

Loon Energy Corporation
Management's Discussion and Analysis
For the three and nine months ended September 30, 2011 and 2010
(US\$, unless otherwise stated)

This Management's Discussion and Analysis ("MD&A") document dated November 29, 2011 is provided by the management of Loon Energy Corporation ("Loon Corp" or "Company") and should be read in conjunction with the unaudited condensed consolidated financial statements for the three and nine months ended September 30, 2011 and September 30, 2010, and the audited consolidated financial statements for the years ended December 31, 2010.

Basis of Presentation

This MD&A is prepared using United States dollars ("US Dollars") which is the reporting currency of the Company. The condensed interim consolidated financial statements for September 30, 2011 are prepared in accordance with IAS 34 Interim Financial Reporting and do not include all of the information required for full annual financial statements. Production and reserves are presented on a before royalties basis consistent with Canadian reporting protocol.

Overview

Loon Energy Corporation is an international oil and gas exploration and development company with management offices in Calgary, Alberta, Canada and in Dubai, United Arab Emirates. Loon Corp was incorporated pursuant to the provisions of the *Business Corporation Act* (Alberta) ("ABCA") on October 30, 2008 to receive certain of the oil and gas assets of Loon Energy Inc. ("Loon") in accordance with a Plan of Arrangement ("Arrangement") under the ABCA. Pursuant to the Arrangement, the assets of Loon in Colombia and Peru were transferred to Loon Corp, each Loon shareholder received one common share of Loon Corp for each Loon share held, the common shares of Loon Corp were listed on the TSX Venture Exchange under the symbol LNE and Loon received \$3.15 million of cash. The implementation of the Arrangement on December 10, 2008 also resulted in Loon changing its name to Kulczyk Oil Ventures Inc. ("Kulczyk Oil").

Operations Overview

Colombia

Buganviles Association Contract

Through a farm-in agreement, the Company earned a 20% non-operated participating interest in a 60,817 hectare block of land covered by the Buganviles Association Contract between Holywell Resources S.A. and Empresa Colombiana de Petróleos ("Ecopetrol"), the Colombian national oil company. The Company earned its interest by paying \$1.0 million of the estimated \$3.4 million "dry-hole" cost of the Delta-1 well plus 20% of costs incurred thereafter. The Company has fulfilled its required work commitments with respect to this contract area. The Delta-1 well came on production late in September 2008. Ecopetrol approved the Operator's Commerciality Application in March 2009. The license for the Buganviles Association Contract has been extended as a result of the production history on the license.

During fiscal 2010, Loon Corp entered into a farm-out agreement with Petrodorado South America S.A. ("Petrodorado") under which Petrodorado agreed to pay Loon Corp's 20% share of the authorized cost to drill and complete two wells in Colombia to earn 75% (net 15%) of Loon Corp's interest in the Buganviles Association Contract, excluding the Delta-1 well. The farm-out agreement included an option for the Company to re-acquire a reversionary interest. The exercise of this option by the Company in November 2010 reduced the working interest earned by Petrodorado from net 15% to net 10%. As a result, at September 30, 2011, Loon Corp holds a net 10% working interest in the Buganviles Association Contract area.

On October 16, 2010, the first of the wells, the Visure-1X exploratory well, commenced drilling and significant oil was encountered in the Lower Guadalupe Formation. The well was perforated and stabilized before being suspended, pending the results of production test analysis. Depending on the results of the production test analysis, the Company will consider a test in the Upper Guadalupe and Barzalosa Formations. The Operator and the joint venture partners are evaluating thermal and chemical production techniques to best develop the discovery in the Lower Guadalupe Formation. The costs to drill Visure-1X have been paid by Petrodorado.

The second well, the Tuqueque-1X exploratory well, commenced drilling in the fourth quarter of 2010, but operations on the Tuqueque-1X well were terminated at a depth of 9,303 feet and plans to deepen the well to 11,300 feet were suspended after encountering drilling challenges. The petrophysical evaluation of the upper part of the well indicated three prospective



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intervals, but testing in 2011 found no appreciable flow of hydrocarbons. The well has been suspended pending further analysis of the testing results. The Operator plans to complete the abandonment of the well by May 2012.

