

**PEARL EXPLORATION AND PRODUCTION LTD.
MANAGEMENT'S DISCUSSION AND ANALYSIS
Three months ended September 30, 2008 and 2007**

Management's discussion and analysis ("MD&A") of Pearl Exploration and Production Ltd.'s (the "Company" or "Pearl") financial condition and results of operations should be read in conjunction with the unaudited consolidated financial statements for the three and nine months ended September 30, 2008 and 2007 as contained in this interim report and the MD&A and audited financial statements for the fifteen months ended December 31, 2007 and twelve months ended September 30, 2006 contained in the Company's 2007 Financial Report. The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and are presented in Canadian dollars unless otherwise indicated. The effective date of this MD&A is November 13th, 2008.

Additional information relating to the Company is available on SEDAR at www.sedar.com and on the Company's web-site at www.pearleandp.com.

Forward-Looking Statements

Forward-looking statements: This document contains statements about expected or anticipated future events and financial results that are forward-looking in nature and, as a result, are subject to certain risks and uncertainties, such as general economic, market and business conditions, the regulatory process and actions, technical issues, new legislation, competitive and general economic factors and conditions, the uncertainties resulting from potential delays or changes in plans, the occurrence of unexpected events, and the Company's capability to execute and implement its future plans. Actual results may differ materially from those projected by management. Although the Company has attempted to identify important factors that could cause the actual events or results to differ materially from those described in forward-looking statements, readers are cautioned that the foregoing list of risks and factors is not exhaustive and there may be other factors that cause events or results not to be as anticipated, estimated or intended. Forward-looking statements are based on management's estimates, beliefs and opinions on the date the statements are made. Although the Company believes that the expectations represented by such forward-looking statements and the assumptions of the Company upon which they are based are reasonable, there can be no assurance that such expectations will prove to be correct. The Company assumes no obligation except as outlined by regulatory requirements to update forward-looking statements if circumstances of management's estimates, beliefs or opinions should change. Additional information on these and other potential factors that could affect the Company's financial results are detailed in documents filed from time to time with the Alberta, British Columbia and Ontario Securities Commissions. Accordingly, readers should not place undue reliance on forward-looking statements. For such statements, we claim the safe harbour for forward-looking statements within the meaning of the Private Securities Legislation Reform Act of 1995.

All references to BOEs are based on a 6 to 1 conversion ratio. BOEs may be misleading, particularly if used in isolation. A BOE conversion of 6 Mcf: 1 bbl is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

OVERVIEW

Pearl is a Canadian-based oil and gas company whose common shares are traded on the TSX Exchange under the symbol "PXX". Pearl's main focus is large, heavy oil projects in Canada and the USA. The Company also holds interests in a number of natural gas properties.

Pearl's core properties include:

- Onion Lake, Saskatchewan – heavy oil;
- Mooney, Alberta – heavy oil;
- Blackrod, Alberta – heavy oil;
- San Miguel, Texas – heavy oil

OPERATIONS UPDATE

Mooney Heavy Oil Project – Alberta

As of the end Q3 2008 Pearl has drilled ten net horizontal wells in our Mooney area thus far in 2008. Four of the eight wells were drilled as part of the polymer pilot which will consist of two polymer injection wells and two producers. Regulatory approval has been obtained for the polymer pilot and polymer injection began in late October of 2008. Preliminary results from the pilot are expected by Q1 2009. Plans for a field wide polymer flood implementation are expected to be finalized by Q2 2009 with the initiation of full field implementation targeted as early as Q4 2009.

In addition we have continued to advance the conversion of the field to a water flood project. During Q3 an additional 1.5 sections were approved for water flood with water injection expected to commence in late Q4 2008 and early Q1 2009.

In addition, one additional section is awaiting waterflood approval which is expected to commence water injection in Q1 2009. The water flood will ultimately assist in both maintaining production levels and increasing reserves as recoveries are expected to increase with the demonstration of pressure maintenance, a decreasing gas/oil ratio ("GOR") and sustained production. In the event that the polymer pilot is successful the investment in the infrastructure implemented for the water flood will be used as base infrastructure for the polymer flood. While the Company expects that the implementation of the water flood will result in both sustained production and higher reserve recovery, in the short term as the field is converted there will be intermittent production disruption in Mooney.

