the limit on the Company's credit facility. The Company's relatively low debt level provides financial flexibility in an environment of depressed gas prices.

ProspEx has also renegotiated its credit facility, and now has a committed facility with a \$40 million limit with the next scheduled credit facility review date at May 31, 2010.

The Company has entered into the following financial derivative sales contracts in order to partially mitigate commodity price risk over the summer and fall of 2009.

<u>Type</u>	<u>Amount (GJ/day)</u>	<u>Term</u>	<u>Price (\$/GJ at AECO)</u>	<u>Type</u>
Firm fixed quantity	2,500	Jul. 1 – Jul. 31, 2009	\$ 3.58	Physical
Firm fixed quantity	2,500	Aug. 1 – Oct. 31, 2009	\$ 4.21	Physical
Costless collar	1,500	Aug. 1 – Oct. 31, 2009	\$ 4.00 - \$ 5.23	Financial

These hedges protect the price to be received for approximately half of the Company's forecasted natural gas production for the period August 1 to October 31, 2009 (after giving effect to the curtailments described above).

Withdrawal of 2009 Guidance

Recent economic and market events and the Company's recent decision to curtail production by approximately 500 boe per day has increased the uncertainty with respect to forecasting annual average production, cash flow and per barrel operating and general administration costs for 2009. With respect to economic and market events, the Company's guidance previously announced on May 25, 2009 was made under the assumption that natural gas prices would be high enough to justify continued production of all the Company's wells. This assumption has not been accurate in that AECO natural gas prices have declined to a level where ProspEx now believes that shareholder value will be maximized if production of certain properties that have lower netbacks or higher natural decline rates is deferred until natural gas prices improve. The Company's guidance was made under the assumption that there would be no curtailment decision by the Company.

In light of the foregoing, the Company is withdrawing all of its previously issued financial guidance for 2009 including the guidance of May 25, 2009. ProspEx intends to continue to focus its 2009 capital spending on the capture of new opportunities and drilling to demonstrate the commerciality of new opportunities on its existing asset base, such as the anticipated pilot test of horizontal drilling at East Kakwa which is planned for the third quarter of 2009.

Reader's Advisory

ProspEx is a Calgary based junior oil and gas company focused on exploration for natural gas in the Western Canadian Sedimentary Basin.

Certain information contained in this press release constitutes forward-looking information or statements including, without limitation, information and statements respecting: anticipated cash flow, capital expenditures, production forecasts, production additions and deletions, reserves and resources additions and deletions, additions to and deletions from the Company's historical and future capital programs, acquisitions or dispositions, operating expenses, G&A, royalties, expected timing of the tie-in of wells, expected timing of the receipt of regulatory approvals and expected timing of the completion of facilities projects.

Statements relating to "reserves" and "resources" are forward-looking information as they involve the implied assessment, based on certain estimates and assumptions that, among others, the reserves and resources described exist in the quantities predicted or estimated.

Forward-looking information and statements are often, but not always, identified by the use of words such as "anticipate", "seek", "believe", "expect", "hope", "plan", "intend", "forecast", "target", "project", "guidance", "may", "might", "will", "should", "could", "estimate", "predict" or similar words or expressions suggesting future outcomes or language suggesting an outlook. By their very nature, forward-looking information and statements involve inherent risks and uncertainties, both general and specific, and risks that predictions, forecasts, projections and other forward-looking information and statements will not be achieved. We caution readers not to place undue reliance on these statements as a number of important factors could cause the actual results to vary materially from the forward-

looking information or statements. These factors include, but are not limited to: the volatility of oil and gas prices; production and development costs and capital expenditures; the imprecision of reserve and resource estimates and estimates of recoverable quantities of oil, natural gas and liquids; the Company's ability to replace and expand oil and gas reserves; environmental claims and liabilities; incorrect assessments of value when making acquisitions or dispositions; increases in debt service charges; the loss of key personnel; the marketability of production; defaults by third party operators; unforeseen title defects; fluctuations in foreign currency and exchange rates; adequacy of insurance coverage; compliance with environmental laws and regulations; changes in tax and royalty laws; the Company's ability to access external sources of debt and equity capital; and the Company's ability to obtain equipment in a timely manner to carry out development activities. Further information regarding these factors may be found under the headings "*Risk Factors*" and "*Industry Conditions*" in the Company's most recent Annual Information Form, under the heading "*Business Risks*" in the Company's Management's Discussion and Analysis for the year ended December 31, 2008, and in the Company's most recent consolidated financial statements, management information circular, quarterly reports, material change reports and news releases available under the Company's profile on SEDAR (www.sedar.com). Readers are cautioned that the foregoing list of factors that may affect future results is not exhaustive. When relying on our forward-looking statements to make decisions with respect to the Company, investors and others should also carefully consider information set forth in the section "Forward-Looking Information" of the Company's most recent Annual Information Form respecting the assumptions upon which the Company bases certain forward-looking information and the uncertainties inherent in such assumptions.

The Company does not assume responsibility for the accuracy and completeness of the forward-looking information or statements and such information and statements should not be taken as guarantees of future outcomes. Subject to applicable securities laws, the Company does not undertake any obligation to revise these forward-looking information or statements to reflect subsequent events or circumstances. Furthermore, the forward-looking information contained in this press release are made as of the date of this document and the Company does not undertake any obligation to update publicly or to revise any of the included forward-looking statements, whether as a result of new information, future events or otherwise, except as required by applicable law. The forward-looking information and statements contained in this press release are expressly qualified by this cautionary statement.

For the purposes of this press release, boes have been calculated on the basis of six thousand cubic feet of gas to one barrel of oil. The term boe may be misleading, particularly if used in isolation. A boe conversion ratio of six thousand cubic feet to one barrel is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

The estimates of reserves and future net revenue for the individual properties may not reflect the same confidence level as estimates of reserves and future net revenue for all properties, due to the effects of aggregation. The Total Proved Reserves of the Company and Total Proved plus Probable Reserves of the Company were estimated by GLJ effective as of December 31, 2008 as 7,139 boe and 10,043 boe respectively.

Netbacks are calculated by subtracting transportation costs, royalties payable and operating costs from the average price received during the period.

