

Arbour Energy Inc.
Management Discussion and Analysis
December 31, 2004

REVISED

NOTICE OF CHANGES MADE TO ORIGINAL FILING

1. Forward Looking Information has been expanded.
2. The MD&A is now dated.
3. Results of Operation have been expanded.
4. The Selected Annual Information now includes the dollar value of the Net Loss.
5. The MD&A now includes Quarterly Results as well as discussion.
6. The Capital Resources section has been separated from Liquidity and further explains the sources of funding.
7. Related Party Transactions have been added.
8. A discussion of the Fourth Quarter has been added.
9. Changes in Accounting Policies have been added.
10. Financial Instruments have been added.

Overview

The following Management Discussion and Analysis (“MD&A”) of the financial results of Arbour Energy Inc. should be read in conjunction with the accompanying audited financial statements and related notes for the year ended December 31, 2004.

For the purpose of reporting production information, reserves and calculating unit prices and costs, natural gas volumes have been converted to a barrel of oil equivalent (“boe”) using six thousand cubic feet (“mcf”) to one barrel of oil. A boe conversion ratio of 6:1 is based upon an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. This conversion conforms with NI 51-101. Boes may be misleading, particularly if used in isolation.

Additional information related to the Company is available for view on SEDAR at www.sedar.com, or by requesting further information from the Company’s head office in Calgary.

Description of Business

Arbour Energy Inc. was incorporated under the Business Corporations Act (Alberta) on April 9, 2001 to carry on exploration and development of crude oil and natural gas reserves.

Operations and Capital Expenditures

As a qualifying transaction, Arbour participated in an exploratory well in the Lochend area of Alberta. This well is currently shut in and will be re-evaluated to determine if further work can be done to establish production.

In 2003, Arbour acquired a 22.5% working interest in an oil and gas well in the Pembina area which currently produces approximately \$ 3,000 per month of revenue to the Company.

During 2003, Arbour experienced significant losses and filed for protection under the Bankruptcy act. As part of the proceedings, the Company filed a proposal to its creditors in which creditors would receive the first \$1,500 of their debt and approximately half of the balance of their debts on a pro rata basis. The Company’s proposal was accepted resulting in a gain on settlement of debt for the Company of \$457,260. Settlement of the debt was funded through \$215,000 held in trust as at December 31, 2003 with the remainder repaid from a private placement of 6,000,000 common shares at \$.05 per share for gross proceeds of \$300,000. During June 2004, the Company was removed from bankruptcy protection and resumed normal operations.

On May 31, 2004, the Company entered into a preliminary agreement with Crazy Hill Resources Ltd. to acquire a producing oil and gas property near Drayton Valley, Alberta comprised of six wells producing oil of 44 BOPD and gas of 60 MCFD. The agreed purchase price was \$1,000,000 consisting of \$350,000 cash and 650,000 common shares at \$1.00 per share. Closing took place on November 1, 2004.

In May, the Company also purchased a 45% working interest in a Farmout Agreement in the Meekwap area in Alberta for one oil well. The purchase price consisted of \$67,500 in cash and 157,500 common shares. After further testing, Arbour has elected not to tie in the well.

The Company has participated in drilling a shallow gas development well in the Kirkpatrick Lake area of Alberta. The capital cost was \$55,000 for a 50% interest and is capable of producing 60 MCFD. Tie in is occurring in May of 2005. Arbour also purchased a 50% interest in 3 additional wells in the same area for \$175,000 cash and 150,000 shares in the company. The net production of one producing well is 60 MCFD.

In August, the Company entered into a \$10,000,000 loan agreement with Merendon Mining Corporation Ltd., a private company incorporated in Alberta. Arbour has an option to purchase 5% of the issued and outstanding shares of Tarsands Recovery Ltd., an entity engaged in development of technology to enhance oil recovery from the Western Canadian Tar Sands, in exchange for the principal balance of the loan plus accrued interest, if any, as well as the issuance of 5,000,000 common shares of the Company.

In November, Arbour purchased a 50% interest in 2 sections of developable land in the Bow Island area in Alberta. Drilling is anticipated to begin sometime in the last quarter of 2005.

Subsequent to year end the Company entered into a Participation Agreement for a 45% working interest in the Sedalia area of Alberta. Drilling is to commence in May of 2005.

