



Emerald Bay Energy

EMERALD BAY ENERGY, INC.

MANAGEMENT DISCUSSION AND ANALYSIS

FOR THE SIX MONTHS ENDED

June 30, 2007

MANAGEMENTS' DISCUSSION AND ANALYSIS

The following discussion and analysis of financial information and related data concerning Emerald Bay Energy, Inc. is reported in Canadian dollars and has been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"), and should be read in conjunction with the audited financial statements for the year ended December 31, 2006.

Non-GAAP Measures – The terms "cash flow from operations" and "cash outflow," which are expressed before changes in non-cash working capital, are used by the Corporation to analyze operating performance, leverage and liquidity. The term "field netback" is also used by the Corporation to analyze performance. Field netback is calculated by deducting from revenue the amount related to royalties, operating costs and transportation. These terms do not have any standardized meaning prescribed by GAAP and therefore might not be comparable with the calculation of a similar measure for other companies. The reconciliation between net earnings and cash flow from operations can be found in the consolidated statements of cash flows in the consolidated financial statements. The Corporation also presents cash flow from operations per share whereby per share amounts are calculated using weighted average shares consistent with the calculation of earnings per share.

Natural gas reserves and volumes are converted to barrels of oil equivalent (boe) on the basis of 6 thousand cubic feet (mcf) of gas to 1 barrel (bbl) of oil. Boe's may be misleading, particularly if used in isolation. A boe conversion of 6 mcf to 1 bbl is based on an energy equivalency conversion method primarily applicable at the burner tip and does not necessarily represent a value equivalency at the wellhead.

Information which is contained herein contains estimates and assumptions which management is required to make concerning future events, and may constitute forward-looking statements under applicable securities laws. Forward-looking statements include plans, expectations, estimates, forecasts and other comments that are not statements of fact. Although such expectations are viewed as reasonable by the Company, no assurance can be given that such expectations will be realized. Such forward-looking statements are subject to risks and uncertainties and may be based on assumption that may cause actual results to differ materially from those implied herein, and therefore are expressly qualified in their entirety by this cautionary statement

OVERVIEW

Emerald Bay Energy, Inc. ("Emerald Bay" or the "Company") is engaged in the business of exploration, development and production of crude oil, natural gas and natural gas liquids.

	For the three months ended		For the six months ended	
	Jun 30 2007 (\$)	Jun 30 2006 (\$)	Jun 30 2007 (\$)	Jun 30 2006 (\$)
Revenues (before royalties)	535,785	564,426	1,255,072	1,499,947
Cash flow (loss) from operations	(54,225)	(95,757)	44,924	25,612
Total assets	5,550,008	4,305,218	5,550,008	4,305,218
Secured debt	2,325,000	-	2,325,000	-

DETAILED REVIEW OF FINANCIAL RESULTS

Net Loss and Cash Flow

	For the three months ended		For the six months ended	
	Jun 30 2007 (\$)	Jun 30 2006 (\$)	Jun 30 2007 (\$)	Jun 30 2006 (\$)
Net loss	(197,749)	(367,210)	(317,327)	(613,660)
Per share	(0.010)	(0.010)	(0.010)	(0.010)
Cash flow (loss) from operations	(54,225)	(95,757)	44,924	25,612
Per share	(0.010)	(0.000)	0.010	0.001

The Company has recorded a net loss of \$289,524 for the six months ended June 30, 2007, compared to a net loss of \$613,660 for the six months ended June 30, 2006. The majority of the net loss relates to depletion, depreciation and amortization expense.

Revenue

	For the three months ended		For the six months ended	
	Jun 30 2007 (\$)	Jun 30 2006 (\$)	Jun 30 2007 (\$)	Jun 30 2006 (\$)
Oil and NGLs	108,963	186,617	251,304	434,750
Per barrel	46.53	61.05	50.64	55.73
Natural gas	426,822	429,095	1,003,768	1,095,385
Per mcf	7.79	6.49	7.94	7.76
Total gross revenue	535,785	615,712	1,255,072	1,530,135
Per boe	46.71	43.78	48.23	48.83

Gross revenue decreased as compared to 2006 as the result of significantly lower commodity prices and lower production volumes.

