CUB ENERGY INC

MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2014 AND 2013

Introduction

The following management discussion and analysis ("MD&A") is a review of operations, current financial position and outlook for Cub Energy Inc. (the "Company" or "Cub") and should be read in conjunction with the audited consolidated financials for the year ended December 31, 2013 and the unaudited consolidated financial statements for the three and six months ended June 30, 2014. Amounts are reported in United States dollars, unless otherwise stated, based upon the financial statements prepared in accordance with International Financial Reporting Standards ("IFRS"). This MD&A is dated as of August 13, 2014.

This MD&A provides management's view of the financial condition of the Company and the results of its operations for the reporting periods indicated. Additional information related to the Company and risk factors is available in the Company's Annual Information Form ("AIF") as filed on the Canadian Securities Administrators' website at www.sedar.com or on the Company's website at www.cubenergyinc.com.

Corporate Overview and Strategy

The Company is a publicly-traded, international energy company engaged in exploration and development of onshore oil and gas properties in the Black Sea region of Europe. The Company aims to bring modern technologies (including dual-completions, hydraulic fracturing and horizontal drilling) to deliver new production and reserves on existing under-developed fields, while identifying new conventional and unconventional prospects for future exploration and appraisal. Key to success in this region is the Company's strong local relationships, key operating partnerships and a history of management experience operating in-country.

Current production is driven by a 30% interest in KUB-Gas LLC ("KUB-Gas") in eastern Ukraine and the Company's 100% operated interest in western Ukraine (Tysagaz). The Company recently acquired additional exploration acreage in eastern Ukraine (Technogasidustria LLC or "TGI").

Barrels of Oil Equivalent Conversion

A barrel of oil equivalent ("boe") or units of natural gas equivalents ("Mcfe") are calculated using the conversion factor of 6 Mcf (thousand cubic feet) of natural gas being equivalent to one barrel of oil. A boe conversion ratio of 6 Mcf:1 bbl (barrel), or a Mcfe conversion ratio of 1 bbl:6 Mcf, is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead and is not based on either energy content or current prices. While the boe ratio is useful for comparative measures, it does not accurately reflect individual product values and might be misleading, particularly if used in isolation. As well, given that the value ratio, based on the current price of crude oil to natural gas, is significantly different from the 6:1 energy equivalency ratio, using a 6:1 conversion ratio may be misleading as an indication of value.

Forward Looking Information

This MD&A contains "forward-looking information" which may include, but is not limited to, statements with respect to the future financial or operating performance of the Company, its petroleum and natural gas projects, the future price of resources, the estimation of reserves, the realization of resource estimates, the timing and amount of estimated future production, costs of production, capital, operating and exploration expenditures, costs and timing of development, costs and timing of future exploration, requirements for additional capital, government regulations, environmental risks, reclamation expenses, title disputes or claims and limitations of insurance coverage. Often, but not always, forward-looking statements can be identified by the use of words such as "plans", "is expected", "budget", "scheduled", "estimates", "forecasts", "intends", "anticipates", or "believes" or variations (including negative variations) of such words and phrases, or state that certain actions, events or results "may", "could", "would", "might" or "will" be taken, occur or be achieved.

Forward-looking statements are based on the opinions and estimates of management as of the date such statements are made and are based on assumptions. They involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company and/or its subsidiaries to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. Such factors include, among others, general business, economic, competitive, political and social uncertainties; the actual results of current exploration activities; actual results of reclamation activities; conclusions of economic evaluations; changes in project parameters as plans continue to be refined; future prices of resources; possible variation recovery rates; failure of plant, equipment or processes to operate as anticipated; accidents, labor disputes and other risks of the industry; political instability; delays in obtaining governmental approvals or financing or in the completion of development or construction activities, as well as those factors discussed in the section entitled "Risk Factors" in the Company's AIF. Although the Company has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in forward-looking statements, there may be other factors that cause actions, events or results to differ from those anticipated, estimated or intended. Forward-looking statements contained herein are made as of the date of this MD&A and the Company disclaims any obligation to update any forward-looking statements, whether as a result of new information, future events or results, except as may be required by applicable securities laws. There can be no assurance that forward-looking statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, readers should not place undue reliance on forward-looking statements.

Reported Results and Equity Investment

The Company's 2014 production growth and use of capital is expected to be driven by the Company's 100% ownership of Tysagaz, whose assets are in western Ukraine as well as its investment in Kub-Gas. The Company plans up to four drilling activities in Tysagaz in 2014 including the recently completed and successful RK-21 well.

The Company has an effective 30% ownership interest in KUB-Gas, a Ukrainian company which owns assets representing a substantial portion of the Company's core operating properties, income and cashflow.

