

## **SAHARA ENERGY LTD.**

### **Management's Discussion and Analysis June 30, 2009**

*This management discussion and analysis ("MD&A") of SAHARA ENERGY LTD. (the "Company", "Corporation" or "Sahara") for the three and six months ended June 30, 2009 contains financial highlights but does not contain the complete financial statements of the Corporation. It should be read in conjunction with the Company's June 30, 2009 unaudited financial statements and its audited financial statements for the year ended December 31, 2008. Additional information is available on SEDAR at [www.sedar.com](http://www.sedar.com). The financial information presented herein has been prepared on the basis of Canadian generally accepted accounting principles ("GAAP"). All references to dollar amounts are in Canadian dollars. This MD&A includes events up to December 7, 2009.*

#### **Forward-Looking Statements**

*The matters discussed in this MD&A include certain forward-looking statements. Forward-looking statements include, without limitation, any statement that may predict, forecast, indicate or imply future results, performance or achievements. Forward-looking statements may be identified, without limitation, by the use of such words as "anticipates", "estimates", "expects", "intends", "plans", "predicts", "projects", "believes", or words or phrases of similar meaning. In addition, any statement that may be made concerning future performance, strategies or prospects and possible future corporate action, is also a forward-looking statement. Forward-looking statements are based on current expectations and projections about future general economic, political and relevant market factors, such as interest rates, foreign exchange rates, equity and capital markets, and the general business environment, in each case assuming no changes to applicable tax or other laws or government regulation. Expectations and projections about future events are inherently subject to, among other things, risks and uncertainties, some of which may be unforeseeable. Accordingly, assumptions concerning future economic and other factors may prove to be incorrect at a future date. Forward-looking statements are not guarantees of future performance, and actual events could differ materially from those expressed or implied in any forward-looking statements made by the Corporation. Any number of important factors could contribute to these digressions, including, but not limited to, general economic, political and market factors in North America and internationally, interest and foreign exchange rates, global equity and capital markets, business competition, technological change, changes in government relations, unexpected judicial or regulatory proceedings and catastrophic events. We stress that the above mentioned list of important factors is not exhaustive. We encourage you to consider these and other factors carefully before making any investment decisions and we urge you to avoid placing undue reliance on forward-looking statements. The Corporation disclaims any intention or obligation to update or revise these forward-looking statements as a result of new information, future events or otherwise, except as required under applicable securities laws.*

## **CORPORATION OVERVIEW AND PRINCIPAL BUSINESS RISKS**

Sahara Energy Ltd. was incorporated under the Business Corporations Act (Alberta) and is listed on the TSX Venture Exchange (“the Exchange”), under the symbol ‘SAH’. The Company is a junior resource exploration company engaged in the acquisition, exploration and development of natural resource properties (primarily oil and gas). The Company’s business is presently focused on the exploration and evaluation of various oil and gas properties in Saskatchewan and Alberta.

The Corporation does not have a history of earnings. The Corporation’s ability to continue as a going concern is dependent upon its ability to attain profitable operations and generate funds there from, and to continue to obtain borrowings from third parties sufficient to meet current and future obligations. For the six months ended June 30, 2009, the Company incurred a net loss of \$835,882 and has an accumulated deficit of \$10,401,116. At June 30, 2009, the Company had a working capital deficiency of \$4,042,407.

The unaudited financial statements for the six months ended June 30, 2009 do not reflect the adjustments or reclassification of assets and liabilities which would be necessary if the Corporation were unable to continue its operations.

## **OVERVIEW AND SIGNIFICANT EVENTS**

Effective March 31, 2008 Sahara purchased all of the outstanding shares in the capital of Mirage Energy Ltd. in exchange for 0.5 of a common share of Sahara for each Mirage common share, for a total purchase price of \$1,072,312. The number of common shares issued by Sahara was 13,403,896. Sahara shares with an assigned value of \$0.08/share. Under the terms of the acquisition, Sahara acquired all of the issued and outstanding shares of Mirage as well as the obligations pursuant to outstanding convertible debentures of Mirage. This acquisition has been accounted for using the purchase method of accounting with the results from operations included from the closing date of the acquisition. Please refer to notes to financial statements for the details and the purchase equation.

For the six months ended June 30, 2009 the Company had net revenues of \$398,314. The Company had a net loss of \$835,882 for the six months ended June 30, 2009.

