MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2014

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This Management’s Discussion and Analysis of financial condition and results of operations (“MD&A”) is based on information available to August 26, 2014 and should be read in conjunction with Madalena Energy Inc.’s (“Madalena” or the “Company”) unaudited condensed interim consolidated financial statements for the three and six months ended June 30, 2014 and the accompanying notes as well as the audited consolidated financial statements for the year ended December 31, 2013 and the accompanying notes. This MD&A contains forward-looking information about our current expectations, estimates, projections and assumptions. See the reader advisory for information on the risk factors that could cause actual results to differ materially and the assumptions underlying our forward-looking information. Madalena’s management prepared the MD&A, while the Audit Committee of the Madalena Board of Directors (the “Board”) reviewed and recommended its approval by the Board. Additional information relevant to the Company’s activities contained in its continuous disclosure documents, including our quarterly and the Annual Information Form (“AIF”) is available on SEDAR at www.sedar.com.

Basis of Presentation

This MD&A and the unaudited condensed interim consolidated financial statements and comparative information have been prepared in Canadian dollars, except where another currency has been indicated and have been prepared in accordance with International Financial Reporting Standards (“IFRS” or “GAAP”) as issued by the International Accounting Standards Board. Production volumes are presented on a before royalties basis.

Non-GAAP Measures

Certain financial measures in this document do not have a standardized meaning as prescribed by IFRS, such as cash flow from operations and netbacks and therefore are considered non-GAAP measures. These measures may not be comparable to similar measures presented by other issuers. These measures have been described and presented in order to provide shareholders and potential investors with additional measures for analyzing our ability to generate funds to finance our operations and information regarding our liquidity. The additional information should not be considered in isolation or as a substitute for measures prepared in accordance with IFRS. The definition and reconciliation of each non-GAAP measure is presented in the Operating Results, Financial Results and Liquidity and Capital Resources sections of this MD&A.

INTRODUCTION AND OVERVIEW

Company Overview

Madalena is an independent, Canadian-based, international and domestic upstream oil and gas company whose main business activities include exploration, development and production of crude oil, natural gas liquids and natural gas.

Internationally, Madalena holds 14 large land blocks within five provinces in Argentina where it is focused on the delineation of large petroleum in-place shale and unconventional resources in the Vaca Muerta and Agrio shales, in addition to multiple tight sand plays. The Company is also implementing horizontal drilling and completions technology to develop high impact conventional and scalable resource plays.

Domestically, Madalena's core area of operations is located in the Greater Paddle River area of west-central Alberta where the Company holds approximately 200 gross (150 net) sections of land (approximately 78% average W.I.) encompassing light oil and liquids-rich gas resource plays. Madalena's primary domestic focus is to exploit its large inventory of horizontal drilling locations on its Ostracod oil and other oil and liquids-rich gas resource plays.

SECOND QUARTER 2014 HIGHLIGHTS

($CDN unless otherwise specified)

- June 24, 2014 - closed a bought deal financing for aggregate gross proceeds of $50 million;
- June 25, 2014 - closed the acquisition (the "Acquisition") of the Argentinean business unit of Gran Tierra Energy Inc. for a total consideration of $74.4 million, including working capital adjustments, payable in $59.2 million cash and $15.2 million in common shares of Madalena. The second quarter results include six days of contribution from the Acquisition. The Acquisition included proved plus probable reserves of 6,513 Mboe at December 31, 2013, production on closing of approximately 3,300 boe/d (~78% oil), 11 exploration and production blocks comprising approximately 890,000 net acres and a fully functional independent business unit in Argentina, with an experienced technical and operational team;
- July 7, 2014 - closed the over-allotment option of the bought deal financing for aggregate gross proceeds of $7.5 million;
- Q2 - 2014 production was 1,569 boe/d – including the six day contribution from the Acquisition;
- Current production is approximately 4,700 – 4,800 boe/d (75% oil & NGLs) net to Madalena;
- Operating netbacks continue to improve and averaged $35.14 per boe compared to $13.71 per boe in Q2–2013, an increase of 156%;
- Operating costs in Argentina averaged $21.60 per boe in Q2 - 2014 as compared to $40.43 per boe in Q2-2013, as the benefits from the optimization of surface fluid handling and gas conservation facilities were realized;
- Well positioned with a strong balance sheet, exiting the quarter with $11.2 million in working capital ($18.2 million following the closing of the over-allotment option for the bought deal financing on July 7, 2014) and unutilized credit facilities of $13 million; and,
- Established a capital budget for the second half of 2014 of $36 million, which will be funded by existing working capital and cash flow. This budget is focused on a combination of high impact horizontal development wells in the Sierras Blancas light oil play, development horizontal wells in the Ostracod oil play, re-entries and work-overs for production optimization, and unconventional shale delineation activities. Comprehensive details are provided under the *Outlook for Second Half of 2014* section shown below.