All of the KUB-Gas shares are held through KUBGAS Holdings Limited ("KUB Holdings"), a private company incorporated in Cyprus, which is 30% owned by the Company and 70% owned by Serinus Energy Inc. ("Serinus"). The Company does not control KUB Holdings and is required under IFRS to record its investment under the equity method of accounting. In doing so, it reports none of the revenues, royalties or production expenses for KUB Holdings within its consolidated statements of operations and cash flows. Similarly the Company does not report the individual assets and liabilities of KUB Holdings and KUB-Gas on its consolidated statements of financial position.

The 30% share of the net assets of KUB Holdings and KUB-Gas attributable to the Company is presented as an "Equity investment in KUB Holdings" within non-current assets on the consolidated statement of financial position. Net profits from the 30% interest are presented as a single line item "income from equity investment" on the statements of operations.

A substantial portion of the financial analysis in this MD&A does not reflect the Company's interest in the results of KUB Holdings and KUB-Gas. The table below summarizes the six months ended June 30, 2014 results reported by the Company in accordance with IFRS, then deducts the single line item "income from equity investment" and adds the 30% share allocable to its equity investment to reflect the gross results of operations attributable to the Company's 30% economic interest and finally the pro-rata net to Cub results which is a non-IFRS measure.

	As Reported	Deduct Equity Investment	Add 30% Allocated from Equity Investment	Pro-rata Net to Cub
Average Daily Production (boe/d)	325	-	1,563	1,888
Revenue	$ 3,394,000	$ -	$ 15,845,000	$ 19,239,000
Cost of sales	1,169,000	-	5,724,000	6,893,000
Gross profit	**2,225,000**	**-**	**10,121,000**	**12,346,000**
Operating expenses				
Selling and general administrative	3,952,000	-	-	3,952,000
Share based payments	667,000	-	-	667,000
Depletion and depreciation	798,000	-	3,016,000	3,814,000
Finance expense (income)	7,000	-	236,000	243,000
Foreign exchange loss	-	-	1,258,000	1,258,000
Accretion and decommissioning obligation	5,000	-	5,000	10,000
	5,429,000	**-**	**4,515,000**	**9,944,000**
Other income				
Income from equity investment	4,466,000	(4,466,000)	-	-
Profit (loss) before tax	**1,262,000**	**(4,466,000)**	**5,606,000**	**2,402,000**
Income tax expense (recovery)	**(15)**	**-**	**1,140,000**	**1,125,000**
Net profit (loss)	**$ 1,277,000**	**$ (4,466,000)**	**$ 4,466,000**	**$ 1,277,000**
Netback ($/boe)				
Revenue	$ 56.85	-	$57.30	$ 57.22
Royalty	(13.46)	-	(13.82)	(13.75)
Production expenses	(10.82)	-	(6.88)	(7.58)
Field netback ($/boe)	**$ 32.57**	**-**	**$ 36.60**	**$ 35.89**
Field netback ($/mcfe)	**$ 5.43**	**-**	**$ 6.10**	**$ 5.98**
Funds from operations(1)	**$ 2,376,000**	**$ (4,095,000)**	**$ 8,613,000**	**$ 6,894,000**
Capital expenditures	**4,108,000**	**-**	**3,776,000**	**7,884,000**
Net working capital (2)	**39,000**	**-**	**827,000**	**866,000**
Long term debt(3)	**2,000,000**	**-**	**715,000**	**2,715,000**

(1) Funds from operations is a non-IFRS measure and is defined as cash flow from operating activities, excluding changes in non-cash working capital related to operating activities. Funds flow demonstrates the ability of the Company to generate funds for future capital investment. Deducted from the fund flows from operations was the $4,095,000 in dividends received from KUB Holdings during the period.

(2) Net working capital is a non-IFRS measure calculated as current assets less current liabilities. Net working capital demonstrates the capacity (or incapacity) to fund existing short-term liabilities with existing current assets.

(3) See "off balance sheet arrangements" located elsewhere in this MD&A. This amount represents the Company's 30% share of the long term portion of the debt.

Results of Operations

(in thousands of US Dollars)	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
Petroleum and natural gas revenue	1,693	823	3,394	1,878
Pro-rata petroleum and natural gas revenue(1)	10,505	9,501	19,239	19,169
Net profit	2,192	326	1,277	602
Earnings per share – basic and diluted	0.01	0.00	0.00	0.00
Funds generated from operations(2)	2,502	724	2,376	2,307
Pro-rata funds generated from operations(3)	4,503	1,828	6,894	4,520
Capital expenditures(4)	3,034	906	4,108	1,229
Pro-rata capital expenditures(4)	4,662	2,037	7,884	3,908
Pro-rata netback ($/boe)	41.46	37.21	35.89	40.53
Pro-rata netback ($Mcfe)	6.91	6.20	5.98	6.76

	June 30, 2014	December 31, 2013
Working capital	39	942
Cash and cash equivalents	2,118	1,617
Long-term debt	2,000	-

Notes:

(1) Pro-rata petroleum and natural gas revenue is a non-IFRS measure that adds the Company's petroleum and natural gas revenue earned in the respective periods to the Company's 30% equity share of the KUB-Gas petroleum and natural gas sales that the Company has an economic interest in.

