

# PETRODORADO ENERGY LTD.

## MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2010

The following is management's discussion and analysis (MD&A) of the operating and financial results of Petrodorado Energy Ltd. ("Petrodorado" or the "Corporation") for the three and six months ended June 30, 2010 as well as information and expectations concerning the Corporation's outlook based on currently available information.

The MD&A should be read in conjunction with the unaudited interim consolidated financial statements for the three and six months ended June 30, 2010 together with the notes related thereto. Additional information relating to Petrodorado is on SEDAR at [www.sedar.com](http://www.sedar.com) or on the Corporation'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 Canadian generally accepted accounting principles (GAAP).*

This MD&A is prepared as of August 17, 2010.

### NON-GAAP MEASURES

Funds generated from operations include all cash from operating activities and are calculated before the change in non-cash working capital. A reconciliation of cash provided by operating activities to funds from operations for the three and six months ended June 30, 2010 are as follows:

<b>Funds from operations (\$)</b>	<b>Q2 2010</b>	<b>Q1 2010</b>	<b>YTD 2010</b>
Cash provided by (used in) operating activities	(578,729)	(83,221)	(661,950)
Change in non-cash working capital	(190,267)	84,964	(105,303)
Funds from (used in) operations	(768,996)	1,743	(767,253)

The non-GAAP measure referred to above does not have any standardized meaning prescribed by GAAP and therefore may not be comparable to similar measures used by other companies. Management uses this non-GAAP measurement for its own performance measures and to provide its shareholders and investors with a measurement of the Corporation's efficiency and of its ability to fund a portion of its future growth expenditures. As there is no standardized meaning, it is unlikely this measure will be comparable to other companies.

### BUSINESS PROFILE AND STRATEGY

The Corporation is primarily engaged in petroleum and natural gas exploration and development activities in Colombia, Peru and Paraguay. Petrodorado's head office is located in Calgary, Alberta, Canada and the Corporation'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. It's highly experienced management team have acquired a significant portfolio of assets with five lower-risk blocks (blocks have an oil discovery) and four potential "company maker" blocks. The Corporation evaluated approximately 44 blocks before selecting these final nine blocks.

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

At present, Petrodorado has beneficial participation in nine oil and gas blocks. A total of 25 drilling prospects and 11 drilling leads have been identified in these blocks with an overall probability of success set at 17%.

### **Colombia**

#### ***Moriche Block***

In January 2010, Petrodorado signed a definitive agreement with Pacific Rubiales Energy Corp. ("PRE") for an undivided 49.5% working interest in the Mauritia East Prospect in the Moriche Block. The Moriche Block consists of approximately 6,229 hectares (approximately 15,392 acres) and is located in the Llanos basin of Colombia. In exchange for this working interest, Petrodorado committed to fund 100% of the total investment for the current exploratory phase for the block, equal to US\$5.53 million.

During the first half of 2010, Petrodorado and PRE successfully completed a discovery well ME-1 as a Mirador producer on the Moriche block at a cost of \$5.8 million net to Petrodorado. The drilling of the ME-1 well completes Petrodorado's commitment to earn the 49.5% working interest in 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 bbls per day (approximately 200 bbls per day net to Petrodorado). Over the next several weeks, the capacity of on-site production facilities will be expanded and the Electro-Submersible Pump (ESP) will be adjusted to place the ME-1 well at optimum production expected to be approximately 600 bbls per day (approximately 300 bbls per day net to Petrodorado). In conjunction with PRE, Petrodorado is planning an additional development well at Moriche which is expected to be drilled in the fourth quarter of 2010.

Production from the ME-1 well is currently being shipped via truck and pipeline to oil storage facilities located on the Northwest coast of Colombia pending sale in November 2010.

#### ***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 199,248 hectare block (gross) 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 in the blocks of Guatiquia (Candelilla Structure) and Corcel.

In 1985, Elf Aquitaine drilled the Metica-1 well in the CPO-5 block, which tested 14.4 API oil and 20.8 API oil in the Los Cuervos and Barco formations. In addition, petrophysical analysis of well logs indicated hydrocarbons in the Carbonera, Mirador, Une and other deeper Palaeozoic horizons.

Petrodorado has identified multiple plays and multiple prospects in the Tertiary (Carbonera, Mirador, Los Cuervos, and Barco) and Cretaceous (Guadalupe, Gacheta and Une) formations targeting 14 to 40 degree API oil.

