



**Candax Energy Inc.**  
**Management's Discussion and Analysis**  
**For the three months ended March 31, 2008**

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## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

The following Management's Discussion and Analysis ("MD&A") for Candax Energy Inc. ("Candax" or the "Company") should be read in conjunction with the accompanying unaudited interim consolidated financial statements for the three months ended March 31, 2008 and the notes thereto, as well as the MD&A and the audited consolidated financial statements for the year ended December 31, 2007. Readers should also refer to a discussion of forward-looking statements contained at the end of this MD&A. Additional information relating to the Company, including its Annual Information Form for the year ended December 31, 2007 is available on SEDAR at [www.sedar.com](http://www.sedar.com). This information is presented as of May 9, 2008.

### **Company Overview**

Candax is engaged in the exploration for, and the acquisition, development and production of, natural gas and crude oil. Candax targets mainly oil and natural gas, but also has natural gas liquids in its portfolio. Candax also owns a 50% interest in Société d'Electricité d'El Bibane ("SEEB"), a Tunisian power generation company. The interests of the Company are located in Tunisia and Madagascar.

### **Commodity Prices**

A combination of supply factors, stock inventory levels, transportation limitations and geopolitical concerns has combined to support oil prices with Brent averaging approximately US \$97 per barrel during the first quarter of 2008. Brent is currently trading in the US \$120 per barrel range.

### **Foreign Exchange Fluctuations**

Candax operates primarily in a US dollar-based environment. The majority of the Company's revenues and expenses are paid in US dollars, although Candax is also exposed to Canadian dollar, Pounds Sterling and Tunisian Dinar expenses. However, being a Canadian company trading on the TSX, Candax has elected to report its financial results in Canadian dollars. Accordingly, all foreign currency amounts presented in Candax's consolidated statements of operations and deficit and cash flows are converted to Canadian dollars for reporting purposes based on the average Canadian to US dollar exchange rate prevailing during the reporting period. The US to Canadian dollar closing exchange rate on March 31, 2008 was \$1.0265 (2007 – \$1.1580) and averaged \$1.0047 (2007 – \$1.1720) during the first quarter of 2008.

### **Capital Structure and Dilution**

At December 31, 2007, the Company had 169,231,606 common shares outstanding. No common share capital transactions were conducted since that date and hence the outstanding common shares as at May 9, 2008 remain at 169,231,606.

At December 31, 2007, the Company had 12,067,500 stock options outstanding at an average exercise price of \$0.78. During the first quarter of 2008, 1,050,000 options were granted at \$0.92 and on April 3, 2008, 1,000,000 options were granted at \$0.73 bringing the total number of options currently issued to 14,117,500 at May 9, 2008 at an average exercise price of \$0.79.

### **Chaal**

The area comprising the Chaal Permit is located in central Tunisia approximately 50 kilometres west of the city of Sfax, covering an area of 1,200 square kilometres. Candax is the operator and at March 31, 2008, held a 60% working interest with Mitsubishi and SMIP holding 20% each.

The first phase of the exploration permit expires May 25, 2008. A two-year extension to the permit has been agreed to, and administrative formalities with the Tunisian Government initiated, which require no additional work program commitments beyond the planned sidetrack.



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Following the suspension of the Chaal-1 well in 2006, Candax and its partners have undertaken a full review of the results and potential future strategies. During 2008, Candax intends to undertake a deviated sidetrack of the Chaal 1 well which is expected to spud in late August or early September. In order to minimise formational damage, which the Company believes was the main cause of the lack of gas production in the original well, the drilling will be undertaken using managed pressure drilling. A contract has been signed with drilling specialists with extensive experience in high-pressure/high-temperature operations. The objective of the Chaal sidetrack is to fully evaluate and test the commerciality of the gas discovery, and will likely include a large acid fracturing to optimize flow from the fractured reservoir, followed by a long-term test.

### **Madagascar**

Block 1101 is a large exploration permit located onshore, northwest Madagascar and covers 14,900 square kilometers. Candax is the operator with a 60% equity interest. Block 1101 is located north of a number of large onshore fields with reported heavy oil in place of approximately 30 billion barrels as well as several lighter oil discoveries.

Following the results from the initial geological fieldwork, geochemistry and gravity/magnetics have confirmed the excellent potential of Block 1101, indicating in excess of 5,000 metres of sedimentary section beneath our block together with numerous oils shows. Candax is currently tendering the planned 2D seismic program, which is expected to commence in the third quarter of 2008. Following the encouraging results from initial exploration studies, planned seismic coverage has been increased to include additional areas of Block 1101. Subject to interpretation of the 2D seismic results and further field work planned for 2008, it is anticipated that the first exploration well will be drilled in 2009.

### **Business Development Activities**

Candax's strategy is to build a high-growth international portfolio of oil and gas assets.

### **Review of Operations**

### **New Accounting Standards**

### **Capital disclosures and financial instruments – disclosures and presentation**

On December 1, 2006, the CICA issued three new accounting standards: Capital Disclosures (Handbook Section 1535), Financial Instruments – Disclosures (Handbook Section 3862), and Financial Instruments – Presentation (Handbook Section 3863). These new standards became effective for the Company on January 1, 2008. Handbook Section 1535 specifies the disclosure of (i) an entity's objectives, policies and processes for managing capital; (ii) quantitative data about what the entity regards as capital; (iii) whether the entity has complied with any capital requirements; and (iv) if it has not complied, the consequences of such non-compliance. The Company has included disclosures recommended by the new Handbook section in Note 9 to the Company's unaudited interim consolidated financial statements.

### **Financial Instruments**

Handbook Sections 3862 and 3863 replace Handbook Section 3861, Financial Instruments – Disclosure and Presentation, revising and enhancing its disclosure requirements, and carrying forward unchanged its presentation requirements. These new sections place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks.