The Company was successful at a crown land sale acquiring 6 sections (1536 hectares) of land at 100% working interest in the Mooney core area.

The Mooney field produced approximately 1,650 Boed during Q3. Production from Mooney was curtailed significantly for approximately nine weeks, beginning at the end of June by approximately 700 Boed. This shut-in was a result of our pipeline provider, on short notice, terminating our ability to ship solution gas that contained higher than permitted CO₂ on their system. To rectify the situation we procured, installed and commissioned an amine plant in less than 10 weeks. As a result we now have the capability to remove excess CO₂ from our gas stream which allows us to ship our gas production to market without interruption to service.

Onion Lake Heavy Oil Project – Saskatchewan

In Onion Lake the Cyclic Steam Stimulation (CSS) thermal pilot continues. The first well ("Z1") has completed the first steam and production cycles, with a peak rate of over 150 Bopd being achieved. The Z1 well began its second injection cycle September 21/08. Steam injection on the second well ("Z2") began on June 20th and the first production cycle commenced on August 11, 2008. Mechanical issues were experienced during the steam cycle on the Z2 well resulting in a small amount of steam entering the reservoir. As a result, the first production cycle of the Z2 well was lower than expected. It is anticipated that the Z2 well will perform similarly to the Z1 well when similar amounts of steam have been injected into the reservoir. We are currently preparing to begin the second steam cycle in the Z2 well.

During Q3 production from Onion Lake average approximately 2,300 Boed; this excludes production from the CSS thermal pilot as net revenue from the pilot is captured as an offset to the net capital costs for that project.

Blackrod Heavy Oil Project – Alberta

At Blackrod, as previously announced the Company closed a transaction on August 20th to acquire an additional 30% working interest in the Blackrod project area. The company paid \$4.5 million in cash and, if successful, will be required to make additional payments totaling up to \$11 million, based on pre-set criteria of success. In September and early October the Company was also successful at 2 separate crown land sales and acquired an additional 36 sections (9,216 net hectares) of oil sands leases contiguous to our project area. Subsequent to the end of Q3 the Company entered into an agreement with Serrano to increase our working interest in the original project area from 65% to 80% in return for the disposal of our interests in Serrano and a carried work program of net \$5 mm over the next twelve months.

Pearl intends to continue its plan to drill 10 to 15 stratigraphic core wells in the 2008/2009 winter to further delineate this deposit and gather additional petrophysical and reservoir fluid characteristic data. The application for the required governmental approvals of the thermal SAGD pilot project was submitted in May of 2008 and is expected to be approved in the next 6 to 12 months.

There is currently no production at Blackrod and we do not anticipate any production coming from Blackrod until our pilot project is operational. We currently anticipate the pilot being operational in 2010.

San Miguel Heavy Oil Project – Maverick Basin, South Texas

At San Miguel, Pearl and its 50% partner TXCO continued steam injection at the Steam Assisted Gravity Drainage ("SAGD") pilot located within the Chittim "B" Lease. Production, temperature, and pressure monitoring of the well pair continue to confirm that the well pair has entered SAGD mode with initial oil flows being observed.

At Saner Ranch, the pilot facility construction is proceeding on schedule with mechanical completion still expected to be completed in early December. The Saner Ranch pilot includes a vertical inverted five spot well pattern and a horizontal three well pattern that both utilize a modified Fracture Assisted Steamflood Technology ("FAST") process. Steam injection into the vertical inverted five spot pattern commenced on August 28 as part of the reservoir warm-up phase with initial indications of connectivity being observed within the inverted 5 spot pattern. The three horizontal wells were completed in September and achieved first steam injection / reservoir warm-up phase as scheduled on October 8, 2008. Preliminary performance results from both patterns are anticipated during the first half of 2009.

By the end of the second quarter of 2009, Pearl expects to be in a position to select which of the three recovery techniques will be used to form the basis of a commercial development project, SAGD or one of the two modified FAST techniques. In addition, work continues on the commercial aspects of a successful project in San Miguel including the method in which the JV will generate energy to produce steam and the markets and value of the production from the project.