Work has commenced to acquire 650 square kilometres of 3D seismic and 240 line kilometres of 2D. Seismic acquisition, processing and interpretation are expected to be completed by the end of 2010. Two firm wells and three optional wells are planned for the first quarter of 2011.

### ***Buganviles Block***

Petrodorado has a 49.5% working interest in the Buganviles Block located in the upper Magdalena basin of Colombia obtained through two separate transactions. The Buganviles Block consists of approximately 22,128 hectares (approximately 54,679 acres) and is located in the upper Magdalena basin of Colombia.

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 is a private (Panama incorporated) oil & gas company with operations in Colombia, South America. The name Holywell was changed to Petrodorado South America S.A. ("Petrodorado SA") during the first quarter of 2010.

In addition, in November 2009, Petrodorado announced it was the successful bidder with PRE (operator) to farm-in on the Buganviles Block to earn a 29.5% working interest. In exchange for this working interest Petrodorado will fund one exploratory well for US\$2.27 million. This first exploration well is expected to commence drilling during the third quarter of 2010. A second and possibly a third well are also planned for the fourth quarter of 2010.

Petrodorado has identified up to six drilling prospects and four drilling leads on the Buganviles Block with a probability of success set at 28%.

### ***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 5,992 hectares (approximately 14,800 acres).

The Corporation has identified three additional drilling prospects on the La Maye Block with a probability of success set at 25%. Petrodorado (in conjunction with the operator) drilled the Noelia-1 as the first exploration oil well on the La Maye Block in October of 2009. A second

exploration well is expected to commence drilling during the fourth quarter of 2010. The first exploration well will be tested in conjunction with the testing of the second well.

In 2009, Petrodorado 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 June 30, 2010, \$2,702,603 had been drawn from the escrow account leaving a \$797,397 restricted cash balance. The operator has agreed to directly fund \$1,003,000 of Petrodorado's obligations for future exploration activity on the La Maye Block. The operator's obligation is accounted for as a long-term receivable on Petrodorado's balance sheet. The combination of the escrow account and the operator receivable (\$1,800,397) is expected to fund Petrodorado's share of remaining wells in the project.

### ***Talora Block***

Petrodorado is party to a participation agreement with a private Colombia based company to earn a 55% interest in the Talora block located in the Upper Magdalena basin of Colombia. The Talora block consists of 65,972 hectares (approximately 163,000 acres) southwest of Bogota.

The Corporation acquired 122km of 2D seismic data during the first quarter of 2010. Petrodorado has identified six drilling prospects and on the Talora Block with a probability of success set at 18%. An exploration well targeting 25 to 35 degree API oil is planned for September 2010.

### ***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 599,000 hectares (approximately 1,617,300 acres) and is located in the foreland basin of the Putumayo mountain range, in the Eastern Cordillera 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 480 kilometres of 2D seismic data to be completed during the first quarter of 2011. Initial environment assessments are underway for the seismic program. To date, Petrodorado has identified six drilling leads on the Tacacho Block and has set the probability of success at 13%.

## **Peru**

In February 2010, Petrodorado signed a definitive agreement with PRE to farm-in on two exploration blocks in Peru. The working interests in Blocks 135 and 138 are subject to Peruvian government and/or regulatory approvals.

### ***Block 135***

Petrodorado has acquired a 45% working interest in Block 135 located in the Marañon Basin of Peru with a gross area of approximately 926,000 hectares (approximately 2.5 million acres). In exchange for this working interest, Petrodorado will fund 45% of the total investment for the second exploratory phase for the block. PRE will retain a 55% working interest in the block. To

date, Petrodorado and PRE have identified two drilling prospects on Block 135 and have set the probability of success at 12%.

### ***Block 138***

Petrodorado has acquired a 45% working interest in Block 138 located in the Ucayali Basin of Peru with a gross area of approximately 370,000 hectares (approximately 1.0 million acres). In exchange for this working interest, Petrodorado will fund 45% of the total investment for the second exploratory phase for the block. PRE will retain a 55% working interest in the block. To date, Petrodorado and PRE have identified four drilling prospects on Block 138 with a probability of success set at 10%.