The Montserrat Formation has potential net pay of 31 feet and is planned to be tested in an updip drilling location. The Company's share of the budgeted costs to drill the Tuqueque-1X well is approximately \$1.4 million, which will be paid by Petrodorado. The Company's remaining authorized costs to drill Tuqueque-1X is \$232,708. The Company has recorded a receivable from Petrodorado for the \$232,708 under the farm-out agreement in respect of the amount payable to the Colombian Operator.

The Buganviles Association Contract lands are located in the Upper Magdalena Valley area of central Colombia.

Peru

In 2010, the Operator, Compañía Española de Petróleos, S.A. ("CEPSA"), and Loon decided to not enter into the second exploration phase and withdraw from Block 127. All petroleum and natural gas property expenditures related to Block 127 were fully written off in 2010. CEPSA and the Company are currently executing an abandonment plan for Block 127. All abandonment activities are expected to be completed in 2012.

Selected quarterly information

Working capital (deficiency)	Periods ended September 30,	
	2011	2010
Current assets	\$ 580,577	\$ 3,460,753
Current liabilities	(598,209)	(2,399,614)
	<u>\$ (17,632)</u>	<u>\$ 1,061,139</u>

Operations Overview	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
General and administrative	\$ 63,148	\$ 179,381	\$ 336,089	\$ 290,786
Stock based compensation	149,800	-	404,875	-
Loss on foreign exchange	264	33,064	5,991	56,574
Depreciation and accretion	699	1,608	1,462	4,778
Impairment of petroleum and natural gas properties	-	1,116,805	-	1,116,805
Income tax (recovery)	-	(121,786)	-	(121,786)
Net loss	<u>(213,911)</u>	<u>(1,209,072)</u>	<u>(748,417)</u>	<u>(1,347,157)</u>
Net loss per share - basic & diluted	<u>\$ (0.00)</u>	<u>\$ (0.01)</u>	<u>\$ (0.01)</u>	<u>\$ (0.01)</u>

	As at September 30,	
	2011	2010
Total assets	<u>\$ 1,112,734</u>	<u>\$ 3,596,003</u>
Decommissioning obligation	<u>\$ 326,964</u>	<u>\$ 214,571</u>

General and Administrative Expenses

The general and administrative expenses for the three and nine months ended September 30, 2011 were \$63,148 and \$336,089, respectively, compared to \$179,381 and \$290,786 for the comparative three and nine months ended September 30, 2010. The general and administrative expenses are lower in the current quarter of 2011 as a result of decreased activities



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for the Company compared to the same quarter in 2010. The general and administrative expenses are higher for the nine months ended September 30, 2011 as compared to the same period ended September 30, 2010 as a result of increased professional fees due to the conversion to IFRS.

Stock based compensation

Stock based compensation expense for the three and nine month periods ended September 30, 2011 were \$149,800 and \$404,875, respectively, (2010: \$nil). The stock based compensation for the nine months ended September 30, 2011, arises from the issuance of options granted to Directors and other key individuals of the Company on November 29, 2010.

Decommissioning obligation

Accretion expense for the three and nine months ended September 30, 2011 was \$699 and \$1,462, respectively (2010: \$1,608 and \$4,778). As of December 31, 2010, the Peruvian and Colombian assets were fully accreted with the exception of the Ventilador, Visure and Tuqueque properties in Colombia. The accretion to the decommissioning obligation for these remaining properties will be recognized over the next 4 years.

Depletion and impairment

Depletion is not taken on the petroleum and natural gas assets until such time as commercial production resumes. No impairment was required for the Buganviles contract area as sufficient probable reserves exist to support the carrying amount of the asset.

Evaluation and Exploration Expenditures

There were no Evaluation and Exploration or Property and Equipment cash expenditures for the three and nine months ended September 30, 2011. The changes in the reported balances resulted from the recognition of the exercise of the 5% working reversionary interest buy-back of the Colombian assets for \$343,337 (December 31, 2010: nil). The Company's share of costs to drill the Tuqueque-1X well are paid by Petrodordo under a farm-out agreement. An additional \$40,000 of decommissioning obligations was recognized for the Visure and Tuqueque properties held in Colombia.

Summary of Quarterly Data

The following tables set forth selected quarterly financial information for the most recent eight financial quarters.