SUMMARY FINANCIAL AND OPERATIONAL RESULTS

	Three months ended June 30		Six months ended June 30	
	2014	2013	**2014**	2013
Financial Canadian - $000s (except per share amounts)				
Oil and gas revenue	**9,144**	3,877	**15,450**	7,487
Net income (loss)	**(3,511)**	(320)	**(3,213)**	(2,640)
Per share – basic and diluted	**(0.01)**	(0.00)	**(0.01)**	(0.01)
Business combination	**74,406**	-	**74,406**	-
Capital expenditures	**2,165**	6,053	**14,712**	23,028
Working capital	**11,234**	7,780	**11,234**	7,780
Equity outstanding – 000s				
Common shares	**525,043**	316,841	**525,043**	316,841
Stock options	**19,305**	15,372	**19,305**	15,372
Operating(1)				
Average Daily Sales				
Crude oil and condensate – Bbls/d	**841**	297	**686**	307
Natural gas – Mcf/d	**3,654**	3,491	**3,318**	3,086
NGLs – Bbls/d	**119**	140	**117**	125
Total - boe /d(2)	**1,569**	1,020	**1,356**	946
Average Sales Prices				
Crude oil and condensate - $/Bbl	**90.31**	78.77	**88.54**	78.70
Natural gas - $/Mcf	**5.09**	3.57	**5.37**	3.45
NGLs - $/Bbl	**50.24**	47.91	**58.22**	52.66
Total - $/boe(2)	**64.08**	41.80	**62.95**	43.72
Operating Netbacks (3)				
$/boe(2)	**35.14**	13.71	**32.82**	14.47

(1) Sales represent production volumes adjusted for inventory changes and losses in Argentina.

(2) Refer to - "Reserves and Other Oil and gas Disclosure" in Advisory.

(3) Operating netback is a non-GAAP measure calculated as the average per boe of the Company's oil and gas sales, less royalties and operating costs.

OUTLOOK FOR SECOND HALF OF 2014

The Company's current production is approximately 4,700 – 4,800 boe/d and with the execution of the second half capital budget of $36 million, the Company is budgeting to exit 2014 with production of 5,200 – 5,400 boe/d, which is expected to be funded by existing working capital and cash flow from operations. At the end of 2014, the Company expects to be in a positive working capital position with no debt and a strong balance sheet with financial flexibility.

The Company is focused on delivering a balanced approach towards horizontal development (focused on conventional oil and gas and scalable resource plays) and the delineation of the Company's unconventional shale and tight sand resources. The Company also has a land base with over 150 net sections (>100,000 net acres) in Western Canada with a large inventory of horizontal development locations. Details of activities for the balance of 2014 and preliminary plans for 2015 are outlined below:

Conventional / Resource Play Development – Horizontal Drilling & Work-over Programs

The Company will implement conventional and horizontal multi-stage frac technology both internationally and domestically to grow the production base.

In Argentina, on the *Coiron Amargo*, *Puesto Morales* and *Rinconada South* blocks, the Company plans to execute horizontal drilling programs in both the Sierras Blancas light oil reservoir and the Loma Montosa oil resource play.

In *Western Canada*, the Company plans to drill additional horizontal Ostracod oil wells to increase oil production and to further advance this oil play.

Horizontal drilling operations in the Sierras Blancas and Ostracod oil developments will proceed through the remainder of 2014 with the drilling of four to five horizontal wells before year end, two of which were recently spudded and are currently drilling – a horizontal Sierras Blancas well in Argentina and a horizontal Ostracod well in Canada;

A multi-well horizontal drilling program in the Loma Montosa oil resource play is also being evaluated for 2015 at the Puesto Morales field.

Additionally, Madalena is planning to execute a multi-well work-over program in 2014 and 2015 to optimize production across its producing fields in Argentina. Specifically, the Company plans to conduct four work-overs starting in September in its Puesto Morales field.

Unconventional Shale & Tight Sand Resources – Advancing a Delineation Strategy

Industry activity near Madalena's unconventional blocks within the Neuquén basin continues to increase and Madalena is well positioned with exposure to the evolving shale and tight sand plays at Corion Amargo, Curamhuele and Cortadera. As part of a balanced business strategy to unlock value, Madalena is planning to conduct vertical and/or horizontal activities in the Vaca Muerta shale, Agrio shale and Mulichinco tight sand plays.

For the remainder of 2014, on the Coiron Amargo block (which is positioned in the most active area of the Neuquén basin for Vaca Muerta shale development and is within the oil window), Madalena plans to continue its delineation activities in the Vaca Muerta shale with a fracture treatment at the CAS.x-15 vertical well (previously drilled) and a new vertical well to be drilled and multi-stage fracced at the CAS.x-16 location. Rigs have been secured for these activities.

Also in 2014, on the Cortadera block, Madalena expects to conduct a re-entry targeting the Mulichinco tight sand in the previously drilled CorS.x-1 deep vertical test.

The Company also plans to progress its Curamhuele block and focus on its unconventional resources in the Agrio shale and Mulichinco tight sands by re-entering two existing wells (Yp.x-1001 and Ch.x-1) to conduct drilling, multi-stage frac and testing operations in these zones of interest. Timing of this work is currently planned to start late in 2014 or Q1-2015 (depending on rig availability). Madalena is working with its partner the provincial oil company to secure a rig and gain a contract extension to allow the work to proceed early in 2015 if required. Madalena's Curamhuele block is within the oil window of the Agrio shale and is directly offset or adjacent to the recently announced Agrio shale discovery by the Argentina state company YPF. In response to offsetting industry activity, Madalena is also further evaluating the Vaca Muerta shale across the Curamhuele block.

Exploration and Appraisal Potential on Multiple Blocks

Madalena's Canadian and Argentine staff is now able to put additional focus on select business development initiatives related to potential block farm-outs. Madalena's strategy is to focus the Company's cash flow and financial resources on its development assets and the delineation of its unconventional resources. The Company is concurrently pursuing a farm-out strategy to create value on select exploration and appraisal blocks.

