Pine Cliff Energy Ltd.

SECOND QUARTER 2012

TSX Venture Exchange: **PNE** www.pinecliffenergy.com

Message to Shareholders:

Pine Cliff Energy Ltd. is pleased to report its second quarter of 2012, which is our first full quarter reporting results since the March 2012 Carrot Creek asset acquisition. Highlights of the second quarter report are as follows:

- Attained record quarterly sales volumes of 972 boe/d for the quarter, as compared to 103 boe/d in the second quarter of 2011, weighted approximately 77 percent natural gas and 23 percent oil and natural gas liquids;
- Added strong geological and financial expertise to our management team;
- Realized funds flow from operations of $520,000 as compared to $103,000 in the same period of 2011;
- Recognized an operating netback of $11.78 per boe as compared to $17.34 per boe the second quarter of 2011;
- Acquired 3-D seismic in the Carrot Creek area to assist in determining the Company's fall and winter drilling program;
- Renewed, subsequent to quarter end, the related party note payable of $7,000,000 to August 31, 2013, allowing the Company increased financial flexibility; and
- Repaid $694,000 of bank debt through fiscally responsible financial management.

We will continue to advance our strategy of providing above average industry returns for short-term investors and high rates of return for long-term investors. We plan to commence the drilling of at least one gross (0.25 net) well prior to the end of 2012 to further increase sales volumes and the Company's oil and liquids weighting. Pine Cliff has a high quality asset base which we believe will have significant upside potential with the recovery of natural gas prices. Pine Cliff continues to anticipate weakness in commodity prices over the short-term but we continue to hold the view that natural gas prices are not sustainable at current levels and will have to increase. The rapid decline in natural gas directed rig counts, oil sands growth, fuel switching and industry LNG export discussions are all promising signals for future recovery of natural gas prices in 2013.

We are focused on innovatively pursuing opportunities to add to or create new material core areas by acquiring additional high-impact assets for future growth through asset or corporate acquisitions, farm-ins or joint ventures. The current downturn in the commodities market is accelerating merger and acquisition activities with recent transactions highlighting the interest in natural gas opportunities in Canada. We anticipate this trend continuing in the third quarter and strongly believe that Pine Cliff remains well positioned to take advantage of this unique situation in the industry.

Pine Cliff draws considerable insight from the experience and guidance of our Board of Directors and we were pleased to further strengthen our Board with the addition of our former Chief Operating Officer, Randy M. Jarock, in May. We look forward to a busy second half of the year with the commencement of our drilling program and remain optimistic that we will be able to capitalize on additional opportunities for growth.

Thank you for your continued support.

Yours truly,

Phil Hodge
President and Chief Executive Officer
August 14, 2012

Please refer to the attached Management's Discussion and Analysis for Reader Advisories regarding forward-looking information, non-IFRS measures and oil and gas measurements. This Message to Shareholders should be read in conjunction with the unaudited condensed interim financial statements of Pine Cliff Energy Ltd. together with Management's Discussion and Analysis for the three and six months ended June 30, 2012 and 2011, which can be found on www.sedar.com and is subject to the same cautionary statements as set out therein.

	Three months ended June 30		Six months ended June 30	
	2012	2011	**2012** [1]	2011
($000s, unless otherwise indicated)				
FINANCIAL				
Oil and gas sales	**2,130**	236	**3,031**	482
Cash flow from operating activities	**1,198**	69	**867**	217
Funds flow from operations [2]	**520**	103	**485**	216
Basic per share ($/share)	**0.01**	0.00	**0.01**	0.00
Diluted per share ($/share)	**0.01**	0.00	**0.01**	0.00
Earnings (loss)	**(450)**	(53)	**263**	(86)
Basic per share ($/share)	**(0.01)**	(0.00)	**0.00**	(0.00)
Diluted per share ($/share)	**(0.01)**	(0.00)	**0.00**	(0.00)
Capital expenditures	**172**	3	**616**	9
Acquisition of the Carrot Creek Assets	**90**	**-**	**22,608**	**-**
Total assets	**29,031**	2,622	**29,031**	2,622
Bank debt	**12,096**	-	**12,096**	-
Related party note payable	**7,000**	-	**7,000**	-
Trade and other payables less trade and other receivables	**517**	13	**517**	13
Cash	**-**	(176)	**-**	(176)
Net debt [3]	**19,613**	(163)	**19,613**	(163)
Weighted-average common shares outstanding (000s)				
Basic	**63,564**	46,146	**60,406**	46,146
Diluted	**63,564**	46,146	**62,149**	46,146
OPERATIONS				
Production [4]				
Natural gas (mcf/d)	**4,517**	614	**3,222**	636
Crude oil (bbls/d)	**30**	-	**20**	-
Natural gas liquids (bbls/d)	**189**	1	**130**	1
Total (boe/d)	**972**	103	**687**	107
Commodity sales prices				
Natural gas ($/mcf)	**2.01**	4.12	**2.02**	4.07
Crude oil ($/bbl)	**79.26**	-	**78.26**	-
Natural gas liquids ($/bbl)	**62.98**	81.55	**66.20**	82.62
Combined ($/boe)	**24.07**	25.17	**24.26**	24.90
Netback ($/boe)				
Operating netback ($/boe) [5]	**11.78**	17.34	**12.18**	16.81