### **Revenue**

Sales, net of royalties for the three months ended March 31, 2008, were \$2.1 million, the same as for the three months ended March 31, 2007. During the first quarter of 2008, the Company sold 25,428 barrels of oil at an average price of US \$82.39 compared to the first quarter of 2007 where 33,720 barrels were sold at an average price of US \$52.70. The decrease in barrels sold was due to the shut-in of Al Manzah



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since late 2007 and the timing of liftings. There was no revenue earned during the quarter from gas or electricity sales as the El Bibane field was shut-in and as a result, electricity generating activities continued to be suspended during the first quarter as described below.

**Production**

The following table summarizes the quarterly production for 2008 and 2007:

<b>BBLs</b>	<b>Q1</b>	
	<b>2008</b>	<b>2007</b>
Oil (bbls/day)	413	420
Gas (mmcf/day)	-	-
BOEs/day	413	420

Where amounts are expressed on a barrel of oil equivalent (boe) basis, natural gas volumes have been converted to barrels of oil equivalent at 6,000 cubic feet to one barrel of oil equivalent (6 mcf = 1 boe). This conversion ratio is the convention used in the oil and natural gas industry and is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. The use of boe may be misleading, particularly if used in isolation.

The BOEs/day produced in Q1 2008 were consistent with Q1 2007 as the lack of production due to the shut-in of Al Manzah, was offset by higher production at Ezzaouia and Robbana.

On July 31, 2007, the drilling of the first well of the three-well development program on the El Bibane oil and gas field commenced with well El Bibane 4 on the northwest flank of the field. An initial pilot hole was drilled to determine key reservoir parameters, and in particular, the current gas-oil and oil-water contacts. The well was then sidetracked and a horizontal producer drilled (560m horizontal section in reservoir). The well was completed in November 2007. The El Bibane 5 crestal gas injector well was completed in December 2007. The re-entry of El Bibane 3 and the drilling of a new horizontal section on the southeastern flank of the field were completed in March 2008 and production from the field resumed in April 2008.

The platform and pipeline installation for EBB3 is continuing, with the jacket installation currently underway. This work has been delayed by more than three weeks because of poor offshore weather conditions, and the Company expects to achieve production from this well in the third week of May. Once EBB3 is on production, Candax will commence operations to initiate gas recycling and fully optimize oil production from the three El Bibane wells. The first equity crude lifting is scheduled for the last week of May. As oil production continues to increase, crude oil sales (liftings) will also accelerate.

Since gas production from El Bibane ceased, operations at the SEEB power plant were also suspended. The plant was placed on care and maintenance mode and all excess staff was released, reducing the carrying costs to an absolute minimum. The Company's share of the operating and maintenance costs for the three months ended March 31, 2008 were \$0.1, million, the same as for the first quarter of 2007. Due to the lack of production from the El Bibane field, the SEEB power plant did not generate any revenues during the first quarter of 2008 and as a result was unable to meet its current obligations under the credit facility. Negotiations with the lenders are on-going as there is no commitment from the lenders to continue to defer principal or interest payments. In the event of a declaration of default by the lenders, the lenders would take control of the SEEB plant and Candax would owe a default payment of US \$0.8 million but would not be liable for the balance of the loans outstanding nor for the deferred principal amounts.

As of May 9, 2008, the El Bibane field (73.8% net ownership by Candax) is currently producing at a steady gross rate of approximately 1,200 bopd and 12 mmcf/d of gas from the EBB4 well only. Approximately 7 mmcf/d of the produced gas is being sold to the SEEB power station (50% net ownership by Candax) which resumed operations and sales of electricity on April 15, 2008 at its maximum rated capacity of 27 MW.



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**Operating Costs**

For the three months ended March 31, 2008, operating costs of \$0.7 million were higher than the same period in 2007 due to a spare parts inventory write-down of \$0.4 million.

**Depletion, Depreciation and Amortization expense**

Depletion, depreciation and amortization expense for the three months ended March 31, 2008, was \$1.1 million, consistent with the same period in 2007 of \$1.0 million. This amount is calculated using the purchase price of the acquired assets and the proved reserves information as at December 31, 2007.

**General and Administrative Costs**

General and administrative costs for the three months ended March 31, 2008, were \$1.8 million, an increase of \$0.7 million over the same period in 2007 as a result of financing expenses related to the acquisition of the credit facility and a decrease in the amount of management time capitalized on development projects.

**Interest expense**

Interest expense for the three months ended March 31, 2008, was \$0.3 million, consistent with the same period in 2007 of \$0.3 million.

**Foreign exchange**

The unrealized foreign exchange gain for the three months ended March 31, 2008 was \$0.1 million, compared to a loss of \$0.1 million for the same period in 2007.

**Selected Quarterly Financial Data (unaudited)**

<i>in thousands of Canadian dollars except per share amounts</i>	<b>Q1</b>	<b>Q2</b>	<b>Q3</b>	<b>Q4</b>	<b>Year</b>
<b>2008</b>					
Sales, net of royalties	2,097	-	-	-	2,097
Loss	(2,298)	-	-	-	(2,298)
Loss per share - basic and diluted	(0.01)	-	-	-	(0.01)
Total assets	185,802	-	-	-	185,802
Long-term financial liabilities	38,129	-	-	-	38,129
<b>2007</b>					
Sales, net of royalties	2,059	552	10,083	167	12,861
Net income (loss)	(894)	(4,541)	2,216	(6,032)	(9,251)
Net income (loss) per share - basic and diluted	(0.01)	(0.03)	0.01	(0.04)	(0.05)
Total assets	136,790	121,274	126,909	147,887	147,887
Long-term financial liabilities	3,046	2,797	2,624	13,565	13,565
<b>2006</b>					
Sales, net of royalties	9,193	1,139	1,923	897	13,152
Net income (loss)	1,638	(460)	(2,159)	970	(11)
Net income (loss) per share - basic and diluted	0.01	(0.00)	(0.01)	(0.00)	(0.00)
Total assets	101,894	140,932	137,984	143,896	143,896
Long-term financial liabilities	11,773	11,174	10,455	3,056	3,056

Revenue for the first quarter of 2008 was consistent with the revenue earned for the first quarter of 2007. The long-term liabilities for the first quarter of 2008 increased significantly from the fourth quarter of 2007 as US \$29 million was drawn down from the credit facility to fund the El Bibane redevelopment program. Revenue for the fourth quarter of 2007 was significantly lower than the fourth quarter of 2006 due to the timing of the crude liftings. Revenue for the third quarter of 2007 was higher than that of the third quarter of 2006 and higher than that of the first or second quarters of 2007 due to the timing of crude oil liftings.