Also subsequent to the year end, Arbour announced that it has acquired all of the issued shares of Canadian Oilsands Recovery Enterprises Ltd. ("COREL") for \$5,300,000 plus 5,000,000 common shares. COREL holds the master operating license relating to oilsands recovery technology and intends to build a commercial plant in the summer of 2005. As at the year end, the Company had made a \$300,000 deposit towards the acquisition.

The Company has also established a US subsidiary, Arbour Energy US, Inc. subsequent to the year end. It has merged with Biltmore Enterprises Inc., a Nevada Corporation. Biltmore Enterprises Inc. changed its name to Arbour Energy U.S., Inc. The company is listed over the counter in the United States.

During the year, the company has raised \$13,480,715 through the issuance of 9,985,715 preferred shares and continues to raise equity financing subsequent to year end.

Selected Annual Information

The following information is derived from the financial statements of the Company for each of the three years ended December 31, 2004, 2003 and 2002.

	2004	2003	2002
Total Revenues and Interest Income	\$ 243,453	72,467	15,143
Net loss before extraordinary items	\$ (601,236)	(1,432,891)	(64,992)
Net loss before extraordinary items per share, basic (1)	\$ (0.074)	(0.294)	(0.021)
Net loss	\$ (601,236)	(1,432,891)	(64,992)
Net loss per share, basic (1)	\$ (0.074)	(0.294)	(0.021)
Total Assets	\$ 16,669,465	363,107	2,185,045
Long Term Liabilities	\$ 13,075,522	58,560	228,080
Cash dividends declared	-	-	-
Number of shares outstanding	13,983,237	4,862,502	1,333,333

(1) Diluted loss per common share has not been disclosed as the effect of common shares issuable upon the exercise of stock options would be anti-dilutive

Results of Operations

2004 was a significant year for Arbour as it turned the corner from protection under the Bankruptcy Act to becoming a going concern in the oil and gas industry. With the acquisition of five producing properties in the last two months of the year, production increased from 1,575 boe in 2003 to 3,638 boe in 2004, a 131% increase. Production revenues increased from \$66,427 in 2003 to 165,590 in 2004, a 149% increase.

Interest income also increased from \$6,040 in 2003 to \$77,863 as a result of a \$10,000,000 loan in 2004.

Production expenses increased from \$23,957 in 2003 to \$94,796 in 2004, a 196% increase also as a result of increased output with the acquisition of new property.

General and administrative expenses increased significantly from \$190,525 in 2003 to \$468,392 in 2004. The Company's focus during the last half of 2004 was

on new acquisitions as well as raising capital and afforded increased operating expenses.

Aside from the write-down of a non-producing property of \$1,866,183 and a ceiling test write-down of a producing property of \$14,196 in 2003, depletion was \$95,403 compared with \$127,196 in 2004 representing a 33% increase.

With newly issued preferred shares with a 5.75% cumulative annual dividend, the Company has accrued \$98,389 of interest in 2004. The preferred shares are convertible to common shares at the option of the holder and were initially recorded at fair value of \$12,577,197. The difference between the principal amount of \$13,480,715 and the fair value is \$903,518. The shares are being accreted such that the liability at maturity will equal the gross proceeds of \$13,480,715. \$18,364 of accretion has been included in interest on the preferred shares bringing the total for the year to \$116,753. There were no interest expenses in 2003.

As the Company elected to early adopt the new recommendation of the CICA for stock-based compensation, both 2003 and 2004 were calculated by the Black-Scholes option pricing model. This is a non-cash transaction which is credited to contributed surplus, and no effect on cash flows of the Company. Stock-based compensation was \$25,107 in 2004 as compared to \$16,281 in 2003.

Adoption of the new recommendations for Asset Retirement Obligations resulted in a change in accounting policy for the previous year provision for future removal and site restoration costs of \$61,481. The new accretion of asset retirement obligations for 2004 was \$2,000.

The overall loss for the year was \$301,236 as compared to \$1,432,891 in 2003.

During 2004, the Company also experienced a foreign exchange loss of \$10,261 with none for the comparative period. A gain on settlement of debt pursuant to the proposal to the Company's creditors under the Bankruptcy Act during 2003 was \$475,260 with no gain for 2004.