[1] The results of the first six months of 2012 include the results of the Carrot Creek Assets for the period of March 1 to June 30, 2012.
[2] Funds flow from operations is a non-IFRS measure that represents the total of funds provided by operating activities, before adjusting for changes in non-cash working capital and changes in interest payable.
[3] Net debt is a non-IFRS measure calculated as the sum of bank debt, related party note payable and trade and other payables less trade and other receivables and cash.
[4] The production for the six months ended June 30, 2012 includes the results of the Carrot Creek Assets for the period of March 1 to June 30, 2012, averaged over 182 days.
[5] Operating netback is a non-IFRS measure calculated as the average per boe of the Company's oil and gas sales, less royalties and operating expenses.

August 14, 2012

INTRODUCTION

The following Management's Discussion and Analysis ("MD&A") is a review of the operations and current financial position for the three and six months ended June 30, 2012 for Pine Cliff Energy Ltd. ("Pine Cliff" or the "Company") and should be read in conjunction with the unaudited condensed interim financial statements as at and for the three and six months ended June 30, 2012, together with the notes related thereto, and the audited consolidated financial statements as at and for the fiscal year ended December 31, 2011, together with the notes related thereto. Additional information relating to the Company may be found on www.sedar.com and by visiting Pine Cliff's website at www.pinecliffenergy.com.

Pine Cliff's head office is based in Calgary, Alberta, Canada. Common shares of the Company are listed and posted for trading on the Toronto Stock Exchange Venture under the symbol "PNE".

READER ADVISORIES

This MD&A contains financial measures that are not defined under International Financial Reporting Standards ("IFRS") and forward-looking statements. Readers are cautioned that the MD&A should be read in conjunction with the Company's disclosure under "Non-IFRS Measures" and "Forward-Looking Information" included at the end of the MD&A.

Other Measurements

All amounts herein are presented in Canadian dollars unless otherwise specified. All references to C$ or $ are to Canadian dollars and references to U.S.$ are to United States dollars.

Where amounts are expressed in a barrel of oil equivalent ("boe" or daily equivalent of "boe/d"), natural gas volumes have been converted to barrels of oil equivalent on the basis that six thousand cubic feet of natural gas ("mcf" or daily equivalent of "mcf/d") is equal to one barrel of oil ("bbl" or daily equivalent of "bbl/d"). This conversion ratio is based on energy equivalence primarily at the burner tip and does not represent a value equivalency at the wellhead. The term boe may be misleading, particularly if used in isolation.

SENSITIVITIES

Pine Cliff's results are sensitive to changes in the business environment in which it operates. The following chart shows the Company's sensitivity to key commodity price variables and interest rates. The sensitivity calculations are performed independently showing the effect of the change of one variable; all other variables are held constant.

Business environment sensitivities		Impact on annual funds flow from operations [1]	
	Change	$000s	$ per share [3]
Crude oil price - Edmonton par ($/bbl) [2]	$1.00	60	0.00
Natural gas price - AECO ($/mcf) [2]	$0.10	170	0.00
Interest rate on variable rate debt	1.0%	120	0.00

[1] This analysis does not adjust for changes in working capital and uses current royalty rates.
[2] Pine Cliff has prepared this analysis using its consolidated June monthly production volumes annualized for twelve months.
[3] Based on Q2-2012 weighted average shares outstanding of 63,564,000.