## **Paraguay**

### ***Pirity Block***

Through a non-binding letter of intent with a private US based company dated September 23, 2009, Petrodorado has the opportunity to negotiate definitive agreements granting Petrodorado up to an undivided 60% working interest in a concession contract with the Government of the Republic of Paraguay in the Pirity Block. The Pirity Block consists of approximately 485,623 hectares (approximately 1,200,000 acres) and is located in the Western Region of Paraguay.

Based upon available information, Petrodorado has identified three drilling prospects and one drilling lead on the Pirity Block. Petrodorado has set the probability of success at 15%. To date, the Corporation has not engaged in any exploration activity or incurred any costs on exploration or development on the Pirity Block.

### ***Loon Acquisition***

On June 19, 2010 Petrodorado and Loon Energy Corporation (“Loon”) announced a non-binding letter of intent dated July 15, 2010 (the "Letter Agreement"), pursuant to which, subject to the entering into of a definitive agreement (the "Definitive Agreement") and certain other conditions, the parties propose for the acquisition of all of the outstanding shares of Loon (the "Proposed Transaction") by Petrodorado.

The Proposed Transaction is an arm's length transaction pursuant to which shareholders of Loon would be entitled to receive common shares of Petrodorado based upon an exchange ratio of five common shares of Loon for each one common share of Petrodorado. Petrodorado would issue approximately 19,200,000 Acquisition Shares to Loon Shareholders under the Proposed Transaction. In addition, with respect to Block 127 in Peru owned by Loon, Petrodorado has agreed to issue additional Acquisition Shares (the “Performance Shares”) equal to a value of \$3,000,000 upon the occurrence of the following:

- (a) \$1,500,000 of Performance Shares upon completion of 300 km of 3D seismic; and
- (b) \$1,500,000 of Performance Shares upon spud of the initial well.

The Performance Shares would be issued at the 10 day weighted average trading price of Petrodorado's common shares immediately prior to each of the occurrences listed above.

The Letter Agreement is non-binding except for obligations relating to a period of exclusive dealing and confidentiality. If a Definitive Agreement is entered into, the parties will cooperate to complete the Proposed Transaction as soon as practical, subject to the receipt of all necessary regulatory and other approvals and satisfaction of all other customary closing conditions. The Proposed Transaction will be completed by way of a plan of arrangement, amalgamation, share exchange or other similar form of transaction. The Proposed Transaction may also be subject to the approval of the shareholders of Loon and/or Petrodorado. Further details concerning the Proposed Transaction will be announced if and when a Definitive Agreement is entered into.

## COMMITMENT SUMMARY

A summary of the estimated capital commitments in \$ millions are as follows:

<b>Block/Country</b>	<b>Petrodorado Interest</b>	<b>Initial Commitment</b>	<b>Spent To date</b>	<b>2010</b>	<b>Remaining 2011</b>	<b>2012</b>
La Maye, Colombia <sup>(1)</sup>	20%	3.5	1.7	1.0	0.4	0.4
Buganviles, Colombia <sup>(2)</sup>	49.5%	9.1	6.3	2.8	-	-
Moriche, Colombia <sup>(3)</sup>	49.5%	5.5	5.8	-	-	-
Talora, Colombia <sup>(4)</sup>	55%	5.9	5.9	-	-	-
Tacacho, Colombia <sup>(5)</sup>	49.5%	8.0	0.4	0.6	7.0	-
CPO-5, Colombia <sup>(6)</sup>	30.0%	6.6	0.6	3.6	2.4	-
Block 135, Peru <sup>(7)</sup>	45%	10.0	-	-	10.0	-
Block 138, Peru <sup>(8)</sup>	45%	8.0	-	8.0	-	-
<b>Total</b>		<b>56.6</b>	<b>20.7</b>	<b>16.0</b>	<b>19.8</b>	<b>0.4</b>

- 1) Petrodorado has funded an escrow account for \$3.5 million for a third party to drill, test and complete four exploration wells. The remaining balance in the escrow account is \$797,000 as at June 30, 2010. Petrodorado also has a receivable of \$1,003,000 due from the La Maye Operator to be satisfied by expenditures to be made by the La Maye Operator on the La Maye Block on Petrodorado's behalf.
- 2) Initial commitment includes the purchase Holywell in February 2010 and the cost to drill one exploration well. The Holywell purchase was completed during the first quarter of 2010 and the first exploration well is scheduled to be drilled during the third quarter of 2010.
- 3) Initial commitment includes the cost to drill, test and complete one oil exploration well. The well was drilled, completed and tested in February 2010 and was placed on production on June 18, 2010.
- 4) Net commitment includes amounts to purchase a 55% interest in the Talora Block, achieve operatorship status for Petrodorado, acquire and process 120 km of 2D seismic data and drill one exploratory well.