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Revenue for the first quarter of 2007 was significantly lower than the first quarter of 2006 also due to the timing of the liftings. Revenue for the second, third and fourth quarters of 2006 was significantly lower than that earned in the first quarter of 2006 due to the timing of the liftings. The long-term financial liabilities as at the end of 2007 were higher than at the end of the third quarter of 2007 due to the draw down of the credit facility as discussed earlier. The long-term financial liabilities as at the end of the first, second and third quarters of 2007 and the fourth quarter 2006 were significantly lower than the other quarters in 2006 as the limited recourse loans were reclassified from long-term to current effective December 31, 2006.

### **Liquidity, Capital Resources and Capital Expenditures**

The Company has a facility with the Bank of Scotland which provides a line of credit of up to US \$50 million. The facility bears interest at the London Interbank Overnight Rate plus 2% and there are no fixed repayment terms. On November 30, 2007, the Company drew down US \$14 million from the facility, and allocated US \$6.0 million, US \$4.5 million of which was released on March 31, 2008, to be used as security for letters of credit issued by the Company. On February 4, 2008, the Company drew down US \$29 million from the facility bringing the outstanding amount on the facility to US \$44.5 million at March 31, 2008.

As at March 31, 2008, the Company had \$23.9 million in cash and cash equivalents. The Company has no exposure to asset-backed commercial paper. Current cash resources, cash from operations and funds available from the credit facility are expected to be adequate to allow the Company to meet its obligations as they fall due.

### **Commitments**

Under the terms of an agreement with the Tunisian government, 20% of the Company's oil production must be sold to the state-owned oil company, ETAP. The production sold under this domestic market obligation receives a price equal to approximately 90% of the U.S. dollar price for the export sales. Oil production is accumulated in a storage facility until a marketable cargo is achieved. Under this agreement, the state-owned company, ETAP, with respect to its 55% rights on the Ezzaouia field production and on behalf of the Government with respect to the domestic market obligation and the Company's Tunisian entities have agreed to optimize tanker lifting volumes. As a result of this reciprocal practice, a short-term volumetric imbalance may arise through an "under/over" lift position. This short-term situation is corrected from future production allocations.

The financial commitments of the Company in relation to construction and drilling programs and related costs for the redevelopment of El Bibane have been substantially fulfilled.

As of March 31, 2008, the Company had procured that a standby letter of credit be issued on its behalf in the amount of US \$1.5 million in favour of the Madagascar Ministry of Industry and Mines in accordance with the terms of the production sharing agreement entered into in November 2006. The letter of credit will be released when the Company has satisfied the commitments set out in the agreement.

### **Critical Accounting Estimates**

A discussion of the Company's significant accounting policies is contained in Note 2 to the 2007 audited consolidated financial statements. Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. These estimates relate primarily to the future development costs associated with proved undeveloped reserves, reserve volumes, future production and revenues, and future costs associated with asset retirement obligations. The Company has its oil and gas reserves, future development costs and future cash flows from those reserves evaluated and reported on by Ryder-Scott Company Petroleum Consultants, independent petroleum reserve engineering consultants. The estimation of these amounts is a subjective process, based on engineering data, forecasted prices and production levels and the timing



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of expenditures. All of these estimates are subject to numerous uncertainties and various interpretations, and consequently will change over time to reflect updated information as it is received.

**Business Risks**

A comprehensive assessment of the Company's business risks is set out in the 2007 Annual Information Form. There are a number of inherent risks associated with oil and gas operations and development. Many of these risks are beyond the control of the Company. The following outlines some of the principal risks and their potential impact on the Company:

***Exploration, Development and Production Risks***

A portion of the current working capital of Candax will be expended on petroleum and natural gas exploration, exploitation and development activities, which are high-risk ventures with uncertain prospects for success. Oil and gas exploration involves a high degree of risk and there is no assurance that expenditures made on future exploration activities by the Company will result in new discoveries of oil, condensate or natural gas that are commercially viable or economically producible. Holders of securities of the Company must rely on the ability, expertise, judgment, discretion, integrity and good faith of management of the Company. It is difficult to project the costs of implementing any exploratory or developmental drilling program due to the inherent uncertainties of drilling in unknown formations, the costs associated with encountering various drilling conditions such as over-pressured zones and tools lost in the hole and changes in drilling plans and locations as a result of prior exploratory wells or additional seismic data and interpretations thereof. Few properties that are explored are ultimately developed into new reserves. In certain instances, the Company may be precluded from pursuing an exploration program or decide not to continue with an exploration program and such an occurrence may have a negative effect on the value of the securities of the Company.

