



MANAGEMENT'S DISCUSSION & ANALYSIS
FOR THE THREE MONTHS AND YEAR ENDED DECEMBER 31, 2009

CANELSON DRILLING INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS

(Stated in thousands, except: for per share amounts; number of drilling rigs; and meters)

As of March 1, 2010

This Management's Discussion and Analysis ("MD&A") for CanElson Drilling Inc. and all of its subsidiaries and joint venture ("CanElson" or the "Corporation") should be read in conjunction with the consolidated financial statements and the notes thereto. The Corporation prepared its consolidated financial statements for the year ended December 31, 2009 in accordance with Canadian generally accepted accounting principles ("GAAP"). All financial measures presented in this MD&A are expressed in Canadian dollars unless otherwise indicated. Additional information regarding the Corporation is available on SEDAR at www.sedar.com.

OVERVIEW

The Corporation is engaged in the manufacture, acquisition and operation of drilling rigs for the oil and gas industry. The Corporation currently operates in the western Canadian sedimentary basin (the "WCSB"), the United States and Mexico. The Corporation's WCSB operations are currently focused in Alberta. The United States operations are currently focused in the Permian Basin in west Texas. The Corporation's Mexico operations are conducted through a joint venture Company, Diavaz CanElson de Mexico, S.A. de C.V. ("DCM" or the "Joint Venture"), of which CanElson holds a 50% ownership interest, and are currently focused in the Misantla-Tampico Basin of Mexico.

2009 was a challenging year for the drilling industry with rig counts in Canada and the United States significantly below record highs of recent years. The Corporation's relative size and strong balance sheet at the start of 2009 permitted CanElson to organically grow its domestic and international operational capabilities and take advantage of specific asset acquisitions. During 2009 the Corporation commenced operations in two new jurisdictions, the United States and Mexico, and expanded its drilling rig fleet by constructing two heavy duty telescopic drilling rigs and acquiring two heavy duty telescopic drilling rigs with top drives, one single drilling rig with a top drive and one free standing (internal guy wired) service rig. During the first quarter of 2010, the Corporation sold the single drilling rig for cash proceeds of \$650. At the date of this MD&A, the Corporation was operating 4 drilling rigs in the WCSB, 2 drilling rigs in west Texas, 2 (net: 1) drilling rigs and 1 (net: 0.5) service rig in the Misantla-Tampico Basin in Mexico. The growth in operational capabilities in Canada, the United States and Mexico has positioned CanElson for future growth in operating activities during 2010.

SELECTED ANNUAL INFORMATION

For the year ended December 31, 2009 and period from incorporation June 30, 2008 to December 31, 2008	2009	% Increase (Decrease)	2008
Revenue	\$6,631	1290%	\$477
EBITDA ⁽ⁱ⁾	\$798	575%	(\$168)
Net and comprehensive income (loss)	(\$401)	-3185%	\$13
Net and comprehensive income (loss) per share			
Basic	(\$0.02)	nm	\$0.00
Diluted	(\$0.02)	nm	\$0.00
Funds flow ⁽ⁱⁱ⁾	\$938	517%	\$152
Current assets	\$7,826	-68%	\$24,500
Total assets	\$54,540	20%	\$45,400
Accounts payable and accrued liabilities	\$6,348	111%	\$3,007
Current portion of bank debt	\$935	nm	\$nil
Bank debt	\$4,065	nm	\$0
Weighted average diluted shares outstanding	26,389	30%	20,236

nm – calculation is not meaningful

NON-GAAP MEASURES

This MD&A contains references to EBITDA and funds flow. These financial measures are not measures that have any standardized meaning prescribed by GAAP and are therefore referred to as non-GAAP measures. The non-GAAP measures used by the Corporation may not be comparable to similar measures used by other companies.

- (i) EBITDA is defined as “income before interest expense (income), income taxes, depreciation and stock based compensation expense.” Management believes that in addition to Net and comprehensive income (loss), EBITDA is a useful supplemental measure as it provides an indication of the results generated by the Corporation’s principal business activities prior to consideration of how these activities are financed, how the results are taxed in various jurisdictions, or how the results are affected by the accounting standards associated with the Corporation’s stock based compensation plan.

	2009	2008
Income (loss) before taxes	\$ (290)	\$ 13
Interest and other income	(146)	(320)
Depreciation	517	40
Stock-based compensation	717	99
EBITDA	\$ 798	\$ (168)

- (ii) Funds flow from operations is defined as “cash provided by operating activities before the change in non-cash working capital”. Funds flow from operations is a measure that provides shareholders and potential investors additional information regarding the Corporation’s liquidity and its ability to generate funds to finance its operations. Management utilizes this measurement to assess the Corporation’s ability to finance operating activities and capital expenditures.

