



Emerald Bay Energy

EMERALD BAY ENERGY, INC.

MANAGEMENT DISCUSSION AND ANALYSIS

**FOR THE QUARTER ENDED
SEPTEMBER 30, 2004**

NOVEMBER 29, 2004

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 unaudited financial statements for the nine months ended September 30, 2004.

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. As a strategic initiative, the Company is also developing technology for down-hole drilling applications, targeting marginal-producing and abandoned wells.

	For the three months ended		For the nine months ended	
	Sept 30 2004 (\$)	Sept 30 2003 (\$)	Sept 30 2004 (\$)	Sept 30 2003 (\$)
Revenues (before royalties)	297,280	265,408	887,586	1,009,486
Research and Development costs	(108,521)	(32,489)	(253,768)	(38,014)
Net income (loss)	(240,656)	(98,829)	(515,749)	(34,333)
Net income (loss) per share (basic and diluted)	(0.02)	(0.01)	(0.04)	(0.01)
Total assets	1,655,045	2,126,761	1,655,045	2,126,761
Secured term debt	-	92,500	-	92,500

After completing a \$ 1,339,000 flow-through financing in the 4th quarter of 2003, the Company embarked on an active exploration program that included data collection, geophysical analysis and drilling during the first half of 2004. Emerald Bay drilled 2 gross wells during the first nine months. (1.1 net) At Edson, Alberta the recently-drilled Cardium well was cased and cemented. The company is currently evaluating the economic potential of certain zones and anticipates this well to be on stream Q1 2005. At Conrad, Alberta testing operations on a directional well were terminated after failing to encounter economic quantities of oil or natural gas. The Company will evaluate the remaining farmout lands to determine if an option well is warranted.

At Clive, Alberta the company has commenced a multiple well coal bed methane drilling program. It is anticipated that drilling will commence in October 2004 with up to 8 wells completed in Q4. Additionally the company has targeted a location for drilling a Belly River gas well in the Clive area in Q4.

Management expects to increase the Company's reserves, production, and cash flow during the remainder of this year and into 2005 as a result of the Company's drilling programs in Alberta. Management also intends to intensify its pursuit of further acquisition, exploitation and exploration

prospects with a view to identifying and capturing opportunities that have the potential to provide an additional core area for the Company.

The development of the Lateral Drainhole Drilling Tool continues at the Company's testing facility in Calgary. Significant progress has been achieved in critical components as we move this tool closer to a commercial product. The Lateral Drainhole Drilling Tool will enable the Company and other oil and gas producing firms to optimize the performance of their wells by getting beyond formation damage and enhance production in a cost-effective manner.

DETAILED REVIEW OF FINANCIAL RESULTS

Net Earnings and Cash Flow

	For the three months ended		For the nine months ended	
	Sept 30 2004 (\$)	Sept 30 2003 (\$)	Sept 30 2004 (\$)	Sept 30 2003 (\$)
Net earnings (loss)	(240,656)	(98,829)	(515,749)	(34,333)
Per share	(0.02)	(0.01)	(0.04)	(0.01)
Cash flow used from operations	(190,026)	(73,428)	(530,514)	94,957
Per share	(0.02)	(0.01)	(0.05)	0.01

The Company has recorded a net loss of \$(515,749) for the nine months ended September 30, 2004, compared to a net loss of \$34,333 for the period ended September 30, 2003. Increased general and administration relating to substantially increased exploration activities and research and development expenses, as well as lower sales revenue, accounted for the majority of the net loss in 2004. The company has significantly increased staffing and consulting services for the year to date compared to the prior year.

Revenue

	For the three months ended		For the nine months ended	
	Sept 30 2004 (\$)	Sept 30 2003 (\$)	Sept 30 2004 (\$)	Sept 30 2003 (\$)
Oil and NGLs	62,456	29,320	176,455	131,108
Per barrel	43.71	32.65	40.56	26.11
Natural gas	234,824	236,088	711,131	878,378
Per mcf	6.90	6.27	6.99	7.23
Total gross revenue	297,280	265,408	887,586	1,009,486
Per boe	41.85	36.97	41.63	40.02

Sales Volumes

	For the three months ended		For the nine months ended	
	Sept 30 2004	Sept 30 2003	Sept 30 2004	Sept 30 2003
Crude oil – barrels per day	5	1	6	6
Natural gas – mcf per day	370	410	373	445
NGLs – barrels per day	10	9	10	13
BOE – barrels per day	77	78	78	92

Gross revenue decreased in 2004 as compared to 2003, as sales volumes decreased to 78 boed from 92 barrels per day. Revenue from natural gas sales were higher in 2003 due to production from the Clive well. This well has reached payout and therefore Emerald's interest in net production has been decreased by 50% in 2004. Total revenue also decreased due to slightly lower prices received in 2004 compared to 2003. Emerald does not currently have any hedges in place.

