

**EXCELSIOR ENERGY LIMITED  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
DECEMBER 31, 2006**

The following discussion and analysis is management's opinion of Excelsior Energy Limited ("Excelsior" or the "Company") historical financial and operational results and should be read in conjunction with the audited financial statements for the 15 month period ended December 31, 2006 and year ended September 30, 2005, together with the notes related thereto. The Company's financial statements have been prepared in accordance with Canadian generally accepted accounting principles. The information has been prepared effective April 16, 2007.

**FORWARD-LOOKING STATEMENTS**

Certain statements contained in this management discussion and analysis ("MD&A") include statements which contain words such as "anticipate", "could", "should", "expect", "seek", "may", "intend", "likely", "will", "believe" and similar expressions, statements relating to matters that are not historical facts, and such statements of our beliefs, intentions and expectations about development, results and events which will or may occur in the future, constitute "forward-looking information" within the meaning of applicable Canadian securities legislation and are based on certain assumptions and analysis made by us derived from our experience and perceptions. Forward-looking information in this MD&A includes, but is not limited to: future oil and gas prices and well production performance, exploitation and exploration successes, continued availability of capital and financing, and general economic, market or business conditions.

Actual results, performance or achievements could differ materially from those expressed in, or implied by, this forward-looking information and, accordingly, no assurance can be given that any of the events anticipated by the forward-looking information will transpire or occur, or if any of them do, what benefits will be derived there from. Except as required by law, Excelsior disclaims any intention or obligation to update or revise any forward-looking information, whether as a result of new information, future events or otherwise.

The forward-looking information contained herein is expressly qualified by this cautionary statement.

**OVERVIEW**

On September 6, 2006, Qeva Group Inc. ("Qeva") and Excelsior Energy Limited ("Excelsior Ltd.") amalgamated under the provisions of the Alberta Business Corporations Act and pursuant to the Amalgamation Agreement. Under the terms of the Amalgamation Agreement, Qeva and Excelsior Ltd. continued as a new corporation carrying on business under the name "Excelsior Energy Limited" ("Excelsior" or "the Company").

Following completion of the amalgamation, Excelsior had 27,556,018 common shares issued and outstanding. Pursuant to the Amalgamation Agreement, Qeva shareholders received one Excelsior common share for every three Qeva common shares and Excelsior Ltd. shareholders received 1.115261 Excelsior common shares for every one Excelsior Ltd. common share. The transaction was accounted for as a net asset purchase by Qeva whereby the fair value of Excelsior Ltd.'s net assets was added to the Company's share capital, net of transaction costs. Following the amalgamation of the two companies, the directors of the Company resolved to adopt a new year-end of December 31 to conform to the most common year end of similar junior oil and gas companies and for more convenient shareholder reporting periods.

For additional information the reader should refer to the Joint Management Information Circular of Qeva and Excelsior Ltd. dated August 02, 2006, and available on SEDAR.

The Company is active in oil sands exploration and appraisal in Alberta and oil exploration and appraisal in the UK North Sea. In addition the Company has minor interests in gas production in Alberta.

Excelsior entered into a farmin agreement dated July 25, 2006, with respect to licence 1078, Block 9/3b in the UK North Sea, a farmin agreement dated August 18, 2006 with respect to Licenses 1079 and 1080, Blocks 9/12b and 9/21 and a farmin agreement dated August 18, 2006 with respect to License 1204, Blocks 9/6, 9/7, 9/8b and 9/11d all in the UK North Sea. The Company filed an amended preliminary short form prospectus on November 16, 2006 to raise a minimum of \$25,000,000 to fulfill the financial commitments of the farmin agreements and earn their farmin interests. Due to difficult market conditions the financing was not completed and the Company withdrew from the farmin agreements.

Subsequently the Company was successful in the 24<sup>th</sup> Offshore UK Licensing Round in February, 2007 and was awarded one license covering two part blocks, 16/1a and 16/6c in the UK North Sea. A number of leads have been identified and mapped in Eocene and Palaeocene aged sand reservoirs which are productive in the neighbouring West Brae Field.