	<u>Q3 2011</u>	<u>Q2 2011</u>	<u>Q1 2011</u>	<u>Q4 2010</u>
Petroleum and natural gas sales	\$ -	\$ -	\$ -	\$ -
Net loss	\$ (213,911)	\$ (280,844)	\$ (253,662)	\$ (1,174,677)
Per share - basic and diluted	\$ (0.01)	\$ (0.00)	\$ (0.00)	\$ (0.01)

	<u>Q3 2010</u>	<u>Q2 2010</u>	<u>Q1 2010</u>	<u>Q4 2009</u> <u>GAAP</u>
Production per day				
<i>Oil and NGL's (bbls)</i>	-	-	-	1
Petroleum and natural gas sales	\$ -	\$ -	\$ -	\$ 8,768
Net loss	\$ (1,209,072)	\$ (85,488)	\$ (52,597)	\$ (269,255)
Per share - basic and diluted	\$ (0.01)	\$ (0.00)	\$ (0.00)	\$ (0.01)

During the three months ended September 30, 2011, the Company recognized \$149,800 of stock based compensation expense with respect to 9,580,000 options issued during the fourth quarter of fiscal 2010. General and administrative expenses for the three months ended September 30, 2011, included legal fees, \$14,000 of management fees and \$3,000 of shared services expenses.



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During the three months ended June 30, 2011, the Company recognized \$126,728 of stock based compensation expense with respect to 9,580,000 options issued during the fourth quarter of fiscal 2010. General and administrative expenses for the three months ended June 30, 2011, included \$52,000 of audit and legal fees, \$14,300 of management fees and \$6,000 of insurance premium expenses.

During the three months ended March 31, 2011, the Company recognized \$128,347 of stock based compensation expense with respect to 9,580,000 options issued during the fourth quarter of fiscal 2010 and \$79,000 of audit fees.

During the fourth quarter of 2010, there were a number of activities the Company engaged in which resulted in higher expenses. The Company issued shares in lieu of salaries with an associated cost of \$441,790. Stock options were issued to senior management and directors with an associated cost of \$423,939 and there was an increased general and administrative activities in connection with the unsuccessful negotiations with Petrodorado regarding what was eventually a failed business combination.

The increase to the net loss in Q3 2010 compared to Q2 2010 is due to the impairment of Peruvian petroleum and natural gas properties (\$1,116,805) and costs associated with a proposed business combination transaction.

The decrease in the net loss in Q1 and Q2 2010 compared to the respective prior quarters was the result of suspended production and decreased corporate activities.

Share Data

The Company is authorized to issue an unlimited number of common shares of which 99,491,364 common shares were outstanding as at September 30, 2011. There was no change to issued share capital as at November 29, 2011.

The Company is also authorized to issue an unlimited number of preferred shares; there are no preferred shares outstanding.

	Number of Shares	Carrying amount
Common Shares		
Balance at December 31, 2009	95,991,364	\$ 15,139,980
Shares issued for compensation	3,500,000	451,256
Balance at December 31, 2010 and September 30, 2011	<u>99,491,364</u>	<u>\$ 15,591,236</u>

	Nine months ended September 30, 2011	2010
Weighted average number of shares outstanding	99,491,364	95,991,364

On November 25, 2010, a total of 3,500,000 shares were issued as compensation for services rendered by certain Officers and Directors of the company.

The following table summarizes information about the share purchase options outstanding as at September 30, 2011:

	Options Outstanding	Weighted Average Exercise Price	Weighted Average Contractual Life (years)
Balance outstanding, December 31, 2009	-	\$ -	-
Options granted	9,580,000	0.13	4.2
Balance outstanding, December 31, 2010 and September 30, 2011	<u>9,580,000</u>	<u>\$ 0.13</u>	<u>4.2</u>



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Related Party Transactions

The Company has no employees, and management and administrative services are provided by the management and staff of Kulczyk Oil pursuant to a services agreement. Administrative costs incurred by Kulczyk Oil for the benefit of the Company are allocated to the Company based on specific identification and an allocation of administrative costs that relate to both Kulczyk Oil and the Company. For the three and nine months ended September 30, 2011, these fees totalled \$2,991 and \$9,186 respectively (2010 - \$3,359 and \$9,450). At September 30, 2011, the Company owed \$5,000 (2010 - \$1,050) to Kulczyk Oil for these services. Certain expenditures of the Company are paid for by Kulczyk Oil on behalf of the Company and as at September 30, 2011 the Company owed \$31,000 (2010 - \$7,217) for these costs. Kulczyk Oil and Loon Energy are related as they have four common directors and officers and the same principal shareholder.

