

# PETRODORADO ENERGY LTD.

## MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE THREE MONTHS ENDED MARCH 31, 2013

The following is management's discussion and analysis ("MD&A") of the operating and financial results of Petrodorado Energy Ltd. ("Petrodorado" or the "Company") for the three months ended March 31, 2013, as compared to the three month period ended March 31, 2012, as well as information and expectations concerning the Company's outlook based on currently available information.

The MD&A should be read in conjunction with the unaudited interim condensed consolidated financial statements as at and for the three month periods ended March 31, 2013 and 2012, prepared in accordance with IFRS (as defined below), together with the accompanying notes and the audited consolidated financial statements and related notes and MD&A as at and for the year ended December 31, 2012. Additional information, including the Company's annual information form for the year ended December 31, 2012, is on SEDAR at [www.sedar.com](http://www.sedar.com) or on the Company's website at [www.petrodorado.com](http://www.petrodorado.com).

*All dollar values are expressed in US dollars, unless otherwise indicated, and are prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standard Board ("IASB").*

This MD&A is prepared as of May 27, 2013.

### NON-IFRS MEASURES

Funds from operations include all cash from operating activities and are calculated before the change in non-cash working capital. A reconciliation of cash used in operating activities to funds used in operations for the three months ended March 31, 2013 and 2012, are as follows:

<b>Funds from operations (\$)</b>	<b>Q1 2013</b>	<b>Q1 2012</b>
Cash used in operating activities	(659,569)	(710,557)
Change in non-cash working capital	176,398	120,691
Funds used in operations	(483,171)	(589,866)

The non-IFRS measure referred to above does not have any standardized meaning prescribed by IFRS and therefore may not be comparable to similar measures used by other companies. Management uses this non-IFRS measurement for its own performance measures and to provide its shareholders and investors with a measurement of the Company's efficiency and of its ability to fund a portion of its future growth expenditures.

## **BUSINESS PROFILE AND STRATEGY**

The Company is primarily engaged in petroleum and natural gas exploration and development activities in Colombia. Petrodorado's head office is located in Calgary, Alberta, Canada and the Company's shares are traded on the TSX Venture Exchange under the trading symbol PDQ.

Petrodorado was formed to explore for and develop petroleum assets in South America, with an initial focus on Colombia, Peru and Paraguay. Its experienced management team have acquired a significant portfolio of assets with four lower-risk blocks (blocks that have an oil discovery) and five more highly prospective blocks. The Company evaluated approximately 55 blocks before selecting these final nine blocks. The Company exited Peru and Paraguay in 2012 and is actively pursuing assets in other jurisdictions to diversify its portfolio.

## **PETROLEUM AND NATURAL GAS PROPERTIES AND OUTLOOK**

At present, Petrodorado has beneficial participation in five oil and gas blocks in Colombia. Multiple drilling prospects and leads have been identified in these blocks.

### **Moriche Block**

Petrodorado has an undivided 49.5% working interest in the Mauritia Este Prospect in the Moriche Block. The Mauritia Este Prospect consists of approximately 3,898 acres (net 1,930 acres) and is located in the Los Llanos basin of Colombia. During 2010, Petrodorado and the operator, Pacific Rubiales Energy Corp. ("**PRE**") successfully completed a discovery well, ME-1, as a Mirador producer on the Moriche block.

The ME-1 well tested at a peak rate of 693 bopd of 14 degree API oil and was put on production on June 18, 2010 at a gross rate of approximately 400 bbl/d (approximately 198 bbl/d net to Petrodorado). Production from ME-1 was shut down on December 4, 2011 due to a failure in the downhole pump. A remedial program was performed in March 2012 resulting in a return to production at a gross rate of approximately 131 bbl/d on April 17, 2012. Production was reduced as of May 2, 2012, due to issues with the surface equipment. This well was shut-in during the third quarter of 2012.

On March 20, 2013, Petrodorado executed a conditional sale agreement with the operating partner of the Moriche Block in which the Company will relinquish its 49.5% working interest held in the Mauritia Este Prospect within the Moriche Block for total consideration of \$3.5 million. Under the agreement, the \$3.5 million cash consideration will be paid to the Company by way of pre-determined quarterly installment payments over the 2013 and 2014 calendar years, during which the purchaser of the block has the option to return the rights of the Moriche Block, under specific circumstances including government approval, to the operating partner (and to the Company) for a 90% return of considerations paid to date. Final assignment of ownership to the rights to the Moriche Block will not be completed until all conditions of the conditional sale agreement are fulfilled.

### **CPO-5 Block**

On June 14, 2010 Petrodorado announced the signing of a farm-in agreement with ONGC Videsh Ltd. ("**ONGC**") for a 30% participating interest in the CPO-5 Block of Colombia. This 492,341 acre block (net

147,702 acres) is located in the Los Llanos basin (Meta Department) and was awarded to ONGC in the 2008 Agencia Nacional de Hidrocarburos (“ANH”) heavy oil bid round. The CPO-5 block is flanked in the North and North West by the recent discoveries by other operators in the blocks of Guatiquia (Candelilla Structure) and Corcel. Petrodorado received ANH approval of the assignment on October 1, 2010. Petrodorado has a commitment for 2013 which has been met subsequent to year end to drill one exploration well in addition to three wells for the second phase of the ANH committed exploration program by 2015.

During 2010, the Company with its partners completed the acquisition of 650 square km of 3D seismic and 240 lineal km of 2D seismic. Seismic processing and interpretation has been completed. The block received its environmental license on August 1, 2012 which approves 15 sites, 3 wells per site, for a total of 45 wells.

The first of the two exploration wells, the Kamal-1X well, was spudded on October 29, 2012 and reached a total depth of 10,500 feet in December 2012. The primary target of the Mirador zone encountered a net pay of 20 feet. This zone was tested using a coil tubing-nitrogen lift and yielded a peak rate of 210 barrels of oil a day of 14° API with high water cut. This test was performed to confirm hydrocarbon production and to determine the optimum placement of a jet pump and not to determine maximum production rates.