	2009	2008
Net Income (loss)	\$ (401)	\$ 13
Non-cash items:		
Unrealized foreign exchange gain	(6)	-
Depreciation	517	40
Stock-based compensation	717	99
Future income taxes	111	-
Funds flow	\$ 938	\$ 152

2009 compared with 2008

The Corporation recorded a net and comprehensive loss of \$401 (\$0.02 per share) compared to net and comprehensive income of \$13 (\$0.00 per share) during the period ended December 31, 2008. 2009 EBITDA and funds flow of \$798 and \$938, respectively, increased from the 2008 period EBITDA and funds flow of (\$168) and \$152, respectively.

During the period from incorporation, June 30, 2008, to December 31, 2008, the Corporation completed construction of one drilling rig and had commenced construction of two additional drilling rigs and conducted operations for 19 operating days in the WCSB. This compares to 243 operating days in the WCSB 2009, 10 operating days in west Texas and the Corporation's subcontracted rigs operating in Mexico commenced operation on November 22, 2009. As a result, the Corporation's comparative 2008 period operations vary significantly from the 2009 year. In 2008 there were no operations in Mexico and the United States.

REVENUE AND OPERATING EXPENSE

The Corporation operates in two geographic segments within one industry segment. Oilfield services are provided in the domestic operating segment (Canada) and the foreign operating segment (United States and Mexico).

	December 31,			
	2009	2008	Change	% Change
Revenue				
Domestic	\$ 5,546	\$ 477	\$ 5,069	1063%
Foreign	1,085	0	1,085	nm
	6,631	477	6,154	1290%
Operating expenses	3,895	223	3,672	1647%
	\$ 2,736	\$ 254	\$ 2,482	977%
Gross margin	41%	53%	-12%	-23%
Operating days (spud to rig release)	⁽ⁱ⁾ 253	19	234	1232%
Revenue per operating day	\$ 26.21	\$ 25.11	1	4%

(i) Operating days includes only those operating days for the Corporation's owned drilling rigs and excludes the subcontracted drilling rigs conducting operations in Mexico.

Revenue recorded during the year ended 2009 increased significantly compared to 2008 as a result of an expanded rig fleet and a full year of operations. During 2009, the Corporation had available for operation an average of 2.3 (net: 2.2) drilling rigs which Corporation utilized to generate significantly more revenue. During 2008, the Corporation had an average 0.1 drilling rigs available for operation.

The Corporation achieved a gross margin of 41% during 2009. Drilling rates in Canada trended downward during 2009 which contributed to an overall lower gross margin in 2009 relative to 2008. In addition, foreign operating segment contracts are integrated service contracts which include additional flow through costs that the Corporation pays on behalf of the customer. Comparatively, in Canada the customer traditionally pays for these costs. For this reason, both revenue and operating expenses on an individual rig will be higher in these geographic segments compared to Canada which will result in lower percentage gross margins relative to Canada's percentage gross margin.

Revenue per operating day averaged increased in 2009. The increase is primarily attributable to DCM's revenues earned which are earned on subcontracted drilling rigs the Corporation does not own.

Domestic Segment

	2009	2008	Change	Change %
Drilling rigs				
Opening balance	1	-		
Construction	1	1		
Acquisition	2	-		
Ending Balance	4	1	3	300%
Operating days (spud to rig release)	243	20	223	1115%
Utilization	32%	100%	-68%	-68%

As the Canadian drilling market deteriorated during 2009 the Corporation continued to assess corporate and asset acquisition opportunities. The Corporation's strong balance sheet provided the liquidity necessary for the Corporation to acquire two 3600 meter heavy duty telescopic drilling rigs with top drives. The timing of the acquisitions allowed the Corporation to immediately deploy the newly acquired rigs with the first acquired rig going to work immediately at the end of November and the second acquired rig going to work immediately at the end of December. This has positioned the Corporation to take advantage of the 2010 winter drilling season with the newly acquired rigs.

Foreign Segment

	2009	2008	Change	Change %
Drilling rigs				
Opening balance	-	-		
Subcontracted (gross: 2; net: 1)	1	-		
Construction	1	0		
Ending Balance	2	0	2	nm
Operating days (spud to rig release)	⁽ⁱ⁾ 10	0	10	nm
Utilization	100%	0%	100%	nm

(i) Operating days includes only those operating days for the Corporation's owned drilling rigs and excludes the sub-contracted drilling rigs conducting operations in Mexico.