ProspEx Resources Ltd.
Consolidated Highlights
For the period ended

(unaudited)	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
FINANCIAL (\$000's)				
Oil and gas revenue	7,370	24,567	20,135	41,945
Net (loss) earnings	(3,899)	2,261	(6,124)	151
Cash flow ⁽¹⁾	2,475	14,926	8,196	24,108
Total assets	159,790	192,681	159,790	192,681
Total net debt ⁽²⁾	23,032	43,224	23,032	43,224
Net (loss) earnings per share (\$ per share)				
Basic	(0.07)	0.04	(0.11)	0.00
Diluted	(0.07)	0.04	(0.11)	0.00
Cash flow per share (\$ per share) ⁽¹⁾				
Basic	0.04	0.26	0.14	0.42
Diluted	0.04	0.25	0.14	0.41
Weighted average common shares (000's)				
Basic	57,385	57,082	57,385	56,814
Diluted	57,385	58,709	57,385	58,400
PRODUCTION VOLUMES				
Natural gas (mcf/d)	14,382	19,957	15,963	19,510
Natural gas liquids (bbls/d)	645	851	728	694
Oil (bbls/d)	47	108	58	88
Total (boe/d)	3,089	4,285	3,446	4,033
SALES PRICES				
Natural gas (\$/mcf)	3.89	9.47	5.15	8.74
Natural gas liquids (\$/bbl)	34.15	79.09	35.21	71.88
Oil (\$/bbl)	<u>64.40</u>	<u>126.37</u>	<u>57.82</u>	<u>114.49</u>
Total (\$/boe)	26.22	63.00	32.28	57.14
OPERATING NETBACKS (\$/boe)				
Price	26.22	63.00	32.28	57.14
Royalties	(1.21)	(11.97)	(4.60)	(10.38)
Operating costs	(9.30)	(8.39)	(8.12)	(9.23)
Transportation	<u>(0.93)</u>	<u>(1.00)</u>	<u>(0.99)</u>	<u>(0.98)</u>
Total	14.78	41.64	18.57	36.55
CAPITAL (\$000's)				
Drilling and completions	104	2,094	3,690	12,145
Facilities	(914)	1,908	(27)	6,620
Land and lease	1,568	1,354	1,889	2,913
Seismic	98	2,562	148	2,826
Capitalized general and administrative	763	697	1,561	1,494
Total exploration & development	1,619	8,615	7,261	25,998
Net property(disposition) acquisitions	(25,383)	(5,448)	(27,461)	6,050
Other capital assets	4	99	7	159
Total	<u>(23,760)</u>	3,266	<u>(20,193)</u>	32,207

(1) Cash flow is defined as cash flow from operations before changes in operating non-cash working capital.

(2) Total net debt is defined as long term debt less working capital (or plus working capital deficiency) excluding unrealized financial instrument gain (loss) and associated future tax assets (liabilities) and other liabilities.

Cash flow and total net debt do not have standardized measures prescribed by Canadian generally accepted accounting principles and therefore may not be comparable with calculation measures for other issuers.

MANAGEMENT DISCUSSION & ANALYSIS

Management's Discussion and Analysis ("MD&A") is management's assessment of the financial and operating results of ProspEx Resources Ltd. ("ProspEx" or the "Company") as well as a prospective view of the Company's activities. The MD&A is for the three and six months ended June 30, 2009, and was prepared as at July 30, 2009. The MD&A should be read in conjunction with the audited consolidated financial statements and MD&A for the year ended December 31, 2008 including the notes related thereto and the consolidated financial statements for the three and six months ended June 30, 2009 together with the notes related thereto. The reader should be aware that historical results are not necessarily indicative of future performance.

SECOND QUARTER HIGHLIGHTS

The second quarter is traditionally a slower period operationally within the oil and gas industry due to spring break up, and with the current economic climate, ProspEx did not participate in the drilling of any wells during the quarter. However, the Company was active in the acquisition and disposition market. On June 1st, the Company closed the disposition of its Medallion property for a sales price of \$28.0 million (prior to closing adjustments) with an effective date of January 1, 2009. This resulted in a reduction in net debt (excluding after tax unrealized financial instrument gains or losses) from the end of the first quarter level of \$49.3 million to \$23.0 million on a newly established credit facility of \$40.0 million.

Natural gas prices continued their downward trend, as concerns of oversupply reduced the overall price received in the quarter to \$26.22 per boe compared to the first quarter price of \$37.25 per boe. This resulted in cash flow before changes in non-cash working capital items of \$2.5 million in the second quarter, a 57% decrease compared to the first quarter. Production for the second quarter averaged 3,089 boe per day, a 19% decrease compared to the first quarter of 2009 reflecting the disposition of the Medallion sale, plant turnarounds and natural production declines.

Capital expenditures for exploration and development (before acquisitions and dispositions) were \$1.6 million during the second quarter of 2009 with the purchase of new undeveloped lands representing the majority of costs incurred.

Business environment

Natural gas prices remain low, driven by high natural gas storage inventories, strong production levels in the United States, liquefied natural gas imports, and reduced demand for natural gas as a result of the global economic downturn. The Company believes these factors suggest that prices will stay low for the balance of 2009. In light of this view, as well as the uncertainty in credit and equity markets, ProspEx intends to maintain its conservative approach in managing the Company's finances, including restricting exploration and development capital spending to be approximately equal to cash flow.

Withdrawal of 2009 Guidance

Recent economic and market events and the Company's recent decision to curtail production by approximately 500 boe per day has increased the uncertainty with respect to forecasting annual average production, cash flow and per barrel operating and general administration costs for 2009. With respect to economic and market events, the Company's guidance previously announced on May 25, 2009 was made under the assumption that natural gas prices would be high enough to justify continued production of all the Company's wells. This assumption has not been accurate in that AECO natural gas prices have declined to a level where ProspEx now believes that shareholder value will be maximized if production of certain properties that have lower netbacks or higher natural decline rates is deferred until natural gas prices improve. The Company's guidance was made under the assumption that there would be no curtailment decision by the Company.

In light of the foregoing, the Company is withdrawing all of its previously issued financial guidance for 2009 including the guidance of May 25, 2009. ProspEx intends to continue to focus its 2009 capital spending on the capture of new opportunities and drilling to demonstrate the commerciality of new opportunities on its existing asset base, such as the anticipated pilot test of horizontal drilling at East Kakwa which is planned for the third quarter of 2009.

Revenue

(\$000's)	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
Natural gas	\$ 5,092	\$ 18,605	\$ 13,578	\$ 32,344
Realized (loss) gain on financial instruments	-	(1,407)	1,316	(1,307)
Total natural gas	5,092	17,198	14,894	31,037
Oil	272	1,245	602	1,832
Natural gas liquids	2,006	6,124	4,639	9,076
Oil and gas revenue	7,370	24,567	20,135	41,945
Unrealized (loss) gain on financial instruments	310	(2,781)	(517)	(7,300)
Total revenue	\$ 7,680	\$ 21,786	\$ 19,618	\$ 34,645

Second quarter oil and gas revenue decreased \$17.2 million or 70% to \$7.4 million in 2009 from \$24.6 million in the second quarter of 2008. This decrease in revenues for the quarter is due to the combination of lower production levels and lower prices incurred in the period, as described below.

Production

<u>Area (boe/d)</u>	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
Deep Basin	944	1,362	965	1,393
West Central Alberta	1,635	1,904	1,866	1,570
Southern Alberta	503	1,009	607	1,059
Other	7	10	8	11
	3,089	4,285	3,446	4,033
<u>Product</u>				
Natural gas (mcf/d)	14,382	19,957	15,963	19,510
Natural gas liquids (bbls/d)	645	851	728	694
Oil (bbls/d)	47	108	58	88
Total (boe/d)	3,089	4,285	3,446	4,033

The second quarter production averaged 3,089 boe per day, compared to first quarter of 2009 production of 3,807 boe per day and the prior year's production of 4,285 boe per day. This decrease from first quarter levels was due to the disposition of the Company's Medallion assets on June 1, 2009 (approximately 240 boe per day impact on average quarterly production), the previously announced shut down of the Ricinus plant for scheduled maintenance (approximately 160 boe per day impact on average quarterly production), as well as natural declines in the Company's production base.