On February 16, 2004, Rick Dawson resigned as a director. On June 11, 2004, Cliff Monar, Michael Gardner and Gary Strashok resigned as directors and Dennis Morice and Heinz Weis were appointed directors. On the same day, Dennis Morice was appointed President and Secretary. On September 9, 2004, Dean Strashok resigned as director. Also, on September 9, 2004, Michael Gardner resigned as Chief Financial Officer and Vice-President, Finance, Gary Holden resigned as Chairman of the Board of Directors and Dean Strashok resigned as Corporate Secretary. On the same day, Dennis Morice was appointed Chief Executive Officer and Chief Financial Officer of the Company. Arthur Wigmore was also appointed a director on September 9, 2004.

On July 6, 2004, the Company delisted its common shares from the TSX Venture Exchange and was listed on the CNQ Exchange.

Quarterly Results

	2004				2003			
	Dec	Sept	June	March	Dec	Sept	June	March
Total Revenue	196,251	17,615	15,871	13,716	17,856	16,735	16,553	21,323
Loss before extraordinary items	(457,683)	(78,062)	(34,472)	(31,019)	(1,380,921)	(17,231)	(20,507)	(14,232)
Per share	(0.06)	(0.006)	(0.003)	(0.01)	(0.28)	(0.004)	(0.004)	(0.03)
Net Loss	(457,683)	(78,062)	(34,472)	(31,019)	(1,380,921)	(17,231)	(20,507)	(14,232)
Per share	(0.06)	(0.006)	(0.003)	(0.01)	(0.28)	(0.004)	(0.004)	(0.03)

Revenue has remained fairly constant over the quarters beginning in 2003 up until the fourth quarter 2004 with production ranging between 3 to 4 boe per day. With the acquisition in the 4th quarter 2004 of the additional 5 producing wells, production increased bordering 28 boe per day. Price per boe ranged from \$37.50 in 2003 to \$49 in the last quarter of 2004.

As well, the loss per quarter over the quarters of 2003 to third quarter 2004 remained at a level from \$14,000 to \$34,000. The significant loss in fourth quarter 2003 is a result of the write-down of a non-producing property of \$1,866,183 and a ceiling test write-down of a producing property of \$14,296. The losses in that quarter were slightly offset by a gain on settlement of debt of \$475,261 as a result of the acceptance of the Company's proposal to creditors after filing for protection under the Bankruptcy Act.

Third and fourth quarter 2004 losses are a result of the Company becoming increasingly active in production operations as well as raising significant capital. During the last half of 2004 the Company raised \$15,630,789 between common and preferred shares. As a result, at year end the Company has a healthy working capital.

Liquidity

In 2004, Arbour raised \$2,150,074 net of expenses from public placements. In exchange, the Company issued 2,150,735 common shares. Of the \$2,150,074 raised, \$107,317 was received subsequent to year end. The company also

converted a short-term note from a shareholder in the amount of \$300,000 in exchange for 6,000,000 common shares.

The Company also raised \$13,480,715 from the placement of 9,985,715 redeemable preferred shares. Of the total raised, \$1,834,609 was received subsequent to year end. In addition, \$39,285 was received as a share subscription deposit. The preferred shares are convertible to common shares but have been recorded at the fair value without the conversion feature. The difference between the principal amount of \$13,480,715 and the fair value of \$12,577,197 is \$903,518 and has been recorded in contributed surplus as the fair value of the conversion feature of the preferred shares.

The Company had a healthy working capital at year end of \$4,619,514 as compared to a working capital deficit last year of \$166,907. The positive working capital is a result of the placements of common and preferred shares as well as \$215,000 from funds held in trust as at December 31, 2003. The Company has also continued to raise money subsequent to year end. Management is of the opinion that there is sufficient cash for both the short term and the long term to meet current capacity. As funds are available through share placements, the Company anticipates further acquisitions of oil and gas properties.

Capital Resources

There are no capital commitments as at December 31, 2004. However, management has entered into an agreement to purchase all of the issued shares of Canadian Oilsands Recovery Enterprises Ltd. for \$5,300,000 effective January 1, 2005. An initial deposit of \$300,000 was made prior to year end towards the acquisition. Payments of \$1,740,000 have been made to the date of this report to the previous shareholders and will continue to be made monthly at the rate of \$120,000 until August 1, 2007 with the final payment of \$20,000 on September 1, 2007. Management anticipates raising additional equity financing to maintain this acquisition.