During the six months ended June 30, 2009 the Company incurred capital expenditures of \$177,347 and disposed of assets for \$45,000. Included in this sale the Company relieved itself on an abandonment liability on its Willesden Green well.

As at June 30, 2009, the Company reported a bank balance of \$1,476 and a working capital deficiency of \$4,042,407. Sahara has been looking at various financing options, including disposal of non-core properties to increase its working capital position.

Subsequent to the reporting period, a total of 14 properties including 9 wells were sold for proceed of \$402,000, to pay down the debt, reduce the accounts payable and reduce the abandonment liabilities.

The Corporation has to deal with significantly lower commodity prices by reducing expenditures as much as possible in order to reduce debt and finance ongoing operational expenses. It is management's view that the Corporation has been able to strengthen its financial position since the year end, with various strategic alternatives, such as a sale of assets and debt restructuring program, to improve its working capital position.

## **OPERATIONAL ACTIVITIES**

For the three months ended June 30, 2009 the Company averaged 64 boepd which consisted of 54 bbls/day of heavy oil and 60 mcf/d (10 boepd) of natural gas.

### Core Area -Heavy Oil – Lloydminster, Alberta

During the reporting period, Sahara did not participate in the drilling of any new wells in our core area. The Sahara 15-14 well was recompleted in the first quarter of 2009, which has increased production. The production suggests that two follow up locations are possible on this 100% owned property.

During the first quarter of 2009 Sahara began a recompletion program through a farm-out agreement. Recompletions were done at well locations 16A, 16B and 16C – 4, which concluded during the second quarter of 2009.

During the reporting period, Sahara focused its effort on reducing the operating expenses to increase company netbacks. This has been achieved through hiring a new field operator that has been able to reduce operating costs and increase well production, which has increased the Company netbacks. Increased heavy oil prices have also been a major factor in contributing to increased netbacks.

### PRODUCTION RELATED INFORMATION

The following tables summarize certain information in respect of Sahara's production, product prices received, royalties paid, operating expenses and resulting netback for the periods indicated below:

	2009		2008	
	Jun. 30	Mar. 31	Dec. 31	Sept. 30
Average Daily Production				
Oil (bbl/d)	54	45	47	66
Gas (Mcf/d)	60	6	9	12
Combined (BOE/d)	64	46	48	68
Average Price Received				
Oil (\$/bbl)	56.75	35.50	42.26	97.94
Gas (\$/Mcf)	3.05	4.62	6.25	9.91
Royalties Paid				
Combined (\$/BOE)	5.94	2.13	7.00	8.16
Production Costs				
Combined (\$/BOE)	30.37	30.92	32.65	31.27
Netback Received				
Combined (\$/BOE)	14.48	2.26	2.46	58.38

### Petroleum and Natural Gas Revenues

Revenues for the three months ended June 30, 2009 were \$296,281, compared to \$250,855 for the three months ended June 30, 2008. The increase in revenue is attributable to higher production volumes, which were partially offset by significantly lower commodity prices in the current year when compared to the prior year. For the six months ended June 30, 2009 revenues were \$441,556, compared to \$1,052,754 for the six months ended June 30, 2008. The decrease in revenues during the current year is the result of significantly lower commodity prices during the current year.

## **Royalties**

Royalties averaged 11.7% for the three months ended June 30, 2009 and 9.8% for the six months ended June 30, 2009. The slight upward trend in royalties is due to increased commodity prices during the second quarter of 2009.

## **Production Expenses**

Production expenses for the three months ended June 30, 2009 were \$177,144, compared to \$176,203 for the three months ended June 30, 2008. For the six months ended June 30, 2009 production expenses were \$304,357, compared to \$512,876 for the six months ended June 30, 2008. The decrease in production during the current year is a result of a reduced number of wells being operated from property sales in the first half of 2008.

## **Operating Netback**

Operating Netbacks for the three months ended June 30, 2009 were \$14.48, compared to \$56.50 for three months ended June 30, 2008. The Operating Netbacks were significantly lower when compared to the same period last year, due to lower commodity prices. For the six months ended June 30, 2009 operating netbacks were \$9.43 compared to \$43.66 for the six months ended June 30, 2008. Lower commodity prices during the current year are the cause of the reduced netbacks.