Commodity Pricing

ProspEx Average Prices	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
Natural gas (\$/mcf)				
Sales price	\$ 3.89	\$ 10.25	\$ 4.69	\$ 9.11
Realized (loss) gain on financial instruments	-	(0.78)	0.46	(0.37)
	3.89	9.47	5.15	8.74
Oil (\$/bbl)	64.40	126.37	57.82	114.49
NGL (\$/bbl)	34.15	79.09	35.21	71.88
Average realized price (\$/boe)	26.22	63.00	32.28	57.14
Unrealized gain (loss) on financial instruments(\$/boe)	1.10	(7.13)	(0.83)	(9.94)
Total average price (\$/boe)	\$ 27.32	\$ 55.87	\$ 31.45	\$ 47.20
Benchmark pricing	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
AECO C Spot (\$/mcf)	\$ 3.62	\$ 10.22	\$ 4.27	\$ 9.06
Edmonton Par – light oil (\$/bbl)	\$ 62.90	\$ 126.07	\$ 56.28	\$ 111.79

Average natural gas sales prices decreased 62% to \$3.89 per mcf in the second quarter of 2009, compared to \$10.25 per mcf in the second quarter of 2008. During the second quarter of 2009, AECO C daily spot prices for natural gas decreased 65% compared to the second quarter of 2008 and the AECO monthly index for the same period decreased 61%. Realized natural gas prices (including realized losses on financial instruments) for the second quarter of 2009 averaged \$3.89 per mcf, a decrease of 59% from \$9.47 per mcf realized in the second quarter of 2008. This decrease reflects the ongoing concern of an oversupply in natural gas markets.

Oil prices received for the second quarter of 2009 were \$64.40 per barrel ("bbl"). This is a 49% decrease from the \$126.37 per bbl received in the second quarter of 2008, consistent with the decrease in benchmark pricing. The price realized for natural gas liquids ("NGLs") in the second quarter of 2009 was \$34.15 per bbl, a decrease of 57% from \$79.09 per bbl in the second quarter of 2008. Overall, oil and NGL prices have declined substantially, as the world wide economic slowdown has reduced demand for commodities.

Financial Instruments

The impact of the changes in the fair values of open financial instruments during the quarter ended June 30, 2009 was an unrealized gain of \$0.3 million. This compares to an unrealized loss of \$2.8 million for the second quarter of 2008.

The financial instruments open as of June 30, 2009 are described below:

<u>Type</u>	<u>Amount (GJ/day)</u>	<u>Term</u>	<u>Price (\$/GJ at AECO)</u>	<u>Type</u>
Firm fixed quantity	2,500	Jul. 1 – Jul. 31, 2009	\$ 3.58	Physical
Firm fixed quantity	2,500	Aug. 1 – Oct. 31, 2009	\$ 4.21	Physical
Costless collar	1,500	Aug. 1 – Oct. 31, 2009	\$ 4.00 - \$ 5.23	Financial

Royalty Expenses

(\$000's)	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
Crown	\$ (42)	\$ 2,862	\$ 1,973	\$ 5,528
Freehold and gross overriding	383	1,806	894	2,090
Total Royalties	\$ 341	\$ 4,668	\$ 2,867	7,618
\$ per boe	\$ 1.21	\$ 11.97	\$ 4.60	\$ 10.38
As a percentage of oil and gas revenue	5%	19%	14%	18%

In the second quarter of 2009, royalties totaled \$0.3 million or 5% of revenue compared to the previous year's \$4.7 million or 19% of revenue. During the first six months of 2009 royalties totaled \$2.9 million or 14% of oil & gas revenue compared to \$7.6 million or 18% of oil & gas revenue for the same period of 2008.

On January 1, 2009 a new royalty framework came into effect in the Province of Alberta. This new framework provides for a greater sensitivity of royalty rate to natural gas prices, and thus royalties in the first six months of 2009 have declined relative to the same period in 2008 due to reduced commodity prices. Royalties in the second quarter of 2009 were also reduced by \$0.5 million of annual adjustments to capital and custom processing costs relating to the Crown royalty share of production.

Operating Costs

	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
Operating costs (\$000's)	\$ 2,613	\$ 3,274	\$ 5,066	\$ 6,774
Operating costs (\$/boe)	\$ 9.30	\$ 8.39	\$ 8.12	\$ 9.23

Operating costs for the first quarter were \$2.6 million or \$9.30 per boe, compared to \$3.3 million or \$8.39 per boe in the second quarter of 2008. Higher second quarter operating costs were due to a combination of maintenance costs at plants in the Ricinus and Kakwa operating areas, as well as an increase in processing fees at Ricinus.

Transportation Expense

	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
Transportation expenses (\$000's)	\$ 262	\$ 389	\$ 619	\$ 721
Transportation expenses (\$/boe)	\$ 0.93	\$ 1.00	\$ 0.99	\$ 0.98

Transportation expense per boe for the three and six months ended June 30, 2009 is consistent with the comparable periods of 2008.

General and Administrative Expenses

	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
Gross general and administrative	\$ 1,769	\$ 1,685	\$ 3,718	\$ 3,620
Recoveries	(155)	(202)	(400)	(470)
Capitalized expenses	(763)	(697)	(1,561)	(1,495)
Net general and administrative expenses	\$ 851	\$ 786	\$ 1,757	\$ 1,655
Net general and administrative expenses (\$/boe)	\$ 3.03	\$ 2.02	\$ 2.82	\$ 2.25

Gross general and administrative costs remained approximately the same compared to the same periods in 2008 but were higher on a per boe basis due to decreases in production.

Loss on Subleasing

During the quarter, the Company subleased a portion of its office space on a temporary basis, resulting in the recognition of \$0.5 million in losses over the term of the subleases.

Interest and Bank Charges

Interest and bank charges of \$0.4 million in the second quarter and \$0.8 million year to date in 2009 were slightly lower compared to the prior year amount of \$0.5 million in the second quarter and \$1.0 million year to date. This is due to lower overall interest rates and lower debt levels.

Depletion, Depreciation and Accretion

	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
Depletion, depreciation and accretion (\$000's)	\$ 8,247	\$ 8,685	\$ 16,988	\$ 16,060
Depletion, depreciation and accretion (\$/boe)	\$ 29.34	\$ 22.27	\$ 27.24	\$ 21.88

Depletion, depreciation and accretion expense per boe in the second quarter of 2009 was \$29.34. This is a 32% increase from the second quarter 2008 rate of \$22.27 per boe. This was due to the proceeds from the Medallion disposition being credited to the depletion cost pool at a lower rate per boe than the overall historical corporate average.

Ceiling Test

The Company performed a ceiling test at June 30, 2009 and determined that the carrying amount of the Company's oil and gas assets was not recoverable as the carrying amount exceeded the sum of the undiscounted cash flows expected to result from the production of the Company's proved reserves. However, the fair value of oil and gas assets exceeded their carrying amount and an impairment loss was not recorded. Fair value was determined based on discounted cash flows from proved plus probable reserves using current forward prices as at June 30, 2009. An impairment loss may be recorded in a future period.

Stock-Based Compensation

Stock-based compensation expenses decreased from \$0.2 million in the second quarter of 2008, to \$0.1 million in the second quarter of 2009. Costs have decreased as the initial grant of stock options and special performance units in 2004 have been fully recognized.

Income Taxes

In the second quarter of 2009, the Company had a future income tax recovery of \$1.8 million compared to an expense of \$1.0 million in the same period in 2008. For the six months ending June 30, 2009 future income tax recovery totaled \$3.0 million, compared to a \$0.2 million expense in June of 2008.