FINANCIAL RESULTS

Net Income (Loss) and Comprehensive Loss

Canadian $000s (except per share amounts)	Three months ended June 30 **2014**	2013	Six months ended June 30 **2014**	2013
Net loss	**(3,511)**	(320)	**(3,213)**	(2,640)
Comprehensive income (loss)	**(5,902)**	(950)	**(12,184)**	(4,038)
Net loss Per share – basic & diluted	**(0.01)**	(0.01)	**(0.01)**	(0.01)

The net loss for the three months ended June 30, 2014 (the "Quarter") was $3.5 million (2013 – $0.3 million). Net lease operating income increases were offset by business combination costs, increased general and administration costs, impairment losses and increased depletion. The net loss for the six months ended June 30, 2014 ("YTD") was $3.2 million (2013 – $2.6 million). Net lease operating income increases were offset by business combination costs, impairment losses and increased depletion. During the Quarter and YTD, the Company realized a foreign exchange gain of $0.4 million (2013 – $1.2 million) and $2.0 million (2013 – $1.2 million), respectively. These gains were a result of beneficial exchange rates between the Argentine peso and the Canadian dollar that existed in the market at the time of funding the Argentina exploration and development activity from Canada.

The increase in the comprehensive loss compared to the net loss was a result of the changes in the Argentine peso to Canadian dollar exchange rate applied to the net assets of the Company's operations in Argentina. The devaluation of the Argentine peso against the Canadian dollar is linked to Argentina's rate of inflation, which has been a persistent problem for several years. During 2013 the value of the Argentine peso declined by 19% against the Canadian dollar. During the three and six months ended June 30, 2014, the value of the Argentine peso declined an additional 15% and 20%, respectively.

Sales Volumes

Average daily sales volumes	Three months ended June 30 **2014**	2013	Six months ended June 30 **2014**	2013
Argentina				
Crude oil (Bbls/d)	**468**	178	**382**	177
Natural gas (Mcf/d)	**773**	146	**428**	140
Total daily production (boe/d)	**597**	203	**453**	201
Canada				
Crude oil and condensate (Bbls/d)	**373**	119	**304**	130
Natural gas (Mcf/d)	**2,881**	3,345	**2,890**	2,946
Natural gas liquids (Bbls/d)	**119**	140	**117**	125
Total daily production (boe/d)	**972**	817	**903**	745
Corporate				
Total daily production (boe/d)	**1,569**	1,020	**1,356**	946
% Oil & NGLs	**61%**	43%	**59%**	45%

Argentina
Crude oil sales volumes for the Quarter and YTD were 468 bbls/d and 382 bbls/d, respectively, of which the Acquisition contributed for 6 days, contributing 98 bbls/d and 49 bbls/d for the Quarter and YTD, respectively. The majority of Madalena's oil volumes excluding the Acquisition came from the two Sierras Blancas horizontal wells that commenced production in December 2013 and May 2014.

Natural gas sales volumes for the Quarter and YTD were 773 mcf/d and 428 mcf/d, respectively, of which the Acquisition contributed for 6 days, contributing 268 mcf/d and 135 mcf/d for the Quarter and YTD, respectively. The majority of Madalena's natural gas volumes excluding the Acquisition came from the two Sierras Blancas horizontal wells that commenced production in December 2013 and May 2014.

Canada
Sales volumes during the Quarter increased 19% to 972 boe/d (51% Oil & NGLs) from 817 boe/d (32% Oil & NGLs) in Q2 – 2013. Increased production was primarily a result of a new Ostracod well commencing production on April 1, 2014.

YTD production increased 21% to 903 boe/d (47% Oil & NGLs) from 746 boe/d (34% Oil & NGLs) YTD 2013 as production additions from the Ostracod project more than offset production declines from the Company's base production. Following the Acquisition and additional drilling and recompletions, the Company is anticipating production increasing to 5,200-5,400 boe/d (75% Oil & NGLs) by year end.

Average Realized Prices

	Three months ended June 30		**Six months ended June 30**	
Canadian $	**2014**	**2013**	**2014**	**2013**
Argentina				
Crude oil – ($/Bbl)	**86.20**	75.87	**85.86**	78.65
Natural gas – ($/Mcf)	**5.72**	4.36	**5.62**	4.22
Total per boe	**75.01**	69.90	**77.65**	72.44
Canada				
Crude oil and condensate – ($/Bbl)	**95.45**	83.09	**91.32**	78.77
Natural gas – ($/Mcf)	**4.92**	3.54	**5.40**	3.41
Natural gas liquids ($/Bbls)	**50.24**	47.91	**58.22**	52.66
Total per boe	**57.36**	34.84	**55.56**	35.99

The Company has the following physical natural gas and oil contracts in place:

Type	**Period**	**Volume**	**Price Floor**	**Price Ceiling**	**Index**
Natural gas fixed	April 1, 2014 to Oct. 31, 2014	500 GJ/d	$3.45 CDN	$3.45 CDN	AECO
Natural gas fixed	April 1, 2014 to Oct. 31, 2014	300 GJ/d	$3.55 CDN	$3.55 CDN	AECO
Natural gas fixed	April 1, 2014 to Oct. 31, 2014	300 GJ/d	$4.43CDN	$4.43 CDN	AECO
Natural gas fixed	April 1, 2014 to Oct. 31, 2014	300 GJ/d	$4.52CDN	$4.52 CDN	AECO
Crude oil call options	Jan. 1, 2014 to Dec. 31, 2014	50 bbl/d	-	$100.00 US	WTI
Crude oil call options	Jan. 1, 2014 to Dec. 31, 2014	50 bbl/d	-	$100.00 US	WTI
Crude oil call options	Jan 1, 2015 to Dec. 31, 2015	50 bbl/d	-	$95.00 US	WTI
Crude Oil Swaps	Feb 1, 2014 to Dec. 31, 2014	50 bbl/d	-	$100 CDN	WTI

The fair value of commodity contracts is determined by discounting the difference between the contracted price and published forward price curves as at the balance sheet date, using the remaining contracted petroleum and natural gas volumes. The fair value of commodity contracts as at June 30, 2014 was a net payable and an unrealized loss of $348,188 (2013 – unrealized gain of $24,800). Realized losses for the Quarter and YTD were $111,772 (2013 - $5,871) and $129,703 (2013 – $5,871) and are included in interest and other income on the Statement of Loss and Comprehensive Loss. The commodity contracts are classified as level 2 within the fair value hierarchy.