There is currently no commercial production in San Miguel and we do not anticipate any commercial production originating from San Miguel until the JV moves into a commercial development of this resource. We have begun to see early production in the Chittum pilot in October.

Other Properties – Alberta, Saskatchewan

In order to enhance the value of certain non-core assets, Pearl initiated a 9 well drilling program at Ear Lake, Salt Lake and Druid in Q3, which is now complete. All of these wells will initiate production in Q4. Overall, the production increase from this program is expected to reach between 400 and 500 bopd by year end.

Production from other non-core Canadian properties averaged 1,800 Boe/d in Q3. It is still the intention to sell these properties once market conditions improve.

Other Properties – U.S.

The Company also holds interests in several other areas in the United States, including Queen City gas fields, the West Rozel and Gunnison Wedge in Utah, Promised Land and Fiddler Creek in Montana and Queen City gas field in Texas. There is limited or no production from these areas and there are only minor evaluation plans contemplated for these lands in 2008. However, the Company believes certain of these lands contain large resource potential and may, based upon further evaluation, be developed in the future.

In September, we agreed to dispose of our land and tangible interests in the Palo Duro basin to Tyner Resources Ltd. (“Tyner”) in exchange for an equity interest in Tyner. This transaction is consistent with our strategy to focus on our 4 core areas and is expected to close prior to year-end.

Production

Q3 production averaged 5,776 boed in line with expectations given that volumes were curtailed in Mooney due to the previously discussed CO2 issue. That situation has now been addressed and full production in Mooney has been restored. We maintain our previous guidance of 6,000 to 7,000 boed for the remainder of the year.

RESULTS OF OPERATIONS

Oil and Gas Production, Pricing and Revenue

	Three months ended		Nine months ended	
	September 30		September 30	
	2008	2007	2008	2007
Daily production / sales volumes ⁽¹⁾				
Oil (bbl/d)	4,401	6,973	6,578	5,852
Natural gas (mcf/d)	8,156	12,608	9,434	12,758
Combined ⁽¹⁾ (boe/d)	5,776	9,093	8,166	7,998
Product pricing (\$)				
Crude oil - per bbl	95.85	41.94	77.68	40.26
Natural gas - per mcf	8.08	5.01	8.54	6.40
Combined - per boe	85.02	39.17	72.78	39.87
Revenue (000's)				
PNG revenue - gross	45,180	32,786	162,849	87,052
Royalties	(11,962)	(7,889)	(40,849)	(19,495)
PNG revenue - net	33,218	24,898	122,000	67,557

* gas production converted at 6:1

(1) Includes small amounts of NGLs not separately identified in the table

For the three months ended September 30, 2008 production has decreased from the prior year three-months ended September 30, 2007 due to the company disposing of non-core properties during the prior quarter representing approximately thirty percent of daily production, natural decline and the unscheduled shut-in of approximately 700 Boed of production in Mooney due to the requirement to install and an amine facility to decrease the CO₂ in our associated gas production. In addition during the current quarter, wells were taken offline in order to complete some drilling in Mooney.

The significant increase in revenue for both the three and nine months ended September 30, 2008 is primarily due to the higher market pricing for heavy oil and natural gas in 2008.

Royalties

	Three months ended September 30		Nine months ended September 30	
	2008	2007	2008	2007
Royalties	11,962	7,889	40,849	19,495
as a percentage of PNG revenue	26%	24%	25%	22%

Royalties represent charges against production or revenue by governments and landowners. Royalties for the three and nine months ended September 30, 2008 increased over the comparable periods of 2007. This increase is consistent with the increase in revenues during the period.

As expected royalties as a percentage of revenue are consistent between 2008 and 2007.