STRATEGIC OBJECTIVES AND BUSINESS

Pine Cliff is actively engaged in the exploration, development and production of natural gas, crude oil and natural gas liquids ("liquids" or "NGLs"). The Company is seeking to acquire material asset positions in the Western Canadian Sedimentary Basin ("WCSB") to enlarge its Carrot Creek core area and create new core areas of production with significant reserves and drilling inventories, while also accelerating current oil and liquids drilling and optimization opportunities.

On March 1, 2012, Pine Cliff purchased assets in the Carrot Creek area of Alberta (the "Carrot Creek Assets") for cash consideration of $23.5 million ($22.6 million after operating funds flow adjustments for January and February 2012). The acquisition had an effective date of January 1, 2012 and provided Pine Cliff with its first core area in the WCSB. The results of the Carrot Creek Assets have been included in the financial results of the Company effective March 1, 2012.

The Carrot Creek Assets are located southeast of the town of Edson, Alberta, Canada and produce liquids rich natural gas as well as a small amount of oil. In addition to the producing assets, Pine Cliff acquired 15.3 net sections of prospective land, some of which has current vertical production. Pine Cliff has a 31% working interest in the Carrot Creek Assets and is the operator of approximately 90% of the Company's production in the area. Pine Cliff anticipates that the land has multi-zone potential which can be further exploited using horizontal drilling technology. Pine Cliff currently plans to commence drilling one gross well (0.25 net well) in the second half of 2012 on an expiring lease. Pine Cliff also plans to drill one well in the Rock Creek zone in early 2013. Horizontal drilling in the Rock Creek formation has been ongoing since 2006 and there have been significant improvements in both the drilling and completions of these wells, resulting in higher reservoir contact, more effective stimulations and improved performance. There are also significant natural gas prospects (over 50 gross potential locations) most of which have been inventoried until natural gas prices improve.

The balance of Pine Cliff's production comes from non-operated properties in the Sundance area in northwest Alberta (the "Sundance Assets"), however the Company does not currently have a large enough land position to make it a significant core area.

Management is pleased with its progress to date and will remain steadfast to its strategic commitment to grow the Company and will continue to aggressively pursue accretive business opportunities during the remainder of 2012 and beyond.

SELECTED QUARTERLY FINANCIAL INFORMATION

	2012		2011				2010	
($000s, unless otherwise indicated)	**Q2**	Q1 [1]	Q4	Q3	Q2	Q1	Q4	Q3 [2]
Average sales volumes (boe/d) [3]	**972**	401	88	100	103	111	129	152
Operating netback ($/boe) [4]	**11.78**	13.11	12.20	15.63	17.34	16.31	15.88	15.96
Oil and gas sales	**2,130**	901	164	220	236	246	280	324
Oil and gas sales, net of royalties	**1,735**	750	159	211	230	231	267	309
Cash flow (deficiency) from operating activities	**1,198**	(331)	(4)	120	69	148	39	243
Funds flow (deficiency) from operations [5]	**520**	(35)	54	83	103	113	119	123
Per share - basic ($/share)	**0.01**	(0.00)	0.00	0.00	0.00	0.00	0.00	0.00
Per share - diluted ($/share)	**0.01**	(0.00)	0.00	0.00	0.00	0.00	0.00	0.00
Earnings (loss)	**(450)**	713	(46)	(74)	(53)	(33)	(917)	(122)
Per share - basic ($/share)	**(0.01)**	0.01	(0.00)	(0.00)	(0.00)	(0.00)	(0.02)	(0.00)
Per share - diluted ($/share)	**(0.01)**	0.01	(0.00)	(0.00)	(0.00)	(0.00)	(0.02)	(0.00)

[1] The results for Q1-2012 include the results of the Carrot Creek Assets for the period of March 1 to March 31, 2012.
[2] Q3-2010 includes the results of Pine Cliff's continuing operations. Pine Cliff's South American assets were classified as discontinued assets during this quarter and sold on September 24, 2010. The Q3-2010 cash flow (deficiency) from total operations was $(547) and the Q3-2010 earnings from total operations was $616,000.
[3] The sales volumes for Q1-2012 includes the results of the Carrot Creek Assets for the period of March 1 to March 31, 2012, averaged over 91 days. Pine Cliff's sales for the month of March 2012 were approximately 1,015 boe/d, inclusive of 930 boe/d from the Carrot Creek Assets.
[4] Operating netback is a non-IFRS measure calculated as the average per boe of the Company's oil and gas sales, less royalties and operating expenses.
[5] Funds flow from operations is a non-IFRS measure that represents the total of funds provided by operating activities, before adjusting for changes in non-cash working capital and changes in interest payable.

