Madalena energy inc.

CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

FOR THE THREE MONTHS ENDED MARCH 31, 2014 AND 2013

(UNAUDITED)

Condensed Interim Consolidated Statements of Financial Position
(Unaudited)

Canadian $000s	Note	**As at March 31 2014**	As at December 31 2013
Assets			
Current assets			
Cash and cash equivalents		**26,248**	14,835
Trade and other receivables		**4,510**	4,057
Other current assets		**1,231**	1,075
		31,989	19,967
Property, plant and equipment	4	**39,028**	39,062
Exploration and evaluation assets	5	**39,214**	35,745
Other non-current assets		**1,881**	1,512
		112,112	96,286
Liabilities			
Current liabilities			
Trade and other payables		**12,526**	11,951
Flow-through share liability		**333**	385
Decommissioning obligations	6	**4,903**	4,947
		17,762	17,283
Shareholders' Equity			
Share capital	7	**180,850**	159,574
Contributed surplus		**12,999**	12,645
Accumulated other comprehensive loss		**(23,674)**	(17,094)
Deficit		**(75,825)**	(76,122)
		94,350	79,003
		112,112	96,286

Commitments (Note 11)

See the accompanying Notes to the Condensed Interim Consolidated Financial Statements.

Condensed Interim Consolidated Statements of Income (Loss) and Comprehensive Loss
(Unaudited)

		Three months ended March 31	
Canadian $000s, except per share amounts	Note	2014	2013
Revenues			
Oil and natural gas revenues		**6,306**	3,609
Royalties		**(764)**	(525)
		5,542	3,084
Interest and other income		**30**	103
Foreign exchange gain (loss)		**1,593**	(48)
		7,165	3,139
Expenses			
Operating		**2,500**	1,878
General and administrative		**1,096**	2,065
Finance costs	6	**47**	37
Share-based compensation	8	**349**	150
Depletion and depreciation	4	**1,918**	1,264
Impairment	5	**658**	-
Unrealized loss on commodity contracts	13	**352**	65
		6,920	5,459
Income (Loss) before income taxes		**245**	(2,320)
Income taxes			
Deferred income tax recovery		**52**	-
Net income (loss)		**297**	(2,320)
Foreign currency translation adjustment		**(6,580)**	(768)
Comprehensive loss		**(6,283)**	(3,088)
Loss per share			
Basic and diluted	12	**(0.00)**	(0.01)

See the accompanying Notes to the Condensed Interim Consolidated Financial Statements.

Madalena energy inc.

Condensed Interim Consolidated Statements of Equity
(Unaudited)

Canadian $000s	Share Capital	Contributed Surplus	Accumulated Other Comprehensive Income	Deficit	Total Equity
	(Note7)				
Balance at December 31, 2013	159,574	12,645	(17,094)	(76,122)	79,003
Net income (loss)	-	-	-	297	297
Other comprehensive loss	-	-	(6,580)	-	(6,580)
Gross proceeds from financings	23,000	-	-	-	23,000
Share issue costs	(1,724)	-	-	-	(1,724)
Share based payments	-	354	-	-	354
Balance at March 31, 2014	**180,850**	**12,999**	**(23,674)**	**(75,825)**	**94,350**
Balance at December 31, 2012	141,676	11,920	(8,373)	(52,837)	92,386
Net loss	-	-	-	(2,320)	(2,320)
Other comprehensive loss	-	-	(768)	-	(768)
Stock options exercised	627	(282)	-	-	345
Share based payments	-	155	-	-	155
Balance at March 31, 2013	142,303	11,793	(9,141)	(55,157)	89,798

See the accompanying Notes to the Condensed Interim Consolidated Financial Statements.

Condensed Interim Consolidated Statements of Cash Flows
(Unaudited)

Canadian $000s	Note	Three months ended March 31 2014	2013
Cash provided by (used in):			
Operating			
Net income (loss)		**297**	(2,320)
Items not affecting cash:			
Depletion and depreciation	4	**1,918**	1,264
Impairment	5	**658**	-
Finance cost		**47**	37
Unrealized loss on commodity contracts	13	**352**	65
Share-based compensation	8	**349**	150
Decommissioning costs incurred	6	**(23)**	(59)
Deferred income tax recovery		**(52)**	-
Change in non-cash working capital	10	**(1,058)**	(1,461)
Net cash used in operating activities		**2,488**	(2,324)
Investing			
Property, plant and equipment additions	4	**(3,744)**	(9,977)
Evaluation and exploration assets additions	5	**(8,804)**	(6,998)
Change in other non-current assets		**(636)**	(86)
Change in non-cash working capital	10	**1,135**	4,861
Net cash used in investing activities		**(12,049)**	(12,200)
Financing			
Shares issued, net of issue costs	7	**21,276**	345
Net cash from financing activities		**21,276**	345
Change in cash and cash equivalents		**11,715**	(14,179)
Cash and cash equivalents, beginning of period		**14,835**	38,253
Impact of foreign exchange on cash balances		**(302)**	(28)
Cash and cash equivalents, end of period		**26,248**	24,046

See the accompanying Notes to the Condensed Interim Consolidated Financial Statements.