The Company anticipates spending \$123,200 on a development drilling program in the second quarter of 2005. This is in addition to \$55,000 advanced during 2004 for that program. Existing proceeds from the placement of shares will fund the program.

Off-Balance Sheet Arrangements

As of December 31, 2004, the Company has no off-balance sheet arrangements.

Related Party Transactions

During 2004 the Company incurred the following related party transactions in the normal course of business:

- 1) Directors' fees paid to the three directors for 2004 of \$17,000. One of the January 2005 directors fees in the amount of \$3,000 was also paid as part of the 2004 payments and is classified as prepaids on the year end financials.
- 2) Management fees and salary paid to the CEO of the Company in the amount of \$45,000.
- 3) \$6,652 was paid to the CEO relating to a vehicle allowance.
- 4) \$16,000 was paid to the CEO of the Company to purchase a vehicle and equipment which is included in petroleum and natural gas properties at year end.

2004 Fourth Quarter

During the 4th quarter of 2004, the Company acquired five producing wells in Drayton Valley which accounted for the significant increase in revenue over the previous seven quarters. Production increased from \$5,000 per month over the last seven quarters to approximately \$55,000 per month starting November 1, 2004. The production represents an increase from slightly over 4 boe per day to 28 boe per day.

The one producing well over the last seven quarters was not subject to royalties. With the acquisition of the five producing wells, the Company is now paying royalties on the gas and NGL production. Royalties in the last quarter were \$8,615.

Production expenses were \$71,305 in the 4th quarter compared to \$6,145 in the 3rd quarter. This dramatic increase reflects costs associated with higher production volumes and increased well servicing costs associated with new wells.

Depletion and depreciation in the 4th quarter totaled \$122,598 versus \$1,594 in the 3rd quarter due to significantly increased production in the 4th quarter.

General and administrative expenses were \$258,724 in the last quarter compared to \$135,783 in the 3rd quarter due to increased overhead costs relating to new operations and significant activity in raising funds.

Stock-based compensation of \$25,107 recorded in the 4th quarter reflected stock options issued in November 2004.

Interest expense was accrued in the 4th quarter in the amount of \$116,753 further to the issuance of redeemable preferred shares in the 4th quarter.

The foreign exchange loss of \$10,261 was related to the conversion of US funds converted at an loss.

A future tax recovery of \$47,845 was recorded in the 3rd quarter and reversed in the 4th quarter.

As a result, the 4th quarter showed a loss of \$457,683 as compared to \$78,062 in the 3rd quarter with a loss per share of \$0.06 as compared to \$0.006 in the 3rd quarter. The Company issued 1,249,266 common shares in the last quarter.

Changes in Accounting Policies

Asset Retirement Obligations

The Company adopted the Canadian Institute of Chartered Accountants' new recommendations for Asset Retirement Obligations effective January 1, 2004.

Previously the Company accrued a provision for future removal and site restoration costs, net of recoveries, which was charged to income on a rational and systematic basis. Under the new recommendations, an asset retirement obligation is recognized at fair value as a liability when incurred, and a concurrent asset retirement cost is capitalized to the related asset and amortized to income over its estimated useful life. Discounted future cash flows are used to measure fair value. Changes to the liability due to the passage of time is recognized in operating expenses as accretion. Changes to the liability arise from revisions to the timing or amount of expected future cash flows and are recognized as an increase or decrease to the carrying amounts of the asset retirement obligation and the related asset retirement capitalized cost.

The change was applied retroactively and the prior year financial statements have been restated. The cumulative effect in the prior year, as of January 1, 2004, of adopting this new recommendation is to decrease the site restoration provision by \$61,481, increase the asset retirement obligations by \$58,560, increase net income by \$2,921 and decrease the deficit in the prior period by \$2,921.