Future oil exploration may involve unprofitable efforts, not only from dry wells, but from wells that are productive but do not produce sufficient net revenues to return a profit after drilling, operating and other costs. Completion of a well does not assure a profit on the investment or recovery of drilling, completion and operating costs. In addition, drilling hazards or environmental damage could greatly increase the cost of operations, and various field operating conditions may adversely affect the production from successful wells. These conditions include: delays in obtaining governmental approvals or consents, shut-ins of connected wells resulting from extreme weather conditions, insufficient storage or transportation capacity or other geological and mechanical conditions. While diligent well supervision and effective maintenance operations can contribute to maximizing production rates over time, production delays and declines from normal field operating conditions cannot be eliminated and can be expected to adversely affect revenue and cash flow levels to varying degrees.

***Petroleum and Natural Gas Reserves***

All evaluations of future net revenues are before consideration of indirect costs such as administrative overhead, other miscellaneous expenses and income taxes. The future net revenues may not be representative of the fair market value of the reserves. There is no assurance that the forecast price and cost assumptions contained in the year end 2007 Ryder Scott Report will be attained and variances may be material. There are numerous uncertainties inherent in estimating quantities of proved and probable reserves, including many factors beyond the control of the Company. The reserves data and net present value of future cash flows set forth represent estimates only.

In general, estimates of economically recoverable petroleum and natural gas reserves and the future net revenues therefrom are based upon a number of variable factors and assumptions, such as historical production from the properties, commodity prices, the assumed effects of regulation by governmental agencies and future operating costs, each of which may vary considerably from actual results. Estimates of the economically recoverable petroleum and natural gas reserves attributable to any particular group of properties, classification of such reserves based on risk of recovery and estimates of future net revenues expected therefrom, prepared by different engineers or by the same engineers at different times, may vary substantially.



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***Fluctuation of Commodity Prices***

Oil and natural gas are commodities whose prices are determined based on world demand, supply and other factors all of which are beyond the control of the Company. Crude oil is influenced by the world economy and OPEC's ability to adjust supply to world demand. Recently crude oil prices have been kept high by political events causing disruptions in the supply of oil, and concern over potential supply disruptions triggered by unrest in the Middle East. Political events trigger large fluctuations in oil price levels. Natural gas prices are influenced by factors within North America. The continued tight supply demand balance for natural gas is causing significant elasticity in pricing. Despite record drilling activity, a strong economy, weather, fuel switching and demand for electrical generation there still exists a tight supply causing prices to remain high.

World prices for oil and natural gas have fluctuated widely in recent years. Future price fluctuations in world prices may continue and may have a significant impact upon the projected revenue of the Company, the projected return from its existing and future reserves and the general financial viability of the Company.

The oil and natural gas prices realized by the Company are affected by factors such as supply and demand, oil quality and transportation adjustments. The Company expects to market its oil and natural gas production in a manner consistent with past practices. In the case of natural gas, the Company has fixed rate sales contracts. The Company's current natural gas production is subject to the provisions of the Petroleum Law, which provides for sales into the Tunisian domestic market at rates less than those which would be realized in the international market. While the Company sells the majority of its Tunisian oil to arms-length purchasers priced on a sale by sale basis at prevailing market conditions, a portion of the oil produced by the Company is required to be sold domestically in Tunisia at rates less than those which would be realized in the international market. There is no assurance that the price paid for the oil produced by the Company will remain at current levels. A decrease in the price obtained for its oil may have a material adverse effect on the financial condition of the Company and its future results of operations.

***Foreign Currency Exchange Rates***

The Company sells its oil production pursuant to marketing agreements that are denominated in US dollars. Many of the operational and other expenses incurred by the Company are paid in US dollars or in local currency of the country where operations are performed. The assets and liabilities of the Company (including reserve information) are recorded in Canadian dollars. As a result, fluctuations in the US dollar against the Canadian dollar and each of these currencies against local currencies in jurisdictions where properties of the Company are located could result in unanticipated and material fluctuations in the financial results of the Company.

***Competition***

A number of other oil and gas companies operate and are allowed to bid for exploration and production licenses and other services in countries in North Africa and the Middle East which are the focus of the business and operations of the Company, thereby providing competition to the Company. Larger companies may have access to greater resources than the Company, may be more successful in the recruitment and retention of qualified employees and may conduct their own refining and petroleum marketing operations, which may give such companies a competitive advantage over the Company. Some of these companies have been conducting operations in Tunisia for considerably longer periods of time than has the Company and thus these companies may be more familiar with the political and business landscape in Tunisia than the Company. In addition, actual or potential competitors may be strengthened through the acquisition of additional assets and interests.

***Environmental Regulation***

The current and future operations of the Company that are conducted in Tunisia are subject to environmental regulations promulgated by the Government of Tunisia. Should the Company initiate



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operations in other countries, such operations will be subject to environmental legislation in such jurisdictions. Current environmental legislation in Tunisia provides for restrictions and prohibitions on spills, releases or emissions of various substances produced in association with oil, condensate and natural gas operations. In addition, certain types of operations may require the submission and approval of environmental impact assessments. The existing operations of the Company are subject to such environmental policies and legislation. Environmental legislation and policy is periodically amended. Such amendments may result in stricter standards and enforcement and in more stringent fines and penalties for non-compliance. Environmental assessments of existing and proposed projects carry a heightened degree of responsibility for companies and their directors, officers and employees. The costs of compliance associated with changes in environmental regulations could require significant expenditures, and breaches of such regulations may result in the imposition of material fines and penalties. In an extreme case, such regulations may result in temporary or permanent suspension of production operations. There can be no assurance that these environmental costs or effects will not have a material adverse effect on the future financial condition or results of the operations of the Company.

***Political Risks***

Tunisia has experienced relative prosperity and stability under the leadership of President Ben Ali over the past two decades. Notwithstanding this relative stability, in the past, Tunisia has been affected by extremist Islamic militant activity. Tunisian authorities have implemented anti-terrorism policies and security precautions. By law, parties organized on the basis of religion, region, race or language are forbidden. Despite this, there are groups in Tunisia dedicated to turning the country into an Islamic republic. The Tunisian government has taken steps to prevent the Islamic militant struggle in neighbouring Algeria from affecting Tunisia by increasing its military presence along the Tunisia/Algeria border, imposing visa restrictions and imposing strict controls on local militants. Tunisia is bordered by both Algeria and Libya. Both countries have experienced periods of civil, political and militant unrest and Libya has been the subject of international sanctions; future unrest in any of the neighbouring countries could affect Tunisia.