Estimated tax pools as at June 30:

(\$000's)	2009		2008	
Canadian development expense	\$	37,473	\$	33,042
Canadian exploration expense		32,101		27,581
Canadian oil & gas property expense		18,649		34,606
Undepreciated capital cost		33,283		46,296
Other		4,499		5,169
	\$	126,005	\$	146,694

Net Earnings

Overall the Company reported a net loss of \$3.9 million for the second quarter of 2009, versus \$2.3 million in net earnings in the same period of 2008. This loss was driven by a drop in oil and gas revenue in the second quarter by \$17.2 million or 70% compared to the same quarter of 2008 and a 32% increase in the depletion & depreciation rate in the quarter.

Capital Expenditures

(\$000's)	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
Drilling and completions	\$ 104	\$ 2,094	\$ 3,690	\$ 12,145
Facilities	(914)	1,908	(27)	6,620
Land and lease	1,568	1,354	1,889	2,913
Seismic	98	2,562	148	2,826
Capitalized G&A	763	697	1,561	1,494
Exploration & development capital expenditures	1,619	8,615	7,261	25,998
Net property acquisitions (dispositions)	(25,383)	(5,448)	(27,461)	6,050
Other capital expenditures	4	99	7	159
Total net capital expenditures	\$ (23,760)	\$ 3,266	\$ (20,193)	\$ 32,207

For the second quarter of 2009, the Company did not participate in any drilling as spring break up restricted access to drilling locations. Of the \$1.6 million invested in exploration and development capital expenditures, \$1.6 million was spent on the acquisition of new undeveloped lands. A \$0.9 million recovery of facility costs reflects the election of partners to participate in facility construction projects.

The Company also disposed of its Medallion property in Southern Alberta, for proceeds of \$28.0 million (prior to closing adjustments) in the quarter. These properties consist of 179 (115 net) producing wells, with net production of approximately 750 boe per day (as of the effective date), along with associated gas gathering and field compression facilities. During the quarter, the Company also closed an acquisition of undeveloped land and approximately 30 boe per day of production in the East Kakwa area at a cost of \$1.5 million (prior to closing adjustments).

Liquidity & Capital Resources

At June 30, 2009, ProspEx had the following financial resources available to fund its capital expenditure program.

(\$000's)	
Working capital deficiency, excluding financial instrument gains/losses and related tax and other current liabilities	\$ (2,082)
Long-term debt	(20,950)
Bank facilities available	40,000
Total capital resources available	\$ 16,968

ProspEx expects that it will be able to fund its 2009 capital program from operating cash flow and the capital resources noted above.

As at June 30, 2009, the Company's ratio of net debt to trailing annualized quarterly operating cash flow was 2.3 to 1.0, which exceeds the Company's guidelines on capital management (which call for a maximum of 2.0 to 1.0) as a result of the effects of lower commodity prices on cash flow. The Company will continue to closely monitor this ratio.

Bank Debt

At June 30, 2009, the Company had a \$40.0 million revolving operating credit facility agreement. The facility revolves for 364-day periods, renewable at the option of the lender. The facility is subject to an annual review on May 31, 2010. The amount of the facility is subject to a borrowing base test performed on a periodic basis by the lenders, based primarily on reserves and using commodity prices estimated by the lenders, as well as other factors. A decrease in the borrowing base could result in a reduction of the credit facility which may require a repayment to the lenders within sixty days of receiving notice of the new borrowing base. The credit facility provides that advances may be made by way of prime rate loans, guaranteed notes (bankers' acceptances) and letters of credit. The credit facility is tested quarterly, in arrears, and bears interest based on a sliding scale. The interest rate varies depending on the Company's debt to cash flow ratio determined quarterly on a grid system, with the grid ranging from debt to cash flow ranges of lower than 1.0:1.0 to greater than 3.0:1.0.

The facility is secured by a general security agreement conveying a first floating charge over all real and personal property and after-acquired assets. The Company is required to meet certain financial based covenants under the terms of this facility. As at June 30, 2009, the Company is in compliance with all covenants in accordance with the terms of the credit facility.

The effective interest rate on the outstanding debt for the second quarter of 2009 is approximately 2.44% annualized.

Share Capital

As at June 30, 2009, ProspEx had 57,385,162 common shares (2008 – 57,199,448), 2,016,269 warrants (2008 – 2,201,983), and 5,060,078 options (2008 – 5,035,553) issued and outstanding. Each warrant and option, upon exercise, entitles the holder to one common share.

As at July 30, 2009, ProspEx had 57,385,162 common shares, 2,016,269 warrants, and 5,060,078 options issued and outstanding.

Contractual Obligations

The Company has committed to certain payments as follows:

Payments due (\$000's)	2009	2010	2011	2012	2013	Thereafter
Long-term debt	\$ -	20,950	-	-	-	\$ -
Building lease	478	934	1,050	1,356	1,433	358
Process fees	189	379	63	-	-	-
Transportation	104	72	-	-	-	-
Other	8	7	-	-	-	-
Total	\$ 779	22,342	1,113	1,356	1,433	\$ 358

Off-Balance Sheet Arrangements

The Company has not entered into any off-Balance Sheet transactions other than previously discussed.

Summary of Quarterly Results

The following table summarizes the quarterly operating statistics of the Company.

	2009		Q4	2008		Q1	2007	
	Q2	Q1		Q3	Q2		Q4	Q3
Financial (\$000's, except per share amounts)								
Oil and gas revenue	7,370	12,765	15,046	19,714	24,567	17,378	15,906	16,004
Net (loss) earnings	(3,899)	(2,225)	487	6,923	2,261	(2,110)	(180)	(1,352)
Per share - basic	(0.07)	(0.04)	0.01	0.12	0.04	(0.04)	0.00	(0.03)
- diluted	(0.07)	(0.04)	0.01	0.12	0.04	(0.04)	0.00	(0.03)
Average Daily Production								
Oil (bbls/d)	47	69	57	65	108	68	125	82
NGL (bbls/d)	645	811	719	722	851	536	515	548
Natural Gas (mcf/d)	<u>14,382</u>	<u>17,561</u>	<u>16,868</u>	<u>18,379</u>	<u>19,957</u>	<u>19,064</u>	<u>19,690</u>	<u>21,743</u>
Total (boe/d)	3,089	3,807	3,587	3,850	4,285	3,781	3,922	4,254
Operating Netbacks (\$/boe)								
Price ⁽¹⁾	26.22	37.25	45.59	55.65	63.00	50.50	44.09	40.89
Royalties	(1.21)	(7.37)	(8.18)	(12.98)	(11.97)	(8.57)	(5.41)	(7.79)
Transportation	(0.93)	(1.04)	(1.00)	(0.91)	(1.00)	(0.96)	(0.86)	(0.89)
Operating Cost	<u>(9.30)</u>	<u>(7.16)</u>	<u>(4.58)</u>	<u>(7.76)</u>	<u>(8.39)</u>	<u>(10.17)</u>	<u>(8.06)</u>	<u>(8.42)</u>
Operating Netback	14.78	21.68	31.83	34.00	41.64	30.80	29.76	23.79

⁽¹⁾ Price excludes unrealized financial instrument gain or loss.

Quarter to quarter results are influenced by many factors. The three main drivers are capital spending, production and commodity prices.

Capital spending is typically more heavily weighted to the winter drilling months, and therefore the fourth and first quarters of the year usually represent approximately 60% of the exploration and development budgets. The second quarter of each year usually has minimal capital spending, reflecting surface access restrictions due to spring break

up conditions. Production additions typically lag capital spending by one or two quarters, resulting in production peaks in the second quarter of each year.