As at the date of this MD&A, the Corporation signed performance based integrated drilling contracts for three drilling rigs to operate in the United States. The first drilling rig was constructed in Q4 2009 and moved to west Texas and commenced drilling operations on December 21, 2009. The second drilling rig was previously constructed in 2009 for operation in Canada and has subsequently been retrofitted for operation in west Texas and was deployed in west Texas in January 2010. It is expected that construction of the third United States drilling rig will be completed in March 2010 for deployment in April 2010. The west Texas area does not traditionally have seasonal operating restrictions; therefore, the Corporation anticipates that its west Texas rig fleet will operate during all 12 months in a calendar year. The west Texas operations were in the start-up phase during 2009 and the Corporation expects the west Texas operations to continue through a start-up phase during the first quarter of 2010 with expected operational efficiencies to be achieved during the second quarter.

During 2009, the Corporation entered into a joint venture agreement with a Mexico based oil and gas services company, formed the Mexican joint venture company DCM and signed 2 performance based integrated drilling rig contracts. Subsequent to DCM signing the drilling rig contracts, DCM entered into an agreement to subcontract 2 drilling rigs from a third party oil and gas services company that had been operating the drilling rigs in the Misantla-Tampico Basin area of Mexico. DCM commenced start-up drilling operations with effect from November 22, 2009. During Q1 2010, DCM commenced service rig operations with 1 service rig operating at the date of this MD&A and a second service rig is expected to

commence operating prior to the end of Q1 2010. The first service rig was contributed by the 50% joint venture partner and CanElson expects to contribute the recently acquired service rig to DCM by the end of Q1 2010. DCM's operations were in the start-up phase during 2009 and the Corporation expects DCM's operations to continue through a start-up phase during the first quarter of 2010.

DEPRECIATION

	2009	2008	Change	Change %
Depreciation	\$ 517	\$ 40	\$ 477	1193%

Substantially all of the Corporation's property and equipment is depreciated based on rig operating days. For this reason, the Corporation's depreciation expense increased significantly as a result of increased operating days in 2009 compared to 2008 as previously discussed.

GENERAL & ADMINISTRATION

	2009	2008	Change	Change %
General & Administration	\$ 1,959	\$ 422	\$ 1,537	364%
Percent of revenue	30%	88%		

General & Administration expense ("G&A") increased significantly from 2009 as a result of a full year of operations, an increase in operational and support staff to support the growing domestic and international operations and significant professional fees associated with establishing international operations. CanElson anticipates G&A will increase in 2010 with the growing operations, however, G&A as percent of revenue is anticipated to decrease.

STOCK BASED COMPENSATION

	2009	2008	Change	Change %
Stock based compensation	\$ 717	\$ 99	\$ 618	624%

The Corporation has an employee stock option plan that provides all option holders the right to common shares for the options exercised. The Corporation follows the fair value method for accounting, using the Black-Scholes option pricing model, whereby compensation expense is recognized for the stock options on the date of grant, and amortized over the option's vesting period. The Corporation's stock based compensation expense increased significantly as a result of a full years operations and a significant increase in office and field employees resulting in additional options being granted.

INTEREST AND OTHER INCOME

	2009	2008	Change	Change %
Interest and other income	\$ 146	\$ 320	\$ (174)	-54%

The Corporation earns interest income on its cash and cash equivalents. At December 31, 2009, the Corporation held no cash equivalents. The Corporation earned significantly less interest income during 2009 as a result of a lower average cash balance and lower average interest rates in 2009 compared to 2008.

INCOME TAXES

	2009	2008	Change	Change %
Current	\$ -	\$ -	\$ -	nm
Future	111	-	111	nm
Income taxes	\$ 111	\$ -	\$ 111	

The Corporation has operations in three jurisdictions and is thus subject to tax rates in Canada, the United States and in Mexico. To date, the Corporation has not paid or accrued any current income taxes. The Corporation has recognized a future income tax expense in relation to its Canadian operating entity. No future income tax reduction has been recognized for the Corporation's United States operating entity, additionally the Corporation has not recognized future tax assets in relation to the Corporation's United States operating entity as there is uncertainty as to the timing and reversal of the related future tax assets. The Corporation's Mexico operating entity has no current period future or current income tax expense nor any related future income tax assets or liabilities at December 31, 2009. The Corporation has available for deduction against future taxable income non-capital losses of approximately \$127.

LIQUIDITY AND CAPITAL RESOURCES

Cash Flows Relating to Operating Activities and Working Capital

	2009	2008	Change	Change %
Funds flow	\$ 938	\$ 152	\$ 786	517%
Changes in working capital	(111)	(1,438)	1,327	-92%
Operating cash flow	\$ 827	\$ (1,286)	\$ 2,113	-164%

The Corporation provides and uses cash flows from operating activities from the operation of drilling rigs. Funds flow increased significantly in 2009 due to a full year of drilling operations compared to only 19 days of drilling operations in 2008.