- 5) Petrodorado to pay 100% of costs to acquire and process 480 km of 2D seismic data (up to a maximum of US\$8 million).
- 6) Includes Petrodorado's 30% share of ANH Phase I commitments on the CPO-5 Block.
- 7) Petrodorado to pay 45% of the second exploration phase of the block. The Commitment amount represents currently budgeted cost to gather and process 525 km of seismic data.
- 8) Petrodorado to pay 45% of the second exploration phase of the block. The Commitment amount represents currently budgeted cost to acquire and process 100 km of seismic data.

The expenditures provided in the above table represent the Corporation'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 and six months ended June 30, 2010, the Corporation generated interest revenue on cash balances and short-term investments. For the three months ended June 30, 2010, Petrodorado generated interest revenue of \$59,717 compared to \$50,209 during the first quarter of 2010. The increase from the first quarter of 2010 is due to improved interest returns on Petrodorado's cash and short-term investment balances. For the first six months of 2010, the Corporation generated interest revenue of \$109,926. The Corporation had no other source of revenue for the three and six months ended June 30, 2010.

<b>Revenue (\$)</b>	<b>Q2 2010</b>	<b>Q1 2010</b>	<b>YTD 2010</b>
	59,717	50,209	109,926

The ME-1 on the Moriche Block in Colombia was put on production on June 18, 2010 at a gross rate of approximately 400 bbls per day (approximately 200 bbls per day net to Petrodorado). Production from the ME-1 well is currently being shipped via truck and pipeline to oil storage facilities located on the Northwest coast of Colombia pending sale in November 2010.

### **General and Administrative Expenses**

General and administrative expenses (G&A) for the three months ended June 30, 2010 were \$641,586 as compared to \$502,049 for the first quarter of 2010. The increase from the first quarter of 2010 was the result of increased wages and salaries for adding key personnel in the Petrodorado Colombia office and higher costs related to investor relations and travel. Year to date, G&A expenses were \$1,143,635. Petrodorado has budgeted \$3 million for G&A expenses in 2010.

<b>General and Administrative Expenses (\$)</b>	<b>Q2 2010</b>	<b>Q1 2010</b>	<b>YTD 2010</b>
Professional Fees	191,796	202,689	394,485
Wages & Salaries	219,930	130,729	350,659
Investor Relations and Travel	101,151	11,965	113,116
Office Rent	58,322	25,554	83,876
Regulatory Fees and Other	70,387	131,112	201,499
	641,586	502,049	1,143,635

### **Business Development Expenses**

During the three months ended June 30, 2010, the Corporation incurred one-time expenses of \$270,542. These expenses relate primarily to developing the Corporation's interest in the CPO-5 Block, one-time tax structuring costs and participation in the June 2010 ANH property auction in Colombia.

<b>Business Development Expenses (\$)</b>	<b>Q2 2010</b>	<b>Q1 2010</b>	<b>YTD 2010</b>
Professional Fees	146,542	-	146,542
Technical Data	100,000	-	100,000
Travel	24,000	-	24,000
Total	270,542	-	270,542

### **Amortization and Accretion**

For the three months ended June 30, 2010, the Corporation recorded amortization and accretion expenses of \$4,527 as compared to \$4,332 during the first quarter of 2010. For the six months ended June 30, 2010, Petrodorado recorded amortization and accretion expenses of \$8,859.

The Corporation recognizes crude oil inventory held in storage tanks. Inventory is valued at the lower of cost and net realizable value. Cost is determined on a first-in, first-out basis and relates to the direct cost of production on an actual basis. Crude oil inventory of \$98,552 has been recognized on the balance sheet with no amounts recognized in expenses during the six months ended June 30, 2010. The inventory cost includes \$55,065 of depletion. At June 30, 2010, petroleum and natural gas properties included undeveloped properties of \$16,058,389 which have been excluded from the depletion calculation.