As previously mentioned, production is a key driver of overall quarterly results. Production is not only influenced by additions as a result of capital programs, but also by natural declines as production from existing wells diminishes over time. With respect to the Company's overall quarterly production profile, production tends to peak in the second quarter of each year, reflecting new additions from the winter drilling programs, and the subsequent quarters reflect declining production as natural decline rates come into play.

World-wide commodity price environments have a significant influence on the overall Company's quarterly results. The Company is an overall price-taker in the oil & gas industry and as a result, world prices drive overall Company revenues. Natural gas prices are currently low, driven by high natural gas storage inventories, strong domestic production levels in the United States, and reduced demand for natural gas as a result of the global economic downturn. In the face of this uncertainty, the Company has adopted a conservative approach by restricting exploration and development capital spending and as a consequence total net oil and gas revenues may not follow traditional quarterly cyclical trends in 2009.

NEW ACCOUNTING PRONOUNCEMENTS

Accounting Standards Adopted and Recent Pronouncements

Convergence with International Reporting Standards – On February 13, 2008, the Canadian Accounting Standards Board confirmed that the effective date for the convergence of Canadian Generally Accepted Accounting Standards for publicly accountable entities to International Financial Reporting Standards ("IFRS") will be January 1, 2011. Although IFRS is principle based and uses a conceptual framework similar to Canadian GAAP, there are significant differences and choices in accounting policies, as well as increased disclosure requirements under IFRS. The Company is currently engaged in preparing for this transition and continues to monitor the developments and assess the impact of these prospective changes to the financial statements.

DISCLOSURE CONTROLS AND POLICIES

Disclosure controls and procedures have been designed to ensure that information required to be disclosed by the Company is accumulated and communicated to the Company's management as appropriate to allow timely decisions regarding required disclosure. The Company's CEO and CFO have concluded, based on their evaluation as of June 30, 2009, that the Company's disclosure controls and procedures as of the end of such period are effective to provide reasonable assurance that material information related to the Company, including its consolidated subsidiary, is made known to them by others within those entities. It should be noted that while the Company's CEO and CFO believe that the Company's disclosure controls and procedures provide a reasonable level of assurance that they are effective, they do not expect that the disclosure controls and procedures will prevent all errors and fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

INTERNAL CONTROLS OVER FINANCIAL REPORTING

The CEO and CFO of the Company are able to certify the design of the Company's internal controls over financial reporting as required under Multilateral Instrument 52-109 of the Canadian Securities Administration with no significant weaknesses in design of these internal controls that require commenting on in the MD&A.

For the second quarter of 2009 there were no changes to the Company's internal controls over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

ADVISORIES

Within the MD&A references are made to terms commonly used in the oil and gas industry. "Cash flow" is not defined by GAAP in Canada and is referred to as a non-GAAP measure. For the purposes thereof, "cash flow" is defined as cash flow from operations before the change in operating non-cash working capital. The MD&A contains the term "cash flow" which should not be considered an alternative to, or more meaningful than "cash flow from operations" as determined in accordance with GAAP. The Company considers cash flow to be a key measure as it demonstrates the Company's ability to generate the cash necessary to fund capital projects and to repay debt. Cash flow presented does not have any standardized meaning prescribed by Canadian GAAP and therefore it may not be comparable with the calculation of similar measures for other entities. Cash flow per share is calculated using the same weighted average number of common shares for the period as used in calculating the net earnings per share calculation.

The following table provides a reconciliation between cash flow from operations and cash flow for the periods below:

(\$000s)	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
Cash flow from operating activities	(5,251)	12,699	3,728	23,806
Change in non-cash working capital	<u>7,726</u>	<u>2,227</u>	<u>4,468</u>	<u>302</u>
Cash flow	2,475	14,926	8,196	24,108

The following table provides a reconciliation of net debt for the periods below:

(\$000's)	As at June 30, 2009	As at December 31, 2008
Accounts receivable	(6,666)	(10,770)
Prepaid expenses	(275)	(693)
Accounts payable and accrued liabilities	9,023	22,078
Long term debt	20,950	40,807
Net debt	23,032	51,422

Boe amounts have been calculated using a conversion rate of six mcf of gas to one barrel of oil. The term boe may be misleading if used in isolation. A boe conversion ratio of one barrel of oil to six mcf of gas is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the well head.

"Netbacks" are calculated by subtracting transportation costs, royalties payable, and operating costs from the average price received during the period.

Forward-looking Information

Certain information regarding ProspEx including, without limitation, management's assessment of future plans and operations, constitutes forward-looking information or statements under applicable securities law and necessarily involve assumptions regarding factors and risks that could cause actual results to vary materially, including, without limitation, assumptions and risks associated with oil and gas exploration, development, exploitation, production, marketing and transportation, loss of markets, volatility of commodity prices, currency fluctuations, royalty rates, imprecision of reserve estimates, environmental risks, competition, incorrect assessment of the value of acquisitions

or dispositions, failure to realize the anticipated benefits of acquisitions and ability to access sufficient capital from internal and external sources.

The reader is cautioned that these factors and risks are difficult to predict and that the assumptions used in the preparation of such information, although considered reasonable by ProspEx at the time of preparation, may prove to be incorrect. Accordingly, readers are cautioned that the actual results achieved will vary from the information provided herein and the variations may be material. Readers are also cautioned that the foregoing list of assumptions, factors and risks is not exhaustive. Additional information on the foregoing assumptions, risks and other factors that could affect ProspEx's operations or financial results are included in ProspEx's public disclosure documents on file with Canadian securities regulatory authorities. In particular see the Risk Factors and Industry Conditions sections of ProspEx's most recent Annual Information Form. ProspEx's reports may be accessed through the SEDAR website (www.sedar.com), at ProspEx's website (www.psx.ca) or by contacting the Company directly. Consequently, there is no representation by ProspEx that actual results achieved will be the same in whole or in part as those set out in the forward-looking information.

Furthermore, the forward-looking information and statements contained in this MD&A are made as of the date of this MD&A, and ProspEx does not undertake any obligation to update publicly or to revise any of the included forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law. The forward-looking information and statements contained herein are expressly qualified by this cautionary statement.