At December 31, 2009, the Corporation had an overall positive net working capital position of \$543 (2008: \$21,493). In addition, the Corporation had available an operating loan with an estimated \$2,700 (2008: \$nil) available to fund operating activities. The significant decrease in the positive working capital position is a result of the significant investing activities undertaken during 2009 related to the construction of drilling rigs.

Cash Flows Relating to Financing Activities

	2009	2008	Change	Change %
Increase in bank debt	\$ 5,000	\$ -	\$ 5,000	0%
Issuance of share capital	-	44,000	(44,000)	-100%
Share issuance costs	-	(1,996)	1,996	-100%
Financing cash flow	\$ 5,000	\$ 42,004	\$ (37,004)	-88%

During the year ended December 31, 2009 bank financing provided the Corporation \$5,000 of cash flows. The Corporation did not generate any additional cash flows from financing activities during 2009. During 2008, the issuance of shares provided the Corporation with \$42,004 of cash flows from financing activities.

As at December 31, 2009 and at the date of this MD&A, the Corporation has outstanding 26,100 common shares, 900 warrants and 1,582 options, each convertible into one common share. At December 31, 2009 the Corporation had 1,367 exercisable options and warrants, which if exercised would provide financing cash flows of \$2,332 for the Corporation.

As at December 31, 2009, the Corporation has the following bank debt available and outstanding (December 31, 2008: \$nil).

Facility	Available Amount	Outstanding at December 31, 2009	Interest rate per annum	Maturity date
<u>Loans available at December 31, 2009</u>				
Operating loan	\$ 5,000 (i)	\$ -	(ii)	due on demand
Evergreen Loan	10,000	5,000	(iii)	(iv)
<u>Additional loan made available subsequent to December 31, 2009</u>				
Capital Loan	5,000 (v)	-	(iii)	(vi)

- (i) Available amount is the lesser of \$5,000 or 75% of accounts receivable less than 90 days. Based on accounts receivable at December 31, 2009, the estimated available amount is approximately \$2,700.
- (ii) Bank debt bears interest at the bank's prime lending rate plus 1.25%, U.S. prime rate plus 1.25% or U.S. Libor rate plus 2.50%.
- (iii) Bank debt bears interest at the bank's prime lending rate plus 1.75%, U.S. prime rate plus 1.75% or U.S. Libor rate plus 3.25%.
- (iv) Advances made under the Evergreen Loan during a calendar year will require interest only payments for the calendar year of the advance, with principal repayments on a monthly five year amortization basis commencing in the subsequent calendar year.
- (v) Subsequent to December 31, 2009, the Corporation increased its credit facility arrangements and obtained an additional \$5.0 million Capital Loan under similar terms to the Evergreen Loan.
- (vi) Advances made shall be repaid on demand, unless and until otherwise demanded, \$83 of principal shall be repaid monthly commencing from the month of initial advance with the balance to be fully repaid within five years of the initial advance.

Cash Flows Relating to Investing Activities

	2009	2008	Change	Change %
Reverse takeover	\$ -	\$ 397	\$ (397)	-100%
Purchase of property & equipment	(25,959)	(20,939)	(5,020)	24%
Changes in non-cash working capital	1,474	2,541	-1,067	-42%
Investing cash flow	\$ (24,485)	\$ (18,001)	\$ (6,484)	36%

The Corporation initiates and manages the construction of drilling rigs and at December 31, 2009 the Corporation was committed to complete the retrofit of Rig 3 for deployment to west Texas with an estimated remaining expenditure of \$1.0 million. In addition, the Corporation committed to complete the construction of Rig 5 for deployment to west Texas at an estimated cost of \$7.3 million. The Corporation has not committed to any further significant capital expenditures.

During 2009 the Corporation incurred \$25,959 (2008: \$20,939) of capital expenditures related to rig construction and asset acquisitions. During 2009, the Corporation started and or completed construction of two heavy duty 3600 meter telescopic double rigs and incurred various other construction and capital projects at an estimated cost of \$13,359. In addition, the Corporation made two asset acquisitions during the fourth quarter of 2009. The first asset acquisition resulted in the Corporation acquiring a heavy duty 3600 meter telescopic double rig with a top drive, one 1200 meter single rig and other rig equipment for cash consideration of \$6,500. Subsequent to December 31, 2009, the Corporation sold the 1200 meter single rig for cash proceeds of \$650. The disposition of the single rig is consistent with the Corporation's objective for its domestic operating segment of having available a domestic drilling rig fleet capable of drilling deep horizontal wells. In the second acquisition, the Corporation acquired for cash consideration of \$6,000 a heavy duty 3600 meter telescopic double rig with a top drive and one free standing (internal guy wired) service rig.