In addition to the political risks, the Company is also subject to the laws of the various levels of government in the countries in which it conducts business. Such legislation may be changed from time to time in response to economic or political conditions, and the implementation of new legislation or modification of existing legislation affecting the oil and gas industry could change the Company's revenues and/or costs and have a material adverse impact on the business, results of operations, financial condition and liquidity.

***Internal Control over Financial Reporting***

Internal controls over financial reporting are procedures designed to provide reasonable assurance that transactions are properly authorized, assets are safeguarded against unauthorized or improper use, and transactions are properly recorded and reported. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance with respect to the reliability of financial reporting and financial statement preparation.

**Evaluation of Disclosure Controls and Procedures and Internal Control over Financial Reporting**

***Disclosure Controls and Procedures***

Disclosure controls and procedures are designed to provide reasonable assurance that all relevant information is gathered and reported to senior management, including the Company's President and Chief Executive Officer and Chief Financial Officer, on a timely basis so that appropriate decisions can be made regarding public disclosure. As at the end of the period covered by this management's discussion and analysis, management of the Company, with the participation of the President and Chief Executive Officer and the Chief Financial Officer, evaluated the effectiveness of the Company's disclosure controls and procedures as required by Canadian securities laws. Based on that evaluation, the President and Chief Executive Officer and the Chief Financial Officer have concluded that, as of the end of the year covered by this management's discussion and analysis, the disclosure controls and procedures were



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effective to provide reasonable assurance that information required to be disclosed in the Company's annual filings and interim filings (as such terms are defined under Multilateral Instrument 52-109 – *Certification of Disclosure in Issuers' Annual and Interim Filings*) and other reports filed or submitted under Canadian securities laws is recorded, processed, summarized and reported within the time periods specified by those laws and that material information is accumulated and communicated to management of the Company, including the President and Chief Executive Officer and the Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

***Internal Control over Financial Reporting***

Internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with Canadian generally accepted accounting principles. The Company's Chief Executive Officer and Chief Financial Officer have ensured the design of internal control over financial reporting.

During the most recent quarter there were no changes in the Company's internal control over financial reporting that materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**Recent Accounting Changes and Effective Dates**

*Effective January 1, 2009*

The CICA has issued a new standard which may affect the financial disclosures and results of operations of the Company for interim and annual periods beginning January 1, 2009. The Company will adopt the requirements commencing in the quarter ended March 31, 2009 and is considering the impact this will have on the Company's financial statements.

Section 3064, Goodwill and intangible assets, establishes revised standards for recognition, measurement, presentation and disclosure of goodwill and intangible assets. Concurrent with the introduction of this standard, the CICA withdrew EIC 27, Revenues and Expenses during the pre-operating period. As a result of the withdrawal of EIC 27, the Company will no longer be able to defer costs and revenues incurred prior to commercial production at new operations.

**Forward-Looking Statements**

This Management's Discussion and Analysis includes "forward-looking statements", within the meaning of applicable securities legislation, which are based on the opinions and estimates of Management and are subject to a variety of risks and uncertainties and other factors that could cause actual events or results to differ materially from those projected in the forward looking statements. Forward-looking statements are often, but not always, identified by the use of words such as "seek", "anticipate", "budget", "plan", "continue", "estimate", "expect", "forecast", "may", "will", "project", "predict", "potential", "targeting", "intend", "could", "might", "should", "believe" and similar words suggesting future outcomes or statements regarding an outlook. Such risks and uncertainties include, but are not limited to, risks associated with the oil and gas industry (including operational risks in exploration development and production; delays or changes in plans with respect to exploration or development projects or capital expenditures; the uncertainty of reserve estimates; the uncertainty of estimates and projections in relation to production, costs and expenses; the uncertainty surrounding the ability of Candax to obtain all permits, consents or authorizations required for its operations and activities; and health safety and environmental risks), the risk of commodity price and foreign exchange rate fluctuations, the ability of Candax to fund the capital and operating expenses necessary to achieve the business objectives of Candax, the uncertainty associated with commercial negotiations and negotiating with foreign governments and risks associated with international business activities, as well as those risks described in public disclosure documents filed by Candax. Due to the risks, uncertainties and assumptions inherent in forward-looking statements, prospective investors in securities of Candax should not place undue reliance on these forward-looking statements. Statements in relation to "reserves" are deemed to be forward-looking statements, as they



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involve the implied assessment, based on certain estimates and assumptions, that the reserves described can be profitably produced in the future.

Readers are cautioned that the foregoing lists of risks, uncertainties and other factors are not exhaustive. The forward-looking statements contained in this press release are made as of the date hereof and the Company undertakes no obligation to update publicly or revise any forward-looking statements contained in this press release or in any other documents filed with Canadian securities regulatory authorities, whether as a result of new information, future events or otherwise, except in accordance with applicable securities laws. The forward-looking statements contained in this press release are expressly qualified by this cautionary statement.