Revenue

	Three months ended June 30		Six months ended June 30	
Canadian $000s, except per boe	**2014**	**2013**	**2014**	**2013**
Argentina				
Crude oil	**3,670**	1,230	**5,937**	2,525
Natural gas	**402**	58	**435**	107
	4,072	1,288	**6,372**	2,632
Canada				
Crude oil and condensate	**3,240**	902	**5,018**	1,846
Natural gas	**1,290**	1,077	**2,822**	1,820
Natural gas liquids	**542**	610	**1,238**	1,189
	5,072	2,589	**9,078**	4,855
Corporate Total	**9,144**	3,877	**15,450**	7,487
Corporate - $/ boe	**64.08**	41.80	**62.95**	43.72

Argentina

Oil and gas sales increased by $2.8 million in the Quarter and $3.8 million YTD from their corresponding periods in 2013 due to the contribution of six days of oil and gas sales from the Acquisition, oil and gas sales from the two new horizontal Sierras Blancas wells and improved prices realized from both the sale of oil and gas.

Canada

Oil sales increased by $2.4 million in the Quarter and $3.1 million YTD from their corresponding periods in 2013 due to increased production and prices realized from the sale of oil. Natural gas sales increased by $0.2 million in the Quarter from their corresponding periods in 2013 as increased prices realized from the sale of gas were partially offset by decreased gas production. Natural gas sales increased by $1.0 million YTD from their corresponding periods in 2013 due to increased production and prices realized from the sale of gas.

Royalties

	Three months ended June 30		Six months ended June 30	
Canadian $000s	**2014**	**2013**	**2014**	**2013**
Argentina				
Royalties	**559**	225	**889**	434
As % of revenue from Argentina	**14%**	17%	**14%**	16%
Canada				
Royalties	**640**	237	**1,074**	553
As % of revenue from Canada	**13%**	9%	**12%**	11%
Corporate total	**1,199**	462	**1,963**	987

Argentina
Royalty expense in the Quarter and YTD increased due to higher production volumes.

Canada
Royalty expense consists of royalties paid to provincial governments, freehold landowners and overriding royalty owners. The increased royalties are a result of higher production volumes and a Gas Cost Allowance adjustment from the Alberta government received by the Company in the Quarter.

Operating Costs

	Three months ended June 30		Six months ended June 30	
Canadian $000s, except per boe	**2014**	**2013**	**2014**	**2013**
Argentina				
Operating costs	**1,173**	745	**2,024**	1,432
$/boe	**21.60**	40.43	**24.66**	39.40
Canada				
Operating costs	**1,758**	1,398	**3,407**	2,589
$/boe	**19.88**	18.81	**20.85**	19.19
Corporate total	**2,931**	2,143	**5,431**	4,021

Argentina
Operating costs in Argentina were $21.60 and $24.66 per boe in the Quarter and YTD, respectively, and have been significantly reduced from 2013 as the benefits from the optimization of surface fluid handling and gas conservation facilities were realized. Following the Acquisition, management expects the average operating costs in the $25 – 27/bbl range.

Canada
In Canada, operating costs have remained consistent in the $20 per boe range and management expects average operating costs in the $20 – 22/boe range in the future.

Netbacks [1]

	Three months ended June 30		Six months ended June 30	
Canadian $	**2014**	**2013**	**2014**	**2013**
Argentina				
Revenue	**75.01**	69.90	**77.65**	72.44
Royalties	**(10.29)**	(12.19)	**(10.83)**	(11.94)
Operating expenses	**(21.60)**	(40.43)	**(24.66)**	(39.40)
Netbacks	**43.12**	17.28	**42.16**	21.10
Canada				
Revenue	**57.31**	34.84	**55.56**	35.99
Royalties	**(7.25)**	(3.19)	**(6.58)**	(4.10)
Operating expenses	**(19.88)**	(18.81)	**(20.85)**	(19.19)
Netbacks	**30.18**	12.84	**28.13**	12.70

Canadian $	Three months ended June 30 2014	2013	Six months ended June 30 2014	2013
Corporate				
Revenue	**64.08**	41.80	**62.95**	43.72
Royalties	**(8.41)**	(4.98)	**(8.00)**	(5.77)
Operating expenses	**(20.53)**	(23.11)	**(22.13)**	(23.48)
Netbacks	**35.14**	13.71	**32.82**	14.47

(1) The term "netback" is a non-GAAP measure and may not be comparable with the calculation of other entities. Netback is calculated as the average unit sales price, less royalties and operating expenses and represents the cash margin for every barrel of oil equivalent sold. The Company uses this measure to analyze operating performance and considers netback a key measure as it demonstrates its profitability relative to current commodity prices.

The Company anticipates netbacks to average $32 – 35/ boe following the Acquisition as higher oil weighting and price are offset by slightly higher operating costs.