Royalties

	For the three months ended		For the nine months ended	
	Sept 30 2004 (\$)	Sept 30 2003 (\$)	Sept 30 2004 (\$)	Sept 30 2003 (\$)
Total royalties	61,555	47,920	138,889	245,339
Per boe	8.67	6.68	6.52	9.73
Percentage of revenue	20.7%	18.1%	15.6%	24.3%

Royalties for the nine months ended September 30, 2004 decreased due to the decrease in total revenue as described above. Royalties decreased as a percentage of revenue due to the price sensitivity of the Company's royalties. The royalty decreased on a BOE basis due to the higher price per BOE in 2003 versus 2004. Higher sales values generally attract a higher royalty rate.

Production Expense

	For the three months ended		For the nine months ended	
	Sept 30 2004 (\$)	Sept 30 2003 (\$)	Sept 30 2004 (\$)	Sept 30 2003 (\$)
Total production expenses	102,475	63,069	239,624	145,545
Per boe	14.43	8.79	11.24	5.77
Percentage of revenue	34.5%	23.8%	27.0%	14.4%

Production expenses increased on a per boe basis to \$11.24 from \$5.77 in 2003 due to workovers on certain wells.

General and administrative expenses

	For the three months ended		For the nine months ended	
	Sept 30 2004 (\$)	Sept 30 2003 (\$)	Sept 30 2004 (\$)	Sept 30 2003 (\$)
General and administrative expense	219,950	208,470	813,327	544,629

In order to carry out the increased activity levels resulting from the company's five year plan, the company substantially increased staffing levels and consulting services relating to exploration activities and research and development. Additionally, new regulatory requirements have increased administrative expense. Furthermore, certain one time costs relating to research and development expenses, capital raising costs, and prior years services have also added to increased general and administrative expenses for the period. The company does not capitalize any administrative costs.

Research and development expenses

	For the three months ended		For the nine months ended	
	Sept 30 2004 (\$)	Sept 30 2003 (\$)	Sept 30 2004 (\$)	Sept 30 2003 (\$)
Research and development expenditures	108,521	32,489	253,768	38,014

Research and development expenses increased substantially in the period ended September 30, 2004, compared to the period ended September 30, 2003. In addition to increased consulting services the company has employed two persons in its efforts to complete development of the lateral drainhole drilling technology in a timely manner. The Company increased its development efforts substantially in 2004 after settlement of the intellectual property litigation as discussed in the annual information circular.

Depletion, depreciation and site restoration expense

	For the three months ended		For the nine months ended	
	Sept 30 2004 (\$)	Sept 30 2003 (\$)	Sept 30 2004 (\$)	Sept 30 2003 (\$)
Depletion, depreciation and amortization	40,608	18,804	108,637	69,541
Asset Retirement Obligation - Accretion	2,635	2,059	7,905	6,627
Total	43,243	20,863	116,542	76,176

Depletion, depreciation and amortization increased in 2004 versus 2003 due to lower reserve volumes arising from the year end engineering review of the Company's properties. Accretion increased in 2004 from 2003 due to the ownership of an increased number of oil and natural gas wells and related facilities in 2004.

Taxes

	For the three months ended		For the nine months ended	
	Sept 30 2004 (\$)	Sept 30 2003 (\$)	Sept 30 2004 (\$)	Sept 30 2003 (\$)
Future income tax expense (recovery)	-	4,538	(146,000)	53,122

The future tax recovery in 2004 as compared to a tax liability in 2003 is due in part to the loss reported in 2004 and as a consequence of changes to the income tax provisions effecting resource companies. Under the terms of the Company's flow-through share agreements, Emerald has committed to incur \$1.4 million of qualifying oil and natural gas exploration and development expenses between January 1, 2004 and December 31, 2004. Emerald has already renounced the income tax benefits of these expenditures to the flow-through shareholders. The future tax impact of the renunciation of flow through shares has been reflected in equity and the future tax balance on the balance sheet.

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, to reinvest its cash flow, and to utilize bank debt.

SHAREHOLDERS EQUITY

As at September 30, 2004, there were 11,708,304 common shares issued and outstanding, and an additional maximum total of 1,170,000 reserved for issuance on the potential exercise of common share purchase options. In addition, 1,590,374 common shares may be issued on the exercise of warrants associated with a December 2003 private placement and flow through share offering.

CONTRACTUAL OBLIGATIONS AND CONTINGENCIES

Under the terms of the Company's flow-through share agreements, the company has committed to incur approximately \$1,339,127 of qualifying oil and natural gas exploration and development expenses between January 1, 2004 and December 31, 2004. Emerald has already renounced the income tax benefits of these expenditures to the flow-through shareholders.

OFF-BALANCE SHEET ARRANGEMENTS

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

TRANSACTIONS WITH RELATED PARTIES

Emerald's initial significant shareholders have continued to support the Company's growth oriented business plan by investing additional funds by way of participating in Emerald's ongoing equity issues. As Emerald executes its growth plan, it is the Company's intention to continue to diversify its shareholder base by attracting new shareholders to participate in future offerings. Note 7 of the unaudited Financial Statements fully detail Emerald's related party transactions.

ACCOUNTING POLICIES

Emerald's accounting policies are stated in Note 2 to the audited Financial Statements. Emerald follows policies that are in accordance with Canadian generally accepted accounting principles.