The second of the two exploration wells, the Loto-1X well, spudded on January 22, 2013, and was drilled to a total measured depth of 10,500 feet. The Loto-1X well targeted the Mirador, Guadalupe and Une sands. Upon completion of drilling, three conventional cores were obtained and logging operations have been concluded. Petrophysical evaluation supported by the conventional cores indicates that the target reservoir sands in the Tertiary, Mirador and Guadalupe formations are oil bearing. Well logs indicate total potential net pay of approximately 80 feet of high quality sand.

A multi-zone testing program was conducted on the Une and Lower and Upper Mirador zones. The testing of the Une zone resulted in extra heavy oil in non-commercial quantities and further testing was abandoned. A co-mingled test of three of the four identified intervals of the Lower and Upper Mirador zones was performed with an electro-submersible pump (“ESP”). An oil rate of 1,500 barrels per day (“bbl/d”) with an 80% water cut was achieved. The gravity of the oil was 17° API. The well displayed an excellent productivity index and potential, and the rate was limited to the capacity of the ESP of 10,000 barrels of fluid per day, and not due to the capacity of the well. Multiple attempts were made to test each zone independently, but due to equipment availability and surface storage limitation a proper test was not conducted.

Current management strategy is to perform further testing with a work-over rig using an ESP and sufficient surface storage capacity to isolate the water producing zone. In addition, the uppermost zone of the Upper Mirador was not tested and will be tested with the work-over rig. The sourcing of the work-over rig and other equipment has started and testing of Loto-1X is expected to recommence in July 2013.

### **La Maye Block**

Petrodorado has an undivided 20% working interest in an exploration and production contract with the ANH in the La Maye Block and an undivided 20% interest in four turn-key test wells and associated tie-in

equipment. The La Maye Block is located in the Lower Magdalena Valley of Colombia and consists of approximately 73,956 acres (net 14,791 acres).

The Company has identified three additional drilling prospects on the La Maye Block with a probability of success set at 25%. Petrodorado Ltd. (the private subsidiary of Petrodorado), in conjunction with the operator, drilled the Noelia-1 well as the first exploration oil well on the La Maye Block in October of 2009. This first exploration well is expected to be tested and a second exploration well is also expected to be drilled and tested as part of Phase 2 of the exploration program in this block as soon as the flood waters recede in the geographic area of Colombia. The Company has identified La Maye as non-core and is pursuing a sale process.

In 2009, Petrodorado Ltd. paid \$3.5 million into an escrow account to satisfy its net commitment to the participation agreement. Petrodorado authorizes draws from this account as certain development milestones are met. As at March 31, 2013, \$1,699,642 had been drawn from the escrow account leaving unspent restricted cash balance of \$1,800,358.

### **Talora Block**

Petrodorado initially earned a 55% interest in the Talora block located in the Upper Magdalena basin of Colombia. The Talora block consists of 58,905 acres (net 38,289 acres) southwest of Bogota, after the first relinquishment. In the fourth quarter of 2010, Petrodorado acquired an additional 20% interest from a third party and acquired PetroSouth Energy Ltd, which also owned a 20% interest, to increase its aggregate working interest to 95%. On October 16, 2011 Petrodorado executed a farmout agreement allocating a 30% working interest to Sintana Energy decreasing Petrodorado's overall working interest to 65%. The terms of the farmout included: 1) a bonus payment of \$5.2 million; 2) the farmee paying 60% of first well costs up to a maximum of \$3.9 million, with costs after the maximum to be paid at 30%; and 3) the farmee paying 45% of the second well costs up to a maximum of \$2.925 million, with costs after the maximum to be paid at 30%. Petrodorado's interest, via a wholly owned subsidiary, has been approved by the ANH.

The Company acquired 122 km of 2D seismic data during the first quarter of 2010. The first exploration well, Verdal 1, targeting the Tetuan and Caballos formations, was spudded on September 15, 2010 and was completed in November 2010, after only reaching the Tetuan formation. The Tetuan formation tested at a peak rate of 770 thousand standard cubic feet per day (mscf/d), and the Company is evaluating advanced engineering solutions to increase this production rate.

ANH approved the extension of the Talora license in two areas. The first area called the "additional exploration" area has a commitment of one exploration well to be drilled by the end of January 2013, which was fulfilled with the drilling of the Dorados-1X well; the second area called the "exploitation" area has a commitment of one appraisal well to be drilled by the end of September 2013.

Petrodorado completed and tested the Dorados-1X well on the Talora Block in the Upper Magdalena Valley of Colombia. This exploratory well was spudded on July 31, 2012, reaching a total depth of 7,282 ft-measured depth and testing conventional Upper and Lower Dorados sands in the Cretaceous sandstone. The main objectives were to reach the Cretaceous Caballos and Tetuan formations, but these formations were not found at the well location. However, an exceptionally thick Cretaceous-Cenomanian sand of 1,850 ft gross was found that had not been previously identified or reported in this basin.

Despite encountering what appeared to be a thick and well-defined gas and oil column with a possible basal water contact while drilling, the well testing results provided little information due to what appears to be significant formation damage. The post-drill well testing program proved the sand section to be a low pressure reservoir system with significant formation damage and evidence that the oil has been emulsified. Petrodorado is currently performing geochemical analysis to determine reservoir potential.

After an evaluation of the results, future plans are expected to include a new undamaged borehole (either by way of sidetrack hole or twin well) designed to overcome the sensitivity of this reservoir to formation damage due to low-pressure conditions, which is common in this part of the basin, in order to further evaluate the Dorados structure, a large thrust anticline with 4-way closure with a potential thick reservoir section.

Petrodorado also takes into consideration that Dorados sands present better pressure regime than the nearby Guando Oil Field (126 MMBO recoverable) located 40 km to the southeast of the Dorados-1X well. Plans are also underway to gather relevant data to evaluate the non-conventional target in the fractured oil shale of the Cretaceous La Luna oil source rock at the earliest possible opportunity.