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Interim Consolidated Financial Statements  
*(unaudited)*

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**Consolidated Balance Sheets (unaudited)**

<b>As at (in thousands of Canadian dollars)</b>	March 31, 2008	December 31, 2007
<b>ASSETS</b>		
<b>Current</b>		
Cash and cash equivalents	\$ 23,943	\$ 22,199
Restricted investment (Note 2)	796	769
Accounts receivable	8,000	5,560
Inventory	4,699	2,338
Deposits and prepaids	290	401
	<u>37,728</u>	<u>31,267</u>
Petroleum and natural gas properties	135,404	103,663
Property, plant and equipment	12,362	12,759
Long-term receivable	308	198
	<u>\$ 185,802</u>	<u>\$ 147,887</u>
<b>LIABILITIES</b>		
<b>Current</b>		
Accounts payable and accrued liabilities	\$ 40,734	\$ 38,119
Current portion of term loan (Note 3)	8,574	2,696
Current portion of limited recourse long-term debt (Note 4)	10,924	9,927
	<u>60,232</u>	<u>50,742</u>
Term loan (Note 3)	35,566	11,182
Limited recourse long-term debt (Note 4)	2,563	2,383
Asset retirement obligation (Note 5)	1,950	1,842
Future income tax liability (Note 6)	3,701	3,342
	<u>104,012</u>	<u>69,491</u>
<b>SHAREHOLDERS' EQUITY</b>		
Capital stock	111,753	111,753
Contributed surplus	2,588	2,419
Accumulated other comprehensive loss (Note 9)	(18,209)	(23,732)
Deficit	(14,342)	(12,044)
	<u>81,790</u>	<u>78,396</u>
	<u>\$ 185,802</u>	<u>\$ 147,887</u>

*The accompanying notes are an integral part of these financial statements.*

**Candax Energy Inc.**  
**Consolidated Statements of Operations and Deficit (unaudited)**

**For the three months ended March 31**

*(in thousands of Canadian dollars except for per share amounts)*

	2008	2007
<b>Revenues</b>		
Sales, net of royalties	\$ 2,097	\$ 2,059
Interest and other income	350	727
	<u>2,447</u>	<u>2,786</u>
<b>Expenses</b>		
Operating costs	704	424
Depletion, depreciation and amortization	1,128	966
General and administrative	1,794	1,116
Interest	318	344
Foreign exchange	(142)	90
Stock-based compensation	169	239
Accretion on asset retirement obligation	42	41
	<u>4,013</u>	<u>3,220</u>
<b>Loss for the period before current and future income taxes</b>	<u>(1,566)</u>	<u>(434)</u>
Current income tax expense	335	460
Future income tax expense	397	-
	<u>732</u>	<u>460</u>
<b>Loss for the period</b>	<u>\$ (2,298)</u>	<u>\$ (894)</u>
Deficit, beginning of period	(12,044)	(2,793)
<b>Deficit, end of period</b>	<u>\$ (14,342)</u>	<u>\$ (3,687)</u>
<b>Loss per share - basic and diluted</b>	(0.01)	(0.01)
<b>Weighted average number of shares outstanding</b>		
- basic	169,231,606	168,874,106
- diluted	170,309,106	168,874,106

*The accompanying notes are an integral part of these financial statements.*

**Candax Energy Inc.**  
**Consolidated Statements of Cash Flows (unaudited)**

**For the three months ended March 31**

*(in thousands of Canadian dollars)*

2008

2007

**OPERATING ACTIVITIES**

Loss	\$	(2,298)	\$	(894)
Items not affecting cash				
Write-down of spare parts inventory		400		-
Stock-based compensation		169		239
Depletion, depreciation and amortization		1,128		966
Future income tax expense		397		-
Accretion on asset retirement obligation		42		41
		(162)		352
Net change in non-cash working capital		(1,171)		(4,344)
		(1,333)		(3,992)

**INVESTING ACTIVITIES**

Decrease in restricted investments		-		265
Investment in long-term receivable		(100)		(117)
Additions to petroleum and natural gas properties		(27,348)		(2,120)
		(27,448)		(1,972)

**FINANCING ACTIVITIES**

Proceeds from credit facility		29,136		-
		29,136		-
Foreign currency translation		1,389		(441)

<b>Net increase (decrease) in cash and cash equivalents</b>		1,744		(6,405)
Cash and cash equivalents, beginning of period		22,199		51,433
<b>Cash and cash equivalents, end of period</b>	\$	23,943	\$	45,028
<b>Cash and cash equivalents are comprised of:</b>				
Cash	\$	23,943	\$	10,850
Short-term investments		-		34,178
	\$	23,943	\$	45,028
Interest paid during the period	\$	-	\$	264
Income taxes paid during the period	\$	1,600	\$	2,859

**Candax Energy Inc.**  
**Consolidated Statements of Comprehensive Income (loss) (unaudited)**

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**For the three months ended March 31**

*(in thousands of Canadian dollars)*

	2008	2007
Loss for the period	\$ (2,298)	\$ (894)
Other comprehensive income (loss):		
Unrealized foreign exchange gain (loss) on translation of self-sustaining foreign operations	5,523	(910)
Income taxes	-	-
Other comprehensive income (loss):	5,523	(910)
Comprehensive income (loss)	\$ 3,225	\$ (1,804)

## **1. Summary of Significant Accounting Policies**

The accompanying unaudited interim consolidated financial statements include the accounts of Candax Energy Inc. ("Candax" or the "Company") and its subsidiaries, and have been prepared in accordance with Canadian generally accepted accounting principles applicable for interim reporting periods. These unaudited notes to the interim consolidated financial statements do not include all disclosures required in the annual financial statements and should be read in conjunction with the audited consolidated financial statements and notes for the year ended December 31, 2007.

These unaudited interim consolidated financial statements have been prepared following the same accounting policies and methods of computation as the annual audited consolidated financial statements for the year ended December 31, 2007 except as described below. In the opinion of management, all adjustments required for a fair presentation are included in these unaudited interim consolidated financial statements in accordance with the accounting policies of the Company.