Kulczyk Oil remains legally responsible for a guarantee issued in August 2007 ("the **Loon Peru Guarantee**") to the Government of Peru regarding the granting of the Block 127 license contract to Loon Peru Limited, a wholly-owned subsidiary of the Company. The Company has entered into an indemnification agreement with Kulczyk Oil in respect of the Loon Peru Guarantee. The transfer of the Loon Peru Guarantee from Kulczyk Oil to the Company requires the formal approval of the Government of Peru which has not yet been obtained. The Company has fulfilled its work commitments under the first phase of the exploration program, and the Company and its partners in the Block announced on October 25, 2010 that the joint venture will not proceed to the second exploration phase.

The above related party transactions were recorded at exchange amounts agreed to by both parties which approximate fair value.

Liquidity and Capital Resources

The Company is an oil and gas exploration and development company with properties principally located in Colombia. Of the Company's properties in Colombia, the Delta-1 well is in the development stage with two other wells in the exploration stage. The properties have no proved reserves at September 30, 2011. The Company does not generate sustained, commercial production from operations.

The Company's consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and settlement of liabilities in the normal course of business and do not reflect adjustments that would otherwise be necessary if the going concern assumption was not valid. To date, the Company's exploration and development operations have been financed by way of equity issuances and by farm-out arrangements with third parties who pay for all or a portion of the Company's expenditures to earn a portion of the Company's ownership interests. The Company's cash and existing farm-out arrangements are not sufficient to fund the exploration and development program over the next twelve months. Additional equity or farm-out arrangements will be required to fund the exploration and development program and there are no guarantees that additional equity or farm-out arrangements will be available when needed.

Forward Looking Statements

This MD&A contains forward-looking statements. These statements relate to future events or future performance of the Company. When used in this MD&A, the words "may", "would", "could", "will", "intend", "plan", "anticipate", "believe", "estimate", "predict", "seek", "propose", "expect", "potential", "continue", and similar expressions are intended to identify forward-looking statements. These statements involve known and unknown risks, uncertainties, and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements. Such statements reflect the Company's current views with respect to certain events, and are subject to certain risks, uncertainties and assumptions. Many factors could cause the Company's actual results, performance, or achievements to vary from those described in this MD&A. Should one or more of these risks or uncertainties materialize, or should assumptions underlying forward-looking statements prove incorrect, actual results may vary materially from those described in this MD&A as intended, planned, anticipated, believed, estimated, or expected. Specific forward-looking statements in this MD&A, among others, include statements pertaining to the following:

- factors upon which the Company will decide whether or not to undertake a specific course of action;
- world-wide supply and demand for petroleum products;



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- expectations regarding the Company's ability to raise capital;
- treatment under governmental regulatory regimes; and
- commodity prices.

With respect to forward-looking statements in this MD&A, the Company has made assumptions, regarding, among other things:

- the impact of increasing competition;
- the ability of farm-out partners to satisfy their obligations;
- the Company's ability to obtain additional financing on satisfactory terms; and
- the Company's ability to attract and retain qualified personnel.

The Company's actual results could differ materially from those anticipated in these forward-looking statements as a result of the risk factors set forth below and elsewhere in this MD&A:

- general economic conditions;
- volatility in global market prices for oil and natural gas;
- competition;
- liabilities and risks, including environmental liability and risks, inherent in oil and gas operations;
- the availability of capital; and
- alternatives to and changing demand for petroleum products.

Furthermore, statements relating to "reserves" are deemed to be forward-looking statements, as they involve the implied assessment, based on certain estimates and assumptions, that the resources and reserves described can be profitable in the future.

The forward-looking statements contained in this MD&A are expressly qualified in their entirety by this cautionary statement. These statements apply only as of the date of this MD&A.

Critical Accounting Estimates

The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reported period. Actual results may differ from these estimates. Information regarding the accounting policies selected by the Company, and the critical accounting estimates used are set out in the notes to the Company's condensed consolidated interim financial statements for the three months ended March 31, 2011 and 2010.