(2) Funds from operations is a non-IFRS measure and is defined as cash flow from operating activities, excluding changes in non-cash working capital.

(3) Pro-rata funds from operations is a non-IFRS measure that adds the Company's funds from operations in the respective periods to the Company's 30% equity share of the KUB-Gas funds from operations that the Company has an economic interest in. The KUB-Gas funds from operations is calculated as the income from equity investment less the KUB-Gas depletion and depreciation.

(4) Capital expenditures includes the purchase of property, plant and equipment and the purchase of exploration and evaluation assets. Pro-rata capital expenditures is a non-IFRS measure that adds the Company's capital expenditures in the respective periods to the Company's 30% equity share of the KUB-Gas capital expenditures that the Company has an economic interest in.

Highlights

- Production averaged 1,868 boe/d (95% natural gas) for the three months ended June 30, 2014 for an increase of 25% over 1,490 boe/d in the same period in 2013;
- Exit rate of 2,154 boe/d at June 30, 2014 for a 10% increase over exit rate of 1,952 boe/d at March 31, 2014;
- Current production of approximately 2,350 boe/d;
- Netback of $41.46/Boe or $6.91/Mcfe for the quarter ended June 30, 2014;
- Received $3,060,000 in dividends from Kub-Gas during the quarter ended June 30, 2014;
- Achieved average natural gas price of $10.23/Mcf and condensate price of $79.86/bbl for the three months ended June 30, 2014;
- On March 14, 2014, the RK-21 well was spud and subsequently tested gas at a maximum rate flow rate of 2.6 MMcf/d through a 12-millimetre choke. The well was tied-in and placed on production on June 2, 2014;
- In May 2014, Cub re-entered the RK-1 well for a test of the deeper Mesozoic sands. The well reached TD of 3,995 metres and Cub completed the evaluation of the Mesozoic sands and the results show the presence of pipeline quality gas from samples taken during testing. It is believed that these sands have the potential to flow at commercial rates after hydraulic fracture stimulation; however, this type of operation is not feasible in the current wellbore. The Company is evaluating a new well to 4,000 metres which will allow stimulation by hydraulic fracturing. The well is currently shut-in and being prepared for a completion attempt in the D-4 reservoir at 1,400 metres;
- KUB-Gas (30%WI) achieved a significant milestone in daily production – over 1 million cubic metres per day ("**MMcm/d**") or approximately 5,885 boe/d (1,766 boe/d Cub WI) late in the second quarter;
- Gas began flowing from the new Kub-Gas (30% WI) Makeevskoye and Olgovskoye production and processing facility on March 6, 2014 resulting in increased capacity to 68 MMcf/d from the previous 30 MMcf/d. Full production gains from the new facility were achieved late in the second quarter of 2014;
- The M-17 well was drilled during the first quarter. Logs indicated 9 metres of net pay in the primary target, the S6 sand, and 2.5 metres of pay in the S5 and 5.5 metres in the deeper S7. They also indicated resource potential 22 metres in the R30c. On test, the S7 achieved a rate of 900 Mcf/d, exceeding the Company's expectations that it would require stimulation to produce at a commercial rate. A bridge plug was set above the S7, and after testing, and the S6 commenced production on June 26, 2014 at an initial rate of 6.0 MMcf/d (1.8 MMcf/d Cub WI). That rate has been increased several times, allowing the well to stabilize at each stage, and it has averaged 8.6 MMcf/d (2.6 MMcf/d Cub WI) since start-up. The S5 and R30c remain behind pipe to be tested and developed at a later date; and
- On June 27, 2014, field operations in eastern Ukraine were suspended temporarily to ensure the continued safety of employees and assets during the ongoing regional conflict in the region. As a result, the NM-4 well that commenced drilling to test a seismically-identified stratigraphic play but was suspended at 102 metres.

Ukraine Royalty Rates

On August 1, 2014, and subsequent to the quarter ended June 30, 2014, the Ukrainian President signed a new law temporarily increasing royalties on natural gas production to 55% from their current level of 28% through December 31, 2014 (five months). The royalty rate will return to 28% on January 1, 2015.

Additionally, under the enacted law, the royalty rate for newly drilled wells will be discounted for two years at a discount coefficient of 0.55. In effect, newly drilled wells put on production after August 1, 2014 will have a royalty rate of 30.25%. This discount coefficient will apply to newly drilled wells for two years.

President Poroshenko signed the new law one day after the Ukraine parliament met in special session and passed the law on July 31, 2014. Cub, along with other private sector gas producers opposed to this royalty increase, prepared a joint letter to the Ukrainian Prime Minister explaining the likely negative effects of such legislation on the domestic energy industry and urging him not to support it. The law that was eventually passed and signed by the President sets a lower royalty rate with less restrictive terms than initially proposed. For Cub, the royalty increase could translate into an approximate 50% reduction in netbacks for the next five months.