Thereafter, the Company entered into a farmin agreement for oil sands exploration and appraisal in the Hangingstone Oil Sands near Fort McMurray, Alberta in February, 2007. Excelsior will ultimately hold a 52.5% working interest in 39 contiguous sections on completion of its farmin obligations. The Company's financial obligations within the farmin agreement totals \$19,300,000 payable in cash (\$14,400,000) and issuance of common shares for its 52.5% working interest.

In March, 2007 the Company completed an equity financing to fund initial capital requirements for the Hangingstone and UK North Sea prospects. The Company issued 6,257,322 common shares at \$0.30 per share and 3,018,000 flow-through common shares at \$0.40 per share for gross proceeds of \$3,089,800.

Excelsior, through its predecessor Qeva, acquired a 26.64% working interest in a petroleum and natural gas lease located in the Hastings area of Alberta effective November 4, 2005. The property contains one natural gas well producing approximately 57 mcf/d (net to Excelsior) for the 15 month period ended December 31, 2006.

The Company's strategy is to capture oil and gas appraisal and development opportunities where it can leverage Management's diverse international experience and field development expertise. This includes heavy oil reservoir engineering and development of complex fields. The scale of the oil sands resource opportunity in Alberta complements Excelsior's international portfolio.

Shares of the Company began trading on the Canadian Trading and Quotation System Inc. on September 8, 2006 under the trading symbol EXEL.

## SELECTED ANNUAL INFORMATION

	2006	2005
Gas revenue	\$193,238	\$ -
General and administrative expense	1,844,323	151,404
Net loss	(\$3,689,781)	(67,611)
Loss/share	(\$0.25)	(\$0.01)
Cash flows used in continuing operations	(1,765,071)	(142,927)
Weighted average number of shares outstanding	15,036,063	9,973,826

## RESULTS OF OPERATIONS

### *Net revenue*

Gas revenue was generated from the non-operated gas well at Hastings Alberta, which was acquired in November, 2005. The well averaged 57 mcf/d (net to Excelsior) for the 15 month period ended December 31, 2006 at an average price of \$7.38 per mcf. Crown royalties (net of Alberta royalty tax credit) of \$29,255 averaged 15% of revenue. Operating costs of \$25,853 averaged \$0.99 per mcf. Depletion for the Hastings property was calculated at a rate of \$5.41 per mcf, totalling \$141,669.

Other revenue of \$82,606 was interest income generated by funds held in short term deposits.

### *General and Administrative Expenses*

General and administrative expenses increased to \$1,844,323 for the period ended December 31, 2006 compared to \$151,404 for the year ended September 30, 2005. Excelsior changed its primary business activity in the year ended September 30, 2005 to petroleum and natural gas exploration, development and exploitation and general and administrative expenses were minimal reflecting Excelsior in the start up phase of activity, compared to the period ended December 31, 2006, which reflected 15 months of active operations. In 2006

consulting and legal services of approximately \$450,000 were provided to Excelsior for support and technical analysis of oil and gas assets pursuant to its new business development objectives. Also included in general and administrative expenses in 2006 were severance costs of \$450,000 paid to former directors and officers of Qeva and \$130,000 relating to the costs of the unsuccessful financing expensed in the fall of 2006. The Company leased office space in 2006 and incurred expenditures associated with maintaining these premises for the 15 month period ended December 31, 2006.

### ***Stock based compensation***

Stock based compensation increased to \$145,176 from \$13,680 reflecting additional option grants in 2006.

### ***Write-down of petroleum and natural gas properties***

During the period ended December 31, 2006 Excelsior was required to withdraw from a farm-in agreement to earn their working interest in a UK North Sea licence. The costs associated with this property totalling \$1,536,519 were written off.

At December 31, 2006 the ceiling test assessment for impairment of the Hastings property resulted in a write-down of \$348,267.