International Financial Reporting Standards

Publicly accountable entities were required to adopt IFRS for interim and annual financial statements for fiscal years beginning on or after January 1, 2011 including comparative figures for the prior year. The Company has transitioned to IFRS effective January 1, 2011 and as such, is reporting under IFRS for the nine months ended September 30, 2011. For further IFRS disclosure, see note 5 in the condensed consolidated interim financial statements for the three and nine months ended September 30, 2011.

Internal Controls over Financial Reporting

The board of directors, through its Audit Committee, is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control. The Audit Committee meets at least annually with the Company's external auditors to review accounting, internal control, financial reporting, and audit matters. Internal controls over financial reporting have not changed significantly since the last reporting period.



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Accounting Standards and Interpretations:

The Company has applied all Standards and Interpretations issued or adopted by the International Accounting Standards Board (“IASB”) and the International Financial Reporting Interpretations Committee (“IFRIC”) of the IASB that are relevant to its operations and effective for annual reporting periods beginning on January 1, 2010. The same accounting policies have been applied for all periods presented. The following recent IFRS pronouncements have not been adopted by the Company.

Future Changes in Accounting Policies

- IFRS 10, “Consolidated Financial Statements” (“IFRS 10”) replaces IAS 27, “Consolidated and Separate Financial Statements” (“IAS 27”) and Standing Interpretations Committee (“SIC”) 12, “Consolidation – Special Purpose Entities”. IFRS 10 revises the definition of control and focuses on the need to have power and variable returns for control to be present. IFRS 10 provides guidance on participating and protective rights and also addresses the notion of “de facto” control. It also includes guidance related to an investor with decision making rights to determine if it is acting as a principal or agent.
- IFRS 11, “Joint Arrangements” (“IFRS 11”) replaces IAS 31, “Interest in Joint Ventures” (“IAS 31”) and SIC 13, “Jointly Controlled Entities – Non-Monetary Contributions by Venturers”. IFRS 11 defines a joint arrangement as an arrangement where two or more parties have joint control. A joint arrangement is classified as either a “joint operation” or a “joint venture” depending on the facts and circumstances. A joint operation is a joint arrangement where the parties that have joint control have rights to the assets and obligations for the liabilities, related to the arrangement. A joint operator accounts for its share of the assets, liabilities, revenues and expenses of the joint arrangement. A joint venturer has the rights to the net assets of the arrangement and accounts for the arrangement as an investment using the equity method.
- IFRS 12, “Disclosure of Interest in Other Entities” (“IFRS 12”) replaces the disclosure requirements previously included in IAS 27, IAS 31, and IAS 28, “Investments in Associates”. It sets out the extensive disclosure requirements relating to an entity’s interests in subsidiaries, joint arrangements, associates and unconsolidated structured entities. An entity is required to disclose information that helps users of its financial statements evaluate the nature of and risks associated with its interests in other entities and the effects of those interests on its financial statements.
- IFRS 13, “Fair Value Measurement” provides a consistent and less complex definition of fair value, establishes a single source for determining fair value and introduces consistent requirements for disclosures related to fair value measurement. IFRS 13 is effective for annual periods beginning on or after January 1, 2013 and applies prospectively from the beginning of the annual period in which the standard is adopted. Early adoption is permitted. The Company is currently evaluating the impact of adopting IFRS 13 on its Consolidated Financial Statements.
- IAS 27, “Separate Financial Statements” has been amended to conform to the changes made in IFRS 10 but retains the current guidance for separate financial statements.
- IAS 28, “Investments in Associates and Joint Ventures” has been amended to conform to the changes made in IFRS 10 and IFRS 11.

The above standards are effective for annual periods beginning on or after January 1, 2013. Early adoption is permitted. The Company is currently evaluating the impact of adopting these standards on its Consolidated Financial Statements.

Management is currently assessing the impact of these standards.

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Approval

The Company's Board of Directors has approved the disclosure contained within this MD&A on November 29, 2011.

Additional Information

Additional information regarding the Company and its business and operations is available on the Company's profile at www.sedar.com. Copies of the information can also be obtained by contacting the Company at Loon Energy Corporation 1170, 700 – 4th Avenue S.W., Calgary, Alberta, Canada T2P 3J4 (Phone: +1 403 264-8877) or by e-mail at rvaniw@loonenergy.com.