General and Administration ("G&A") Expenses

Canadian $000s	Three months ended June 30 2014	2013	Six months ended June 30 2014	2013
Argentina	1,030	426	1,462	855
Canada	1,617	787	2,281	2,413
	2,647	1,213	**3,743**	3,278

G&A expenses for the Quarter were higher than the comparable period in 2013 in Argentina as a result of the six days of increased G&A from the acquisition and increased administration costs from the existing operations. In Canada, increased compensation and office and administration costs for the Quarter as compared to Q2-2013 were the primary causes for increased G&A expenses.

Business Combination Expenses

Business combination expenses relating to the Acquisition were $1.7 million for the Quarter and YTD, respectively, (2013 – nil and nil) consisting primarily of legal and financial advisory fees.

Finance Cost

In Argentina, accretion expense was $19,000 (2013 – $17,000) for the Quarter and $37,000 (2013 – $37,000) YTD. In Canada, accretion expense was $29,000 (2013 - $17,000) for the Quarter and $58,000 (2013 - $34,000) YTD.

Share-based Compensation

The Company has issued Stock Options as incentive programs that allow officers, directors, consultants and employees to purchase shares in the Company.

Share based compensation was $344,000 in the Quarter (2013 - $294,000) and $693,000 YTD (2013 - $444,000).

Depletion and Depreciation

	Three months ended June 30		Six months ended June 30	
Canadian $000s	**2014**	**2013**	**2014**	**2013**
Argentina	**1,113**	530	**2,022**	1,048
Canada	**1,318**	886	**2,326**	1,633
	2,431	1,416	**4,348**	2,681
$/boe	**17.03**	15.27	**17.72**	15.66

Depletion and depreciation expense for the Quarter and YTD increased due to higher depletion rates and production volumes.

Impairment

The Company has recorded an impairment charge on its Canadian exploration and evaluation assets of $1.9 million (2013 – nil) and $2.6 million (2013 – nil) for the Quarter and YTD, respectively. The impairment primarily relates to drilling and completion costs incurred in 2014 relating to one well that commenced drilling in 2013 that has been deemed to be uneconomic.

Transactions with Related Parties

A director of the Company is a partner of a law firm that provides legal services to the Company. During the Quarter and YTD, the Company incurred fees of $0.5 million (2013 - $0.1 million) and $0.6 million (2013 - $0.3 million, respectively, from this firm for legal fees related to legal matters of which $0.4 million is included in accounts payable and accrued liabilities at June 30, 2014.

A director of one of the Company's subsidiaries provides legal and consulting services to the Company. During the Quarter and YTD, the Company incurred fees of $5,838 (2013 - $188,748 for the comparative Quarter and for the comparative YTD).

Business Combination and Capital Expenditures

Canadian $000s	Three months ended June 30 2014	2013	Six months ended June 30 2014	2013
Argentina business combination	**74,406**	-	**74,406**	-
Capital Expenditures				
Argentina				
Land	**-**	403	**15**	406
Geological and geophysical	**39**	1,150	**1,737**	1,157
Drilling and completions	**824**	1,363	**5,482**	3,145
Well equipment and facilities	**559**	98	**294**	237
Other	**15**	563	**902**	891
Argentina Total	**1,437**	3,577	**8,430**	5,836
Canada				
Land	**-**	47	**22**	114
Geological and geophysical	**35**	17	**41**	17
Drilling and completions	**353**	987	**4,061**	14,105
Well equipment and facilities	**326**	1,385	**2,094**	2,781
Other	**14**	40	**64**	175
Canada total	**728**	2,476	**6,282**	17,192
Total Capital Expenditures	**2,165**	6,053	**14,712**	23,028

On June 25, 2014, the Company acquired all of the outstanding shares of the Argentine business unit of Gran Tierra Energy Inc. for cash consideration of $59.2 million (including working capital of $5.1 million) and 29,831,537 common shares at a fair value of $0.51 per common share (the "Acquisition"). The Acquisition, which provides the Company with a significant platform to grow its Argentina production, included Proved and Probable reserves of 6,513 Mboe at December 31, 2013, 11 exploration and production blocks comprising approximately 890,000 net acres and a fully functional independent business unit in Argentina, with an experienced technical and operational team.

Capital expenditures for the Quarter and YTD in Argentina were primarily related to the Acquisition that closed in late June. Other activity during the Quarter and YTD related to the drilling and casing of the CAS.x-15 vertical well and the shooting of a 75 square km 3D seismic program at Curamhuele.

In Canada, activity YTD has primarily been directed to the Ostracod oil project. Completion costs were incurred on two wells, one well was equipped and tied-in and pumping units have now been installed on four Ostracod wells.

FINANCIAL POSITION, LIQUIDITY AND CAPITAL RESOURCES

Liquidity, working capital and shareholders' equity

Canadian $000s	June 30 2014	December 31 2013
Working capital	**11,234**	8,016
Shareholders' equity	**150,594**	79,003

The Company's capital management objective is to have sufficient capital to be able to execute its business plan. The Company manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying oil and natural gas assets. The Company considers its capital structure to include shareholders' equity, loans and borrowings and working capital. The Company may issue shares or enter into joint venture partnerships to fund its capital commitments.

At June 30, 2014, the Company had a revolving operating demand loan credit facility with the National Bank of Canada to a maximum of $10 million with interest charged at the bank's prime rate plus 1.0% per annum. Security for this facility is provided by way of a charge over the petroleum and natural gas assets of the Company. The facility includes a working capital ratio covenant, whereby the Company's working capital deficiency (excluding any unrealized hedging gains or losses) may not exceed $10 million. Standby fees associated with the facility are 0.25% per annum on the undrawn portion.

In addition, The Company has an acquisition / development demand loan credit facility with the National Bank of Canada to a maximum of $3 million with interest charged at the bank's prime rate plus 1.5% per annum.