Financial Instruments

Credit concentration

During the year, the Company entered into a loan agreement with Merendon Mining Corporation Ltd., a private company incorporated in Alberta, for \$10,000,000. The loan interest is initially at 3.5% and escalates at a rate of 0.5% per year. The Company has an option to purchase 5% of the issued and outstanding shares of Tarsands Recovery Ltd., a private company incorporated in Alberta engaged in development of technology to enhance oil recovery from the Western Canadian Tar Sands, in exchange for the principal balance of the loan. The Company has a charge on those shares as security for the loan. If Merendon was unable to meet its obligations, or if the security was insufficient to

recover the recorded value of the loan, the impact on the Company could be material and could impact its ability to continue as a going concern. As at the year end, management does not believe that there are any concerns with respect to the collectability of the loan.

Virtually all of the Company's accounts receivable are with customers in the oil and gas industry and are subject to normal industry credit risks.

Interest rate risk

This is the risk that the value of a financial instrument might be adversely affected by a change in the interest rates. The loan receivable and redeemable preferred shares are at fixed interest rates thereby minimizing cash flow and interest rate exposure. In seeking to minimize the risks from interest rate fluctuation, the Company manages exposure through its normal operating and financing activities.

Fair value of financial instruments

The carrying amount of cash and cash equivalents, share subscriptions receivable, notes receivable, accounts receivable, accrued interest payable, accounts payable and accruals approximates their fair value due to the short-term maturities of these items.

As at year end, the carrying values of the loan receivable and redeemable preferred shares approximate their fair value.

Business Risks

Competitive Conditions

Arbour is a member of the petroleum industry, which is highly competitive on all levels. The Company competes with other companies for all of its business inputs, including exploration and development prospects, access to commodity markets, experienced technical personnel and available capital.

The Company strives to be competitive by maintaining a strong financial condition and by utilizing current technologies to enhance exploration, development and operational activities. The Company recognizes that it is a small player in the industry and, as such, seeks profitable joint venture relationships in order to access the technical and industry expertise of other companies.

Arbour competes with others in this area, bidding for mineral rights at Crown land sales and acquiring producing properties and working interests in projects already partly owned. To mitigate the effects of competition, Arbour generally

tries to obtain operatorship and to own as large a working interest as possible in its producing properties to control the access to, and timing of, its field operations, particularly drilling.

Environmental Considerations

The Company is pro-active in its approach to environment concerns. Procedures are in place to ensure that the utmost care is taken in the day to day management of its oil and gas properties. All government regulations and procedures are followed. The Company believes in well abandonment and site restoration in a timely manner to ensure minimal damage to the environment and lower overall costs to the Company.

The Company's estimated asset retirement obligations are provided using the Canadian Institute of Chartered Accountants' new recommendations. Under the new recommendations, an asset retirement obligation is recognized at fair value when incurred, and a concurrent asset retirement cost is capitalized to the related asset and amortized to income over its estimated useful life. At December 31, 2004, the Company had \$260,643 of asset retirement obligations.

Risk Factors

Dividends

The Company has paid no dividends on its shares since incorporation.

Commodity Prices

The Company's revenues, future rate of growth, results of operations, financial condition and ability to borrow funds or obtain additional capital, as well as the carrying value of its properties, are substantially dependent upon prevailing prices of oil and natural gas. Historically, the markets for oil and natural gas have been volatile, and such markets are likely to continue to be volatile in the future. Prices for oil and natural gas are subject to wide fluctuation in response to relatively minor changes in the supply of and demand for oil and natural gas, market uncertainty and a variety of additional factors that are beyond the control of the Company. These factors include the level of consumer product demand, weather conditions, domestic and foreign governmental regulations, the price and availability of alternative fuels, political conditions in the Middle East, the foreign supply of oil and natural gas, the price of foreign imports and overall economic conditions. It is impossible to predict future oil and natural gas price movements with certainty. Declines in oil and natural gas prices may materially adversely affect the Company's financial condition, liquidity, ability to finance planned capital expenditures and results of operations.

Resource Exploration and Development

Drilling with respect to the oil and gas properties in which the Company has an interest are at an exploratory stage and involve the drilling of test wells which may not be successful or economic. Resource exploration and development is a speculative business and involves a high degree of risk, which even a combination of experience, knowledge and careful evaluation may not be able to avoid. There is no assurance that even if commercial quantities of oil and gas are discovered, that an oil and gas property will be brought into commercial production.