<b>Amortization and Accretion Expenses (\$)</b>	<b>Q2 2010</b>	<b>Q1 2010</b>	<b>YTD 2010</b>
	4,527	4,332	8,859

### **Stock-Based Compensation**

For the three months ended June 30, 2010, the Corporation recorded a stock-based compensation expense of \$705,893 compared to \$2,524,513 for the first quarter of 2010. The decrease in stock-based compensation quarter over quarter relates to the 28 million of stock options issued to

directors, officers, employees and consultants during the first quarter of 2010 with no new stock options being issued during the second quarter of 2010. As the Corporation applied a graded vesting schedule and with over one third vesting at the date of grant, there was more stock-based compensation recorded during the first quarter of 2010. Stock-based compensation for the six months ended June 30, 2010 was \$3,230,406.

Stock-based compensation for the three and six months ended June 30, 2010 was calculated using the Black-Scholes pricing model using a risk free rate of 2.5%, volatility of 60%, an expected life of five years, a forfeiture rate of 10% and a zero dividend yield.

<b>Stock-Based Compensation Expenses (\$)</b>	<b>Q2 2010</b>	<b>Q1 2010</b>	<b>YTD 2010</b>
	705,893	2,524,513	3,230,406

### **Foreign Exchange Gain (Loss)**

The Corporation generated a foreign exchange loss of \$1,027,979 for the second quarter of 2010 compared to a foreign exchange gain of \$1,342,594 for the three months ended March 31, 2010. The difference in foreign exchange gains (losses) quarter over quarter is due to a reduction in the value of the Canadian dollar against the US dollar over the second quarter of 2010. For the six months ended June 30, 2010, Petrodorado generated a foreign exchange gain of \$314,615.

<b>Foreign Exchange Gain (Loss) (\$)</b>	<b>Q2 2010</b>	<b>Q1 2010</b>	<b>YTD 2010</b>
	(1,027,980)	1,342,594	314,615

Effective January 1, 2010, the Corporation changed its reporting currency from Canadian dollars to US dollars, as the Corporation anticipates that the majority of its future income stream and sources of new capital and financing will be denominated in US dollars. The Corporation has restated prior period comparative information.

Effective January 1, 2010, the Corporation reclassified all entities within the corporate group from integrated to self-sustaining foreign operations. Accordingly, all entities now use the US dollars as their functional currency. This change was made due to significant changes in facts and circumstances as follows:

1. The Corporation acquired 100% of the issued and outstanding shares of Holywell Resources S.A. ("Holywell") on February 1, 2010. The Corporation expects to conduct all of its future Colombian operations through Holywell. The Holywell acquisition was in US dollars with future operating activity in the company anticipated to be also in US dollars.
2. The vast majority of the Corporation's expenditures, commencing in the first quarter were transacted in US dollars and even a greater percentage will be conducted in US dollars in the future, as the US dollar is the predominant currency in South America.
3. It is anticipated that future petroleum and natural gas revenues from recent and future drilling will be denominated in US dollars.

4. As a greater percentage of expenditures will be US dollars the corporation will pursue sources of new capital in the same US dollar currency.

The Corporation prospectively adopted the current rate method of foreign currency translation as of January 1, 2010. Under this method revenues and expenses are translated using the average exchange rates for the applicable period, assets and liabilities are translated using the exchange rates in effect on the balance sheet dates, and shareholder's equity is translated using historical rates in effect at the date of each transaction. Resulting exchange differences are reported as a separate component of other comprehensive income.

For the period ended December 31, 2009, the Corporation recorded \$948,382 as an adjustment to opening accumulated other comprehensive income. This amount is the result of the prospective adoption of the current rate method for currency translation of the accounts of the Corporation's reclassified self-sustaining foreign operations, adoption of the US dollar as functional currency for the parent entity and the change in reporting currency from Canadian to United States dollars.

### **Net Loss and Comprehensive Loss**

The Corporation generated a net loss and comprehensive loss of \$2,590,810 for the three months ended June 30, 2010 compared to a net loss and comprehensive loss of \$1,638,091 for the three months ended March 31, 2010. The increase in the loss quarter over quarter was due to higher G&A costs and foreign exchange losses generated during the second quarter of 2010 partially offset by higher interest revenue and lower stock-based compensation expenses. Year to date, the Corporation generated a net loss and comprehensive loss of \$4,228,901 for the six months ended June 30, 2010.