### **Tacacho Block**

In January 2010, Petrodorado acquired a 49.5% working interest in the Tacacho Block located in the Putumayo Basin of Colombia. The Tacacho block measures approximately 598,008 acres (net 296,014 acres) and is located in the foreland basin of the Putumayo mountain range, in the Eastern Cordillera area of Colombia. PRE has a 50.5% working interest in the block. The 24 month-long exploration program includes the acquisition, processing and interpretation of 521 kilometres of 2D seismic data. ANH issued a six month extension to the 24 month period. Initial environmental assessments are underway for the seismic program. The commencement of the seismic acquisition is planned for the fourth quarter of 2013. The operator has informed Petrodorado that they have decided to reschedule the planned stratigraphic well until evaluation of the new seismic data is completed.

### **Buganviles Block**

Petrodorado has a varying working interest (30% to 59.5%) in the Buganviles Block located in the upper Magdalena basin of Colombia obtained through three separate transactions. The Buganviles Block consists of approximately 73,794 acres (net 43,907 acres).

In February 2010, Petrodorado obtained a 20% undivided working interest in the Buganviles Block through the purchase of all of the issued and outstanding shares of Holywell Resources S.A. (“**Holywell**”) from a private vendor for the aggregate cash purchase price of approximately \$6.3 million. Holywell was a private (Panama incorporated) oil & gas company with operations in Colombia. The name Holywell was changed to Petrodorado South America S.A. during the first quarter of 2010.

Prior thereto, in November 2009, Petrodorado entered in to a farm-in agreement with PRE to acquire a 29.5% working interest in the Visure prospect and 25% working interest in the Tuqueque prospect.

In addition, in September 2010, Petrodorado acquired an additional 10% working interest in the block through a farm-in agreement with Loon Energy Corp. The farm-in terms were satisfied with Petrodorado

having paid 100% (20% net) of the drilling costs for the two exploration wells Visure 1X and Tuqueque 1X.

Overall Petrodorado's position in the block is as follows:

Visure Prospect	59.5%
Tuqueque Prospect	55%
Rest of the block	30%

The first of these exploration wells, the Visure-1X well, located in the Visure prospect to the south-eastern border of the Bugarviles Block, was drilled in the fourth quarter of 2010 to evaluate a structural trap, similar to the nearby producing Abanico field, to the northeast. The well was tested in the Lower Guadalupe Formation at a stabilized average production rate of 46 bbl/d with 14 barrels of water per day. Oil gravity was 15.6° API. The Visure-1X well was suspended, with different production techniques being evaluated, based on the production test analysis, in order to economically produce the oil encountered in the Lower Guadalupe Formation. A cyclic steam injection pilot is being planned for this well.

The second exploration well, the Tuqueque-1X well was spudded on November 4, 2010, with the Caballos formation at 11,300 feet as the primary target. The well was suspended after two side tracks to reach the Caballos formation at a depth of 9,303 feet. Two secondary target formations were identified as the Monsarrate and the Olini. Three intervals in the Olini were tested and did not produce significant hydrocarbons. The Monsarrate is planned to be tested at a later date via a new drill up dip from the Tuqueque-1X location.

The operator has applied for a two year extension of the contract with a suggested work program given the current exploration license expired on June 30, 2012. As of May 27, 2013, an official response from the Colombian Government regarding the requested license extension has yet to be received. As such, the Company recognized impairments as of December 31, 2012, in relation to exploration and evaluation costs incurred within this exploration area. If the license extension is eventually received from the Colombia government, recovery of previously recorded impairments of these exploration and evaluation costs will be analyzed by management.

## **CALIFORNIA FARM-IN**

The Company has diversified its portfolio by entering into a more stable regulatory and high netback environment as an addition to its high impact exploration assets in Colombia.

On May 9, 2013, the Company entered into an agreement with Solimar Energy Ltd. (TSXV: SXS) regarding a heavy oil opportunity (gross: 1,720 acres) in the San Joaquin Basin of California for a non-operated working interest of 15% wherein the Company will pay 100% of Phase I up to a maximum of \$2.5 million, with costs in excess of the maximum to be paid at 15%, towards the appraisal and development of the Kreyenhagen Field. This will include drilling, coring, testing and fracking of up to 4 wells as well as creating reservoir models and thermal simulations. Within 30 days of the completion of this initial phase, the Company has the option to enter Phase II and increase its working interest to 40% (non-operated) by committing an additional \$4 million maximum, with costs in excess of the maximum to be paid at 40%, towards a thermal steam pilot. The Company will also earn a 12% non-operated working interest in the Kreyenhagen Shale Oil acreage (gross: 8,265 acres) if it elects to enter this

second phase. If the Company elects not to enter into Phase II, the Company will retain the original 15% working interest. This 1,720-acre project area has government approval over 225 acres where work will be conducted. The Company estimates a gross resource potential of approximately 47 mmbbl of 14°-17° API oil in the pilot area alone. The Company expects Phase I to be completed by the end of Q3 2013.

## COMMITMENT SUMMARY

The expenditures provided in the table below represent the Company's estimated cost to satisfy contractual commitments. Actual expenditures to satisfy these commitments, initiate production or create reserves may differ from these estimates.

<b>Block/Country</b>	<b>Interest</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>Total</b>
Talora, Colombia <sup>(1)</sup>	65%	5.5	-	-	-	5.5
Tacacho, Colombia <sup>(2)</sup>	49.5%	9.3	9.0	-	-	18.3
CPO-5, Colombia <sup>(3)</sup>	30.0%	-	-	3.6	-	3.6
La Maye, Colombia <sup>(4)</sup>	20.0%	0.3	1.5	-	-	1.8
San Joaquin, California <sup>(5)</sup>	15.0%	2.5	-	-	-	2.5
<b>Total</b>		<b>17.6</b>	<b>10.5</b>	<b>3.6</b>	<b>-</b>	<b>31.7</b>

1) Net commitment represents 1 well required by September 2013.

2) Petrodorado commitment to acquire and process 480 km<sup>2</sup> of 2D seismic data (to pay 100% of costs up to a maximum of \$8 million, 49.5% of costs thereafter).