Both facilities are subject to a periodic review by the bank and the next review scheduled for September 1, 2014. The facilities were unutilized at June 30, 2014.

As the credit facilities are a demand loan, it may be called at any time. Accordingly, there is no assurance that the credit facilities will be renewed when the current scheduled review is completed.

Argentine Foreign Currency Restrictions

Historically, Madalena has not repatriated funds from Argentina. As a result of expanding our operations in Argentina through the Acquisition, there may be reason to repatriate funds in future periods. While the Company does not believe there are prohibitive restrictions to repatriate after-tax funds to Canada, the Argentina government has a number of monetary and currency exchange control measures, including authorizations by the Argentine Central Bank being required to transfer funds abroad. If the Central Bank does not grant such authorization for our Argentina subsidiaries to make these payments, our ability to use funds from our Argentine operations for other purposes will be impacted.

Share capital issued and options granted

Outstanding Share Capital

In the first quarter of 2014, the Company issued 32,857,225 common shares at a price of $0.70 per common share, including 4,285,725 common shares issued pursuant to the exercise of the over-allotment option in full by the Underwriters, for aggregate gross proceeds of $23.0 million.

In June 2014, the Company issued 98,100,000 common shares at a price of $0.51 per common share for aggregate gross proceeds of $50.0 million.

In June 2014, the Company issued 29,831,537 common shares issued pursuant to Acquisition.

On July 11, 2014, 5,350,000 options were granted to certain employees and consultants of the Corporation and its subsidiaries; 5,000,000 of which related to employees in Argentina as a result of the Acquisition. Each Option has an exercise price of $0.50 per share and is exercisable for a period of five years from the date of grant.

In July 2014, the over-allotment option was exercised in full by the Underwriters, for aggregate gross proceeds of $7.5 million.

Financial Instruments

Other than the commodity contracts discussed earlier in this report, the Company's financial instruments comprise cash and cash equivalents, trade and other receivables, and trade and other payables. Carrying values reflect the current fair value of the Company's financial instruments due to their short-term to maturity.

Decommissioning Obligations

Decommissioning obligations result from net ownership interests in property, plant and equipment and are a critical accounting estimate. There are significant uncertainties related to settling decommissioning obligations and the impact on the financial statements could be material. The eventual timing of and costs to settle these obligations could differ from current estimates. The main factors that can cause expected decommissioning obligations to change are changes to laws and regulations, construction of new facilities, changes in reserve estimates and reserve lives and changes in technology.

The business combination in Argentina added a significant number of producing wells and associated facilities and with this expanded operating portfolio, the Company expects that decommissioning obligations for all of its Argentina portfolio will be settled by US$.

At June 30, 2014, inflation rates of 2% were used in both Argentina and Canada (December 31, 2013 – 10.9% and 2% for Argentina and Canada, respectively). The risk free rate used to discount the liability was 2.5% (December 31, 2013 – 17.18%) in Argentina and up to 2.8% (December 31, 2013 – up to 3.0%) in Canada.

Contractual Obligations

Development & Exploration commitments

Coiron Amargo Block (35% working interest)

The Coiron Amargo block is divided into two regions called Coiron Amargo Norte (northern portion of the block) and Coiron Amargo Sur (southern portion of the block). Coiron Amargo Norte is currently under a 25 year exploitation (development) concession which was approved by the Province of Neuquén in 2012.

In October 2013, following an application and approval process by Madalena and its partners, the exploration period for Coiron Amargo Sur was extended until November 8, 2014 by way of an official decree signed by the Province of Neuquén in Argentina. The remaining work commitments in Coiron Amargo Sur (to be fulfilled by an upcoming Vaca Muerta shale well scheduled to be drilled in the second half of 2014) are estimated at approximately USD$1.94 million plus VAT (net to Madalena) as of June 30, 2014. After satisfying these remaining work commitments, Madalena has the ability to extend Coiron Amargo Sur through further exploration, evaluation and/or exploitation (development) phases. Madalena and its partners at Coiron Amargo have already initiated discussions with the regulators related to a multi-year block contract for Coiron Amargo Sur.

Curamhuele Block (90% working interest)

In June 2013 the exploration period was extended until November 8, 2014 by way of an official decree signed by the Province of Neuquén. As part of the block commitments to date, Madalena has executed a 3D seismic program in the first half of 2014 which is currently in the geotechnical processing stage to identify additional exploration and appraisal leads across the block. To satisfy the remaining work commitments on the block, Madalena is actively working to source the appropriate drilling rig suitable to conduct a re-entry program as planned. Madalena has been in communication with the Province of Neuquén and its partner (Gas y Petroleo) related to execution timelines for the re-entry program. At this time, based on rig availability and lead times for equipment, Madalena expects to execute the remaining commitments on the block starting in late 2014 or Q1 2015.

Madalena's remaining share of future work commitments associated with the Curamhuele block as of June 30, 2014 is approximately US$12.3 million plus VAT. After satisfying these remaining work commitments, Madalena expects to either convert certain area(s) of the acreage into an exploitation (development) concession and/or enter into a new exploration period(s) or unconventional evaluation phase, to further explore and appraise the Curamhuele block.

Cortadera Block (37.8% working interest)
On January 15, 2014, the joint venture partnership on the Cortadera Block, in which Madalena is a partner, signed an amended contract agreement to formalize a multi-year agreement for the extension of the initial exploration period and inclusion of subsequent exploration periods. Subsequent to that agreement and following an application and approval process, the first exploration period for Cortadera was extended by way of an official decree which was signed by the Province of Neuquén in Argentina. This extension provides the partnership until October 26, 2014 to satisfy the remaining work commitments on the block, which involves the upcoming re-entry work. Madalena believes that its share of any work performed is not expected to be significant.