### **Capital disclosures and financial instruments – disclosures and presentation**

On December 1, 2006, the CICA issued three new accounting standards: Capital Disclosures (Handbook Section 1535), Financial Instruments – Disclosures (Handbook Section 3862), and Financial Instruments – Presentation (Handbook Section 3863). These new standards became effective for the Company on January 1, 2008. Handbook Section 1535 specifies the disclosure of (i) an entity's objectives, policies and processes for managing capital; (ii) quantitative data about what the entity regards as capital; (iii) whether the entity has complied with any capital requirements; and (iv) if it has not complied, the consequences of such non-compliance. The Company has included disclosures recommended by the new Handbook section in note 8 to these interim financial statements.

### **Financial Instruments**

Handbook Sections 3862 and 3863 replace Handbook Section 3861, Financial Instruments – Disclosure and Presentation, revising and enhancing its disclosure requirements, and carrying forward unchanged its presentation requirements. These new sections place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks.

### **Recent Accounting Pronouncements**

#### *Effective January 1, 2009*

The CICA has issued a new standard which may affect the financial disclosures and results of operations of the Company for interim and annual periods beginning January 1, 2009. The Company will adopt the requirements commencing in the quarter ended March 31, 2009 and is considering the impact this will have on the Company's financial statements.

Section 3064, Goodwill and intangible assets, establishes revised standards for recognition, measurement, presentation and disclosure of goodwill and intangible assets. Concurrent with the introduction of this standard, the CICA withdrew EIC 27, Revenues and Expenses during the pre-operating period. As a result of the withdrawal of EIC 27, the Company will no longer be able to defer costs and revenues incurred prior to commercial production at new operations.

## **2. Restricted Investment**

Restricted investment represents a \$0.8 million debt service reserve held by the Arab Banking Corporation as security for principal and interest payments to be made by SEEB under its limited recourse long-term debt (see Note 4).

**Candax Energy Inc.**  
**Notes to the Consolidated Financial Statements (unaudited)**  
*(in thousands of Canadian dollars unless otherwise stated)*

**3. Term Loan**

	Rate	(\$000s)	
		March 31, 2008	December 31, 2007
Term Loan	LIBOR +2%	\$ 44,140	\$ 13,878
Less: current portion		(8,574)	(2,696)
		<b>\$ 35,566</b>	<b>\$ 11,182</b>

On January 30, 2008, the credit facility was increased from US \$20 million to US \$50 million under the same terms and conditions. On February 4, 2008, the Company drew down US \$29 million from the facility bringing the outstanding amount on the facility to US \$43 million at March 31, 2008. The term of the loan is 5 years and bears interest at LIBOR +2%. The loan is secured by the Company's oil producing assets in Tunisia. US \$1.5 million of the credit facility is being used as security for a letter of credit issued by the Company. (see Note 10(b)).

For the 3 months ended March 31, 2008, interest expense in the amount of \$0.5 million has been recorded in the consolidated balance sheets in petroleum and natural gas properties.

**4. Limited Recourse Long-Term Debt**

	Rate	(\$000s)	
		March 31, 2008	December 31, 2007
Limited recourse SEEB debt			
Project financing (US\$ based)	LIBOR +1.5% +2% default margin*	\$ 3,633	\$ 3,475
Project financing (Euro based)	ADB** +2% +2% default margin*	7,234	6,452
Due to Caterpillar Power Ventures Inc.	13%	2,392	2,383
Due to Caterpillar Power Ventures Inc.	LIBOR +0.4%	228	-
		<b>13,487</b>	<b>12,310</b>
Amounts due within one year			
Due to Caterpillar Power Ventures Inc.		(57)	-
Project financing (US\$ based)		(3,633)	(3,475)
Project financing (Euro based)		(7,234)	(6,452)
		<b>(10,924)</b>	<b>(9,927)</b>
		<b>\$ 2,563</b>	<b>\$ 2,383</b>

\* the 2% default margin commenced May 2006 as principal payments were deferred and the loans were technically in default

\*\* African Development Bank Base Rate

On March 18, 2002, SEEB and its joint venture partner closed a US\$22.2 million limited-recourse project financing, 50% of which was subsequently converted into Euros. Security for the financing is limited to the project assets and a corporate non-performance guarantee of US \$0.8 million. Candax's share of the project financing at March 31, 2008 is \$10.9 million. All required interest and principal payments are expected to be repaid through operating cash flows of the SEEB power plant. The proceeds of this project financing were used to fund construction costs of the SEEB plant which commenced operations May 9, 2003. As disclosed in Note 12, the required principal payments have not been made due to a lack of cash resources at SEEB and as a result the loan is in default. Since the loan is in default it may be

called by the lenders at anytime and therefore the entire amount of the non-recourse loan is considered current.

Also included in the limited recourse SEEB debt is an amount of \$2.4 million in respect of Candax's share of additional project financing provided by Caterpillar Power Ventures Inc. ("CPVI") to complete the SEEB project. There are no fixed repayment terms nor will the lender demand repayment in 2008. The venture plans to repay this debt with SEEB operating cash flows, however this is not anticipated to occur until the second quarter of 2008. Accordingly, this additional financing has been classified as a long-term obligation.

Also included in the limited recourse SEEB debt is an amount of \$0.2 million in respect of Candax's share of funding advances made to SEEB by CPVI during 2007. These were reclassified to long-term debt subject to a loan agreement executed during the quarter. The loan is repayable by SEEB in equal quarterly payments over a term of 4 years.

For the three months ended March 31, 2008, interest expense in the amount of \$0.3 million (2007 - \$0.3 million) has been recorded in the consolidated statements of operations and deficit.

**5. Asset Retirement Obligation**

<b>For the three months ended March 31, 2008</b>		
Balance at December 31, 2007	\$	1,842
Accretion expense		42
Foreign exchange		66
<b>Balance at March 31, 2008</b>	<b>\$</b>	<b>1,950</b>

The total undiscounted amount of estimated cash flows required to settle the obligation is \$5.3 million at March 31, 2008, which has been discounted using a credit-adjusted risk-free rate of 9%. Most of these obligations are not expected to be paid until 2021.