### ***Sale of oil and gas properties***

In the quarter ended December 31, 2005 management of Qeva decided to divest of its producing property in the Forgan West area of Saskatchewan and entered into a purchase and sale agreement that was closed in June, 2006. This property represented all producing property in 2005. Net income from these assets sold has been separately disclosed representing discontinued operations in the amount of \$75,813 in 2006 (2005 - \$52,545). A gain from the sale of the property of \$34,053 was recognized.

### ***Capital expenditures and dispositions***

Petroleum and natural gas properties increased to \$571,937 in 2006 from nil in 2005. All property costs in 2005 related to the Forgan West property sold in 2006 and were reclassified to assets held for sale. Costs in 2006 primarily reflect the acquisition of the Hastings oil and gas producing property by the Company during the year net of depletion, depreciation and impairment.

### ***Asset retirement obligation***

Asset retirement obligations increased to \$ 4,707 in 2006 from nil in 2005 as a result of selling all producing property from 2005 and reclassifying the asset retirement obligation to current liabilities of assets held for sale. The asset retirement obligation at December 31, 2006 represents the estimate for, and accumulated accretion of, the working interest in one well acquired during the period at Hastings, Alberta.

## **LIQUIDITY AND CAPITAL RESOURCES**

At December 31, 2006 the Company had working capital of \$3,921,612 (2005 - \$294,661) which included \$3,965,957 of cash and cash equivalents (2005 - \$254,035).

The Company's primary source of cash for the period ended December 31, 2006 was funds received from the sale of common shares through private placement offerings, funds received on exercise of warrants, funds received from the sale of gas from its working interest holdings in producing property at Hastings, Alberta and the sale of the Forgan West property in Saskatchewan.

At April 16, 2006 Excelsior had 38,963,433 common shares outstanding.

On March 23, 2007 the Company completed an equity financing to fund initial capital requirements for the Hangingstone and UK North Sea prospects. The Company issued 6,275,322 common shares at \$0.30 per share and 3,018,000 flow-through common shares at \$0.40 per share for gross proceeds of \$3,089,800.

There are 2,549,341 stock options and 2,017,042 warrants to purchase common shares of the Company as of April, 16, 2007.

At December 31, 2006 the Company has no debt or credit facilities. The Company has entered into an agreement for the provision of office space until November 2007.

During 2007 the Company estimates the capital requirements for the Hangingstone property and UK North Sea licence will be approximately \$19,800,000. The Company's primary source of cash for the next fiscal year will be the issuance of share capital.

## **INCOME TAXES**

The Company has loss carry-forwards totalling approximately \$2,653,913. No tax asset for the value of these losses has been recorded for accounting purposes as the Company does not believe that it currently meets the criteria of the losses being utilized being more likely than not.

## **RELATED PARTY TRANSACTIONS**

During the 15 month period ended December 31, 2006, the Company paid consulting fees in the amount of \$192,300 (2005 - \$86,461) to companies controlled by directors and officers of the Company and severance payments in the amount of \$450,000 (2005 - \$nil) were made to former directors and officers of Qeva or companies controlled by directors and officers of the Company prior to the amalgamation.

Officers and directors were issued 516,667 common shares for participation in a private placement for proceeds of \$40,000 and for settlement for services valued at \$37,499 (amount payable at September 30, 2005) during the 15 month period ending December 31, 2006.

The Company utilizes the services of a law firm of which an officer of the Company is a partner. During the period ended December 31, 2006 the Company expended \$ 133,886 (2005 - \$nil).

During the year ended September 30, 2005, the Company acquired an interest in petroleum and natural gas properties from a party related by virtue of common directors. The purchase price was \$100,000 less net revenues earned between the contractual effective date and the acquisition date for an adjusted price of \$32,796. The transaction was not in the normal course of business but was recorded at the exchange amount which was supported by an independently prepared engineering reserve report.

Included in accounts payable and accrued liabilities are amounts payable to companies controlled by a director of the Company in the amount of \$nil (2005 - \$32,500). The amount was non-interest bearing with no specific terms of repayment. The director was issued 325,000 common shares for the forgiveness of this outstanding balance of \$32,500 (note 9b iii).