Tabular amounts in thousands of Canadian dollars, except per share amounts

1. Reporting Entity

Madalena Energy Inc. (the "Company" or "Madalena") is involved in the exploration, development and production of oil and natural gas in in Argentina and in Alberta, Canada and its principal place of business is Suite 200, 707 – 7th Avenue S.W., Calgary, Alberta, T2P 3H6.

The condensed interim consolidated financial statements are comprised of the results of the Company and the following wholly-owned subsidiaries in the indicated legal jurisdictions:

- Madalena Austral S.A. (Argentina)
- Madalena Ventures International Holding Company Inc. (Barbados)
- Madalena Ventures International Inc. (Barbados)

2. Basis of Preparation

Future operations

These Condensed Interim Consolidated Financial Statements have been prepared on the basis that the Company is a going concern and will realize assets and discharge liabilities in the normal course of operations for the foreseeable future. Presently, Madalena has limited cash flow from operating activities. The Company currently relies substantially on equity financing to pay for exploration activities. Therefore, the Company's ability to continue operations is dependent on identifying commercial oil and gas reserves, generating profitable operations and raising sufficient capital to complete planned exploration and development activities. The outcome of these matters cannot be predicted at this time.

Statement of Compliance

These Condensed Interim Consolidated Financial Statements have been prepared in accordance with International Accounting Standard 34, "*Interim Financial Reporting*". These condensed interim consolidated financial statements follow the same accounting policies and method of computation as the annual Consolidated Financial Statements for the year ended December 31, 2013, except as identified in Note 3. The disclosures provided below are incremental to those included with the annual Consolidated Financial Statements. Certain information and disclosures normally included in the notes to the annual Consolidated Financial Statements have been condensed or have been disclosed on an annual basis only. Accordingly, these Condensed Interim Consolidated Financial Statements should be read in conjunction with the annual Consolidated Financial Statements for the year ended December 31, 2013, which have been prepared in accordance with IFRS.

The Condensed Interim Consolidated Financial Statements were approved and authorized for issue by the Company's Board of Directors on May 29, 2014.

3. Changes in Accounting Policies

New and Amended Standards and Interpretations Adopted.

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

There were no new or amended standards issued during the three months ended March 31, 2014 that are applicable to the Company in future periods. 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.

4. Property, Plant and Equipment

Canadian $000s	Oil and Natural Gas Assets	Corporate	Total
Cost			
At December 31, 2012	35,181	292	35,473
Additions	22,643	(15)	22,628
Effect of change in foreign exchange rates	(3,674)	(8)	(3,682)
At December 31, 2013	54,150	269	54,419
Additions	3,810	15	3,825
Effect of change in foreign exchange rates	(2,804)	(4)	(2,808)
At March 31, 2014	**55,156**	**280**	**55,436**

Canadian $000s	Oil and Natural Gas Assets	Corporate	Total
Accumulated depreciation and depletion			
At December 31, 2012	(4,598)	(161)	(4,579)
Depreciation and depletion	(6,647)	(25)	(6,672)
Impairment	(5,000)	-	(5,000)
Effect of change in foreign exchange rates	1,067	6	1,073
At December 31, 2013	(15,178)	(180)	(15,358)
Depreciation and depletion	(1,873)	(8)	(1,881)
Effect of change in foreign exchange rates	827	4	831
At March 31, 2014	**(16,224)**	**(184)**	**(16,408)**

Canadian $000s			
Net book value			
At December 31, 2013	38,972	90	39,062
At March 31, 2014	**38,932**	**96**	**39,028**

At March 31, 2014, the net book value of the Argentinean and Canadian PP&E assets were $12.5 million (December 31, 2013 - $12.0 million) and $26.5 million (December 31, 2013 - $27.1 million), respectively.

PP&E assets consist of costs less depletion, depreciation and impairment of the Company's assets in Argentina and Canada. The amounts capitalized as PP&E assets in Argentina at March 31, 2014 includes $3.4 million of Value Added Tax ("VAT") (December 31, 2013 - $3.3 million). VAT is payable on goods and services supplied to the Company and is not recoverable from the Government of Argentina; however, the Company is allowed to retain VAT on any sales that it collects to the extent of the VAT recorded and paid on previous expenditures.