Q2-2012 highlights

During the second quarter of 2012, Pine Cliff reports that it:

- Maintained a strong financial position, including the repayment of $694,000 of bank debt;
- Attained record average daily sales volumes of 972 boe/d as compared to 103 boe/d in the second quarter of 2011. The increase is due to the acquisition of the Carrot Creek Assets;
- Achieved quarterly funds flow from operations of $520,000 (second quarter of 2011 – funds flow from operations of $103,000), due to increased revenues from the Carrot Creek Assets, offset by higher royalties, operating, general and administration, and interest expenses; and
- Reported a quarterly loss of $450,000 (second quarter of 2011 – loss of $53,000), mainly a result of non-cash depletion and depreciation and share-based payment expenses.

SALES VOLUMES

	Three months ended June 30		Six months ended June 30	
Total sales volumes by product	**2012**	2011	**2012**	2011
Natural gas (mcf)	**411,068**	55,874	**586,467**	115,184
Crude oil (bbls)	**2,767**	-	**3,634**	-
NGLs (bbls)	**17,220**	74	**23,576**	153
Barrels of oil equivalent	**88,498**	9,386	**124,954**	19,350
Oil and liquids weighting	**23%**	1%	**22%**	1%

	Three months ended June 30		Six months ended June 30	
Average daily sales volumes by product	**2012**	2011	**2012**	2011
Natural gas (mcf/d)	**4,517**	614	**3,222**	636
Crude oil (bbls/d)	**30**	-	**20**	-
NGLs (bbls/d)	**189**	1	**130**	1
Total (boe/d)	**972**	103	**687**	107

Pine Cliff's sales volumes increased by 844% in the second quarter of 2012 to 972 boe/d as compared to 103 boe/d in the second quarter of 2011. The significant increase was a result of the Carrot Creek Assets being included in the full second quarter 2012 results, whereas in 2011 sales were only from the Sundance Assets. These increases have been partially offset by production disruptions during the second quarter of 2012 associated with turnaround activity and compressor downtime. The Carrot Creek Assets produce liquids rich gas and oil, contributing to the increase in liquids weighting to 23% in the second quarter of 2012, as compared to just 1% in the second quarter of 2011.

Pine Cliff's sales volumes for the six months ended June 30, 2012 were 687 boe/d as compared to 107 boe/d in the six months ended June 30, 2011. The year-to-date sales volumes for 2012 are lower than the second quarter of 2012 as the sales volumes of the Carrot Creek Assets are included for only four out of six months and averaged over 182 days.

OPERATING NETBACKS

The components of the operating netback are summarized as follows:

	Three months ended June 30		Six months ended June 30	
	2012	2011	**2012**	2011
($ per boe)				
Oil and gas sales	**24.07**	25.17	**24.26**	24.90
Royalties	**4.46**	0.66	**4.37**	1.09
Operating expenses	**7.83**	7.17	**7.71**	7.00
Operating netback	**11.78**	17.34	**12.18**	16.81

Pine Cliff generated an operating netback of $11.78 per boe for the three months ended June 30, 2012 as compared to $17.34 per boe for the three months ended June 30, 2011. This reduction is a result of slightly lower commodity prices, higher royalties per boe, and higher operating expenses per boe.

Pine Cliff generated an operating netback of $12.18 per boe for the six months ended June 30, 2012 as compared to $16.81 per boe for the six months ended June 30, 2011. This reduction is a result of lower commodity prices, higher royalties per boe, and higher operating expenses per boe.