ProspEx Resources Ltd.
Consolidated Balance Sheets
(unaudited)

(Stated in thousands of dollars)

June 30, 2009 **December 31, 2008**

Assets

Current assets

Accounts receivable	\$	6,666	10,770
Prepaid expenses		275	693
Unrealized financial instrument gain (note 6)		310	828
		<u>7,251</u>	<u>12,291</u>

Property, plant and equipment, net

		<u>152,539</u>	<u>190,693</u>
	\$	<u>159,790</u>	<u>202,984</u>

Liabilities

Current liabilities

Accounts payable and accrued liabilities	\$	9,023	22,078
Current portion of future income tax liability (note 2)		90	240
Current portion of other liabilities (note 3)		229	-
		<u>9,342</u>	<u>22,318</u>

Long-term debt (note 1)

20,950 40,807

Other liabilities (note 3)

295 -

Asset retirement obligation (note 4)

4,338 6,462

Future income tax liability (note 2)

6,295 9,119

Total liabilities

41,220 78,706

Shareholders' Equity

Common shares (note 5)		90,802	90,802
Common share performance warrants (note 5)		1,233	1,233
Contributed surplus (note 5)		7,174	6,758
Retained earnings		19,361	25,485
Total shareholders' equity		<u>118,570</u>	<u>124,278</u>
	\$	<u>159,790</u>	<u>202,984</u>

See accompanying notes to consolidated financial statements

ProspEx Resources Ltd.
Consolidated Statements of Loss, Comprehensive Loss and Retained Earnings
For the period ended
(unaudited)

(Stated in thousands of dollars, except per share amounts)	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
Revenue				
Oil and gas	\$ 7,370	24,567	20,135	41,945
Unrealized financial instrument gain (loss) (note 6)	310	(2,781)	(517)	(7,300)
Royalties	(341)	(4,668)	(2,867)	(7,618)
	<u>7,339</u>	<u>17,118</u>	<u>16,751</u>	<u>27,027</u>
Expenses				
Depletion, depreciation and accretion	8,247	8,685	16,988	16,060
Operating	2,613	3,274	5,066	6,774
Transportation	262	389	619	721
General and administrative	851	786	1,757	1,655
Interest and bank charges	439	515	755	1,024
Stock-based compensation	105	236	209	431
Loss on subleasing (note 3)	524	-	524	-
	<u>13,041</u>	<u>13,885</u>	<u>25,918</u>	<u>26,665</u>
(Loss) earnings before income taxes	(5,702)	3,233	(9,167)	362
Income taxes (note 2)				
Future reduction	(1,803)	972	(3,043)	211
Net (loss) earnings and comprehensive loss for the period	(3,899)	2,261	(6,124)	151
Retained earnings, beginning of period	23,260	15,815	25,485	17,925
Retained earnings, end of period	<u>\$ 19,361</u>	<u>18,076</u>	<u>19,361</u>	<u>18,076</u>
Net (loss) earnings per share				
Basic	\$ (0.07)	0.04	(0.11)	0.00
Diluted	\$ (0.07)	0.04	(0.11)	0.00

See accompanying notes to consolidated financial statements

ProspEx Resources Ltd.
Consolidated Statements of Cash Flows
For the periods ended,
(unaudited)

(Stated in thousands of dollars)

	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
Operations				
Net (loss) earnings for the period	\$ (3,899)	2,261	(6,124)	151
Items not involving cash				
Depletion, depreciation and accretion	8,247	8,685	16,988	16,060
Stock-based compensation	105	236	209	431
Future income taxes (reduction)	(1,803)	972	(3,043)	211
Sublease loss	524	-	524	-
Unrealized financial instrument (gain) loss	(310)	2,781	517	7,300
Asset retirement expenditures	(389)	(9)	(875)	(45)
	<u>2,475</u>	<u>14,926</u>	<u>8,196</u>	<u>24,108</u>
Changes in non-cash working capital	(7,726)	(2,227)	(4,468)	(302)
	<u>(5,251)</u>	<u>12,699</u>	<u>3,728</u>	<u>23,806</u>
Financing				
(Decrease) increase in long-term debt	(16,521)	(2,910)	(19,858)	7,669
Issuance of common shares	-	912	-	1,418
	<u>(16,521)</u>	<u>(1,998)</u>	<u>(19,858)</u>	<u>9,087</u>
Investments				
Exploration and development expenditures	(1,619)	(8,615)	(7,261)	(25,998)
Proceeds on property disposal	26,886	5,448	28,964	(6,050)
Property acquisition	(1,503)	-	(1,503)	-
Deposit on property acquisition	-	-	-	1,175
Other capital expenditures	(4)	(99)	(7)	(159)
	<u>23,760</u>	<u>(3,266)</u>	<u>20,193</u>	<u>(31,032)</u>
Changes in non-cash working capital	(1,988)	(7,435)	(4,063)	(1,861)
	<u>21,772</u>	<u>(10,701)</u>	<u>16,130</u>	<u>(32,893)</u>
Change in cash	-	-	-	-
Cash, beginning of period	-	-	-	-
Cash, end of period	\$ -	-	-	-

See accompanying notes to consolidated financial statements

Notes to Consolidated Financial Statements

For the three and six months ended June 30, 2009
(unaudited)

The interim unaudited consolidated financial statements of ProspEx Resources Ltd. (the "Company" and/or "ProspEx") have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The Company is engaged in the acquisition, exploration, development and production of oil and natural gas in Canada.

The interim unaudited consolidated financial statements have been prepared by management following the same accounting policies and methods of computation as the audited consolidated financial statements for the period ended December 31, 2008 except as described below. Preparation of financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses and disclosure of contingent assets and liabilities at the date of the financial statements. Actual results may differ from these estimates. In the opinion of management, these interim consolidated financial statements contain all adjustments of a normal and recurring nature to present fairly the Company's financial position as at June 30, 2009 and the results of its operations and cash flows for the three and six months ended June 30, 2009. The disclosures included below are incremental to those included with the annual consolidated financial statements except as disclosed below. The interim consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto in the Company's annual report for the year ended December 31, 2008.

1. LONG TERM DEBT

At June 30, 2009, the Company had a \$40.0 million revolving operating credit facility agreement. The facility revolves for 364-day periods, at which time the Company can request approval from the lender for an extension for an additional 364 day period or convert the outstanding bank indebtedness to a one-year term loan. The facility is subject to an annual review on May 31, 2010. The amount of the facility is subject to a borrowing base test performed on a periodic basis by the lenders, based primarily on reserves and using commodity prices estimated by the lenders, as well as other factors. A decrease in the borrowing base could result in a reduction of the credit facility which may require a repayment to the lenders within sixty days of receiving notice of the new borrowing base. The credit facility provides that advances may be made by way of prime rate loans, guaranteed notes (bankers' acceptances) and letters of credit. The credit facility is tested quarterly, in arrears, and bears interest based on a sliding scale. The interest rate varies depending on the Company's debt to cash flow ratio determined quarterly on a grid system, with the grid ranging from debt to cash flow ranges of lower than 1.0:1.0 to greater than 3.0: 1.0.

The facility is secured by a general security agreement conveying a first floating charge over all real and personal property and after-acquired assets. The Company is required to meet certain financial based covenants under the terms of this facility. As at June 30, 2009, the Company is in compliance with all covenants in accordance with the terms of the credit facility.

The effective interest rate on the outstanding debt for the second quarter of 2009 is approximately 2.44% annualized.

2. FUTURE INCOME TAXES

The provision for future income taxes differs from the amount computed by applying the combined expected Canadian Federal and Provincial tax rates to earnings before income taxes. The reasons for these differences are as follows:

(\$000's)	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
(Loss) Earnings before taxes	\$ (5,702)	\$ 3,233	\$ (9,167)	\$ 362
Rate (%)	29.00%	29.50%	29.00%	29.50%
Computed expected reduction for future income taxes	(1,654)	954	(2,659)	107
Increase (decrease) in taxes resulting from:				
Stock-based compensation expensed	30	70	60	127
Effect of change in tax rate	(211)	(195)	(490)	(168)
Other	32	143	46	145
Income tax reduction	\$ (1,803)	\$ 972	\$ (3,043)	\$ 211

The current future income tax liability at June 30, 2009 of \$0.1 million (December 31, 2008 - \$0.2 million) results from the future tax impact of the unrealized financial instrument gain.