During the comparative 2008 period, the Corporation completed and or substantially completed the construction of two heavy duty 3600 meter telescopic double rigs and partially started construction of a third heavy duty 3600 meter telescopic double rig.

Contractual Obligations

In the normal course of business, the Company incurs contractual obligations related to vehicle and premise leases and bank debt. The minimum annual payments for contractual obligations for the next five years are as follows:

		2010	2011	2012	2013	2014	Thereafter	Total
Bank debt	(i)	\$ 1,100	\$ 1,100	\$ 1,100	\$ 1,100	\$ 1,100	\$ -	\$ 5,500
Commitments	(ii)	157	146	107	89	-	-	499
Total		\$ 1,257	\$ 1,246	\$ 1,207	\$ 1,189	\$ 1,100	\$ -	\$ 5,999

(i) Includes principal and interest. Interest has been calculated based upon debt balances and interest rates at December 31, 2009

(ii) Includes office premises and vehicle lease payments

In addition to the above contractual maturities, the Corporation has: (1) decided to complete a retrofit of one drilling rig and construct another drilling rig at a total estimated remaining cost of \$8,300 with costs expected to be incurred in 2010; and (2) sub-contracted two drilling rigs through its Mexican joint venture company for a term ending November 2010, subject to the length of the customer contract. Future payments are variable depending upon the operating performance of the drilling rigs.

SUMMARY OF QUARTERLY RESULTS

	2009				2008	
	Q4	Q3	Q2	Q1	Q4	Q3
Revenue	\$3,021	\$629	\$ Nil	\$2,981	\$477	\$ Nil
EBITDA	\$45	(\$168)	(\$491)	\$1,412	(\$168)	(\$1)
Net and comprehensive income (loss)	(\$236)	(\$295)	(\$564)	\$694	\$13	(\$1)
Net and comprehensive income (loss) per share	(\$0.01)	(\$0.01)	(\$0.02)	\$0.03	\$ Nil	\$ Nil
Funds flow	\$45	(\$97)	(\$477)	\$1,467	\$152	\$1
Current assets	\$7,826	\$17,212	\$17,510	\$19,724	\$24,500	\$439
Total assets	\$54,540	\$43,946	\$43,986	\$45,805	\$45,400	\$439
Accounts payable and accrued liabilities	\$6,348	\$630	\$546	\$2,005	\$3,007	\$28
Current portion of bank debt	\$935	\$0	\$0	\$0	\$0	\$0
Bank debt	\$4,065	\$0	\$0	\$0	\$0	\$0
Weighted average diluted shares outstanding	26,406	26,342	26,322	26,336	21,002	4,100

The seasonal operating environment of the oil and gas services industry in Canada affects the quarterly results of the Corporation. The Corporation's strongest operating results are generally expected to be in the first and fourth quarters, as was the case in 2009. Utilization rates typically decline during the second quarter as spring breakup weather conditions hinder mobility of the Corporation's equipment. It is expected that prospectively the Corporation's United States and Mexico operations will partially decrease the overall seasonality of the Corporation's operations.

Overall, in 2009 the Corporation experienced a strong first quarter as 2 drilling rigs operated in Alberta for a

significant portion of the quarter. The second and third quarters were slow due to breakup weather conditions and general weak market conditions. Net loss in the fourth quarter narrowed with the addition of gross 5 (net: 4) drilling rigs to its rig fleet in the second half of the fourth quarter. The positive effect of the increase in fourth quarter operating activity was offset by increased general and administration expenses primarily in relation to the start-up of operations in relation to the Corporation's foreign operating segment.

FOURTH QUARTER ANALYSIS

	2009	2008	Change	% Change
Revenue				
Canada	\$ 1,121	477	644	135%
Foreign	969	0	969	nm
	3,021	477	2,544	533%
Operating expenses	2,108	223	1,885	845%
	\$ 913	\$ 254	\$ 659	259%
Gross margin	30%	53%	-23%	-43%
Drilling rigs available for operation at end of period				
Domestic	4	1	3	300%
Foreign (gross: 3; net: 2)	2	-	2	nm
Ending Balance	6	1	5	500%
Drilling operating days				
Domestic	129	20	109	545%
Foreign (1)	10	0	10	nm
Utilization				
Domestic	57%	100%	-43%	-43%
Foreign	100%	0%	100%	nm

1. Operating days includes only those operating days for the Corporation's owned drilling rigs and excludes the sub-contracted drilling rigs conducting operations in Mexico.