3) Includes Petrodorado's 30% share of the ANH commitment of 3 exploration wells for the second phase of the exploration program by 2015.

4) Net commitment represents completion of Phase 1 (testing of Noelia-1 well) and execution of Phase 2 (drilling & testing of additional well). These expenditures are funded through the designated escrow account in restricted cash.

5) Petrodorado commitment towards Phase I of the exploration program.

The expenditures provided in the above table represent the Company's estimated cost to satisfy contract requirements. Actual expenditures to satisfy these commitments, initiate production or create reserves may differ from these estimates.

## DISCUSSION OF OPERATING RESULTS

### Revenue

During the three months ended March 31, 2013 and 2012 the Company generated no oil and gas revenues (\$111,429 for the year 2012). To date, all oil and gas revenue realized by the Company has been on account of oil and gas production from the ME-1 well of the Moriche Block. Oil and gas production was suspended during the three months ended March 31, 2012, due to required work-over maintenance, with production resuming in the second quarter of 2012. However, this well was shut-in during the third quarter of 2012. Overall 2012 revenue was the result of the sale of 1,020 barrels of oil at an average sales price of \$109 per barrel of oil.

In addition, interest and other revenue on cash balances and short-term investments was \$139,463 and \$208,370 for the three months ended March 31, 2013 and 2012, respectively (\$596,795 for the year 2012).

<b>Revenue (\$)</b>	<b>Q1 2013</b>	<b>Q1 2012</b>	<b>Year 2012</b>
Oil and gas sales, net of royalties	-	-	111,429
Interest and other	139,463	208,370	596,795
<b>Total Revenue</b>	<b>139,463</b>	<b>208,370</b>	<b>708,224</b>

No production was realized from the ME-1 well, for the three months ended March 31, 2013 and 2012. Production from the ME-1 well is shipped via truck and pipeline to oil storage facilities located on the Northwest coast of Colombia pending sales, which occur on an infrequent basis. As of December 4, 2011, production on the ME-1 well was suspended due to required work-over maintenance necessary in order to sustain production that would be economically feasible. As of April 17, 2012, the necessary maintenance had been completed and production of 131 bbl/d was being realized before being reduced in May 2012 due to issues with the surface equipment. Ultimately, this well was shut-in during the third quarter of 2012.

#### **Operating Costs**

During the three months ended March 31, 2013 and 2012, the Company incurred nil and \$141,725, respectively, in operating costs, including transportation. Given the ME-1 well was shut-in during the third quarter of 2012, no operating costs were incurred in the first quarter for 2013. While no production was realized in the first quarter of 2012, costs incurred related to the work-over maintenance performed on the ME-1 well.

#### **General and Administrative Expenses**

General and administrative expenses (“G&A”) for the periods ended March 31, 2013 and 2012 were \$580,900 and \$655,317, respectively. The decrease in G&A for the three months ended March 31, 2013 when compared to March 31, 2012, is primarily due to a reduction in investor relations activity and overall professional fees incurred in 2012 as well as administrative cost recoveries realized as operator of the exploratory activities of the Dorado-1X well in the Talora Block. Petrodorado budgets \$3.5 million for G&A expenses for the 2013 year (\$4 million for the 2012 year). G&A was \$2.8 million for the year ended December 31, 2012, an improvement over budget of \$1.2 million.

<b>General and Administrative Expenses (\$)</b>	<b>Q1 2013</b>	<b>Q1 2012</b>	<b>Year 2012</b>
Professional Fees	76,226	110,949	563,290
Wages & Salaries	313,090	343,207	1,076,753
Fees, Rent, Investor Relations and Other	191,584	201,161	1,181,574
<b>Total</b>	<b>580,900</b>	<b>655,317</b>	<b>2,821,617</b>

## Finance Costs

During the periods ended March 31, 2013 and 2012, the Company incurred \$34,002 and \$45,271, respectively, in finance costs due to the recording of accretion expense on provisions related to decommissioning obligations and equity tax payable.

<b>Finance Costs (\$)</b>	<b>Q1 2013</b>	<b>Q1 2012</b>
Accretion of decommissioning obligations	5,926	4,474
Accretion of equity tax payable	28,076	40,797
<b>Total</b>	<b>34,002</b>	<b>45,271</b>

## Foreign Exchange Loss (Gain)

The Company generated a foreign exchange gain of \$1,704,565 for the three months ended March 31, 2013, and a foreign exchange loss of \$1,493,155 for the three months ended March 31, 2012. The gain and loss are a direct effect of opposing movements in the strength of the Canadian dollar and Colombian peso when compared to the US dollar in each respective period.

## Stock-Based Compensation

For the three months ended March 31, 2013, the Company recorded a stock-based compensation of \$128,620 (\$504,697 - March 31, 2012), of which nil was capitalized in exploration and evaluation assets (\$101,169 - March 31, 2012).

The stock-based compensation arose due to a total of 10,980,000 and 30,000,000 options being granted during the year ended December 31, 2011 and 2010, respectively, and 5,685,000 options being granted during the year ended December 31, 2012. No options have been granted in the 2013 year-to-date period. The decrease in stock-based compensation expense is primarily due to the fact that the majority of outstanding options were fully vested prior to the beginning of the 2013 year, resulting in a reduced quarterly stock-based compensation expense on account of the reduced amount of options still vesting.

<b>Stock-Based Compensation (\$)</b>	<b>Q1 2013</b>	<b>Q1 2012</b>
Expensed	128,620	403,528
Capitalized	-	101,169
<b>Total (to Contributed Surplus)</b>	<b>128,620</b>	<b>504,697</b>

## Depletion and Depreciation

For the three months ended March 31, 2013, the Company recorded depletion and depreciation expense of \$24,000 (\$81,297 for the comparative period to March 31, 2012). Expenses recorded in each of these time periods consist of depreciation of general fixed assets held by the Company. No depletion was recorded for the first quarter of 2013 or 2012 given oil and gas production was not realized during either of these time periods.

## **Net Loss and Comprehensive Loss**

For the three months ended March 31, 2013, the Company generated net income of \$1,076,506 (net loss of \$2,611,923 for the comparative period to March 31, 2012), and a comprehensive loss of \$1,290,542 (\$543,008 for the same period to March 31, 2012).