## **General and Administrative Costs**

General and administrative (“G & A”) expenses for the six months ended June 30, 2009 were \$86,507, compared to \$319,391 for three months ended June 30, 2008. For the six months ended June 30, 2009 (“G & A”) expenses were \$193,240 compared to \$467,360 for the six months ended June 30, 2008. The (“G & A”) costs were significantly lower compared to the same periods last year, as the Company reduced office space, staff and corresponding salaries and wages.

## **Stock-based compensation**

Stock based compensation measures the implicit cost of compensating key personnel through the issuance of stock options. Sahara stock-based compensation expenses incurred for the three months ended June 30, 2009 were \$16,710, compared to \$nil for the three months ended June 30, 2008. For the six months ended June 30, 2009 stock-based compensation was \$41,766 compared to \$146,500 for the six months ended June 30, 2008. Stock based compensation was lower during 2009 due to the expiry of stock options and a reduced number of stock options vesting during the current period.

## **Interest Expense**

Interest expenses for the three months ended June 30, 2009 were \$47,402, compared to \$24,660 for three months ended June 30, 2008. Interest expense was higher during the second quarter of 2009 as a result of interest on debentures and shareholder loans. For the six months ended June 30, 2009 interest expense was \$93,875 compared to \$93,981 for the six months ended June 30, 2008.

## **Depletion Depreciation and Accretion**

Depletion, depreciation and accretion expenses were \$612,019 for the three months ended June 30, 2009 and \$299,300 for the three months ended June 30, 2008. For the six months ended June 30, 2009 depletion, depreciation and accretion expenses was \$833,631 compared to \$857,821 for the six months ended June 30, 2008. Depletion, depreciation and accretion expenses are higher on a rate per unit basis for 2009 when compared to rates used in 2008.

## **Income tax**

Sahara does not have current income tax payable and does not expect to pay current income taxes in 2009 as the Company had estimated tax pools available of \$11,067,513 at June 30, 2009.

## **LIQUIDITY AND CAPITAL RESOURCES**

The Company had a working capital deficiency of \$4,042,407 for the quarter ended June 30, 2009. Included in the working capital deficiency are \$1,337,020 convertible debentures that mature on June 29, 2009. The debentures have yet to be redeemed.

The debentures are convertible at the option of the holder into 1,337,020 units, each unit consisting of one common share and one common share purchase warrant at a price of \$0.50 per share. The warrants expire June 29, 2009.

## **COMMITMENTS AND CONTINGENCIES**

The following is a summary of commitments and contingencies for the reporting period.

### a) Commitments

Premises lease: The Company entered into a lease agreement for a period of five years that calls for annual basic rent payments of \$214,900 per year. The Company currently has two sub-lease agreements in place that provides a recovery of \$112,389 during 2008. The new lease agreement reduces the Company's commitment to approximately \$60,000 per annum. The new lease agreement expires September 2014.

### b) Contingencies

During the first two quarters of 2009 four of the Company's creditors filed claims against the Company totalling \$190,474. Of this amount, \$121,248 has been paid and payment agreements have been reached. Additional payments have been made with the proceeds from the sale of properties. The Company anticipates that the related outstanding will be settled in full by December 31, 2009.

## **RELATED PARTY TRANSACTIONS**

The Company had the following related party transactions during the period measured at the exchange rate, which is the amount established and agreed to by the related parties and which are similar to those negotiable with third parties:

On June 30, 2009 the Company had promissory notes payable of \$367,500 of which \$320,000 is owed to senior management and directors of the Company.

During the current year consulting fees were paid to a corporation controlled by an officer of the Company of \$66,000. Interest of \$16,000 was charged on promissory notes payable to certain officers, directors and corporations under their control.

## **SUBSEQUENT EVENTS**

Four of the Company's creditors filed claims against the Company totalling \$190,474. Of this amount, \$121,248 has been paid and payment agreements have been reached. Additional payments have been made with the proceeds from the sale of properties. The Company anticipates that the related outstanding will be settled in full by December 31, 2009.

The Company sold 14 properties. The proceeds from these sales, \$402,000, were used to pay down outstanding engineering evaluations costs and audit fees as well as other various corporate debt. The sale

of these properties also reduces substantial abandonment and reclamation liabilities to the Company.