<b>Net Loss and Comprehensive loss (\$)</b>	<b>Q2 2010</b>	<b>Q1 2010</b>	<b>YTD 2010</b>
	2,590,810	1,638,091	4,228,901

### **Funds from Operations**

The Corporation generated negative funds from operations of \$768,996 for the three months ended June 30, 2010 as compared to positive funds from operations of \$1,743 for the three months ended March 31, 2010. The change quarter over quarter was due to the higher net loss generated during the second quarter of 2010 and lower stock-based compensation expense.

### **CAPITAL EXPENDITURES**

For the three months ended June 30, 2010, the Corporation spent \$1.2 million in capital expenditures. These expenditures related to pre-drilling costs at CPO-5, Talora and Tacacho and costs related to bringing the Moriche ME-1 on production in June, 2010.

### **LIQUIDITY AND CAPITAL RESOURCES**

The Corporation'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 June 30, 2010, Petrodorado had working capital of \$42 million comprised

primarily of cash and short term investments. This working capital will be used to fund exploration and development activities on Petrodorado's oil and gas properties and for general corporate purposes.

On June 11, 2010 the Corporation executed facility letter with a major international bank for a US\$5 million demand operating loan. The purpose of the loan is for general operating purposes and is available by way of overdraft or by letters of credit up to US\$4.8 million. The operating loan is secured by a security agreement over cash, credit balances and deposit instruments in the amount of US\$5 million.

As at June 30, 2010 there were no overdrafts or letters of credit outstanding under the operating loan. On July 7, 2010, a letter of credit of US\$4.8 million was issued under the operating loan as partial consideration for the farm-in agreement with ONGC for a 30% participating interest in the CPO-5 Block in Colombia.

Petrodorado's consolidated financial statements have been prepared on the going concern basis in accordance with Canadian generally accepted accounting principles, which assumes that the Corporation will continue in operation for the foreseeable future and be able to realize its assets and discharge its liabilities and commitments in the normal course of business.

The Corporation's oil and gas interests are in the early production stage and the Corporation has not yet determined whether its petroleum and natural gas properties contain reserves that are economically recoverable. 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, confirmation of the Corporation's interests in the properties, the political stability of Colombia, Peru and Paraguay and the ability of the Corporation to secure adequate sources of financing to fund the development of its assets and put them into production and then achieving future profitable production. The outcome of these matters cannot be predicted with certainty at this time which could raise doubt about the going concern assumption.

## **RELATED PARTY TRANSACTIONS**

During the first half of 2010, the Corporation repaid advances from the President of the Corporation and two companies who are minority shareholders of the Corporation, in amounts of \$95,220, \$150,000 and \$150,000 respectively.

## **FINANCIAL INSTRUMENTS AND OTHER INSTRUMENTS**

The carrying values of the Corporation's financial instruments, consisting of cash and cash equivalents, short-term investments, accounts receivable, restricted cash, other receivables, accounts payable and accrued liabilities approximate their fair values due to the short-term maturity of such instruments. Unless otherwise noted, it is management's opinion the Corporation is not exposed to significant interest, currency or credit risks arising from these financial instruments.

## SHARE CAPITAL

### Common Shares

<b>Balance, December 31, 2009</b>	394,218,311
Options exercised	910,000
<b>Balance, June 30, 2010</b>	<b>395,128,311</b>

### Options

<b>Balance, December 31, 2009</b> <sup>(1)</sup>	910,000
Options exercised	(910,000)
Options issued	28,000,000
<b>Balance, June 30, 2010</b>	<b>28,000,000</b>

### Warrants<sup>(2)</sup>

<b>Balance, December 31, 2009</b>	214,285,000
Warrants exercised <sup>(3)</sup>	(50,000)
<b>Balance, June 30, 2010</b>	<b>214,235,000</b>

- 1) As at December 31, 2009, there were 910,000 stock options outstanding with an exercise price of \$0.10 per share. All of these options were exercised during the first quarter of 2010. On January 31, 2010, the Corporation issued stock options to acquire 28 million common shares of the Corporation at a price of \$0.49 per common share. The options are exercisable on or prior to January 31, 2015 subject to the provisions of the Corporation's stock option plan. Each option is for a five year term, expiring on January 31, 2015. The options vest over three years (1/3 on issuance and 1/3 on each of the first and second anniversary of the grant date).
- 2) The Corporation issued the warrants to purchase common stock in December 2009. The warrants are exercisable at a price of \$0.35 per share until December 3, 2012.
- 3) During the quarter ended June 30, 2010 50,000 warrants were exercised for cash.
- 4) As at August 17, 2010, the number of outstanding common shares, options and warrants were the same as June 30, 2010.