The depletion expense calculation for the three months ended March 31, 2014 included $28.4 million (December 31, 2013 – $30.6 million) for estimated future development costs associated with proved and probable reserves.

5. Exploration and Evaluation Assets

Canadian $000s	
Cost	
At December 31, 2012	35,760
Additions	20,491
Impairment	(14,719)
Effect of change in foreign exchange rates	(5,787
At December 31, 2013	35,745
Additions	8,736
Impairment	(658)
Effect of change in foreign exchange rates	(4,609)
At March 31, 2014	**39,214**

At March 31, 2014, the net book value of the Argentinean and Canadian E&E assets were $27.6 million (December 31, 2013 - $28.6 million) and $11.6 million (December 31, 2013 - $7.1 million), respectively.

The Company has recorded an impairment charge of $658,000 (December 31, 2013 – $14.7 million) on its Canadian exploration and evaluation assets at March 31, 2014 relating to the remaining costs incurred on two wells abandoned during the first quarter of 2014.

The amounts capitalized as Argentina E&E assets at March 31, 2014 included $7.1 million of VAT (December 31, 2013 - $6.4 million).

6. Decommissioning Obligations

Canadian $000s	**Three months ended March 31 2014**	**Year ended December 31 2013**
Balance, beginning of period	**4,947**	5,191
Incurred from development activities (Note 4)	**-**	210
Incurred from exploration activities (Note 5)	**-**	50
Accretion expense	**47**	137
Revision of estimates	**11**	(448)
Obligations settled	**(23)**	(92)
Effect of change in foreign exchange rates	**(79)**	(101)
Balance, end of period	**4,903**	4,947

The total undiscounted amount of cash flows required to settle Madalena's decommissioning obligations is approximately $8.3 million (December 31, 2013 – $8.7 million) with the majority of the costs to be incurred between 2018 and 2030. The decommissioning obligations have been estimated using existing technology at current prices and discounted using discount rates that reflect current market assessments of the time value of money and the risks specific to each liability. Inflation rates of 10.9% and 2% were used to calculate the future value of the undiscounted decommissioning obligations in Argentina and Canada, respectively (December 31, 2013 – 10.9% and 2%). The risk free rate used to discount the liability was 19.53% (December 31, 2013 – 17.18%) in Argentina and up to 2.81% (December 31, 2013 – up to 2.99%) in Canada.

7. Share Capital

The Company is authorized to issue an unlimited number of common shares. The holders of common shares are entitled to receive dividends as declared by the Company and are entitled to one vote per share.

Share Capital

	Number of Shares 000s	Share Capital $000s
Balance at December 31, 2012	314,307	141,676
Shares issued pursuant to financing	46,763	19,454
Share issue costs	-	(1,766)
Flow through share liability	-	(936)
Stock options exercised	2,959	1,146
Balance at December 31, 2013	364,029	159,574
Shares issued on financing	32,857	23,000
Share issue costs	-	(1,724)
Balance at March 31, 2014	**396,886**	**180,850**

On February 11, 2014, the Company closed a bought deal financing of 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 $23,000,058.

8. Stock Based Compensation

Under the Company's stock option plan, directors, officers, employees and certain consultants are eligible to receive options to acquire common stock of the Company. The exercise price of the granted options is no less than the closing trading price per share on the last day preceding the date of the grant. Total options granted cannot exceed 10% of the issued and outstanding common shares of the Company. Options granted to directors, officers, employees and consultants may vest immediately or over three years on each anniversary of the grant date. Options expire three to five years from the grant date. There are no cash settlement alternatives for employees under the Company's stock option plan.

The weighted average share price of the Company's common shares on the exercise date during the three months ended March 31, 2014 was $0.40.

During the period ended March 31, 2014, no options were granted to any officers, employees, consultants and directors of the Corporation and its subsidiaries. Movements in the number of stock options outstanding and their related weighted average exercise prices are summarized as follows:

Number of share options

	Number of options 000s	Weighted average exercise price CDN$
Outstanding at December 31, 2012	22,334	0.47
Granted	7,260	0.36
Exercised	(2,959)	0.21
Forfeited	(1,842)	0.42
Expired or cancelled	(5,263)	0.76
Outstanding at December 31, 2013 and March 31, 2014	**19,530**	**0.40**
Exercisable at March 31, 2014	**8,277**	**0.48**

9. Related Parties

A director of the Company is a partner of a law firm that provides legal services to the Company. During the three months ended March 31, 2014, the Company incurred fees of $92,900 (2013 - $195,000) from this firm for legal fees related to legal matters of which $7,900 is included in accounts payable and accrued liabilities at March 31, 2014.