OIL AND GAS SALES

	Three months ended June 30				Six months ended June 30			
	2012		2011		**2012**		2011	
(000s, except per boe amounts)	**$**	**$ per boe**	$	$ per boe	**$**	**$ per boe**	$	$ per boe
Natural gas [1]	**826**	**2.01**	230	4.12	**1,186**	**2.02**	469	4.07
Crude oil	**219**	**79.26**	-	-	**284**	**78.26**	-	-
NGLs	**1,085**	**62.98**	6	81.55	**1,561**	**66.20**	13	82.62
Total sales	**2,130**	**24.07**	236	25.17	**3,031**	**24.26**	482	24.90

[1] Per unit values are expressed in $ per mcf.

Oil and gas sales increased by 803% from $236,000 in the second quarter of 2011 to $2,130,000 in the second quarter of 2012, reflecting a full quarter of increased sales volumes from the Carrot Creek Asset acquisition that closed on March 1, 2012. The increase in sales volumes was offset by a lower commodity price environment in 2012. Pine Cliff's realized price in the three months ended June 30, 2012 was $24.07 per boe as compared to $25.17 per boe in the same period of 2011. Pine Cliff's increased weighting towards oil and liquids mainly offset the significant decrease in natural gas prices.

For the six months ended June 30, 2012, oil and gas sales were $3,031,000 ($24.26 per boe) as compared to $482,000 ($24.90 per boe) for the same period of 2011; an increase of $2,549,000. This increase is primarily a result of the increased sales volumes from the Carrot Creek Asset acquisition, offset by a lower commodity price environment for gas and liquids.

Commodity prices and foreign exchange rates

Pine Cliff's financial results are significantly influenced by fluctuations in commodity prices, including price differentials. The following table shows select market benchmark prices and foreign exchange rates in the last six quarters to assist in understanding volatility in prices and foreign exchange rates that have impacted Pine Cliff's business.

	Q2-2012	Q1-2012	Q4-2011	Q3-2011	Q2-2011	Q1-2011
Natural gas						
NYMEX (U.S.$/mmbtu) [1]	2.26	2.77	3.61	4.19	4.36	4.14
AECO (C$/mcf)	1.89	2.15	3.19	3.65	3.86	3.79
Crude oil						
WTI (U.S.$/bbl)	93.49	102.93	94.06	89.76	102.56	94.10
Edmonton light (C$/bbl)	84.42	92.70	97.86	92.24	103.58	88.39
Foreign exchange						
C$/U.S.$	1.0102	1.0012	1.0231	0.9802	0.9677	0.9860

[1] mmbtu is the abbreviation for millions of British thermal units. One mcf of natural gas is approximately 1.02 mmbtu.

The average NYMEX gas price in the United States has decreased by 48% in the second quarter of 2012 as compared to the second quarter of 2011, whereas benchmark AECO natural gas prices in Canada decreased by 51% in the second quarter of 2012 as compared to the same period of 2011. NYMEX is linked to AECO through transportation tariffs from the respective hubs to common markets and through foreign exchange rates. The price differentials between these two benchmarks have increased substantially in 2012, due in part to storage level issues in Canada as a result of a warmer than average winter. Although the natural gas pricing environment has been steadily weakening, some recoveries are starting to be seen with NYMEX price levels reaching greater than $3.00 per mmbtu in July. AECO prices averaged $1.89 per mcf for the three months ended June 30, 2012, while Pine Cliff's realized natural gas price was $2.01 per mcf.

WTI oil prices averaged U.S.$93.49 per bbl in the second quarter of 2012 as compared to U.S.$102.56 per bbl in the second quarter of 2011. Canadian crude prices are based upon refiner postings at Edmonton, Alberta and are linked to WTI through transportation tariffs to common markets and the foreign exchange rate. In 2012, the price differentials between Edmonton light oil prices and WTI widened substantially, due in part to refinery outages and seasonal turnarounds as well as transportation capacity issues. WTI slipped as low as approximately U.S.$77.00 per bbl in June, but has strengthened to over U.S.$90.00 per bbl in the latter part of July and into August. In the three months ended June 30, 2012, the realized price of Pine Cliff's oil was $79.26 per bbl as a result of quality adjustments to the posted Edmonton light crude oil prices.

Under normal circumstances, the average price of NGLs tracks the price of oil. However, in the later part of the second quarter of 2012, changes in the supply and demand for NGLs negatively affected the relationship between the price of NGLs and the price of oil. In the three months ended June 30, 2012, the realized price of Pine Cliff's NGLs was $62.98 per bbl, representing 75% of the Edmonton light crude oil prices as compared to 77% in the six months ended June 30, 2012.