However, given that this will reduce our netbacks by approximately 50% and resulting cash flow for the next five months, the Company will be re-evaluating its work programs for the remainder of 2014 to preserve its capital options.

Ukraine Gas Prices and Currency

During the first quarter ended March 31, 2014, natural gas prices declined per the terms of a temporary agreement between Russia and Ukraine and was also materially impacted by the devaluation of the Ukrainian Hryvnia ("UAH") which went from approximately 8.2 UAH/USD to 11.4 UAH/USD by the end of the first quarter or a 39% decline. The combination of Natural gas price declines and devaluation of the local currency resulted in the Company receiving approximately $8.63/Mcf during the first quarter of 2014. For operating expenses and capital expenditures incurred and paid in UAH, the Company benefits from the lower equivalents in US dollars.

During the second quarter ended June 30, 2014, the temporary agreement between Russian and Ukraine was terminated and gas prices materially increased. The gas price realized in second quarter was $10.23/Mcf, which has continued into July and August of 2014. The exchange rate also reached a more stable level versus the USD and was 11.4 UAH/USD at the end of the second quarter of 2014. Subsequent to the quarter ended June 30, 2014, the exchange rate reached levels above 13.00 UAH/USD. The future of natural gas prices in Ukraine is currently subject to a high degree of uncertainty and it is unknown what the future prices the Company will receive on its Ukraine production.

Ukraine KUB-Gas Assets (30% Interest)

On June 27, 2014, the Company and its partner announced that they decided to suspend temporarily developmental field operations at KUB-Gas to ensure the continued safety of employees and assets during the ongoing regional conflict in eastern Ukraine. KUB-Gas contractors were refusing to support continued developmental operations at the time. As such, KUB-Gas is continuing with production, but suspending developmental field operations until the situation stabilizes. The Vergunskoye and Krutogorovskoye fields at KUB-Gas, which are located in the area close to the city of Lugansk, have been temporarily shut in. The production from these fields represents approximately 2% of the Company's total production. There has been some improvement in the security situation in the vicinity of the Company's main producing fields, and KUB-Gas is in discussions with service providers regarding the potential of resuming drilling and completion operations, but it is not yet possible to predict when and if that may occur.

Prior to cessation of developmental field operations, the Company completed and tested the M-17 well, this well was drilled in the first quarter of 2014 to a total depth of 3,445 metres. During the second quarter, the well was cased and the service rig began completion operations. Logs indicated pay in the S5 and S6 zones, and resource potential in the R30c and S7 sections, the S7 tested 900 Mcf/d without stimulation. The S6 was tested at multiple rates, the highest of which was 6.6 MMcf/d. The S6 zone was placed on production on June 26, 2014 and averaged 6.4 MMcf/d (1.9 MMcf/d net to Cub) as at June 30, 2014.

The O-11 well was spud on April 4, 2014 after the drilling rig moved on from M-17. It reached its planned depth of 3,230 metres in late May, and was cased and the rig released. In June, the well was perforated, and experienced a strong air blow, followed by gas to surface. The well was shut in for a pressure build up. No further testing will be undertaken at this time.

The NM-4 well was spud on June 16, and drilled to a depth of 102 metres. Surface casing was run and cemented in place prior to suspending drilling operations.

Ukraine Tysagaz Assets (100% Interest)

During the quarter ended June 30, 2014, the RK-21 well tested gas at a maximum rate flow rate of 2.6 MMcf/d through a 12-millimetre choke. The well was tied-in and placed on production on June 2, 2014.

In May 2014, Cub re-entered the RK-1 well for a test of the deeper Mesozoic sands. The well reached TD of 3,995 metres and Cub completed the evaluation of the Mesozoic sands and the results show the presence of pipeline quality gas from samples taken during testing. It is believed that these sands have the potential to flow at commercial rates after hydraulic fracture stimulation. This type of operation is not feasible in the current wellbore. The Company is evaluating a new well to 4,000 metres which will allow stimulation by hydraulic fracturing. The well is currently shut-in and being prepared for a completion attempt in the D-4 reservoir at 1,400 metres.

Ukraine TGI Assets (100% Interest)

During 2013, the Company initiated multiple 3D seismic campaigns on its TGI assets and, in 2014, has been focused on the processing and interpretation of these acquisitions.

Turkish Assets

In March 2014, the Company and its Turkish partner entered into a settlement agreement in which the Company relinquished its interest in the eleven Turkish licenses in consideration of receipt of $250,000 from the restricted cash account, consisting of a reimbursement of past expenditures and a return of half the balance in the restricted cash account. The remaining balance of $324,000 in the restricted cash account was transferred to the Turkish partner. The Company was also released from any and all claims, liabilities and commitments. The Company continues to examine further upstream oil and gas opportunities in Turkey.