The components of the long term future income tax liability are as follows:

(\$000's)	June 30, 2009	December 31, 2008
Property, plant and equipment	\$ (7,248)	\$ (10,697)
Asset retirement obligation	1,084	1,773
Loss on sublease	152	-
Share issue costs	217	305
	(5,795)	(8,619)
Valuation allowance	(500)	(500)
Future income tax liability	\$ (6,295)	\$ (9,119)

At June 30, 2009, the Company had estimated tax pools available to reduce future taxable income of \$126.0 million (December 31, 2008 - \$154.6 million).

Capitalized stock based compensation resulted in an increase to future tax liabilities of \$0.1 million during the quarter (2008 - \$0.1 million).

3. OTHER LIABILITIES

(\$000's)	June 30, 2009	December 31, 2008
Loss on sublease	\$ 524	\$ -
Less current portion	229	-
Long term portion of loss on sublease	\$ 295	\$ -

The loss on sublease relates to the subleasing of a portion of the Company's head office space. This provision represents the present value at a 7.0% discount rate of the difference between the original head lease rate and the estimated amounts recoverable under the sublease terms.

4. ASSET RETIREMENT OBLIGATION

The Company has estimated the net present value of its total asset retirement obligation at June 30, 2009 to be \$4.3 million (2008 - \$6.0 million) based on a total future liability of \$10.6 million (2008 - \$21.2 million). The total future liability was estimated based on the Company's net ownership interest in all wells and facilities, estimated costs to

reclaim and abandon the wells and facilities and the estimated timing of when the costs will be incurred. These payments are expected to be made over the next 45 years with the majority of costs incurred between 2029 and 2038. A 7% interest rate and 2% inflation rate were used to calculate the present value of the asset retirement obligation.

(\$000's)	
Balance, at January 1, 2009	\$ 6,462
Liabilities incurred	41
Liabilities settled	(875)
Change in timing of estimated cash flows	1,041
Assets sold	(2,570)
Accretion expense	239
Balance, at June 30, 2009	\$ 4,338

5. SHAREHOLDERS' EQUITY

(a) Common Shares & Common Share Performance Warrants Issued

	June 30, 2009		June 30, 2008	
	Number of Shares/Warrants (000's)	Amount (\$000's)	Number of Shares/Warrants (000's)	Amount (\$000's)
Common shares				
Balance at the beginning of the period	57,385	\$ 90,802	56,453	\$ 90,543
Flow-through shares tax adjustment	-	-	-	(2,218)
Issued on exercise of stock options	-	-	232	746
Exercise of stock options	-	-	-	357
Shares issued on exercise of warrants	-	-	514	1,034
Issue costs, net of future tax reduction	-	-	-	(34)
Balance at the end of the period	57,385	\$ 90,802	57,199	\$ 90,428
Common share performance warrants				
Balance at the beginning of the period	2,016	\$ 1,233	2,716	\$ 1,661
Exercised	-	-	(514)	(314)
Balance at the end of the period	2,016	\$ 1,233	2,202	\$ 1,347
Share Capital at the end of the period		\$ 92,035		\$ 91,775

All outstanding performance warrants entitle the holder to acquire a common share at a price of \$1.40 and expire on October 1, 2009.

(b) Contributed Surplus

(\$000's)	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
Balance at the beginning of the period	\$ 6,965	\$ 6,004	\$ 6,758	\$ 5,614
Stock-based compensation	209	472	416	862
Exercise of stock options	-	(357)	-	(357)
Balance at the end of the period	\$ 7,174	\$ 6,119	\$ 7,174	\$ 6,119

(c) Stock Options

Changes in outstanding stock options are summarized below:

	June 30, 2009		June 30, 2008	
	Options (000's)	Weighted Average Exercise Price	Options (000's)	Weighted Average Exercise Price
Outstanding at beginning of period	5,160	\$ 3.44	4,656	\$ 3.62
Granted	617	0.70	612	3.32
Exercised	-	-	(232)	3.22
Forfeited	(717)	3.52	-	-
Outstanding at end of period	5,060	3.10	5,036	\$ 3.60

The following table summarizes stock options outstanding and exercisable at June 30, 2009:

Range of exercise price	Options outstanding			Options exercisable	
	Number of outstanding at period end (000's)	Weighted average remaining contractual life (years)	Weighted average exercise price	Number exercisable at period end (000's)	Weighted average exercise price
\$ 0.70 - \$ 1.95	881	4.8	\$ 0.86	-	-
\$ 1.96 - \$ 3.22	1,518	0.7	\$ 3.19	1,351	\$ 2.44
\$ 3.23 - \$ 4.46	2,661	2.5	\$ 3.79	1,814	\$ 3.82
	5,060	2.4	\$ 3.10	3,165	\$ 3.56

617,000 options were granted during the second quarter of 2009. The fair value of options granted during the second quarter of 2009 was \$0.3 million. The fair value is determined using the Black-Scholes option pricing model, with weighted average assumptions for grants as follows:

	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
Risk free interest rate	1.8%	n/a	1.8%	3.2%
Expected life	5 years	n/a	5 years	5 years
Expected volatility	100%	n/a	100%	47%
Expected dividend yield	Nil	n/a	Nil	Nil
Forfeiture rate	10%	n/a	10%	10%

The estimated fair values of the options are being amortized against earnings and capitalized to property, plant and equipment over the vesting period. During the three months ended June 30, 2009, a total of \$0.1 million (2008 - \$0.2 million) of stock-based compensation was recorded against income and \$0.1 million (2008 - \$0.2 million) was capitalized. During the six months ended June 30, 2009, a total of \$0.2 million (2008 - \$0.4 million) of stock-based compensation was recorded against income and \$0.2 million (2008 - \$0.4 million) was capitalized.

(d) Per Share Amounts

	Three months ended June 30, 2009	Three months ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
Weighted average common shares basic	57,385,162	57,081,774	57,385,162	56,813,545
Dilutive securities:				
Stock options	-	247,737	-	200,826
Performance warrants	-	1,379,670	-	1,385,890
Diluted	57,385,162	58,709,181	57,385,162	58,400,261

For the three months ended June 30, 2009, all options outstanding (2008 – 3,133,000) were excluded from the diluted calculations as they were anti-dilutive. For the six month year to date all 5,060,078 options were excluded due to their anti-dilutive impact (2008 – 3,208,750).

6. FINANCIAL INSTRUMENTS, RISK MANAGEMENT AND CAPITAL MANAGEMENT STRATEGY

Overview

The Company has exposure to a number of risks from its use of financial instruments including:

- Credit risk
- Liquidity risk
- Market risk

This note presents information about the Company's exposure to each of the above risks and the Company's objectives, policies and processes for measuring and managing risk, and the Company's management of capital. Further quantitative disclosures are included throughout these financial statements.

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Board has implemented and monitors compliance with risk management policies.

The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to market conditions and the Company's activities.

Credit Risk

Credit risk relates to the Company's receivables from joint venture partners and petroleum and natural gas marketers and the risk of financial loss if a customer, partner or counterparty to a financial instrument fails to meet its contractual obligations. A substantial portion of the Company's accounts receivable are with customers in the energy industry and are subject to normal industry credit risk. The Company generally grants unsecured credit but routinely assesses the financial strength of its partners and marketers.