The fourth quarter of 2009 was an active quarter for the Corporation, one which saw the commencement of operations in the United States and Mexico, the resulting from past management efforts. These efforts resulted in the Corporation establishing operations in west Texas, with the first of three contracted drilling rigs commencing operation during Q4 2009. Additionally, the Corporation's Mexican Joint Venture commenced operations with two subcontracted drilling rigs during Q4 2009. The Corporation's Canadian operations doubled its rig fleet from two to four with the acquisition of two heavy duty telescopic double drilling rigs with top drives that were immediately deployed for operation in Canada. The significant growth in operations required the Corporation to undertake a significant capital program and thus the Corporation incurred \$20,156 of capital expenditures to fund the above noted projects.

During the fourth quarter of 2009, the Corporation had operating gross 7 (net: 6) drilling rigs, compared to 1 in the fourth quarter of 2008. The result was significant quarter-over-quarter growth in revenue, EBITDA and funds flow. Net comprehensive loss for the fourth quarter of \$236 (\$0.01 per share) compares to net comprehensive income of \$13 (\$0.00 per share) for Q4 2008. The decrease in net comprehensive income quarter-over-quarter is primarily a result of increased stock based compensation expense, a significant decrease in interest income in the comparative quarter from \$319 in Q4 2008 to \$6 in Q4 2009, a significant increase in depreciation expense from \$40 in Q4 2008 to \$210 in Q4 2009 and a significant increase in general and administration expenses from \$442 in Q4 2008 to \$889 in Q4 2009.

OUTLOOK

The weak global economy continued from 2008 into 2009 but appears to have given way to modest economic recovery, in part buoyed by significant amounts of government stimulus. Both developed and developing nations seem to be predicting low to modest growth for 2010. The strength and length of the economic recovery may be affected by how long governments are willing to continue with deficits and leave stimulus programs in place. This modest economic recovery experienced in the second half of 2009 has seen oil prices recover as the price of oil seems to have found some support around \$70 per barrel. However, natural gas prices have remained low and continued to be volatile in the second half of 2009 and there remain significant diverging views as to what the 2010, and beyond, outlook for natural gas prices will be.

During the second half of 2009, we have seen an increase in customer demand and modest upward pressure on day rates. In 2010, the Canadian Association of Oilwell Drilling Contractors is predicting a modest recovery for the drilling industry. However, we believe this recovery will be magnified for drilling companies that have the ability to drill deep horizontal wells as we expect the average measured depth, and therefore the average well time, to trend upwards as our customer's capital programs are focused on deeper horizontal plays. As our modern Canadian rig fleet is capable of drilling a majority of these types of wells, we believe we are positioned to grow in the Canadian market place as the number of drilling rigs competing in this part of the Canadian drilling market is significantly less than the total Canadian rig count.

Our United States area of focus is in the west Texas area of the Permian Basin which is a mature oil basin. Our customers in the Permian Basin are focused on drilling a high volume of infill drilling locations to measured depths of approximately 3300 meters. Current oil prices support an increase in activity in this area. In particular, new work and better rates in the Permian Basin will be awarded to those drilling contractors who can compete by drilling on a performance basis.

The Mexico oil and gas services market has significant room for growth in services that help optimization of drilling and well servicing operations. In particular, we believe there is an opportunity for the application of Canadian drilling techniques in Mexico which will help reduce the total well-time and increase the speed with which new production can be brought on stream. As an oil dominated market, the Mexican market place is subject to commodity price movements.

With three established platforms for growth, a Board of Directors and management team with a wealth of knowledge and experience, a strategic Mexico Joint Venture partner, along with a commitment to field presence, highly qualified experienced drilling crews, a modern fleet of drilling rigs, opportunity for international growth and a firm resolve for Aboriginal relationships and Aboriginal workers, we believe there is significant opportunity for growth.

FINANCIAL INSTRUMENTS

Financial instruments comprised of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities and bank debt. The fair values of cash and cash equivalents, accounts receivable and accounts payable and accrued liabilities approximate their carrying amounts due to their short-term maturities. The fair value of bank debt approximates its carrying value due to the floating interest rate associated with the debt instrument.

RELATED PARTY TRANSACTIONS

For the year ended December 31, 2009 the Corporation incurred \$181 of expenses included in general and administrative expenses and property and equipment (2008: \$260 included in general administration expense and share issue costs) relating to professional services provided by a law firm of which one of the Corporation's directors is a partner. At December 31, 2009, \$70 (2008: \$47) was accrued within accounts payable and accrued liabilities.

All of the transactions occurred in the normal course of operations and are recorded at the exchange amount, which is the amount of consideration established and agreed to by the related parties

CONTINGENCY

Subsequent to December 31, 2009, the Corporation received a statement of claim from a company claiming use of confidential and proprietary information, solicitation of clients, consultants and employees by certain officers and staff of the company. No estimate of the claim can be made. The Corporation does not view the claim as having any merit; accordingly no provision for any liability is presented in these consolidated financial statements.