Summary of Quarterly Results

The following table sets out selected unaudited consolidated financial information for each of the last eight quarters ended up to and including June 30, 2014. The information contained herein is taken from the consolidated financial statements of the Company for each of the aforementioned quarters.

Quarter Ended	Jun 30, 2014	Mar 31, 2014	Dec 31, 2013	Sept 30, 2013
Revenue	1,693,000	1,701,000	745,000	627,000
Cost of sales	502,000	667,000	343,000	388,000
Income from equity investment	3,389,000	1,077,000	2,836,000	3,816,000
Operating expenses	2,403,000	3,026,000	8,308,000	3,325,000
Net profit (loss)	2,192,000	(915,000)	(3,886,000)	271,000
Earnings (loss) per share	0.01	(0.00)	(0.02)	0.00
Working Capital (deficit)	39,000	(306,000)	942,000	3,769,000

Quarter Ended	Jun 30, 2013	Mar 31, 2013	Dec 31, 2012	Sept 30, 2012
Revenue	823,000	1,055,000	606,000	546,000
Cost of sales	452,000	561,000	266,000	271,000
Income from equity investment	2,351,000	2,153,000	1,982,000	1,741,000
Operating expenses	2,358,000	2,309,000	2,714,000	1,740,000

Net profit (loss)	326,000	276,000	(136,000)	54,000
Earnings (loss) per share	0.00	0.00	(0.00)	0.00
Working Capital (deficit)	10,232,000	10,611,000	9,577,000	(229,000)

Revenue and Cost of Sales

During the quarter ended June 30, 2014, the Company's gross profit from its Tysagaz operations in western Ukraine increased to $1,191,000 from $371,000 in the 2013 comparative period. The increased profit relates to the RK-22 and RK-21 wells, which were brought on production late 2013 and late Q2 2014, respectively.

During the six months ended June 30, 2014, the gross profit from its Tysagaz operations was $2,225,000 as compared to $865,000 for the comparative 2013 period. The revenue during the current period increased due to the new RK wells and was offset somewhat by the lower gas price as the Company realised $9.46/Mcf in the six months ended June 30, 2014 as compared to $11.77/Mcf in the comparative 2013 period.

Income from Equity Investment

The Company accounts for its 30% indirect ownership in KUB Holdings as an investment under the equity method. During the quarter ended June 30, 2014, KUB-Gas generated gross revenues of approximately $29,372,000 (2013 - $28,929,000) and net income of $11,272,000 (2013 – $7,838,000). This resulted in an income from equity investment for the quarterly period to the Company of $3,389,000 (2013 - $2,351,000), an increase of approximately 44% period over period as KUB Holdings netbacks increased in the current period.

During the six months ended June 30, 2014, KUB-Gas generated gross revenues of approximately $52,818,000 (2013 - $57,638,000) and net income of $14,862,000 (2013 – $15,014,000). This resulted in an income from equity investment for the quarterly period to the Company of $4,466,000 (2013 - $4,504,000) which was relatively flat period over period. Despite an increase in production during the current six month period, the lower gas price realised in the first quarter at KUB-Gas period and the devaluation of the local Ukrainian currency by 44% lead to a lower netbacks and net income. In the six months ended June 30, 2014, Kub-Gas reported a $4,192,000 loss on foreign exchange (net to Cub is $1,258,000) as it held US denominated debt (EBRD Loan Facility) in its Ukrainian subsidiary.

The Company estimates that its pro-rata portion of cash flow from operations from KUB Holdings to be approximately $8,613,000 for the six months ended June 30, 2014.

Selling and General Administrative Expenses

Selling and general administrative expenses were $1,736,000 during the quarter ended June 30, 2014, as compared to $1,998,000 in the comparative 2013 period for a decrease of $262,000. During the six months ended June 30, 2014, selling and general administrative expenses were $3,952,000 as compared to $3,949,000 in the comparative 2013 period. The Company did initiate cost cutting efforts during the current quarter and expects to the see the effects of those efforts in the upcoming quarters. Some of the significant items contained within selling and general administrative expenses are as follow:

Professional fees

Professional fees decreased to $198,000 during the quarter ended June 30, 2014 from $306,000 in the comparative 2013 period representing a 35% decrease. During the six months ended June 30, 2014, professional fees were $489,000 as compared to $630,000 in the comparative 2013 period. The Company's professional costs during the respective periods reflected the costs of being a public issuer including third party engineering reports and yearend financial audits. The decrease in professional fees reflects the lower level of corporate activity in 2014 as compared to 2013.

Office and administration

Office and administration costs decreased to $173,000 in the quarter ended June 30, 2014, from $249,000 in the comparative 2013 quarter. During the six months ended June 30, 2014, office and administrative costs decreased to $386,000 from $463,000 as the Company made cost costing efforts.