PNG Operating Expenses and Netbacks

	Three months ended September 30				Nine months ended September 30			
	2008		2007		2008		2007	
	Total	Per boe	Total	Per boe	Total	Per boe	Total	Per boe
Average daily production	5,776		9,093		8,166		7,998	
Gross PNG revenue	45,180	85.02	32,786	39.17	162,849	72.78	87,052	39.87
Royalties	(11,962)	(22.51)	(7,889)	(9.43)	(40,849)	(18.26)	(19,495)	(8.93)
Net PNG revenue	33,218	62.51	24,897	29.74	122,000	54.52	67,557	30.94
Operating costs	(9,272)	(17.45)	(12,245)	(14.64)	(39,609)	(17.70)	(33,327)	(15.26)
Transportation	(686)	(1.29)	(498)	(0.59)	(2,886)	(1.29)	(2,571)	(1.18)
PNG netback	23,260	43.77	12,154	14.51	79,505	35.53	31,659	14.50

Operating Expenses

Third quarter operating costs on a per boe basis were higher when compared to the same period in 2007, averaging \$17.45 for the three months ended September 30, 2008 in comparison to \$14.64 per boe in 2007. For the nine months ended September 30, 2008 operating costs were \$17.70 per boe as compared to \$15.26 for the nine months ended September 30, 2007. The increase in per unit operating costs for the nine month period is principally due to several factors including: (i) high cost of propane incurred in Q1; (ii) timing of focusing resources on developing efficiencies with regards to operating costs; and (iii) \$2.2 million or \$1.02 per boe of underestimated 3rd party costs that related to prior periods that was recognized in the first quarter. Installation of a fuel gas system has helped to alleviate the high cost of propane in the second and third quarters.

PNG netbacks are significantly higher in both the three and nine months ended September 30, 2008 when compared to 2007 results. The increase is due to the higher price of oil and gas in 2008.

General and Administrative Expenses ("G&A")

General and administrative expenses were \$3.6 million in the third quarter of 2008 compared to \$4.3 million in 2007. On a per unit basis, G&A was \$6.71 per boe compared to \$5.10 per boe in 2007. General and administrative costs have increased by \$1.61 per boe from the same period in 2007 due to a decrease in production. The gross costs have decreased by \$0.7 million due to a corporate focus on decreasing administrative costs and an overall decrease in

corporate acquisition activities but offset slightly by higher exchange related costs associated with moving our shares from the Toronto venture exchange (TSX-V) to the main exchange (TSX).

G&A for the nine months ended September 30, 2008 was \$10.0 million or \$4.46 per boe compared to \$10.8 million or \$4.94 per boe in 2007. The decrease of \$0.48 per boe from 2007 is again principally due to the same reasons noted for the above three months ended September 30, 2008.

Depletion, Depreciation and Accretion (“DD&A”)

DD&A expense was \$13.7 million or \$25.73 per boe for the three months ended September 30, 2008 in comparison to \$23.4 million or \$27.98 per boe for the three months ended September 30, 2007. For the nine months ended September 30, 2008 DD&A expense was \$57.7 million or \$25.79 per boe in comparison to \$63.3 million or \$28.98 for the same period of 2007. The lower rate in 2008 is due to increased proved reserves as a result of the significant drilling and acquisition activity in 2007.

Interest Expense

Interest expense for the three months ended September 30, 2008 was \$0.03 million in comparison to \$1.2 million for the three months ended September 30, 2007. Interest expense relates to the Company's bank debt. The Company had an average debt level of \$0.4 million and an effective interest rate of 6.24% for the three months ended September 30, 2008. Lower interest expense is due to a lower dependence on debt financing during the period.

For the nine months ended September 30, 2008 interest expense was \$0.8 million in comparison to \$2.9 million for the same period in 2007. The Company's average debt balance was \$14.9 million with an effective interest rate of 5.42% for the nine months ended September 30, 2008. Lower interest expense is due to a lower dependence on debt financing during the period.

Change in unrealized loss on gas pricing contracts

The change in unrealized loss on gas pricing contracts for the nine months ended September 30, 2007 relates to gas contracts acquired as part of the Atlas acquisition in December, 2006.

Other items

For the three and nine months ended September 30, 2008 there was a dilution gain of \$2.3 million recorded on the investment in Serrano and a \$2.6 million writedown of the investment in Asset-backed commercial paper (“ABCP”). Both of these items are discussed in more detail in note 5 of the financial statements. For the nine months ended September 30, 2007 a \$13.3 million gain was recorded on the sale of its Gulf of Mexico leases in exchange for shares of Bayou Bend Petroleum Ltd.