Sales Volumes

	For the three months ended		For the six months ended	
	Jun 30 2007	Jun 30 2006	Jun 30 2007	Jun 30 2006
Crude oil – barrels per day	9	14	11	13
Natural gas – mcf per day	595	727	698	780
NGLs – barrels per day	16	19	16	30
BOE – barrels per day	125	155	144	173

Sales volumes decreased to 144 boed from 173 barrels per day due to reduced production from the Twining and Clive as several wells were shut in during the period for infrastructure maintenance and well optimization workovers.

General and administrative expenses

	For the three months ended		For the six months ended	
	Jun 30 2007 (\$)	Jun 30 2006 (\$)	Jun 30 2007 (\$)	Jun 30 2006 (\$)
General and administrative expense	353,327	310,511	642,703	678,493

General and administrative expenses decreased in 2007 compared to 2006. Additionally, increased activity levels have led to increased staffing. The company does not capitalize any administrative costs.

Depletion, depreciation and site restoration expense

	For the three months ended		For the six months ended	
	Jun 30 2007 (\$)	Jun 30 2006 (\$)	Jun 30 2007 (\$)	Jun 30 2006 (\$)
Depletion, depreciation and amortization	221,850	269,177	487,308	465,955
Asset Retirement Obligation - Accretion	674	1,969	1,348	3,938
Total	222,524	271,146	488,656	469,893

Depletion, depreciation and amortization increased in 2007 as compared to 2006 due to significantly higher capital costs.

LIQUIDITY AND CAPITAL RESOURCES

In order to support Emerald's growth oriented business plan, the Company's strategy is to fund its capital expenditure program by issuing common and flow-through shares, as well as cash from operations, to reinvest and also to utilize bank debt.

SHAREHOLDERS EQUITY

As at June 30, 2007, there were 27,903,277 common shares issued and outstanding, and an additional maximum total of 2,429,904 reserved for issuance on the potential exercise of common share purchase options. In addition, 3,624,500 common shares may be issued on the exercise of warrants.

CONTRACTUAL OBLIGATIONS AND CONTINGENCIES

The Company operates its office under lease arrangement for Three (3) years commencing October 1, 2006 and ending September 30, 2009.

OFF-BALANCE SHEET ARRANGEMENTS

Emerald did not enter into any off-balance sheet arrangements.

TRANSACTIONS WITH RELATED PARTIES

During the quarter, a payment of interest on a note due from a related party was received. A law firm in which a director is a partner has charged the Corporation \$8,116 in legal fees, a consulting firm in owned by a director and officer has charged the Corporation \$46,640 in consulting

ACCOUNTING POLICIES

Emerald's accounting policies are stated in Note 2 to the audited Financial Statements for the years ended December 31, 2006 and December 31, 2005. Emerald follows policies that are in accordance with Canadian generally accepted accounting principles.

LEGAL MATTERS

In 2005, an oilfield service provider commenced legal action against the Company relating to the loss of a tool in the well bore of one of the Company's wells claiming total damages of \$193,121. As a result of this incident the Company has counterclaimed for \$760,000 plus additional damages. In the opinion of management, the outcome of this action is not determinable at this time.

BUSINESS RISKS

The oil and gas industry is subject to risks in (among others):

- finding and developing reserves,
- commodity prices received for such reserves,
- availability of equipment, manpower and supplies,
- availability and cost of capital to achieve projected growth,
- effect of weather on drilling and production, and
- operating in an environmentally appropriate fashion.

Emerald Bay mitigates these business risks by:

- Having assets in several diverse fields.
- Maintaining cost-effective operations.
- Operating our own properties were possible to control the amount and timing of capital expenditures.
- Using new technology to maximize production and recoveries and reduce operating costs.
- Drilling wells in areas with multiple zone potential.