During the third quarter of 2009 the Company embarked on a debt restructuring plan in which the Company offered an immediate cash settlement payment of 10% of all outstanding balances to certain creditors. Twenty creditors agreed to this offer and received payments totalling \$18,006. The Company also offered Sahara common shares at a price of \$0.15 as payment on further outstanding debt. The Company proposes to issue 953,099 shares for a debt reduction of \$142,965. The proposal is subject to TSXV approval and the Company cannot obtain approval until the stock resumes trading. The total debt write down was \$323,025.

The Company's marketing agent went into receivership in July 2008 at which time Sahara still had not received oil revenues for July and August 2008 production. The Company has now written down the outstanding receivable of \$316,739 due from their marketing agent to \$7,000 based on The Court of Queens bench decision which was handed down on August 24, 2009.

The Company moved into smaller office space at the same location during the fourth quarter of 2009. The new lease is for \$60,000 per year. This represents a saving of \$65,000 per year.

## **CONTROLS AND PROCEDURES**

As the Corporation is classified as a Venture Issuer under applicable securities legislation, it is required to file basic Chief Executive Officer and Chief Financial Officer Certifications, which it has done for the six months ended June 30, 2009. The Corporation makes no assessment relating to establishment and maintenance of disclosure controls and procedures as defined under Multilateral Instrument 52-109 as at June 30, 2009.

## **BUSINESS RISKS**

The Corporation is engaged in the exploration and development of crude oil. The Corporation's business is inherently risky and there is no assurance that hydrocarbon reserves will be discovered and economically produced.

- **Environment**

All phases of the oil business present environmental risks and hazards and are subject to environmental regulation pursuant to a complex blend of federal, provincial, and municipal laws and regulations. Although the Corporation believes that it is in material compliance with current applicable environmental regulations, no assurance can be given that environmental laws will not result in a curtailment of production or materially increase the costs of production, development, and exploration activities or otherwise adversely affect the Corporation's financial condition, results from operations and or prospects.

- **Financial**

Financial risks associated with the petroleum industry include fluctuation in commodity prices, interest rates, and currency exchange rates. Other financial risks include, but are not limited to, the availability of funds through equity markets and or debt to invest in capital projects to support the Corporation's growth.

- **Operational**

Operational risks include competitive environmental factors, reservoir performance uncertainties and dependence upon third parties for commodity transportation and processing and a complex regulatory environment. The Corporation closely follows the applicable government regulations.

The Corporation carries insurance coverage to protect itself against those potential losses that could be economically insured against.

- **Commodity Price Risk Management**

The Corporation does not have any contracts in place to protect against commodity price changes.

- **Fair Value of Financial Instruments**

The Corporation's financial instruments consist of cash and cash equivalents, accounts receivable, line of credit, accounts payable and accrued liabilities, and note payable. Management has utilized valuation methodologies available as at the year end and has determined that the carrying amounts of such financial instruments approximate their fair value in all cases due to the short-term maturity of these instruments.

- **Foreign Currency Exchange Risk**

The Corporation is exposed to foreign currency fluctuations as crude oil to be received are referenced in United States dollar denominated prices.

It is management's opinion that the Corporation is not currently exposed to commodity price risk, credit risk or interest rate risk except as described above. The Corporation does not use derivative instruments to reduce exposure to commodity price or foreign currency exchange risk.

## **SIGNIFICANT ACCOUNTING POLICIES AND ESTIMATES**

The Corporation prepares its financial statements in accordance with GAAP. The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities, and the reported amounts of revenues and expenses for the year of the financial statements. Significant accounting policies and methods used in the preparation of the financial statements are described in notes of the audited financial statements for the year ended December 31, 2008, as well as in the *Accounting Policies – Accounting Standards Implemented by the Corporation in 2008* discussed below.

The Corporation evaluates its estimates and assumptions on a regular basis, based on historical experience and other relevant factors. Included in the financial statements are estimates used in determining the fair value of investments, revenue recognition and other matters. Actual results could differ materially from those estimates and assumptions.

## **ACCOUNTING POLICIES – ACCOUNTING STANDARDS IMPLEMENTED BY THE CORPORATION IN 2008**

The Corporation's accounting policies are disclosed in the notes to the 2008 audited annual financial statements and in the following disclosure of the impact of new accounting standards implemented by the Corporation in the year ended December 31, 2008.

### *Capital Disclosures*

On January 1, 2008, the Corporation prospectively adopted CICA Section 1535 Capital Disclosures. This Section establishes standards for disclosing information about an entity's objectives, policies and processes for managing its capital structure. The disclosures have been included in notes to the audited financial statements for the year ended December 31, 2008.