The net income result for the three months ended March 31, 2013, when compared to the net loss of the comparative period in 2012, arose primarily due to the contrasting foreign exchange results in these comparative quarters, as discussed previously. Similarly, contrasting amounts in other comprehensive income were realized in these comparative periods due to contrasting movements in currency strength with regards to the Canadian dollar and Colombian peso when compared to the US dollar.

## **Funds used in Operations**

For the three months ended March 31, 2013, the Company used funds in operations of \$483,171 (funds used in operations of \$589,866 for the comparative period to March 31, 2012). The decrease in funds used in operations relates primarily by the decrease in operating and general and administrative expenses incurred during the three months ended March 31, 2013.

## **CAPITAL EXPENDITURES**

For the three months ended March 31, 2013 and 2012, the Company spent \$3.8 million and \$1.1 million, respectively, in exploration and evaluation capital expenditures.

For the expenditures in the three months ended March 31, 2013, the Company spent \$3.6 million in CPO-5 in the drilling program of the Loto-1X well. The Company also performed environmental and security work for \$0.2 million in Tacacho.

For the period ended March 31, 2013, the Company capitalized \$128,203 of general and administrative expenses (March 31, 2012 - \$143,415) and nil of stock-based compensation (March 31, 2012 - \$101,169) to exploration and evaluation assets. The Company does not hold any tangible exploration assets.

For capital expenditures in property, plant and equipment, the Company spent nil and \$7,000 for the three months ended March 31, 2013 and 2012, respectively.

## **LIQUIDITY AND CAPITAL RESOURCES**

The Company's approach to managing liquidity is to ensure a balance between capital expenditure requirements and cash provided by operations, available credit facilities and working capital. As at March 31, 2013, the Company had working capital of \$32.9 million (down from \$38.0 million at December 31, 2012) comprised primarily of short term investments. The decrease in working capital is primarily due to funds used in operating activities as well as exploration and evaluation capital expenditures. As at March 31, 2013 the Company also had \$5.6 million of non-current restricted cash. This working capital and restricted cash is expected to be used to fund exploration and development activities on Petrodorado's oil and gas properties and for general corporate purposes. As such, the

Company has total capital resources of \$38.5 million to fund exploration, development activities and operating expenses.

The Company is pursuing its strategy of focusing on its high impact Colombian exploration blocks as well as identifying the production potential on the California asset in 2013. This will include the execution of the outlined exploration drilling and testing programs in the CPO-5, Talora and La Maye Blocks, the acquisition of over 1,000 km of 2D seismic in the Tacacho Block, and the realization of the data gathering phase in the San Joaquin Basin of California through a fully funded budget of approximately \$19.1 million for the remainder of the 2013 year. Included within this plan are amounts required to meet contractual commitments as outlined in the "Commitment Summary" section.

On December 21, 2010, a \$3.0 million letter of credit was issued through a Colombian bank to the ANH in respect to the drilling obligations on the CPO-5 Block. This letter of credit is secured by a \$3,121,536 term deposit made at the Colombian bank.

A further \$403,920 letter of credit was issued through a Colombian bank on December 20, 2010 to the ANH to guarantee the Company's capital expenditure obligations with its partner, PRE, in the Tacacho Block. This letter of credit is secured by a \$421,407 term deposit made at the Colombian bank.

The Company's oil and gas interests are in the early production stage and the Company has only determined whether its petroleum and natural gas properties contain reserves that are economically recoverable on one of its Blocks to date, namely Moriche, which has since been sold. Accordingly, the recoverability of amounts recorded as petroleum and natural gas properties is dependent upon the existence and discovery of economically recoverable oil and gas reserves on the remaining blocks, the political stability of Colombia and the ability of the Company to secure adequate sources of financing to fund the development of its assets and put them into production and then achieve future profitable production. The outcome of these matters cannot be predicted with certainty at this time.

## **FINANCIAL INSTRUMENTS AND OTHER INSTRUMENTS**

The carrying values of the Company's financial instruments, consisting of cash and cash equivalents, short-term investments, cash calls receivable, accounts receivable, restricted cash, other receivables, accounts payable and accrued liabilities, approximate their fair values due to the short-term maturity of such instruments. The fair value of non-current restricted cash approximates its carrying value because interest rates are variable and reflective of market rates. The equity tax payable balance was recorded at discounted value, due to its long term maturity, which represents its fair value at such date. Unless otherwise noted, it is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from these financial instruments.

## **SHAREHOLDERS' EQUITY**

### **Common shares**

At March 31, 2013, the Company was authorized to issue an unlimited number of common shares, with no par value, with holders of common shares entitled to one vote per share and to dividends, if

declared. Outstanding common shares as of March 31, 2013, were 482,547,066 (December 31, 2012 - 482,547,066).

### Stock options

The Company has adopted a rolling stock option plan whereby options can be granted from time to time to directors, officers, employees and consultants at the discretion of the Board of Directors. The number of options that can be granted is limited to 10% of the total shares issued and outstanding. A summary of the changes in stock options is presented below:

	Number of options	Weighted average exercise price (CDN\$)
<b>Balance, January 1, 2012</b>	37,980,000	\$ 0.45
Options issued	5,685,000	0.20
Expired options	(666,667)	0.73
Forfeitures	(1,333,333)	0.55
Stock options amended (old price)	(13,980,000)	0.49
Stock options amended (new price)	13,980,000	0.25
<b>Balance, December 31, 2012 and March 31, 2013</b>	41,665,000	\$ 0.33
<b>Exercisable, March 31, 2013</b>	<b>34,943,327</b>	<b>\$ 0.35</b>

No stock options were granted during the three months ended March 31, 2013.