**6. Income taxes**

The future tax liability of \$3.7 million at March 31, 2008 relates to the difference in the unclaimed tax deductible costs of capital assets in Tunisia and the related carrying value. The carrying value is based on the fair value of net assets acquired in the acquisition. When the assets are amortized there will be an associated tax benefit for accounting purposes. The liability is based on consolidated accounting values and any cash liability for income tax purposes is not triggered unless the underlying assets are sold. The approximate value of tax pools available in Tunisia are \$174.1 million.

**7. Capital Stock**

**Stock Options**

In April 2005, the Board of Directors established a share incentive plan to provide additional incentive to its directors, officers, employees and consultants for their efforts on behalf of the Company in the conduct of its affairs. The maximum number of common shares reserved for issuance under the share option plan comprising part of the share incentive plan may not exceed 10% of the number of common shares outstanding. Under the terms of the plan, all options vest immediately, unless otherwise specified. All options granted under the plan expire no later than the tenth anniversary of the grant date.

**Candax Energy Inc.**  
**Notes to the Consolidated Financial Statements (unaudited)**  
*(in thousands of Canadian dollars unless otherwise stated)*

The following table summarizes the options outstanding in accordance with the Company's share incentive plan:

	Weighted Average Exercise Price	Number of Options
<b>Outstanding - beginning of period</b>	<b>\$ 0.78</b>	<b>12,067,500</b>
<b>Transactions during the period:</b>		
Granted	0.92	1,050,000
Exercised	-	-
<b>Outstanding - end of period</b>	<b>\$ 0.80</b>	<b>13,117,500</b>
<b>Options exercisable - end of period</b>	<b>\$ 0.79</b>	<b>11,642,499</b>

Even though the average market price of the common shares during the period was higher than the exercise price of many of the outstanding options, there is no dilutive effect on the loss per share.

Using the fair value method, the compensation expense is amortized over the three-year vesting period of the options. For the three months ended March 31, 2008, the Company recorded a stock-based compensation expense of \$0.2 million (2007 - \$0.2 million) relating to share options. The fair value of the share options granted during the period was \$0.6 million and the unamortized cost of such is \$0.5 million.

The fair value was estimated on the date of the grant using the Black-Scholes fair value option-pricing model and the following assumptions:

	2008	2007
Expected volatility	75%	60%
Risk-free interest rate	3.76%	3.88%
Term	5 years	5 years
Dividend yield	nil	nil

## 8. Capital Management

The Company manages its capital to ensure that the Company and its subsidiaries will be able to continue as a going concern while attempting to maximize the return to shareholders through the optimization of a reasonable debt and equity balance commensurate with current operating requirements. The capital structure consists of debt, (notes 3 and 4), cash and cash equivalents and shareholders' equity excluding accumulated other comprehensive income (loss). The Company raises capital, as necessary, to meet its needs and take advantage of perceived opportunities and, therefore, does not have a numeric target for its capital structure.

	<b>March 31, 2008    December 31, 2007</b>	
Total debt	\$ 57,627	\$ 26,188
Less: Cash and cash equivalents	23,943	22,199
Net debt	33,684	3,989
Shareholders' equity	81,790	78,396
<b>Total Capital</b>	<b>\$ 115,474</b>	<b>\$ 82,385</b>

**9. Accumulated Other Comprehensive Loss**

The balance in accumulated other comprehensive loss represents the cumulative amount of unrealized foreign exchange losses on translation of self-sustaining foreign operations.

**10. Commitments**

(a) Under the terms of an agreement with the Tunisian government, 20% of the Company's oil production must be dedicated to the domestic market. The production sold under this domestic market obligation receives a price equal to 90% of the US dollar price for the Brent-based export sales. Oil production is accumulated in a storage facility until a marketable cargo is achieved. Under this agreement, the state-owned oil company, ETAP, with respect to its 55% rights on the Ezzaouia field production and on behalf of the Government with respect to the domestic market obligation and the Company's Tunisian entities have agreed to optimize tanker lifting volumes. As a result of this reciprocal practice, a short-term volumetric imbalance may arise through an "under/over" lift position. This short-term situation is corrected from future production allocations.

(b) As of March 31, 2008, the Company has issued a standby letter of credit in the amount of US \$1.5 million in favour of Madagascar Ministry of Industry and Mines in accordance with the terms of the production sharing agreement entered into in November 2006. The letter of credit will be released when the Company has satisfied the commitments as outlined in the agreement.

**11. Segmented Information**

By generation source:

	Oil and gas operations		Electricity generation operations		Total	
	2008	2007	2008	2007	2008	2007
<b>For the three months ended March 31</b>						
Sales (net of royalties)	\$ 2,097	\$ 2,059	\$ -	\$ -	\$ 2,097	\$ 2,059
Depletion, depreciation and amortization	731	478	397	488	1,128	966
Interest expense	-	-	318	344	318	344
Net income (loss)	(1,531)	112	(767)	(1,006)	(2,298)	(894)
<b>As at March 31, 2008 and December 31, 2007</b>						
Capital assets	135,404	103,663	12,362	12,759	147,766	116,422

**12. Subsequent Events**

Limited recourse long-term debt default.

As described in Note 4, the Company has a 50% joint venture interest in the SEEB power plant and as a result, has limited recourse long-term debt in the amount of \$10.9 million. Due to the lack of production from the El Bibane field, the SEEB power plant has not generated revenues during the period and as a result was unable to meet its current obligations under the credit facility. Negotiations with the lenders are on-going as there is no commitment from the lenders to continue to defer principal payments. In the event of a declaration of default by the lenders, the lenders would take control of the SEEB plant and Candax would owe a default payment of US \$0.8 million but would not be liable for the balance of the loans outstanding nor for the deferred principal amounts.