Salaries

During the current quarter, salaries to staff and directors fees increased to $862,000 from $504,000 during the comparative 2013 quarter. During the six months ended June 30, 2014 salaries increased to $1,799,000 from $1,093,000 as compared to the 2013 period. The Company increased the number of directors, executives, management and staff in the second half of 2013 as it increased general corporate activity and development efforts. The Company has been taking cost cutting measures which went into effect late in the second quarter of 2014.

Consulting

Consulting fees were $141,000 during the current quarter as compared to $209,000 during the comparative 2013 quarter and consulting fees were $320,000 during the six months ended June 30, 2014 as compared to $373,000 during the comparative 2013 period. The Company retains consultants periodically on an as needed basis to assist in operations and administration.

Travel

During the current quarter, travel costs were $270,000, for a decrease of $194,000 from the comparative 2013 quarter which totaled $464,000. Travel costs also decreased $263,000 between the six months ended June 30, 2014 as compared to the 2013 period. Travel expenses include costs associated with international operations, investor marketing and business development.

Business development and investor relations

During the quarter, business development and investor relations expenses were $25,000 as compared to $188,000 in the comparative period in 2013. The Company also reduced the expenditures during the six months ended June 30, 2014 as its business development and investor relations expenses decreased from $310,000 in 2013 to $71,000 in 2014. The expenses consisted of investor awareness activities which have been reduced recently due to cost cutting and the unrest in eastern Ukraine.

Share Based Payments

The Company recorded $290,000 in share based payments for the vesting of stock options to directors, officers, employees and consultants as determined by the black-scholes option price model for the quarter ended June 30, 2014 as compared to $45,000 in related expenses in the comparative quarter. For the six months ended June 30, 2014, the expense was $667,000 as compared to $123,000 for the 2013 comparative period. The Company experienced a higher expense in 2014 due to a material stock option grant in July, 2013.

Net Profit

During the quarter ended June 30, 2014, the Company recorded a net profit of $2,192,000 or $0.01 per share as compared to $326,000 or $0.00 per share in the comparative 2013 period. During the six months ended June 30, 2014, the Company recorded a net profit of $1,277,000 or $0.00 per share as compared to $602,000 or $0.00 per share in the comparative 2013 period.

Foreign Currency Translation Loss

During the six months ended June 30, 2014, the Company recorded a foreign currency translation loss on foreign operations of $23,542,000 as compared to a loss of $303,000 in the comparative 2013 period. The losses relate to the revaluation of the Company's foreign assets and liabilities from the local Ukrainian currency to the US dollar in accordance with the Company's accounting policy for the translation of its subsidiaries. The carrying value of the assets of the Ukrainian subsidiaries were materially impacted by the devaluation of the local currency which decreased approximately 39% in the first quarter of 2014 as the Ukrainian currency went from approximately 8.2 UAH/USD at December 31, 2013 to 11.4 UAH/USD at March 31, 2014. The currency at June 30, 2014 was 11.8 UAH/USD which caused a translation loss during the quarter ended June 30, 2014 of $2,226,000 as compared to $61,000 in the comparative 2013 period. The losses materially lowered the carrying value of the Ukrainian property, plant and equipment, the value of the equity investment in KUB Holdings, the Company's Ukrainian exploration and evaluation assets and deferred income tax liability. These losses do not impair the ability of those assets or liabilities to perform their intended purpose. If the Ukrainian currency were to appreciate, some or all of these unrealized losses would be recouped. Subsequent to the quarter ended June 30, 2014, the exchange rate reached levels above 13.00 UAH/USD.

Liquidity, Capital Resources and Financings

At June 30, 2014, the Company had a cash balance of $2,118,000 (December 31, 2013 – $1,617,000) and working capital of $39,000 (December 31, 2013 – $942,000). The Company had no long-term debt or capital leases other than the Pelicourt line of credit. The Company has historically been able to successfully raise funds through the issuance of common shares or debt.

The Company has access to a $5,000,000 unsecured line of credit with Pelicourt Limited, a significant shareholder of the Company which has a common director. The line of credit bears interest at 9% per annum payable semi-annually and the principal of the line of credit is due in full on September 30, 2016. The Company drew down $2,000,000 during the six months ended June 30, 2014.

During the six months ended June 30, 2014, the Company received dividends in the amount of $4,095,000 from KUB Holdings and subsequent to June 30, 2014, the Company received further dividends of $1,740,000.

The major uses of cash continue to be the purchase of property and equipment and the further exploration and evaluation of its oil and gas assets on its 100% owned western Ukraine assets. During the six months ended June 30, 2014, the Company used $3,537,000 of its cash on the purchase of property, plant and equipment and $571,000 on exploration and evaluation activities as compared to $907,000 and $322,000, respectively, in the comparative 2013 period. The property, plant and equipment additions for 2014 consisted of the drilling and completion of the RK-21 well and the re-entry of RK-1 in western Ukraine.

During the six months ended June 30, 2014, KUB-Gas incurred approximately $12,586,000 of capital expenditures on property, plant and equipment of which the Company's 30% equity share was $3,776,000 and included the continuing costs of the new gas facility, drilling and completion of the O-24 and M-17 wells and related tie-in costs, where applicable.