	Common Shares	Stock Options
<b>As at May 27, 2013</b>	482,547,066	41,665,000

### ADOPTION OF NEW AND REVISED ACCOUNTING STANDARDS

On January 1, 2013, the Company adopted new standards with respect to IFRS 10 “Consolidated Financial Statements”, IFRS 11 “Joint Arrangements”, IFRS 12 “Disclosure of Interests in Other Entities”, IFRS 13 “Fair Value Measurement”, and complied with amended disclosure requirements as found in IFRS 7 “Financial Instrument: Disclosures”. The adoption of these standards had no impact on the amounts recorded for the periods presented in the associated interim condensed consolidated financial statements for the period ended March 31, 2013.

IFRS 9 “Financial Instruments” (“**IFRS 9**”) will replace IAS 39 “Financial Instruments: Recognition and Measurement” (“**IAS 39**”). IFRS 9 uses a single approach to determine whether a financial asset is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. The new standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39. IFRS 9 is effective for annual periods beginning on or after January 1, 2015. The Company is currently evaluating the impact of IFRS 9 on its consolidated financial statements.

## USE OF ESTIMATES AND JUDGMENTS

The timely preparation of the financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and reported amounts of assets and liabilities and income and expenses. Accordingly, actual results may differ from these estimates. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected. Significant estimates and judgments made by management in the preparation of these financial statements are outlined below.

### **Critical judgments in applying accounting policies**

The following are the critical judgments that management has made in the process of applying the Company's accounting policies and that have the most significant effect on the amounts recognized in these consolidated financial statements:

#### ***i) Identification of cash-generating units***

The Company's assets are aggregated into cash-generating units, for the purpose of calculating impairment, based on their ability to generate largely independent cash flows. By their nature, these estimates and assumptions are subject to measurement uncertainty and may impact the carrying value of the Company's assets in future periods.

#### ***ii) Impairment of petroleum and natural gas assets***

Judgments are required to assess when impairment indicators, or reversal indicators, exist and impairment testing is required. In determining the recoverable amount of assets, in the absence of quoted market prices, impairment tests are based on estimates of reserves, production rates, future oil and natural gas prices, future costs, discount rates, market value of land and other relevant assumptions.

#### ***iii) Exploration and evaluation assets***

The application of the Company's accounting policy for exploration and evaluation assets requires management to make certain judgments as to future events and circumstances as to whether economic quantities of reserves have been found in assessing economic and technical feasibility.

#### ***iv) Income taxes***

Judgments are made by management to determine the likelihood of whether deferred income tax assets at the end of the reporting period will be realized from future taxable earnings. To the extent that assumptions regarding future profitability change, there can be an increase or decrease in the amounts recognized in respect of deferred tax assets as well as the amounts recognized in profit or loss in the period in which the change occurs.

### **Key sources of estimation uncertainty**

The following are the key assumptions concerning the sources of estimation uncertainty at the end of the reporting period, that have a significant risk of causing adjustments to the carrying amounts of assets and liabilities.

**i) Reserves**

The assessment of reported recoverable quantities of proved and probable reserves include estimates regarding production profile, commodity prices, exchange rates, remediation costs, timing and amount of future development costs, and production, transportation and marketing costs for future cash flows. It also requires interpretation of geological and geophysical models in anticipated recoveries. The economical, geological and technical factors used to estimate reserves may change from period to period. Changes in reported reserves can impact the carrying values of the Company's petroleum and natural gas properties and equipment, the calculation of depletion and depreciation, the provision for decommissioning obligations, and the recognition of deferred tax assets due to changes in expected future cash flows.

The Company's petroleum and natural gas reserves represent the estimated quantities of petroleum, natural gas and natural gas liquids which geological, geophysical and engineering data demonstrate with a specified degree of certainty to be economically recoverable in future years from known reservoirs and which are considered commercially producible. Such reserves may be considered commercially producible if management has the intention of developing and producing them and such intention is based upon (i) a reasonable assessment of the future economics of such production; (ii) a reasonable expectation that there is a market for all or substantially all the expected petroleum and natural gas production; and (iii) evidence that the necessary production, transmission and transportation facilities are available or can be made available. Reserves may only be considered proven and probable if the ability to produce is supported by either actual production or conclusive formation tests. The Company's petroleum and gas reserves are determined pursuant to National Instrument 51-101, Standard of Disclosures for Oil and Gas Activities.

**ii) Decommissioning obligations**

The Company estimates future remediation costs of production facilities, wells and pipelines at different stages of development and construction of assets or facilities. In most instances, removal of assets occurs many years into the future. This requires assumptions regarding abandonment date, future environmental and regulatory legislation, the extent of reclamation activities, the engineering methodology for estimating cost, future removal technologies in determining the removal cost and liability-specific discount rates to determine the present value of these cash flows.

**iii) Business combinations**

In a business combination, management makes estimates of the fair value of assets acquired and liabilities assumed which includes assessing the value of oil and gas properties based upon the estimation of recoverable quantities of proven and probable reserves being acquired.

**iv) Share-based payments**

All equity-settled, share-based awards issued by the Company are recorded at fair value using the Black-Scholes option-pricing model. In assessing the fair value of equity-based compensation, estimates have to be made regarding the expected volatility in share price, option life, dividend yield, risk-free rate and estimated forfeitures at the initial grant date.

**v) Tax provisions**

Tax provisions are based on enacted or substantively enacted laws. Changes in those laws could affect amounts recognized in profit or loss both in the period of change, which would include any impact on cumulative provisions, and in future periods. Deferred tax assets (if any) are recognized

only to the extent it is considered probable that those assets will be recoverable. This involves an assessment of when those deferred tax assets are likely to reverse.

## **PRINCIPAL BUSINESS RISKS**

The Company's business and results of operations are subject to a number of risks and uncertainties which are outlined under the heading "Risk Factors" in the Annual Information Form for the year ended December 31, 2012 and also including, but not limited to the following:

### **Crude Oil and Natural Gas Development**

Exploration, development, production of oil and natural gas involves a wide variety of risks which include but are not limited to the uncertainty of finding oil and gas in commercial quantities, securing markets, commodity price fluctuations, exchange and interest rate exposure and changes to government regulations, including regulations relating to prices, taxes, royalties and environmental protection. The oil and gas industry is intensely competitive and the Company competes with a large number of companies with greater resources.