Income Taxes

The provision for future income taxes for the quarter ended September 30, 2008 was \$2.6 million compared to a recovery of \$5.4 million for the three months ended September 30, 2007. As at September 30, 2008, the Company has recognized a future tax liability of \$1.9 million due to the decrease of our tax pool balances as a result of our asset sales during 2008 and due to the high revenues we have realized thus far in 2008.

For the nine months ended September 30, 2008, future income taxes were \$2.6 million in comparison to a recovery of \$5.0 million for the comparable period in 2007. Reasons for the significant change year to year are noted above for the three month period.

Current tax of \$1.9 million for the nine months ended September 30, 2008 is comprised of Saskatchewan capital tax and resource surcharge. The \$8.3 million tax expense for the same period of 2007 was a result of the sale of certain assets in the United States

Net Income (Loss)

Net income for the quarter ended September 30, 2008 was \$1.9 million in comparison to a net loss of \$13.7 million for the quarter ended September 30, 2007. Earnings for the nine months ended September 30, 2008 were \$4.8 million, a \$43.4 million improvement over the nine months ended September 30, 2007 reported net loss of \$38.5 million. The significant increase in 2008 net income is principally due to increased revenues caused by the high market price for heavy oil and natural gas in the first nine months of 2008.

LIQUIDITY AND CAPITAL RESOURCES

At September 30, 2008, the Company had \$47.0 million of remaining credit capacity available under its \$37.0 million extendible term credit facility and \$10.0 million demand revolving credit facility.

At September 30, 2008, the Company had working capital surplus of \$36.2 million compared to a working capital deficit of \$34.2 million at December 31, 2007.

Funds from operations were \$21.0 million for the three months ended September 30, 2008 compared to funds from operations of \$6.3 million for the three months ended September 30, 2007. For the nine months ended September 30, 2008 funds from operations were \$68.5 million as compared to \$11.5 million for the nine months ended September 30, 2007. The improvement in funds from operations is principally due to higher commodity prices and to a lesser extent higher average production and lower G&A expenses.

Net cash used in financing activities for the quarter ended September 30, 2008 was \$5.0 million compared to net cash from financing activities of \$44.4 million for the quarter ended September 30, 2007. During the current quarter the Company repaid \$5.0 million on its credit facility. Significant financing activities from the quarter ended September 30, 2007 included (i) the net repayment of \$14.0 million of debt, and (ii) the net proceeds of \$58.4 million from an equity financing.

Net cash from financing activities was \$nil for the nine months ended September 30, 2008 in comparison to net cash from financing activities of \$24.3 million for the nine months ended September 30, 2007. The repayment of \$5.0 million on the Company's bank loan was the only financing activity for the current period. Significant financing activities from the nine months ended September 30, 2007 included (i) a net repayment of \$34.7 million of the Company's debt, and (ii) net proceeds of \$58.4 million from equity financing, and (iii) \$0.6 million from the exercise of stock options.

Net cash used in investing activities was \$22.0 million for the three months ended September 30, 2008 compared to net cash used in investing activities of \$42.8 million for the three months ended September 30, 2007. During the current quarter, the Company sold certain non-core heavy oil producing assets for \$3.8 million and spent \$39.5 million on exploration, development and lease acquisition activities. Investing activities during the quarter ended September 30, 2007 included \$47.4 million spent on exploration, development and lease acquisition activities.

Net cash used in investing activities for the nine months ended September 30, 2008 was \$13.9 million compared to net cash used in investing activities of \$113.4 million in the same period of 2007. In addition to the \$79 million from the sale of assets, the Company spent \$74.6 million on exploration, development and lease acquisition activities during the first nine months of 2008. During the nine months ended September 30, 2007 the Company's exploration, development and lease acquisition activities totaled \$140.8 million, corporate acquisition costs totaled \$11.3 million and the sale of Bayou Bend shares generated \$10.0 million.

During Q3 the Company announced that it had increased its capital budget for 2008 to approximately \$135 million, up from the original budget of \$61.0 million. Since the time of our announcement to expand our budget, the world price of oil and the North American price of natural gas have declined dramatically. In-turn the prices that we receive for our products have also been dramatically impacted by the decreasing broader market values for these commodities.