## **NEW ACCOUNTING STANDARDS AND POLICIES**

### **Inventory**

Inventory consists of crude oil held in storage. Inventory is valued at the lower of cost and net realizable value. Cost is determined on a first-in, first-out basis and relates to the direct cost of production on an actual basis.

### **Transition to International Financial Reporting Standards (“IFRS”)**

In February 2008, the CICA’s Accounting Standards Board confirmed that IFRS will replace Canadian GAAP in 2011 for profit-oriented Canadian publicly accountable enterprises. The Corporation will be required to report its results in accordance with IFRS beginning in 2011. The Corporation has developed a changeover plan to complete the transition to IFRS by January 2011, including the preparation of 2010 required comparative information. Petrodorado will be required to report its results in accordance with IFRS beginning in 2011.

The Corporation is assessing the potential impacts of this changeover and has developed its implementation plan accordingly. In the first half of 2010, we moved into the implementation phase of our IFRS project which focused on accounting policy decisions, modifications to IT systems and accounting processes.

The Corporation is currently in the process of evaluating the impact of accounting policy changes and the effect these changes will have on our financial statements. Petrodorado will disclose additional information on the impact of the changes throughout 2010. Any amendments to existing IFRS standards or implementation of new IFRS standards could lead to additional changes.

The quantitative impact on the future financial position and results of operations is not reasonably determinable at this point in time, however, the Corporation expects the highest impact will be in the following areas:

### ***Property, Plant and Equipment***

Under Canadian GAAP, Petrodorado follows the CICA’s guideline on full cost accounting in which all costs directly associated with the acquisition of, the exploration for, and the development of natural gas and crude oil reserves are capitalized on a country-by-country cost centre basis. Costs accumulated within each country cost centre are depleted using the unit-of-production method based on proved reserves determined using estimated future prices and costs. Upon transition to IFRS, the Corporation will be required to adopt new accounting policies for exploration and evaluation costs and development costs.

Exploration and evaluation costs are those expenditures for an area or project for which technical feasibility and commercial viability have not yet been determined. Under IFRS, Petrodorado intends to initially capitalize these costs as Exploration and Evaluation assets on the balance sheet. When the area or project is determined to be technically feasible and commercially viable,

the costs will be transferred to PP&E. Unrecoverable exploration and evaluation costs associated with an area or project will be expensed.

Development costs include those expenditures for areas or projects where technical feasibility and commercial viability have been determined. Under IFRS, the Corporation expects to continue to capitalize these costs within PP&E on the balance sheet. However, the costs will be depleted on a unit-of-production basis over an area level (unit of account) instead of the country cost centre level currently utilized under Canadian GAAP. The Corporation has not finalized the areas or the inputs to be utilized in the unit-of-production depletion calculation. Under IFRS, divestitures will generally result in a gain or loss recognized in net earnings. Under Canadian GAAP, proceeds of divestitures are normally deducted from the full cost pool without recognition of a gain or loss unless the deduction would result in a change to the depletion rate of 20 % or greater, in which case a gain or loss is recorded.

The Corporation expects to adopt the IFRS 1 exemption, which allows the Corporation to deem its January 1, 2010 IFRS PP&E costs to be equal to its Canadian GAAP historical net book value. On January 1, 2010, the IFRS exploration and evaluation costs will be equal to the Canadian GAAP unproved properties balance and the IFRS development costs will be equal to the full cost pool balance. Petrodorado will allocate this full cost pool over reserves to establish the area level depletion units.

#### ***Asset Retirement Obligation***

Under Canadian GAAP, ARO is initially measured as the estimated fair value of the retirement and decommissioning expenditures expected to be incurred. Existing liabilities are not re-measured using current discount rates. Under IFRS, ARO is measured as the best estimate of the expenditure to be incurred and requires the use of current discount rates at each re-measurement date. Generally, the change in discount rates results in a balance being added to or deducted from PP&E.

As a result of Petrodorado's intended use of the IFRS 1 assets exemption, the Corporation is required to revalue any January 1, 2010 ARO balance and recognize the adjustment in retained earnings.