The Company's ability to obtain reserves in the future will depend not only on its ability to develop its current properties but also on its ability to acquire new prospects and producing properties. The acquisition, exploration and development of new properties also require that sufficient capital from outside sources will be available to the Company in a timely manner. The availability of equity or debt financing is affected by many factors many of which are beyond the control of the Company.

### **Foreign Operations**

There are a number of risks associated with conducting foreign operations over which the Company has no control, including political instability, potential and actual civil disturbances, ability to repatriate funds, changes in laws affecting foreign ownership and existing contracts, environmental regulations, oil and gas prices, production regulations, royalty rates, income tax law changes, potential expropriation of property without fair compensation and restriction on exports.

### **Addition of Reserves and Resources**

The Company's future crude oil and natural gas reserves, production, and cash flows to be derived therefrom are highly dependent on the Company successfully discovering and developing or acquiring new reserves and resources. The addition of new reserves and resources will depend not only on the Company's ability to explore and develop properties but also, in the case of reserves, on its ability to select and acquire suitable producing properties or prospects. There can be no assurance that the Company's exploration, development or acquisition efforts will result in the discovery and development of commercial accumulations of oil and natural gas.

### ***Reserve Estimates***

There are numerous uncertainties inherent in estimating quantities of reserves, including many factors beyond the control of the Company. Estimates of reserves depend in large part upon the reliability of available geological and engineering data and require certain assumptions to be made in order to assign reserve volumes. Geological and engineering data is used to determine the probability that a reservoir

of oil and/or natural gas exists at a particular location, and whether, and to what extent, such hydrocarbons are recoverable from the reservoir. Accordingly, the ultimate reserves discovered by the Company may be significantly less than the total estimates.

### **Exploration Risks**

The exploration of the Company's properties may from time to time involve a high degree of risk that no production will be obtained or that the production obtained will be insufficient to recover drilling and completion costs. The costs of seismic operations and drilling, completing and operating wells are uncertain to a degree. Cost overruns can adversely affect the economics of the Company's exploration programs and projects. In addition, the Company's seismic operations and drilling plans may be curtailed, delayed or cancelled as a result of numerous factors, including, among others, equipment failures, weather or adverse climate conditions, shortages or delays in obtaining qualified personnel, shortages or delays in the delivery of or access to equipment, necessary governmental, regulatory or other third party approvals and compliance with regulatory requirements.

### **CAUTION REGARDING FORWARD-LOOKING INFORMATION**

This MD&A offers our assessment of the Company's future plans and operations as of May 27, 2013 and may contain forward-looking information. All statements other than statements of historical fact are forward-looking statements. Such information is generally identified by the use of words such as "anticipate", "continue", "estimate", "expect", "may", "plan", "will", "project", "should", "believe" and similar expressions. Statements relating to "reserves" or "resources" are also forward-looking statements, as they involve the implied assessment, based on certain estimates and assumptions, that the reserves described exist in the quantities predicted or estimated and that the resources and reserves described can be profitably produced in the future. All such statements involve known and unknown risks, uncertainties and assumptions.

Management believes that the expectations reflected in the forward-looking information are reasonable but no assurance can be given that these expectations will prove to be correct. Such forward-looking information included in this MD&A should not be unduly relied upon as the plans, assumptions, intentions or expectations upon which it is based may not occur. Actual results or events may vary from the forward-looking information.

In particular, this MD&A may contain forward-looking information pertaining to the following:

- the resource potential of the Company's assets,
- the Company's growth strategy and opportunities,
- performance characteristics of the Company's oil properties and estimated capital commitments and probability of success,
- crude oil production and recovery estimates and targets,
- the existence and size of the oil reserves and resources,
- the Company's drilling plans,
- capital expenditure programs and estimates, including the timing of activity,
- the Company's plans for, and results of, exploration and development activities,
- projections of market prices and costs,

- the supply and demand for oil,
- expectations regarding the ability to raise equity and debt capital on acceptable terms and to add continually to reserves through acquisitions and development, including the ability to negotiate and complete the agreements contemplated in this MD&A,
- the timing for receipt of regulatory approvals, including ANH approvals, and
- treatment of the Company under governmental regulatory regimes and tax laws.

The purpose of providing any financial outlook in this MD&A is to illustrate how the business of the Company might develop without the benefit of specific historical financial information. Readers are cautioned that this information may not be appropriate for other purposes.

The forward looking information herein is based on certain assumptions and analysis by the management of the Company in light of its experience and perception of historical trends, current conditions and expected future developments and other factors that it believes are appropriate and reasonable under the circumstances. The forward looking information herein is based on a number of assumptions, including but not limited to:

- the availability on acceptable terms of funds for capital expenditures,
- the availability in a cost-efficient manner of equipment and qualified personnel when required,
- continuing favourable relations with Latin American governmental agencies,
- continuing strong demand for oil,
- the stability of the regulatory framework governing royalties, taxes and environmental matters in Colombia and any other jurisdiction in which the Company may conduct its business in the future,
- the Company's future ability to market production of oil successfully to customers,
- the Company's future production levels and oil prices,
- the applicability of technologies for recovery and production of the Company's oil reserves,
- the existence and recoverability of any oil reserves,
- geological and engineering estimates in respect of the Company's resources and reserves,
- the geography of the areas in which the Company is exploring, and
- the impact of increasing competition on the Company.