The discovery of oil and gas reserves is dependent upon a number of factors not the least of which is the technical skill of the exploration personnel involved. The commercial viability of oil and gas reserves, once discovered, is also dependent upon a number of factors which may be beyond the control of the Company, including marketability and price, proximity to infrastructure, government regulations and environmental protection requirements.

While not the operator of exploration programs on its resource properties, the Company does participate in operations that are subject to the risks normally incidental to the operation and development of resource properties, including the drilling of such properties. In respect of oil and natural gas well, unexpected formations or pressures, blow-outs and fires could be encountered, all of which could result in personal injuries, loss of life and damage to property for which the Company may be ascribed some responsibility. In accordance with customary industry practice, the Company may not be able to or may elect not to insure against all such risks.

Certain oil and gas properties in which the Company has an interest may be difficult to access during break-up or inclement weather, which are risks normally encountered by most industry participants.

Title Matters

The Company has investigated its rights to participate in the exploration and development of its various resource properties and to, the best of its knowledge, those rights are in good standing. No assurance, however, can be given that applicable governments will not revoke, or significantly alter the conditions of, the applicable underlying grants and authorizations and that such grants and authorizations will not be challenged or impugned by third parties.

Competition

The oil and gas industry is intensely competitive and the Company must compete in all aspects of its business with a substantial number of other companies which have greater technical or financial resources. As a result, the Company may be unable to acquire rights to exploit additional resource properties on terms it considers acceptable. Accordingly, there can be no assurance that the Company

will acquire any interest in additional properties that would yield reserves or result in commercial operations.

Environmental and Other Regulatory Requirements

All phases of the Company's operations are subject to environmental regulation in the various jurisdictions in which it operates. Environmental legislation is evolving in a manner which will require stricter standards and enforcement, increased fines and penalties for non-compliance, more stringent environmental assessments of proposed projects and a heightened degree of responsibility for companies and their officers, directors and employees. There is no assurance that future changes in environmental regulation, if any, will not adversely affect the Company's operations. Environmental hazards may exist on the properties in which the Company holds interests which are unknown to the Company at present which have been caused by previous or existing owners or operators of the properties.

Government approvals and permits are currently, and may in the future be, required in connection with the operations in which the Company participates. To the extent such approvals are required and not obtained, exploration and development of the properties may be curtailed or prohibited from proceeding.

Failure to comply with applicable laws, regulations and permitting requirements may result in enforcement actions thereunder, including order issued by regulatory or judicial authorities causing operations to cease or be curtailed, and may include corrective measures requiring capital expenditures, installation of additional equipment, or remedial actions. Parties engaged in operations on resource properties may be required to compensate those suffering loss or damage by reason of the activities thereon and may have civil or criminal fines or penalties imposed for violations of applicable laws or regulations.

Conflicts of Interest

The directors of the Company are engaged and will continue to be engaged in the search for resource property interests on their own behalf and on behalf of other companies, situations may arise where the directors and officers may be in direct competition with the Company. Conflicts of interest, if any, which arise will be subject to and governed by the procedures described in the *Business Corporation Act* (Alberta) which require a director or officer of a company to disclose any interest in transactions involving the Company and, in the case of directors, to refrain from voting on any matter in respect of such interested transactions unless otherwise permitted under such Act.

Forward Looking Statement

This discussion and analysis may contain "forward-looking statements" that reflect Arbour Energy's current expectations and projections about its future

results. When used in this MD&A, words such as “estimate”, “intend”, “expect”, “anticipate” and similar expressions are intended to identify forward-looking statements, which, by their very nature, are not guarantees of Arbour Energy’s future operational or financial performance, and are subject to risks and uncertainties and other factors that could cause Arbour Energy’s actual results, performance, prospects or opportunities to differ materially from those expressed in, or implied by, these forward-looking statements. These risks, uncertainties and factors may include, but are not limited to: unavailability of financing, failure to identify a commercially viable oil or gas reserves, fluctuations in the market valuation for oil or gas, difficulties in obtaining required approvals for the development of an oil or gas project and other factors.

Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this MD&A or as of the date otherwise specifically indicated herein. Due to risks and uncertainties, including the risks and uncertainties identified above and elsewhere in this MD&A, actual events may differ materially from current expectations. Arbour Energy disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Calgary, Canada
May 30, 2005