Receivables from petroleum and natural gas marketers are normally collected on the 25th day of the month following production. The Company sells the majority of its production to two petroleum and natural gas marketers therefore is subject to concentration risk. To date the Company has not experienced any collection issues with its petroleum and natural gas marketers. Joint venture receivables are typically collected within one to three months of the joint venture bill being issued to the partner. The Company attempts to mitigate the risk from joint venture receivables by obtaining joint venturer approval of significant capital expenditures prior to expenditure. The Company does not typically obtain collateral from petroleum and natural gas marketers or joint venturers; however in certain circumstances, it may elect to cash call a joint venturer in advance of the work.

As at June 30, 2009 the Company's receivables consisted of \$3.0 million (December 31, 2008 - \$4.3 million) from joint venturers, \$1.9 million (December 31, 2008 - \$4.2 million) of receivables from petroleum and natural gas marketers and \$1.8 million (December 31, 2008 - \$2.3 million) of other receivables. Of the \$6.7 million in total accounts receivable, \$0.4 million is aged over 90 days.

The carrying amount of accounts receivable and cash and cash equivalents represents the maximum credit exposure. The Company does not have an allowance for doubtful accounts as at June 30, 2009 and did not provide for any doubtful accounts nor was it required to write-off any receivables during the quarter ended June 30, 2009.

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they are due. The Company's approach to managing liquidity is to ensure, as far as possible, that it will have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions without incurring unacceptable losses or risking harm to the Company's reputation.

The Company prepares annual capital expenditure budgets, which are regularly monitored and updated as considered necessary. Further, the Company utilizes authorizations for expenditures on both operated and non-operated projects to further manage capital expenditures. To facilitate the capital expenditure program, the Company has a revolving reserve based credit facility, as outlined in note 1. The Company also attempts to match its payment cycle with collection of petroleum and natural gas revenues on the 25th day of each month.

The following are the contractual maturities of financial liabilities and associated interest payments due as at June 30, 2009:

Financial Liability (\$000's)	< 1 year	1 - 2 years	2 - 5 years	Thereafter
Accounts payable and accrued liabilities	\$ 9,023	-	-	-
Long-term debt	-	20,950	-	-
Total	\$ 9,023	20,950	-	-

Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, commodity prices, and interest rates will affect the Company's net earnings or the value of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable limits, while maximizing returns.

The Company utilizes both financial derivatives and physical delivery sales contracts to manage market risks. All such transactions are conducted in accordance with the risk management policy that has been approved by the Board of Directors.

Foreign Currency Exchange Risk

Foreign currency exchange rate risk is the risk that the fair value of financial instruments or future cash flows will fluctuate as a result of changes in foreign exchange rates. Although substantially all of the Company's petroleum and natural gas sales are denominated in Canadian dollars, the underlying market prices in Canada for petroleum and natural gas are impacted by changes in the exchange rate between the Canadian and United States dollars. Given that changes in exchange rate have an indirect influence, the impact of changing exchange rates cannot be accurately quantified. The Company had no forward exchange rate contracts in place as at or during the three and six months ended June 30, 2009.

Commodity Price Risk

Commodity price risk is the risk that the fair value of financial instruments or future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for petroleum and natural gas are impacted by world economic

events that dictate the levels of supply and demand. The Company attempts to mitigate commodity price risk through the use of financial derivative sales contracts. The following contracts were in place as of June 30, 2009:

<u>Type</u>	<u>Amount (GJ/day)</u>	<u>Term</u>	<u>Price (\$/GJ at AECO)</u>	<u>Type</u>
Firm fixed quantity	2,500	Jul. 1 – Jul. 31, 2009	\$ 3.58	Physical
Firm fixed quantity	2,500	Aug. 1 – Oct. 31, 2009	\$ 4.21	Physical
Costless collar	1,500	Aug. 1 – Oct. 31, 2009	\$ 4.00 - \$ 5.23	Financial

The contracts in place during the three months ended June 30, 2009 resulted in an unrealized gain of \$0.3 million (June 30, 2008 - \$2.8 million loss) and no realized gain or loss (June 30, 2008 - \$1.4 million loss). During the six months ended June 30, 2009 the contracts in place resulted an unrealized loss of \$0.5 million (2008 - \$7.3 million loss) and a realized gain of \$1.3 million (2008 - \$1.3 million loss)

Interest Rate Risk

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The Company is exposed to interest rate fluctuations on its credit facility which bears a floating rate of interest. The Company had no interest rate swaps or financial contracts in place as at or during the three and six months ended June 30, 2009. For the three and six months ended June 30, 2009, a difference in the interest rate of 1% would change net earnings after tax by an estimated \$0.1 million (2008 - \$0.1 million), assuming all other variables are constant.

Capital Management Strategy

The Company's policy on capital management is to maintain a prudent capital structure to allow the Company to fund future development. The Company considers its capital structure to include shareholders' equity, bank debt, and working capital.

(\$000's)	June 30, 2009	December 31, 2008
Shareholders' equity	\$ 118,570	\$ 124,278
Long-term debt	20,950	40,807
Working capital deficiency excluding unrealized financial instrument gain or losses and associated future tax assets or liabilities	2,311	10,615

The Company manages its capital programs in order to maintain a prudent capital structure as changes in economic conditions occur. The Company may and has from time to time issued shares and adjusted spending to manage current or projected operating cash flows and debt levels.

The Company monitors its capital base using the ratio of net debt to annualized operating cash flow. This ratio is calculated as net debt, as defined as long term debt less working capital (or plus working capital deficiency) excluding unrealized financial instrument gain (loss) and associated future tax assets (liabilities) and other liabilities; divided by annualized cash flow from operations before changes in non-cash working capital (based on the most recent operating quarter). The Company's guideline is to maintain a ratio of approximately 1.0 to 1.0, not exceeding 2.0 to 1.0. This ratio will fluctuate depending on fluctuations of the commodity and business cycles. The Company prepares annual capital expenditure budgets which are updated periodically to monitor this ratio. The annual budget is approved by the Board of Directors with updates reviewed by the Board throughout the year.

As at June 30, 2009 the Company's ratio of net debt to annualized operating cash flow was 2.3 to 1.0, and compares to the ratio of 1.2 to 1.0 for the year ended December 31, 2008.

The Company's share capital is not subject to any external restrictions. The bank debt facility has no restrictions other than the limitation of borrowing under the facility on an annual basis and an adjusted working capital covenant ratio of 1.0 to 1.0. As at June 30, 2009, the Company is in compliance with all flow-through share expenditure requirements as well as all bank facility requirements.

There have been no changes to the Company's capital management strategy during the quarter ended June 30, 2009.

7. ADDITIONAL DISCLOSURES

Interest and Taxes Paid

Net cash interest paid during the quarter was \$0.1 million (2008 - \$0.7 million). Cash taxes paid during the period was \$nil (2008 - \$nil). On a year to date basis, net cash interest paid to June 30, 2009 was \$0.5 million (2008 - \$1.1 million). Year to date cash taxes paid to June 30, 2009 was \$nil (2008 - \$nil).

8. COMMITMENTS

The Company has committed to certain future payments as follows:

Payments due (\$000's)	2009	2010	2011	2012	2013	Thereafter
Long-term debt	\$ -	20,950	-	-	-	\$ -
Building lease	478	934	1,050	1,356	1,433	358
Process fees	189	379	63	-	-	-
Transportation	104	72	-	-	-	-
Other	8	7	-	-	-	-
Total	\$ 779	22,342	1,113	1,356	1,433	\$ 358

Contact Information

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