ACCOUNTING POLICIES AND CRITICAL ACCOUNTING ESTIMATES

Application of critical accounting estimates

The significant accounting policies used by the Corporation are disclosed in the audited financial statements for the periods ended December 31, 2009 and 2008. Certain accounting policies require that management make appropriate decisions with respect to the formulation of estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Management reviews its estimates on a regular basis. The emergence of new information and changed circumstance may result in actual results or changes to estimated amounts that differ materially from current estimates.

The accounting estimates considered to have the greatest effect on the Corporation's consolidated financial results are as follows:

Depreciation

Depreciation of the Corporation's property and equipment incorporates estimates of useful lives and residual values. These estimates may change as the Corporation establishes a longer operating history or as general market conditions change.

Long lived assets

On a periodic basis, management assesses the carrying value of long-lived assets for indications of impairment. This requires the Corporation to forecast future cash flows to be derived from utilization of these

assets based on assumptions about future operating conditions. These assumptions may change as more experience is obtained or as general market conditions change.

Accounts receivable

The Corporation is subject to credit risk on accounts receivable balances and assesses the recoverability of accounts receivable on an ongoing basis. To date the Corporation has not established an allowance for doubtful accounts for uncollectible accounts receivable balances as all accounts receivable are deemed to be collectible. Assessing accounts receivable for impairment involves significant judgment and uncertainty, including estimates of future events. Changes in circumstances underlying these estimates may result in the Corporation recognizing an allowance against accounts receivable.

Recent pronouncements

Transition to International Financial Reporting Standards

In 2006, the Canadian Accounting Standards Board (“AcSB”) published a new strategic plan that will significantly affect financial reporting requirements for Canadian companies. The AcSB strategic plan outlines the convergence of Canadian Generally Accepted Accounting Principles (“GAAP”) with International Financial Reporting Standards (“IFRS”) over an expected five-year transitional period. In February 2008, the AcSB announced that 2011 is the changeover date for publicly-listed companies to use IFRS, replacing Canada’s own GAAP. The date refers to interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. The transition date of fiscal 2011 will require restatement for comparative purposes of amounts reported by the Corporation for the 2010 fiscal year. The effect of IFRS on the Corporation’s current financial statements has not yet been determined. The Corporation will monitor any changes in both its activities and in IFRS that may effect its adoption of these standards in 2011 and has set in place a plan to progress the transition to IFRS.

The Corporation has undertaken its IFRS transition project, which includes three key phases: initial assessment; design and development; and implementation.

Initial assessment – the Corporation has established its IFRS project team and has developed a preliminary timeline to comply with the changeover date, recognizing that specific project activities and timelines may change as a result of future developments.

Design and development – the Corporation is conducting an indepth review of accounting and reporting differences and is in the process of evaluating and selecting appropriate IFRS accounting policies as well as examining potential IFRS 1 exemptions.

Implementation – This phase includes the integration of solutions into processes and accounting systems required for the conversion to IFRS and for parallel reporting required during the year of transition. Required system and process changes are planned to be completed by the end of Q2 2010. The Corporation is monitoring the International Accounting Standards Board’s active projects and all changes to IFRS prior to January 1, 2011 will be incorporated as required.

New Accounting Standards

In January 2009, the CICA issued new standards relating to business combinations (section 1582), consolidated financial statements (section 1601) and non-controlling interests (section 1602). Section 1582 will be harmonized with IFRS 3, “Business Combinations” and will require most assets acquired and liabilities assumed, including contingent liabilities to be measured at fair value and that all acquisition costs to

be expensed. Section 1602 will harmonize with the requirements of International Accounting Standard (“IAS”) 27, “Consolidated and Separate Financial Statements” and requires that non-controlling interests be recognized as a separate component of equity and that net earnings be calculated without a deduction for non-controlling interest. Section 1601 in combination with Section 1602 replaces the former consolidated statements standard (1600) and establishes standards for the preparation of consolidated financial statements. These standards are effective January 1, 2011 with early adoption permitted. Based on the Corporation’s consolidated financial statements at December 31, 2009, the Corporation does not anticipate these changes will have a material affect to its consolidated financial statements.

RISKS AND UNCERTAINTIES

There are a number of risk factors facing the Corporation. A summary of certain risk factors relating to the Corporation’s business is in the Annual Information Form filed with SEDAR, available at www.sedar.com and incorporated herein by reference. Also refer to the cautionary statement regarding “Forward-Looking Information”.