The Company remains dedicated to our capital budget philosophy; which is to fund capital budgets based on available cash flow from operations, non-core asset sales and to limit the timing of our capital expenditures such that we will only ever use a maximum of 50% of our current borrowing base. As such, as a result of the dramatic decrease in current commodity prices we have deferred several of the projects in our recently announced budget increase to \$135 million to result in a firm budget of approximately \$110 million for 2008. This decreased budget is still principally focused on Mooney: accelerating the polymer pilot, expansion of the water flood and related infrastructure and delineation drilling in the western portion of the eastern field. However, some production increases and pilot advancement activities will be delayed by this capital budget cut. It is the intention of the Company to re-instate these deferred projects when the price of oil and natural gas increase, resulting in increased cash flow from operations that is available for capital investment.

While there are no current plans to raise additional funds in the form of either debt or equity, in the future as our projects move from pilot projects to development projects, the Company may consider additional issuances of common shares or debt instruments to assist with financing these developments to the extent that sufficient cash flow from operations is inadequate. The Company may consider divesting additional non-core oil and gas assets or farming out interests in oil and gas properties to finance its operations. Accordingly, the Company's consolidated financial statements are presented on a going-concern basis.

CAPITAL EXPENDITURES

Capital expenditures for the three and nine months ended September 30, 2008 and 2007 are as follows:

	2008	2007	2008	2007
Land	1,207,620	812,108	2,071,613	1,616,811
Seismic	407,647	218,122	968,861	1,227,589
Drilling and completion	27,830,145	35,186,887	41,335,656	103,390,831
Equipment	5,236,987	5,576,523	24,424,744	23,277,153
Other	-	700,423	561,003	1,967,417
Total exploration and development	34,682,399	42,494,063	69,361,877	131,479,801
Corporate acquisition	-	-	-	8,809,049
Property acquisitions	4,797,608	11,678,057	5,235,356	17,381,053
Property dispositions	(3,760,800)	(6,726,454)	(79,097,031)	(15,573,771)
Total capital expenditures	35,719,207	47,445,666	4,499,798	142,096,132

RELATED PARTY TRANSACTIONS

Tanganyika Oil Company Ltd. ("Tanganyika") provides administrative and technical services to the Company from time to time based upon time and expenses incurred by Tanganyika. For the nine months ended September 30, 2008, Tanganyika charged the Company \$58,643 (2007 - \$127,773). Tanganyika and Pearl have certain directors and officers in common.

Namdo Management Services Ltd. ("Namdo") provides executive and support services to the Company. For the nine months ended September 30, 2008, the Company paid Namdo \$135,000 (2007 - \$78,000). Namdo is a private corporation owned by Lukas H. Lundin, a director of the Company.

RISKS AND UNCERTAINTIES

The Company is exposed to a number of risks and uncertainties inherent in exploring for, developing and producing crude oil and natural gas. These risks and uncertainties include, but are not limited to, the following:

- risk of finding and producing reserves economically;
- uncertainty associated with obtaining drilling licenses and other regulatory consents and approvals;
- production risks associated with sour hydrocarbons;
- marketing reserves at acceptable prices;
- cost of capital risk associated with securing the needed capital to carry out the Company's operations;
- risk of fluctuating oil and natural gas prices;
- risk of fluctuating foreign currency exchange rates;
- risk of governmental policies, social instability or other political, economic or diplomatic developments in its operations;
- market risks associated with investing the Company's cash reserves in interest bearing depository instruments; and
- environmental risks related to its oil and gas properties.

Many of the previously mentioned risks are beyond the Company's control, and it is impossible to ensure that any exploration drilling program or piloting program will ultimately result in commercial operations. The Company does not currently utilize derivative instruments to hedge its commodity price, foreign currency exchange or interest rate risks.

Pearl strives to minimize and manage these risks in a number of ways, including:

- Employing qualified professional and technical staff;
- Communicating openly with members of the public regarding its activities;
- Concentrating in a limited number of areas;
- Utilizing the latest technology for finding and developing reserves;
- Constructing high-quality, environmentally sensitive, safe production facilities; and
- Maximizing operational control of drilling and producing operations.