The actual results, performance and achievements of the Company could differ materially from those anticipated in these forward-looking statements as a result of the risks and uncertainties set forth elsewhere in the MD&A and the following risks and uncertainties:

- global financial conditions,
- general economic, market and business conditions,
- volatility in market prices for oil and natural gas, the stock market, foreign exchange rates and interest rates,
- risks inherent in oil and gas operations, exploration, development and production,
- risks inherent in the Company's international operations, including security, political, sovereignty and legal risks in Colombia,
- the failure by counterparties to make payments or perform their operational or other obligations to the Company in compliance with the terms of contractual arrangements between the Company and such counterparties,
- risks related to the timing of completion of the Company's projects and plans,
- uncertainties associated with estimating oil and natural gas reserves and resources,

- competition for, among other things, capital, acquisitions of resources, undeveloped lands and skilled personnel,
- the Company's ability to hold existing leases through drilling or lease extensions or otherwise,
- incorrect assessments of the value of acquisitions or title to properties,
- the failure of the Company or the holder of certain licenses or leases to meet specific requirements of such licenses or leases,
- claims made in respect of the Company's properties or assets,
- geological, technical, drilling and processing problems, including the availability of equipment and access to properties,
- environmental risks and hazards,
- failure to estimate accurately abandonment and reclamation costs,
- the inaccuracy of third parties' reviews, reports and projections,
- rising costs of labour and equipment,
- the failure to engage or retain key personnel,
- changes in income tax laws or changes in tax laws and incentive programs relating to the oil and gas industry, and
- the other factors discussed under "Principal Business Risks" in this MD&A.

Readers are cautioned that the foregoing lists of assumptions, risks and uncertainties are not exhaustive. The forward-looking information contained in this MD&A is expressly qualified by this cautionary statement. The forward-looking information speaks only as of the date of this MD&A, and the Company does not undertake any obligation to publicly update or revise any forward-looking information except as required by applicable securities laws.

## SELECTED QUARTERLY INFORMATION

The following table sets out selected unaudited quarterly financial information of Petrodorado and is derived from unaudited quarterly financial data prepared by management in accordance with IFRS.

	Q1 2013	Q4 2012	Q3 2012	Q2 2012
Total revenue	\$ 139,463	\$ 142,654	\$ 140,006	\$ 217,194
Net income (loss)	1,076,506	(19,096,885)	1,040,883	486,532
Comprehensive income (loss)	(1,290,542)	(20,459,040)	5,177,759	(1,832,773)
Net income (loss) per share (basic & diluted)	0.00	(0.04)	0.00	0.00

	Q1 2012	Q4 2011	Q3 2011	Q2 2011
Total revenue	\$ 208,370	\$ 631,657	\$ 1,115,228	\$ 2,393,452
Net income (loss)	(2,611,923)	(3,455,890)	2,820,055	(2,636,055)
Comprehensive income (loss)	(543,008)	(995,528)	(5,981,662)	(1,686,082)
Net income (loss) per share (basic & diluted)	(0.01)	(0.01)	0.01	(0.01)

Revenue recorded is primarily based on the timing of oil and gas sales. In Q2 2011, the Company generated oil and gas revenues of \$2,270,162 as a result of the sale of 20,269 barrels of oil (total production on hand to date) at an agreed upon sales price of \$112 per barrel. In Q3 2011, the Company generated oil and gas revenues of \$1,017,249 as a result of the sale of 9,432 barrels of oil (total production on hand) at a settled price of \$112 per barrel. In Q4 2011, the Company generated oil and gas revenues of \$453,395 (net of royalties) as a result of the sale of 4,478 barrels of oil (total production on hand) at a settled price of \$112 per barrel. The decrease in quarterly revenue of \$563,854 from Q3 2011 to Q4 2011 was due to a decrease in production of 4,954 barrels of oil when comparing the two periods. Oil and gas sales were not realized in Q1 2012 given there was no oil and gas production in the quarter. In Q2 2012, the Company generated oil and gas revenues of \$111,429 as a result of the sale of 1,020 barrels of oil at an average sales price of \$109 per barrel. Oil and gas sales were not realized in Q3 2012, Q4 2012, or Q1 2013 given there was no oil and gas production in these quarters. Overall, the decrease in 2012 quarterly oil and gas revenue is due to the significant reduction of oil production from the Company's only producing well (ME-1), which has been shut-in as of Q3 2012.

Fluctuations in quarter-to-quarter net income (loss) are primarily on account of varying foreign exchange rates (with resulting foreign exchange gains/losses recorded) as well as the timing of oil and gas sales throughout the fiscal year (see previous paragraph). Q2 2011 incurred a foreign exchange loss of \$1,567,387 as foreign exchange rates changed due to a continually weakening US dollar. Q3 2011 experienced large fluctuations in foreign exchanges rates as the US dollar strengthened considerably resulting in a foreign exchange gain of \$6,630,846 for the three-month period. In Q4 2011, the Company recorded a foreign exchange loss of \$1,258,213; this was due to the strengthening of the Canadian dollar and Colombian peso compared to the US dollar in the quarter. In Q1 2012, the continued weakening of the US dollar resulted in further foreign exchange loss of \$1,493,155. In contrast, the US dollar strengthened significantly in Q2 2012, resulting in a foreign exchange gain of \$1,503,052 for the quarter. In Q3 2012, a return to a weakening US dollar resulted in a foreign exchange loss of \$3,019,471, only being offset by the recorded gain of \$4,752,650 due to the divestiture of Peru assets. Q4 2012 experienced a foreign exchange gain of \$1,296,737 as the US dollar strengthened marginally against the Canadian dollar and had no significant change in strength when compared to the Colombian peso. Furthermore, impairment losses of \$19,019,892 (\$18,735,892 of exploration and evaluation assets and \$284,000 of property, plant and equipment) were also recognized in Q4 2012, contributing to the overall loss in the quarter. In Q1 2013, a foreign exchange gain of \$1,704,565 was realized as an improvement in the strength of the US dollar was experienced against the Canadian dollar and Colombian peso.

## OUTLOOK

The Company's nine month capital program for the remainder of 2013 has been set at \$19.1 million, expected to be fully funded from current working capital within the Company. The work program and budget is expected to include the following:

- Drilling of the Dorados-1X side track well
- Further testing of the Loto-1X and Kamal-1X wells on the CPO-5 Block
- Acquiring and processing 480 km<sup>2</sup> of 2D seismic data on the Tacacho Block
- Conducting the data gathering phase in the California property
- Pending the recession of flood waters in the Lower Magdalena Valley, testing of the Noelia-1 exploration well and drilling of 1 additional exploration well in the La Maye Block
- Continuing with the environmental stewardship and social initiatives in the Company's area of operations.