Financial Instruments Risks

Credit risk arises from the potential that a counterparty will fail to meet its obligations. The Corporation is normally exposed to credit risk through its accounts receivable balances. The Corporation manages credit risk by assessing the credit worthiness of its customers before providing services and on an ongoing basis as well as monitoring the amount and age of balances outstanding. The Corporation views credit risks on its accounts receivable as normal for the industry. The Corporation does not have any accounts receivable at December 31, 2009 that are believed uncollectible. The Corporation’s cash is deposited with two Canadian chartered banks and management believes the risk of credit loss is remote.

The Corporation is exposed to interest rate risk on its floating rate bank debt. The Corporation has the ability to enter into economic hedges on its interest bearing bank debt, but has not done so to date. Management believes that a 1% interest rate change during the next 12 month reporting period would be reasonably possible. During 2010, a 1% change in the interest rate on the outstanding \$5,000 of bank debt would increase (decrease) net and comprehensive loss by \$50.

The Corporation is exposed to foreign currency fluctuations on its financial instruments primarily in relation to its U.S. dollar denominated cash, accounts receivable and accounts payable. The Corporation monitors its foreign currency exposure and attempts to minimize the effect of fluctuations in the U.S. dollar by maintaining appropriate levels of cash and accounts receivable to offset corresponding U.S. dollar denominated accounts payable. The Corporation believes a fluctuation of the U.S. dollar relative to the Canadian dollar of 5% during the next 12 month reporting period would be reasonably possible.

The Corporation believes a fluctuation of the U.S. dollar relative to the Canadian dollar of 5% during the next 12 month reporting period would be reasonably possible.

	2009
Cash	\$ 51
Accounts receivable	1,566
Accounts payable	(1,760)
Net U.S. dollar exposure	<u>\$ (143)</u>
Effect of plus (minus) 5% change in the U.S. dollar to Canadian dollar exchange rate on net loss	<u>\$ 7</u>

With operations commencing in Mexico during the year, it is expected the Corporation will be exposed to

fluctuations in the Mexican peso relative to the Canadian dollar. At December 31, 2009, the Corporation was not exposed to significant foreign currency risk on its financial instruments related to the Mexican peso.

Liquidity Risks

The Corporation is exposed to liquidity risk. Liquidity risk is the exposure of the Corporation to the risk of not being able to meet its financial obligations as they become due. The Corporation manages liquidity risk through management of its capital structure, monitoring and reviewing actual and forecasted cash flows and the effect on bank covenants (see “Liquidity and Capital Resources”), and maintaining unused credit facilities where possible to ensure there are available cash resources to meet the Corporation’s liquidity needs. The Corporation’s existing credit facilities and cash flow from operating activities is expected to be greater than anticipated capital expenditures and the contractual maturities of the Corporation’s financial liabilities for 2009. This expectation could be adversely affected by a material negative change in the oil and gas services business in North America.

FORWARD LOOKING INFORMATION

This MD&A contains forward-looking information in the “Risks and Uncertainties” and “Outlook” sections including statements regarding: our expected growth and outlook; the drilling industry’s outlook; and that the economic recovery in 2010 in the drilling industry will be magnified for companies that can drill deep horizontal wells. This forward-looking information involves material assumptions and known and unknown risks and uncertainties, certain of which are beyond the Corporation’s control. Those assumptions include: the assumption that the jurisdictions in which we operate will experience low to moderate economic growth in 2010; there will be a modest recovery in the drilling industry in 2010; and our customer’s capital programs will be focused on deeper wells in 2010. Further, there are risk factors and uncertainties that could the Corporation’s actual results performance or achievements to differ materially from the forward-looking information, including the risks set out in the “Risks and Uncertainties” section and risks associated with: loss of markets; volatility of commodity prices; currency fluctuations; delays resulting from our inability to obtain required regulatory approvals and ability to access sufficient capital from internal and external sources; general economic conditions in Canada, the United States and Mexico; industry conditions; changes in laws and regulations and the interpretation and enforcement thereof, including changes in government policy regarding deficit spending and stimulus packages; increased competition; lack of qualified personnel or management; fluctuations in foreign exchange or interest rates; stock market volatility and market valuations of companies with respect to announced transactions and the final valuations thereof; and obtaining required approvals of regulatory authorities. The Corporation’s actual results, performance or achievements could differ materially from those expressed in, or implied by, this forward-looking information and, accordingly, no assurances can be given that any of the events anticipated by the forward-looking information will transpire or occur, or if any of them do so, what benefits the Corporation will derive therefrom. The forward-looking information is made as at the date of this MD&A and the Corporation does not undertake any obligation to update publicly or to revise any of the included forward-looking information, whether as a result of new information, future events or otherwise, except as may be required by applicable securities laws.