ENVIRONMENTAL RISKS

All phases of the oil and natural gas business present environmental risks and hazards and are subject to environmental regulation pursuant to a variety of federal, provincial and local laws and regulations. Compliance with such legislation can require significant expenditures and a breach may result in the imposition of fines and penalties, some of which may be material. Environmental legislation is evolving in a manner expected to result in stricter standards and enforcement, larger fines and liability and potentially increased capital expenditures and operating costs. In 2002, the Government of Canada ratified the Kyoto Protocol (the "Protocol"), which calls for Canada to reduce its greenhouse gas emissions to specified levels. There has been much public debate with respect to Canada's ability to meet these targets and the government's strategy or alternative strategies with respect to climate change and the control of greenhouse gases. Implementation of strategies for reducing greenhouse gases, whether to meet the limits required by the Protocol or as otherwise determined, could have a material impact on the nature of oil and natural gas operations, including those of the Company. Given the evolving nature of the debate related to climate change and the control of greenhouse gases and resulting requirements, it is not possible to predict either the nature of those requirements or the impact on the Company and its operations and financial condition.

NEW ACCOUNTING STANDARDS ADOPTED

As disclosed in the December 31, 2007 annual audited consolidated financial statements, on January 1, 2008, the Company adopted the new CICA Handbook Sections 3862 "Financial Instruments – Disclosures", 3863 "Financial Instruments – Presentation", and 1535 "Capital Disclosures". The adoption of these standards has had no material impact on the Company's net income or cash flows. Additional information on the implementation of these new standards can be found in Note 3 to the Interim Consolidated Financial Statements.

RECENT ACCOUNTING PRONOUNCEMENTS

Goodwill and Intangible Assets

As of January 1, 2009, Pearl will be required to adopt Section 3064 "Goodwill and Intangible Assets," which revises the requirement for recognition, measurement, presentation and disclosure of intangible assets and replaces the existing Goodwill and Intangible Asset standard. The adoption of this standard should not have a material impact on the Company's consolidated financial statements.

International Financial Reporting Standards

In January 2006, the CICA Accounting Standards Board ("AcSB") adopted a strategic plan for the direction of accounting standards in Canada. As part of that plan, the Accounting Standards Board confirmed in February, 2008 that International Reporting Standards ("IFRS") will replace Canadian GAAP for profit-oriented Canadian publicly accountable enterprises in 2011. Pearl is assessing the potential impact of this change and developing a plan accordingly.

INTERNAL CONTROLS OVER FINANCIAL REPORTING

The Company has, under the supervision of its chief financial officer, designed a process for internal control over financial reporting, which process has been effected by the Company's board of directors and management. The process was designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP and incorporates policies and procedures as described above. There have been no changes in the Company's systems of internal control over financial reporting that would materially affect, or is reasonably likely to materially affect, the company's internal controls over financial reporting.

It should be noted that a control system, including the Company's disclosure and internal controls and procedures, no matter how well conceived can provide only reasonable, but not absolute, assurance that the objectives of the control system will be met and it should not be expected that the disclosure and internal controls and procedures will prevent all errors or fraud.

OUTLOOK

The Company plans to continue pursuing large North American heavy oil resource opportunities to add to its portfolio, to seek to rationalize non-core assets, and to focus on conversion of resources to reserves and development of its existing interests in the USA and Canada.

BOEs

Throughout this MD&A the calculation of barrels of oil equivalent (boe) is calculated at a conversion rate of six thousand cubic feet (mcf) of natural gas for one barrel of oil and is based on an energy equivalence conversion method. BOEs may

be misleading, particularly if used in isolation. A boe conversion ratio of 6 mcf:1 bbl is based on an energy equivalence conversion method primarily applicable at the burner tip and does not represent a value equivalence at the wellhead.

Non-GAAP Measures

Included in this report are references to terms commonly used in the oil and gas industry, such as, cash flow and funds from operations which represent cash flow from operating activities expressed before changes in non-cash working capital, long-term receivable and asset retirement costs incurred and are used by the Company to analyze operating performance, leverage and liquidity. These terms do not have standardized meanings prescribed by GAAP and therefore may not be comparable with the calculations of similar measures for other entities. Consequently, these are referred to as non-GAAP measures.