## **RISK FACTORS**

The Company is exposed to a variety of business risks and uncertainties in the international petroleum industry including the uncertainty of finding reserves, developing and marketing those reserves, availability of drilling and related equipments, commodity prices, and changes in government regulations.

Excelsior addresses these risks by employing and contracting highly skilled and motivated personnel and focusing management's efforts in areas where they have existing knowledge and using current technology to assess projects and control costs. The Company will be implementing a corporate insurance program common within industry practice in 2007.

Excelsior will undertake to obtain equity financing to fund the \$14.4 million capital budget for the Hangingstone project for remaining land, related costs and a 24 well core drilling program. The equity financing required for this project will allow Excelsior to earn its 52.5% working interest pursuant to the farmin agreement. The Company's ability to raise equity financing will be subject to market conditions at that time.

## **OUTLOOK**

The Company will focus its efforts primarily on the Hangingstone Oil Sands project in 2007. In April, 2007 the seismic acquisition was completed comprising of 135 kilometres of 2D seismic data with processing expected to be completed

on or around April 30, 2007. Excelsior will undertake to obtain equity financing to fund the \$14.4 million capital budget for this project for remaining land and related costs and a 24 well core drilling program.

Excelsior anticipates initiating a program to re-process 3D seismic on its UK North Sea licence in 2007. The cost of this program is budgeted to be \$500,000.

## **SUMMARY OF QUARTERLY RESULTS**

During the preparation of the Company's annual financial statements for the 15 month period ended December 31, 2006, it was determined the measurement and classification of certain transactions/estimates during the period was incorrect and not in accordance with Canadian generally accepted accounting principles. The transactions for which restatement is required occurred, and were initially accounted for, prior to the amalgamation on September 6, 2006 and the resulting change in the management of the Company. After reviewing the nature of the transactions and considering the most appropriate treatment under Canadian GAAP, the Board of Directors, acting on the unanimous recommendation of management and the Audit Committee, approved restatement of the interim periods affected. These transactions have been accurately reflected in the audited financial statements as at December 31, 2006.

The following transactions require restatement in the period in which the transaction occurred:

- Stock based compensation expense during the period was overstated as a result of an error in the calculation of the fair value of stock options granted and warrants issued. In addition, the fair value of warrants issued in connection with various financings was incorrectly expensed instead of being applied to reduce share capital. During the period, as applicable by quarter, stock based compensation expense will be reduced by an aggregate of \$565,682, share capital will be reduced by \$397,999 and contributed surplus will be reduced by \$167,683.
- Certain fees for share issuances, and capital costs relating to a North Sea asset subsequently written off in the quarter ended December 31, 2006, all of which were expensed in the interim periods, should have been capitalized or charged against shareholders' equity. Consequently:
  - general and administrative expenses for prior quarters will be reduced by \$262,646;
  - operating costs for prior quarters will be reduced by \$46,880;
  - depletion and depreciation for prior quarters will be reduced by \$15,626;
  - share capital at December 31, 2006 will be reduced by \$47,320; and
  - petroleum and natural gas properties at December 31, 2006 were unchanged although the carrying value of the properties during the interim periods varied from those previously reported by \$277,832;

- Cash will increase and general and administrative expenses will be reduced by \$43,063 in the quarter ended September 30, 2006 resulting from a duplicate entry.
- Recognition of certain net revenues for the quarter ended September 30, 2006 was inadvertently duplicated. Consequently, for this quarter, revenue will be reduced by \$20,893, royalty expense will be reduced by \$12,330, operating costs will be reduced by \$1,518 and accounts receivable will be reduced by \$7,045.

The total cumulative effect of the foregoing adjustments for the 2006 interim periods is a \$926,852 reduction in the previously reported net loss of \$2,320,433 for the 12 month period ended September 30, 2006.