Price differentials for commodities have the potential to remain volatile for the remainder of 2012.

ROYALTIES

	Three months ended June 30				Six months ended June 30			
	2012		2011		**2012**		2011	
(000s, except per boe amounts)	**$**	**$ per boe**	$	$ per boe	**$**	**$ per boe**	$	$ per boe
Total	**395**	**4.46**	6	0.66	**546**	**4.37**	21	1.09
% of oil and gas sales	**19%**		3%		**18%**		4%	

Royalties for the three and six months ended June 30, 2012 were $4.46 and $4.37 per boe, respectively, as compared to $0.66 and $1.09 per boe for the three and six months ended June 30, 2011, respectively. As a percentage of oil and gas sales, royalties averaged 18% in the first six months of 2012 (three months ended June 30, 2012 – 19%) as compared to 4% in the first six months of 2011 (three months ended June 30, 2011 – 3%). The increase in royalties on a per boe basis and as a percentage of oil and gas sales is due to the increased oil and liquids weighting and higher production volumes per well resulting from the Carrot Creek Asset acquisition. Royalty rates, which are dependent on production volumes per well and commodity prices, are presently higher for oil and liquids than natural gas.

OPERATING EXPENSES

	Three months ended June 30				Six months ended June 30			
	2012		2011		**2012**		2011	
(000s, except per boe amounts)	**$**	**$ per boe**	$	$ per boe	**$**	**$ per boe**	$	$ per boe
Operating expenses	**695**	**7.83**	67	7.17	**966**	**7.71**	135	7.00
% of oil and gas sales	**33%**		28%		**32%**		28%	

As compared to the same periods in 2011, operating expenses per boe increased 9% and 10% in the three and six months ended June 30, 2012, respectively, to $7.83 and $7.71 per boe, respectively. The increase in operating expenses is primarily due to a different operating environment and product mix in the Carrot Creek Assets as compared to the legacy Sundance Assets, such that oil and liquids production results in a higher average per boe cost to produce and transport to market than gas production. Pine Cliff is committed to seeking ways to increase efficiencies in the field which should decrease the operating expenses per boe in future periods.

GENERAL AND ADMINISTRATIVE EXPENSES

	Three months ended June 30				Six months ended June 30			
	2012		2011		**2012**		2011	
(000s, except per boe amounts)	**$**	**$ per boe**	$	$ per boe	**$**	**$ per boe**	$	$ per boe
Total	**317**	**3.58**	60	6.39	**724**	**5.79**	110	5.68
Less: non-recurring transaction costs	**10**	**0.11**	-	-	**174**	**1.39**	-	-
	307	**3.47**	60	6.39	**550**	**4.40**	110	5.68
% of oil and gas sales	**14%**		25%		**18%**		23%	

General and administrative expenses ("G&A"), excluding non-recurring transaction costs related to the Carrot Creek Asset acquisition, decreased on a per boe basis to $3.47 and $4.40 per boe in the three and six months ended June 30, 2012, respectively, as compared to $6.39 and $5.68 per boe in the three and six months ended June 30, 2011, respectively. On an absolute dollar basis, G&A has increased considerably as a reflection of the revitalized strategic focus of the Company which has, most notably, increased staffing costs. Going forward, G&A expenses should be comparable to the second quarter of 2012 on a per boe basis, as sales volumes in the second quarter include a full quarter of production from the Carrot Creek Assets.

On January 2, 2012, Philip Hodge was appointed President and Chief Executive Officer and became the first employee of the Company. Pine Cliff hired a Senior Geologist in the first quarter and a Controller in the second quarter. In 2011, Pine Cliff did not have any employees. To keep G&A at a low level, Pine Cliff continues to engage Bonterra Energy Corp. ("Bonterra"), a related party, to provide some executive, administrative and technical services. As Pine Cliff continues to grow, the Company expects to hire more staff as required.

SHARE-BASED PAYMENTS

	Three months ended June 30				Six months ended June 30			
	2012		2011		**2012**		2011	
(000s, except per boe amounts)	**$**	**$ per boe**	$	$ per boe	**$**	**$ per boe**	$	$ per boe
Total	**186**	**2.10**	-	-	**313**	**2.50**	-	-
% of oil and gas sales	**9%**		0%		**10%**		0%	

The Company has an equity settled stock-based compensation plan. Stock options are granted to certain officers, directors, employees and service providers, with the term and vesting period of the options granted being determined at the discretion of the Company's Board of Directors. An option's maximum term is five years.