Under the amended agreement, and subsequent to conducting the upcoming re-entry work, the partnership at Cortadera has the option to enter into subsequent exploration periods involving a second exploration period extending to October 25, 2018 and a third exploration period upon which the partnership has the option to enter into subsequent exploration periods extending to October 25, 2021, or extend the Cortadera Block through potential further evaluation and/or exploitation phases.

Santa Victoria Block (100% working interest)

This block was part of the recent Acquisition. It is a 100% working interest operated property covering 516,846 gross acres in the Noroeste Basin. The contract is currently in the second of three exploration phases. This phase requires a minimum of work commitments of US$3.75 million plus VAT by April 2015.

Flow-through Shares Commitments
During 2013, the Company completed a CEE flow through share financing in the amount of $5.7 million. As at June 30, 2014, $3.8 million of the CEE flow-through funds had been expended. The Company has until December 31, 2014 to expend the remaining CEE flow through funds in the amount of $1.9 million on qualified expenditures.

ANNUAL AND QUARTERLY FINANCIAL RESULTS

Quarterly Financial Results

Canadian $000s, except shares outstanding	Q2 2014	Q1 2014	Q4 2013	Q3 2013
Revenues	**9,144**	6,306	5,633	4,840
Net income (loss)	**(3,510)**	254	(20,527)	(118)
Shares outstanding – 000s	**525.4**	396.8	364.0	338.7
Net income (loss) per share – basic and diluted	**0.01**	(0.00)	(0.06)	(0.00)

	Q2 2013	Q1 2013	Q4 2012	Q3 2012
Revenues	3,877	3,610	3,012	1,762
Net loss	(320)	(2,320)	(5,075)	(916)
Shares outstanding (‘000s)	316.8	316.1	314.3	314.3
Net loss per share – basic and diluted	(0.00)	(0.01)	(0.02)	(0.0)

Generally, the Company’s increase in revenues during the Quarter can be attributed to increasing oil production in both Argentina and Canada.

The Company recorded impairment charges in Q2-2014, Q4-2013 and Q4-2012 of $1.9 million, $19.7 million and $2.5 million, respectively, impacting the net loss recognized of $3.5 million, $20.5 million and $5.1 million in Q4-2013 and Q4-2012, respectively. The Company also incurred $1.7 million of business combination costs relating to the Acquisition in Q2-2014.

The Company issued 32.8 million shares during Q1 2014 for gross proceeds of $23.0 million and issued 128.2 million shares during Q2 2014 for gross proceeds and partial consideration for the Acquisition totalling $65.3 million.

CRITICAL ACCOUNTING JUDGEMENTS, ESTIMATES AND ACCOUNTING POLICIES

For more details regarding the Company’s critical accounting judgments, estimates and accounting policies the following should be read in conjunction with the Company’s 2013 annual MD&A.

Management is required to make judgments, estimates and assumptions in the application of accounting policies that could have a significant impact on our financial results. Actual results may differ from those estimates and those differences may be material. The estimates and assumptions used are subject to updates based on experience and the application of new information. The Company’s critical accounting policies and estimates are reviewed annually by the Audit Committee of the Board. Further details on the basis of presentation and significant accounting policies can be found in the Company’s notes to the Consolidated Financial Statements and annual MD&A for the year ended December 31, 2013.

Critical Accounting Judgments in Applying Accounting Policies

Critical judgments are those judgments made by Management in the process of applying accounting policies that have the most significant effect on the amounts recognized in the Company’s annual and interim Consolidated Financial Statements and accompanying notes. On January 1, 2014, as required, the Company adopted the amendments to IAS 32 and IFRIC 21. See discussion below under Changes in Accounting Policies for details. Further information on Management’s critical accounting judgments in applying accounting policies can be found in the notes to the Consolidated Financial Statements and annual MD&A for the year ended December 31, 2013.

Critical accounting estimates

Critical accounting estimates are those estimates that require Management to make particularly subjective or complex judgments about matters that are inherently uncertain. Estimates and underlying assumptions are reviewed on an ongoing basis and any revisions to accounting estimates are recognized in the period in which the estimates are revised. For 2014, there have been no changes to the Company's key sources of estimation uncertainty. Further information on the Company's key sources of estimation uncertainty can be found in the notes to the Consolidated Financial Statements and annual MD&A for the year ended December 31, 2013.

Changes in Accounting Policies

The IASB issued International Financial Reporting Interpretations Committee Interpretation ("IFRIC") 21, "Levies" which was adopted by the Company on January 1, 2014. The IFRIC clarifies that an entity should recognize a liability for a levy when the activity that triggers payment occurs. The adoption of this interpretation did not impact the Condensed Interim Consolidated Financial Statements.

Effective January 1, 2014, the Company adopted, as required, amendments to IAS 32, "Financial Instruments: Presentation" ("IAS 32"). The amendments clarify that the right to offset financial assets and liabilities must be available on the current date and cannot be contingent on a future event. IAS 32 did not impact the Condensed Interim Consolidated Financial Statements.

Future Accounting Pronouncements

A description of standards and interpretations that will be adopted by the Company in future periods can be found in the notes to the annual Consolidated Financial Statements for the year ended December 31, 2013. In May 2014, the International Accounting Standards Board issued IFRS 15 Revenues from Contracts with Customers ("IFRS 15"). IFRS 15 provides a single, principles based five-step model to be applied to revenue recognition from all contracts with customers and applies to an annual reporting period beginning on or after 1 January 2017. The impact of this standard on the Company has not been determined,

RISK MANAGEMENT

For a full understanding of the risks that impact the Company, the following discussion should be read in conjunction with the Company's 2013 annual MD&A.