#### ***Impairment***

Under Canadian GAAP, Petrodorado is required to recognize an impairment loss if the carrying amount exceeds the undiscounted cash flows from proved reserves for the country cost centre. If an impairment loss is to be recognized, it is then measured at the amount the carrying value exceeds the sum of the fair value of the proved and probable reserves and the costs of unproved properties.

Under IFRS, Petrodorado is required to recognize and measure an impairment loss if the carrying value exceeds the recoverable amount for a cash-generating unit. Under IFRS, the recoverable amount is the higher of fair value less cost to sell and value in use. Impairment losses, other than goodwill, are reversed under IFRS when there is an increase in the recoverable amount.

Petrodorado will group its assets into cash-generating units based on the independence of cash inflows from other assets or other groups of assets.

### ***Income Taxes***

In transitioning to IFRS, the Corporation's future taxes will be impacted by the tax effects resulting from the IFRS changes discussed above. Petrodorado continues to assess the impact that the IFRS income tax principles may have on the Corporation.

### **PRINCIPAL BUSINESS RISKS**

The Corporation's business and results of operations are subject to a number of risks and uncertainties, including but not limited to the following:

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 Corporation competes with a large number of companies with greater resources.

The Corporation'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 Corporation 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 Corporation.

There are a number of risks associated with conducting foreign operations over which the Corporation 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 Corporation currently has no reserves. The Corporation's future crude oil and natural gas reserves, production, and cash flows to be derived therefrom are highly dependent on the Corporation successfully discovering and developing or acquiring new reserves and resources. The addition of new reserves and resources will depend not only on the Corporation'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 Corporation's exploration, development or acquisition efforts will result in the discovery and development of commercial accumulations of oil and natural gas.

## **Exploration Risks**

The exploration of the Corporation'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 Corporation's exploration programs and projects. In addition, the Corporation'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 Corporation's future plans and operations as of August 17, 2010 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 Corporation's assets,
- the Corporation's growth strategy and opportunities,
- performance characteristics of the Corporation's oil properties and estimated capital commitments,
- crude oil production and recovery estimates and targets,
- the existence and size of the oil reserves and resources,
- the Corporation's drilling plans,
- capital expenditure programs and estimates, including the timing of activity,

- the Corporation'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 and bank lending facility contemplated in this MD&A,
- the timing for receipt of regulatory approvals, and
- treatment of the Corporation 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 Corporation 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 Corporation 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 regulatory framework governing royalties, taxes and environmental matters in Colombia, Peru and Paraguay and any other jurisdictions in which the Corporation may conduct its business in the future,
- the Corporation's future ability to market production of oil successfully to customers,
- the Corporation's future production levels and oil prices,
- the applicability of technologies for recovery and production of the Corporation's oil reserves,
- the existence and recoverability of any oil reserves,
- geological and engineering estimates in respect of the Corporation's resources,

- the geography of the areas in which the Corporation is exploring, and
- the impact of increasing competition on the Corporation.

The actual results, performance and achievements of the Corporation 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 Corporation's international operations, including security, political, sovereignty and legal risks in Colombia, Peru and Paraguay,
- the failure by counterparties to make payments or perform their operational or other obligations to the Corporation in compliance with the terms of contractual arrangements between the Corporation and such counterparties,
- risks related to the timing of completion of the Corporation'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 Corporation'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 Corporation or the holder of certain licenses or leases to meet specific requirements of such licenses or leases,
- claims made in respect of the Corporation'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 Corporation 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 Canadian GAAP.

\$	Q2 2010	Q1 2010	Q4 2009	Q3 2009
<b>Revenue</b>	59,717	50,209	9,432	39
<b>Net Loss and Comprehensive Loss</b>	2,590,810	1,638,091	206,976	7,132
<b>Net Loss Per Share</b>	0.01	0.00	0.00	0.00

Revenue consists of interest on cash balances and short term investments. Interest revenue increased in Q1 2010 as compared to Q4 2009 due to increased average cash and short term investment balances in Q1 2010 compared to Q4 2009.

Net loss and comprehensive loss increased in Q2 2010 compared to Q1 2010 due to higher general and administrative costs quarter over quarter, foreign exchange losses experienced during Q2 2010 and partially offset by lower stock-based compensation expenses. Similarly, net loss and comprehensive loss increased in Q1 2009 over Q4 2009 as the company commenced full operational activities during Q1 2010.