10. Supplemental Cash Flow Information

Changes in non-cash working capital

Canadian $000s	Three months ended March 31 2014	2013
Trade and other receivables	**(675)**	(1,162)
Other current assets	**(342)**	(157)
Trade and other payable	**1,094**	4,719
Change in non-cash working capital	**77**	3,400
Attributable to:		
Operating activities	**(1,058)**	(1,461)
Investing activities	**1,135**	4,861
	77	3,400

11. Commitments

Rental Commitments

Canadian $000s	2014	2015	2016	2017
Leased office premises	133	149	154	13

Leased office premises includes estimated operating costs.

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 are estimated at approximately USD$1.94 million plus VAT (net to Madalena) as of March 31, 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.

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.
The Company continues to examine opportunities in respect of a possible a joint venture or other transaction to accelerate exploration and development activities on the block. RBC Capital Markets, Madalena's exclusive advisor to its Neuquen basin assets, is in communication with a broad spectrum of parties to solicit interest in a joint venture or other transaction with the Company. The Company cautions that there are no assurances that an acceptable joint venture arrangement or other transaction will be reached.

Madalena's remaining share of future work commitments associated with the Curamhuele block as of March 31, 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.

Flow-through Shares Commitments

During 2013, the Company completed a CEE flow through share financing in the amount of $5.7 million. As at March 31, 2014, $1.9 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 $3.8 million on qualified expenditures.

12. Net Income (Loss) Per Share

The following table reconciles the weighted average number of common shares used in the basic and diluted net loss per share calculations:

Basic and diluted loss per share

	Three months ended March 31	
	2014	**2013**
Net income (loss) - $000s CDN	297	(2,320)
Weighted average number of common shares:		
Basic – 000s	381,917	314,992
Diluted -000s	398,520	314,992

For the three months ended March 31, 2014, a total of 16,603,333 share options were included in the calculation of diluted earnings per share as they were dilutive. All share options were excluded from the preceding calculation for the three months ended March 31, 2013 as their effect is anti-dilutive.

13. Financial Instruments and Risk Management

The Company is exposed to various risks that arise from its business environment and the financial instruments it holds. The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework, policies and procedures. The following outlines the Company's risk exposures and explains how these risks and its capital structure are managed.

Market risk

Changes in commodity prices, interest rates and foreign currency exchange rates can expose the Company to fluctuations in its net earnings and in the fair value of its financial assets and liabilities.

Commodity price risk

Price fluctuations for both crude oil and natural gas are determined by world supply and demand factors. Additionally, a significant part of the Company's oil and gas revenue is from an oil property in Argentina. Oil prices in Argentina are subject to domestic market discounts which result in prices significantly below benchmark prices. The Company has the following physical natural gas and oil contracts.

Type	Period	Volume	Price Floor	Price Ceiling	Index
Natural gas fixed	April 1, 2014 to Oct. 31, 2014	500 GJ/d	$3.45CDN	$3.45 CDN	AECO
Natural gas fixed	April 1, 2014 to Oct. 31, 2014	300 GJ/d	$3.55CDN	$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 US	WTI
Crude oil call options	Jan. 1, 2014 to Dec. 31, 2014	50 bbl/d	-	$100 US	WTI
Crude oil call options	Jan. 1, 2015 to Dec. 31, 2015	50 bbl/d	-	$95 US	WTI
Crude oil swap	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 March 31, 2014 was a net liability and an unrealized loss of $351,800 (March 31, 2013 - $65,114). Realized losses as at March 31, 2014 were $17,931 (2013 - $nil) and are included in interest and other income on the statement of income (loss) and comprehensive loss. The commodity contracts currently on the condensed interim consolidated final statements are classified as level 2 within the fair value hierarchy.

14. Segmented information

The Company is engaged primarily in the exploration and development of oil and gas. The Company's reportable segments are based on geographic area and comprise Canada and Argentina. The Company's operations in Barbados are not a reportable segment and are included in the Argentina segment because the level of activity in Barbados was not significant at March 31, 2014 and March 31, 2013.

	As at and for three months ended March 31, 2014		
Canadian $000s	Canada	Argentina	Total
Total assets	65,767	46,345	112,112
Total liabilities	(10,022)	(7,740)	(17,762)
Revenues	4,006	2,300	6,306
Income (Loss)	196	101	297
Capital expenditures	5,555	6,993	12,548

	As at and for three months ended March 31, 2013		
Canadian $000s	Canada	Argentina	Total
Total assets	69,055	40,914	109,969
Total liabilities	(16,458)	(3,713)	(20,171)
Revenues	2,266	1,343	3,609
Loss	(1,732)	(588)	(2,320)
Capital expenditures	14,716	2,259	16,975