### Selected Quarterly Information

	2006 – As Originally Filed			
	Q4	Q3	Q2	Q1
Revenue	\$27,064	\$62,482	\$27,795	\$87,890
Stock based compensation expense	-	-	149,869	560,989
General and administrative expense	815,679	332,605	270,705	286,090
Cash used in operating activities	(667,873)	(351,392)	(353,014)	(204,129)
Net loss	(806,852)	(258,318)	(455,234)	(800,029)
Loss/share	(\$0.02)	(\$0.01)	(\$0.01)	(\$0.05)

	2006 – As Restated				
	Q5	Q4	Q3	Q2	Q1
Revenue	\$8,900	\$27,064	\$41,589	\$27,795	\$87,890
Stock based compensation expense	-	-	-	78,171	67,005
General and administrative expense	444,953	708,547	178,806	225,927	286,090
Cash used in operating activities	(442,483)	(560,741)	(181,965)	(292,610)	(188,503)
Net loss	(2,296,200)	(684,094)	(95,936)	(323,132)	(290,419)
Loss/share	(\$0.08)	(\$0.02)	(\$0.00)	(\$0.01)	(\$0.01)

The interim financial statements have been reclassified to conform to the presentation in the December 31, 2006 financial statements.

### DISCLOSURE CONTROLS AND PROCEDURES

Disclosure controls and procedures are defined under Multilateral Instrument 52-109 - Certification of Disclosure Controls in Issuers' Annual and Interim Filings as controls and other procedures of an issuer that are designed to provide reasonable assurance that information required to be disclosed by the issuer in its annual filings or other reports filed or submitted under securities legislation is recorded, processed, summarized and reported within the time periods specified in securities legislation and include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in its annual filings or other reports filed or submitted under securities legislation is accumulated and communicated to the issuer's management to allow timely decisions regarding required disclosure.

The Company has a small staff with varying degrees of knowledge concerning the various regulatory disclosure requirements. In many circumstances, the

various regulatory requirements are relatively new, subject to interpretation, and complex. The Company is not of sufficient size to justify a separate department or one or more staff member specialists in this area. Therefore the Company relies upon its advisors/consultants to assist it and as such they form part of the disclosure controls and procedures and in light of this, the Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of the Company's disclosure controls and procedures as of December 31, 2006 and have concluded that they are adequate and effective to ensure accurate and complete disclosure. Management intends to formalize adequate disclosure controls and procedures by designing and implementing a disclosure policy and trading policy in 2007.

## **INTERNAL CONTROLS OVER FINANCIAL REPORTING**

Internal controls over financial reporting are defined in Multilateral Instrument 52-109 as a process designed by, or under the supervision of, the chief executive officer and chief financial officer, and effected by the issuer's board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with the issuer's generally accepted accounting principles ("GAAP") and include those policies and procedures that:

- pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Company
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company, and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the annual financial statements or interim financial statements.

Excelsior's management has assessed the design of internal controls over financial reporting as at December 31, 2006 and have identified certain material weaknesses which are as follows:

- lack of adequate procedures and documentation of internal controls to ensure records were maintained in reasonable detail to fairly reflect the transactions of the Company
- due to the limited number of staff at Excelsior it is not possible to achieve segregation of incompatible functions
- Excelsior's information systems are subject to general control deficiencies including the lack of effective controls over system access, change management, back-up procedures, spreadsheets and documentation, and
- Excelsior does not have the in-house expertise to deal with complex taxation, accounting and reporting issues

These weaknesses in internal controls over financial reporting result in a more than remote likelihood that a material misstatement would not be prevented or detected. Excelsior has limited human resources to design and establish internal controls over financial reporting and relies on management and the Board of Directors to mitigate the risks of material misstatement through close scrutiny of all related activities to compensate for the weaknesses in internal controls. However, we do not have reasonable assurance that this risk can be reduced to a remote likelihood of a material misstatement. Management intends to remediate these weaknesses when the Company's growth in human resources allows.

#### **ADDITIONAL INFORMATION**

Additional information about Excelsior and its business activities is available on SEDAR at [www.sedar.com](http://www.sedar.com).