Outlook

For the remainder of 2014, the Company will continue on its 100% owned and operated Tysagaz assets in western Ukraine. The RK-1 well is currently shut-in and being prepared for a completion attempt in the D-4 reservoir at 1,400 metres. The Company plans to drill the RK-23 development well in the third quarter of 2014.

The Company is re-evaluating the balance of its capital program in light of the recent temporary increases in royalty rates through the end of the year.

Operations at KUB-Gas in eastern Ukraine are temporarily suspended to ensure the continued safety of employees and assets during the ongoing regional conflict in the region. The Company continues to monitor the security situation and the potential of re-commencing field operations as soon as possible. The Company has four imminent drilling locations, including two exploration wells (NM-4 and M-22), and two development wells (M-15 and M-18). Success on any of these will open up additional development and exploration locations.

Once field operations resume, the Company has planned fracture stimulations for four wells in Ukraine, including NM-3, O-11, O-15 and possibly the S7 zone in M-17. The NM-3 well is a potential oil discovery made in July 2013. The Visean formation is tight and unable to flow unstimulated. If the fracture is successful, it will be the first commercial oil well on Company licences, and will set up several additional development locations.

Ukraine's political and economic situation has been volatile since the former Government's decision not to sign the Association Agreement and the Deep and Comprehensive Free Trade Agreement with the European Union in late November 2013. Political and social unrest, which escalated into violent conflicts in February 2014, has resulted in the Ukrainian parliament initiating the resignation of the president, election of a new President (Petro Poroshenko) in May 2014, change of government and heads of key governing bodies. It also led to the deepening of the ongoing economic crisis, widening of the state budget deficit, depletion of the National Bank of Ukraine's foreign currency reserves and, as a result, a further downgrading of the Ukrainian sovereign debt credit ratings. In February 2014, following the significant devaluation of the national currency, the National Bank of Ukraine introduced certain administrative restrictions on currency conversion transactions that require Ukrainian companies to convert 50% of all incoming foreign transfers to the local Ukrainian currency. The National Bank of Ukraine also imposed a restriction that US and other foreign denominated loans in Ukraine could not be repaid in advance of their maturity dates.

With the new government in place, President Poroshenko signed the Association Agreement with European Union -- the same agreement that was rejected in November 2013. The International Monetary Fund committed to a $17 billion two-year aid program to help the country's economy recover.

After the annexation of Crimea to the Russian federation in March 2014, political violence escalated in eastern Ukraine with pro-Russian rebels ceasing various government buildings in the Donetsk and Lughansk regions. This ongoing conflict between the pro-Russian rebels and Ukraine army raised security concerns surrounding the Company's eastern Ukraine assets.

The final resolution and the effects of Ukraine's political and economic crisis are difficult to predict and could negatively affect the Company's results and financial position. With the uncertainty of gas prices and fiscal terms in Ukraine, it is possible that the programs could get further constrained.

Outstanding Share Data

Issued and outstanding as at the date of this MD&A:

Type	Number
Common Shares	311,746,285
Warrants	9,185,563
Stock options	22,109,000
Total Issued and Outstanding	343,040,848

Off Balance Sheet Arrangements

The Company, through its wholly-owned subsidiary, Gastek, is an indirect owner of 30% of KUB-Gas and has provided a cross-indemnity of up to 30% of the European Bank for Reconstruction and Development ("EBRD") Loan Facility to Serinus to offset Serinus' 100% direct guarantee of the EBRD Loan Facility outstanding from time to time. As at June 30, 2014, the remaining balance of the EBRD Loan Facility was approximately $6,091,000 of which the Company has guaranteed $1,827,000 or 30%. Subsequent to the quarter ended June 30, 2014, a further scheduled payment was made and the current remaining balance was approximately $4,300,000 of which the Company has guaranteed $1,290,000.

Commitments

Ukraine

The Company has an obligation to incur certain capital expenditures to comply with the Ukrainian exploration license requirements. Under these license maintenance commitments, the Company is required to explore its licensed fields. Although these commitments are not binding and may be modified based on results of exploration work, the Company's potential capital expenditures relating to qualifying activities on gas and gas condensate fields will be material during the period from 2014 to 2015 as part of the planned exploration and development program. Justified deviation from the capital expenditures is permitted and should be agreed with the licensor, while failure to commit exploration works and substantiate the different capital expenditure schedule may result in termination of the license.

Office Space

The Company has a lease agreement for office space in Houston, Texas which expires in May 2020. The commitment is approximately $166,000 per year for the term of the lease.

Transactions with Related Parties

Transactions with related parties are incurred in the normal course of business and are measured at the fair value, which is the amount of consideration established and approved by the related parties. During the six months ended June 30, 2014, there were no related party transactions other than the Pelicourt line of credit-see "Liquidity, Capital Resources and Financing".