The Company is exposed to a number of risks through the pursuit of its strategic objectives. Some of these risks impact the oil and gas industry as a whole and others are unique to its operations. Actively managing these risks improves the Company's ability to effectively execute its business strategy. The Company's exposure to liquidity risk, safety risk, capital project execution and operating risk, reserves replacement risk, environmental risk and regulatory risk has not changed substantially since December 31, 2013. For a further and more in-depth discussion of our risk management see the Company's annual MD&A for the year ended December 31, 2013.

A description of the risk factors and uncertainties affecting the Company can be found in the Advisory and a full discussion of the material risk factors affecting the Company can be found in our Annual Information Form for the year ended December 31, 2013.

ADVISORY

Forward Looking Statements

This MD&A may include forward-looking statements including opinions, assumptions, estimates and management's assessment of future plans and operations, expected depletion, depreciation and accretion expenses, expectations as to the taxability of the Company and planned capital expenditures and the timing and funding thereof. When used in this document, the words "anticipate," "believe," "estimate," "expect," "intent," “may,” “project,” “plan”, “should” and similar expressions are intended to be among the statements that identify forward-looking statements. Forward-looking statements are subject to a wide range of risks and uncertainties, and although the Company believes that the expectations represented by such forward-looking statements are reasonable, there can be no assurance that such expectations will be realized. Any number of important factors could cause actual results to differ materially from those in the forward-looking statements including, but not limited to, risks associated with petroleum and natural gas exploration, development, exploitation, production, marketing and transportation, the volatility of petroleum and natural gas prices, currency fluctuations, the ability to implement corporate strategies, the state of domestic capital markets, the ability to obtain financing, incorrect assessment of the value of acquisitions, failure to realize the anticipated benefits of acquisitions, changes in petroleum and natural gas acquisition and drilling programs, delays resulting from inability to obtain required regulatory approvals, delays resulting from inability to obtain drilling rigs and other services, labour supply risks, environmental risks, competition from other producers, imprecision of reserve estimates, changes in general economic conditions, ability to execute farm-in and farm-out opportunities, and other factors, all of which are more fully described from time to time in the reports and filings made by the Company with securities regulatory authorities.

Statements relating to “reserves” or “resources” are deemed to be forward looking statements, as they involve the implied assessment, based on certain estimates and assumptions, that the reserves and resources described can be profitably produced in the future.

The forward looking statements contained in this MD&A are expressly qualified by this cautionary statement. Readers are cautioned not to place undue reliance on forward-looking statements, as no assurances can be given as to future results, levels of activity or achievements. Except as required by applicable securities laws, the Company does not undertake any obligation to publicly update or revise any forward-looking statements.

Reserves and Other Oil and Gas Disclosure

Any references in this MD&A to test rates, flow rates, initial and/or final raw test or production rates, early production, test volumes behind pipe and/or "flush" production rates are useful in confirming the presence of hydrocarbons, however, such rates are not necessarily indicative of long-term performance or of ultimate recovery. Such rates may also include recovered "load" fluids used in well completion stimulation. Readers are cautioned not to place reliance on such rates in calculating the aggregate production for Madalena. In addition, the Vaca Muerta and Agrio shales are unconventional resource plays which may be subject to high initial decline rates.

Analogous Information

Certain information in this MD&A may constitute "analogous information" as defined in National Instrument 51-101 - Standards of Disclosure for Oil and Gas Activities ("**NI 51-101**"), including, but not limited to, information relating to areas, assets, wells, industry activity and/or operations that are in geographical proximity to or believed to be on-trend with lands held by Madalena. Such information has been obtained from public sources, government sources, regulatory agencies or other industry participants. Management of Madalena believes the information may be relevant to help define the reservoir characteristics within lands on which Madalena holds an interest and such information has been presented to help demonstrate the basis for Madalena's business plans and strategies. However, management cannot confirm whether such analogous information has been prepared in accordance with NI 51-101 and the Canadian Oil and Gas Evaluation Handbook and Madalena is unable to confirm that the analogous information was prepared by a qualified reserves evaluator or auditor. Madalena has no way of verifying the accuracy of such information. There is no certainty that the results of the analogous information or inferred thereby will be achieved by Madalena and such information should not be construed as an estimate of future production levels or the actual characteristics and quality Madalena's assets. Such information is also not an estimate of the reserves or resources attributable to lands held or to be held by Madalena and there is no certainty that such information will prove to be analogous in the future. The reader is cautioned that the data relied upon by

Madalena may be in error and/or may not be analogous to such lands to be held by Madalena.

Numerical Amounts

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

This MD&A uses the term "netback" which is a term that does not have standardized meanings under GAAP and this non-GAAP measurement may not be comparable with the calculation of other entities. The Company uses this measure to analyze operating performance.

The term "netback", which is calculated as the average unit sales price, less royalties and operating expenses, represents the cash margin for every barrel of oil equivalent sold. The Company considers this a key measure as it demonstrates its profitability relative to current commodity prices. This term does not have any standardized meaning prescribed by GAAP and, therefore, might not be comparable with the calculation of a similar measure for other companies.

ABBREVIATIONS

The following is a summary of the abbreviations used in this MD&A:

Oil and Natural Gas Liquids		**Natural Gas**	
Bbl	barrel	Mcf	thousand cubic feet
Bbls/d	barrels per day	WI	Working interest
NGLs	Natural gas liquids		
boe	barrel of oil equivalent		
boe/d	barrel of oil equivalent per day		