## Financial Instruments

On January 1, 2008, the Corporation prospectively adopted the following two new CICA standards: Financial Instruments - Disclosures (Section 3862) and Financial Instruments - Presentation (Section 3863), which replace Financial Instruments - Disclosure and Presentation (Section 3861). The new disclosure standard increases the emphasis on the risks associated with both recognized and unrecognized financial instruments and how those risks are managed. The new presentation standard carries forward former presentation requirements.

## International Financial Reporting Standards (“IFRS”)

In February 2008, the Accounting Standards Board (“AcSB”) confirmed that the use of IFRS will be required in 2011 for publicly accountable enterprises in Canada. In April 2008, the AcSB issued an Omnibus Exposure Draft that publicly accountable enterprises be required to apply IFRS, in full and without modification, on January 1, 2011.

The adoption date of January 1, 2011 will require the restatement, for comparative purposes, of amounts reported by the Corporation for its year ended December 31, 2010, and of the opening balance sheet as at January 1, 2010. The AcSB proposes that CICA Handbook Section – *Accounting Changes*, paragraph 1506.30, which would require an entity to disclose information relating to a new primary source of GAAP that has been issued but is not yet effective and that the entity has not applied, not be applied with respect to Exposure Draft.

The Corporation is continuing to assess the financial reporting impacts of the adoption of IFRS and, at this time, the impact on future financial position and results of operations is not reasonably determinable or estimable. The Corporation does anticipate a significant increase in disclosure resulting from the adoption of IFRS and is continuing to assess the level of disclosure required as well as systems changes that may be necessary to gather and process the information.

## QUARTERLY SUMMARY

Below is a summary of the Corporation’s financial results for the past eight quarters. This information should be read in conjunction with the unaudited quarterly and audited annual financial statements of the Corporation available at [www.sedar.com](http://www.sedar.com).

Financial (\$)	2009		2008				2007	
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
<b>Operating (\$)</b>								
Revenues	296,281	145,275	224,476	603,599	349,905	531,952	677,091	709,224
Royalties	34,679	8,768	(61,751)	(44,412)	4,873	17,634	(106,449)	(142,528)
Other revenue	31	174	(74,462)	162	412	74,676	6,393	59
Revenues, net of royalties	261,602	136,507	162,726	559,349	355,191	624,062	577,035	566,755
Production expenses	177,144	127,214	122,530	195,046	196,168	228,018	526,404	480,852
<b>Operating income (\$)</b>	<b>84,458</b>	<b>9,467</b>	<b>40,196</b>	<b>364,303</b>	<b>159,023</b>	<b>396,044</b>	<b>50,631</b>	<b>85,903</b>
G & A / other expenses (\$)	93,248	111,726	135,083	268,761	585,035	334,116	879,808	347,631
Depletion & depreciation (\$)	612,019	221,612	(88,494)	232,647	237,276	390,102	6,565,256	358,613
<b>Net Income (Loss) (\$)</b>	<b>(564,876)</b>	<b>(271,006)</b>	<b>(1,530,990)</b>	<b>(137,105)</b>	<b>(663,288)</b>	<b>(328,174)</b>	<b>(7,394,433)</b>	<b>(620,341)</b>
<b>Production</b>								
Average (BOE/day)	64	46	48	68	30	92	206	98
<b>Period End Balances (\$)</b>								
Working Capital	(4,042,407)	(4,143,036)	(3,894,401)	(1,868,515)	(2,218,069)	(2,518,577)	(4,124,328)	(4,792,236)
Total Assets	7,370,928	8,373,536	8,309,138	10,439,155	11,201,496	12,161,340	14,724,617	27,511,024
Total Liabilities	5,076,692	5,531,134	5,220,786	5,821,749	6,369,794	6,551,001	8,713,513	16,350,953
Shareholders’ Equity	2,294,236	2,842,402	3,088,352	4,603,007	4,831,702	5,609,710	3,472,035	6,546,850
<b>Shares Outstanding</b>	<b>38,036,032</b>	<b>38,036,032</b>	<b>38,036,032</b>	<b>38,036,032</b>	<b>38,036,032</b>	<b>24,632,406</b>	<b>24,632,406</b>	<b>19,368,083</b>