Critical Accounting Estimates

Management makes a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these consolidated financial statements in conformity with IFRS. Actual results could differ from those estimates. Significant estimates included:

- To value the equity investment in KUB Holdings, management obtains financial information from the majority owner and adjusts the carrying value of the investment. The equity investment in KUB Holdings is subject to all estimates included in the financial information from the majority owner including estimates of impairment losses.
- The determination of Cash Generating Units ("CGU") requires judgment in defining a group of assets that generate cash inflows that are largely independent of the cash inflows from other assets or groups of assets. CGUs are determined by similar geological structure, shared infrastructure, geographical proximity, commodity type, similar exposure to market risks and materiality.

- Amounts recognized for depletion and depreciation and amounts used for impairment calculations are based on estimates of petroleum and natural gas reserves. By their nature, the estimates of reserves, including the estimates of future prices, costs, discount rates and the related future cash flows, are subject to measurement uncertainty. These estimates are also used in assessing impairment for exploration and evaluation assets.
- Amounts recognized for decommissioning obligations, if any, and the related accretion expense requires the use of estimates with respect to the amount and timing of decommissioning expenditures. Other provisions are recognized in the period when it becomes probable that there will be a future cash outflow.
- Charges for share-based payment and the value of warrants are based on the fair value at the date of issuance. These instruments are subject to the estimation using pricing models such as the Black-Scholes option pricing model, which is based on assumptions such as volatility, dividend yield, risk free rate of return and expected term. A forfeiture rate is estimated on the grant date and is adjusted to reflect the actual number of options that vest.
- Allocation of the purchase price of acquisitions requires estimates as to the fair market value of the assets acquired and judgment is required in determination if the transaction constitutes a business or an asset acquisition.
- Tax interpretations, regulations and legislations in the jurisdictions in which the Company operates are subject to change. As such, income taxes are subject to measurement uncertainty. Deferred income tax assets are assessed by management at the end of the reporting period to determine the likelihood that they will be realized from future taxable earnings.
- Judgment is required to determine the functional currency of the parent and its subsidiaries. These judgments are continuously evaluated and are based on management's experience and knowledge of the relevant facts and circumstances.

New Standards and Interpretations

a) New Accounting Standards Effective in 2014

In May 2013, IASB issued IFRIC 21 Levies, which sets out the accounting for an obligation to pay a levy that is not income tax. The interpretation addresses what the obligating event is that gives rise to the recognition of a liability to pay a levy. The Company performed an assessment of the impact of IFRIC 21 and concluded it did not have a significant impact on its consolidated financial statements.

b) New Accounting Standards Issued But Not Yet Effective

In November 2009, the IASB issued IFRS 9 Financial Instruments as the first step in its project to replace IAS 39 Financial Instruments: Recognition and Measurement. In February 2014, the IASB tentatively decided that the mandatory effective date of IFRS 9 would be annual periods beginning on or after January 1, 2018. The Company is currently assessing the impact of adopting IFRS 9 on its consolidated financial statements.

Annual Improvements 2010-2012 Cycle was issued by IASB in December 2013. The annual improvement process is comprised of minor revisions, clarifications or corrections to the standards. The following standards have been amended: IFRS 2, IFRS 3, IFRS 8, IFRS 13, IAS 16, IAS 24 and IAS 38. These amendments are effective for annual periods beginning on or after July 1, 2014. Earlier application is permitted.

Annual Improvements 2011-2013 Cycle was issued by IASB in December 2013. The annual improvement process is comprised of minor revisions, clarifications or corrections to the standards. The following standards have been amended: IFRS 1, IFRS 3, IFRS 13 and IAS 40. These amendments are effective for annual periods beginning on or after July 1, 2014. Earlier application is permitted.

Financial Instruments and Other Instruments

The Company's financial instruments consist of cash, restricted cash, trade and other receivables, trade and other payables and accrued liabilities and provisions.

Management believes that these financial instruments expose the Company to a limited amount of currency or credit risks. The fair market values of cash, restricted cash, investment, trade and other receivables, line of credit and trade and other payables and accrued liabilities approximate their carrying values. Provisions are based on expected future cash outflow.

Non-IFRS Measures

The financial information presented in this MD&A has been prepared in accordance with IFRS except for the terms "funds from operations", "netback", "working capital" and "pro-rata net to Cub" which are not recognized measures under IFRS and do not have standardized meanings prescribed by IFRS. These non-IFRS measures are presented for information purposes only and should not be considered an alternative to, or more meaningful than information presented in accordance with IFRS. Management believes funds from operations, netback, working capital and pro-rata net to Cub may be useful supplemental measures as they are used by the Company to measure operating performance and to evaluate the timing and amount of capital required to fund future operations. The Company's method of calculating these measures may differ from those of other companies and, accordingly, they may not be comparable to measures used by other companies. The Company calculates "funds from operations", "netback", "working capital" and "pro-rata net to Cub" as presented earlier in this document.