POLITICAL, REGULATORY AND ENVIRONMENTAL RISKS

Separate from the business risks above are political, regulatory and environmental risks. Emerald Bay mitigates environmental risk directly related to its own operation through its insurance program and by diligent care and attention in the field. However, Emerald Bay is unable to mitigate political, regulatory and environmental risks that stem from sources outside its own operations. In the past year there have been strong examples of all of the above. On the political front there was the October 31, 2006 announcement of the federal government's intentions to tax income trusts. This event resulted in a significant erosion of value in the trust sector. As the trust sector had been the main exit strategy for junior oil and gas companies, this also resulted in a significant drop in the market value of the junior oil and gas sector. This event was not only distressing to shareholders of these companies, but also increased the effective cost of raising public equity.

Regulatory risk has been observed in the increased time required to obtain various approvals. Such delays result in projects being started later than planned or being brought on production later than planned.

Perhaps the most significant risk that will be faced by the industry in the coming years is the environmental risk. This risk perhaps should be labeled the political environmental risk. There have been various rumours of carbon, or other green taxes or measures that would adversely affect the industry and therefore Emerald Bay. Emerald Bay welcomes well thought out measures to improve and make cleaner the world that we all live and work in. However, Emerald Bay would be remiss not to mention the risk that hasty legislation may have a significant adverse effect on the industry and therefore, the company.

DISCLOSURE CONTROLS AND PROCEDURES OVER FINANCIAL REPORTING

Disclosure controls and procedures are designed to provide reasonable assurances that all relevant information is gathered and reported to senior management, including the Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO"), and that management has evaluated the effectiveness of the Corporation's disclosure controls and procedures as defined in Multilateral Instrument 52-109 of the Canadian Securities Administrators and has concluded that such disclosure controls and procedures are effective. However, they do not expect that the disclosure controls and procedures or internal control over financial reporting will prevent all errors or fraud. An economically feasible control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

INTERNAL CONTROLS OVER FINANCIAL REPORTING

The CEO and CFO of Emerald Bay Energy are responsible for designing internal controls over financial reporting or causing them to be designed under their supervision in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP. The company

assessed the design of its internal control over financial reporting as of December 31, 2006. During this process, management identified certain weaknesses in internal controls over financial reporting which are as follows:

- Due to the limited number of staff at Emerald Bay, it is not economically feasible to achieve complete segregation of incompatible duties.
- Due to the limited number of staff, the Corporation does not have a sufficient number of financial personnel with the technical accounting knowledge to address all complex and non-routine accounting transactions that may arise.

These weaknesses in internal controls over financial reporting result in a possibility that a material misstatement would not be prevented or detected. Management and the board of the directors work to mitigate the risk of a material misstatement in financial reporting. However, there can be no assurance that this risk can be reduced to less than a remote likelihood of a material misstatement.

SELECTED QUARTERLY INFORMATION

Financial Highlights

	Jun 30, 2007	Mar 31, 2007	Dec 31, 2006	Sep 30, 2006	Jun 30, 2006	Mar 31, 2006	Dec 31, 2005	Sep 30, 2005
\$000's except per share amounts								
Total revenue, net of royalty	400	576	485	532	388	662	880	330
Cash Flow (deficiency) from operations	(54)	99	83	104	(96)	121	58	(36)
Per share – basic and diluted	(0.010)	(0.010)	0.010	(0.003)	(0.003)	0.004	0.010	(0.004)
Net loss	(198)	(120)	(261)	(164)	(367)	(246)	(74)	(133)
Per share – basic and diluted	(0.010)	(0.010)	(0.010)	(0.010)	(0.010)	(0.010)	(0.010)	(0.010)
Capital expenditures	415	969	1,457	(198)	1,017	215	241	(89)
Total assets	5,550	5,980	5,391	4,072	4,305	4,563	6,705	3,699
Net working capital (debt)	(2,603)	(2,132)	(1,263)	(388)	(782)	(1,910)	894	389