In the first six months of 2012, Pine Cliff granted stock options to purchase 3,575,000 common shares at a weighted average exercise price of $0.42 per share. During the second quarter of 2012, 110,000 of those options were forfeited, resulting in an ending balance of 3,465,000 stock options outstanding. In the three and six months ended June 30, 2012, Pine Cliff recorded share-based payment expense of $186,000 and $313,000, respectively, (June 30, 2011 – nil) related to the stock options issued.

DEPLETION AND DEPRECIATION

	Three months ended June 30				Six months ended June 30			
	2012		2011		**2012**		2011	
(000s, except per boe amounts)	**$**	**$ per boe**	$	$ per boe	**$**	**$ per boe**	$	$ per boe
Oil and gas assets	**853**	**9.64**	145	15.45	**1,201**	**9.61**	299	15.45
Office furniture and equipment	**-**	**-**	-	-	**-**	**-**	-	-
Total	**853**	**9.64**	145	15.45	**1,201**	**9.61**	299	15.45
% of oil and gas sales	**40%**		61%		**40%**		62%	

Pine Cliff's depletion and depreciation expense decreased 38% on a per boe basis in both the three and six months ended June 30, 2012, as compared to the same periods in 2011. The reduction in depletion and depreciation expense per boe in 2012 is due in part to an increase in oil and gas reserves as a result of the acquisition of the Carrot Creek Assets. Additionally, Pine Cliff prospectively began depleting all of its oil and gas properties and facilities using the unit-of-production method over their proved plus probable reserve life ("Proved plus Probable Method"); a change from the unit-of-production method over their proved developed reserve life ("Proved Developed Method") for oil and gas properties and the straight-line method for production facilities. This change of estimate was due to management of the Company believing that the Proved plus Probable Method provides a better reflection of the estimated service life of the related assets.

FINANCE EXPENSES

	Three months ended June 30				Six months ended June 30			
	2012		2011		**2012**		2011	
(000s, except per boe amounts)	**$**	**$ per boe**	$	$ per boe	**$**	**$ per boe**	$	$ per boe
Unwinding of the discounted value of decommissioning liabilities	**10**	**0.11**	1	0.10	**16**	**0.13**	2	0.10
Interest and bank charges	**203**	**2.29**	-	-	**310**	**2.48**	-	-
Total	**213**	**2.40**	1	0.10	**326**	**2.61**	2	0.10
% of oil and gas sales	**10%**		0%		**11%**		0%	

In the three and six months ended June 30, 2012, Pine Cliff incurred finance expenses of $213,000 and $326,000, respectively, as compared to insignificant amounts in the three and six months ended June 30, 2011. Finance expenses in 2012 predominately consist of interest on the related party note payable, interest on Pine Cliff's revolving demand credit facility and bank charges incurred as a result of the implementation of the revolving demand credit facility. Amounts drawn under the revolving demand credit facility are in the form of Canadian prime lending rate based loans, guaranteed notes or letters of credit. The revolving demand credit facility bears interest at the prime lending rate plus 0.75% per annum. The related party note payable bears interest at 5% per annum. Overall, Pine Cliff realized an effective interest rate of 4.3% for the six months ended June 30, 2012.

INCOME TAXES

	Three months ended June 30				Six months ended June 30			
	2012		2011		**2012**		2011	
(000s, except per boe amounts)	**$**	**$ per boe**	$	$ per boe	**$**	**$ per boe**	$	$ per boe
Deferred tax expense (recovery)	**(79)**	**(0.89)**	10	(1.07)	**(1,308)**	**(10.47)**	1	0.05

During the second quarter of 2012, a deferred tax recovery of $79,000 was recorded, as compared to a deferred tax expense of $10,000 in the second quarter of 2011. The second quarter 2012 recovery is primarily related to temporary differences arising from the book basis of Pine Cliff's property and equipment and decommissioning liability relative to the tax basis.

Pine Cliff recognized a deferred income tax recovery of $1,308,000 in the six months ended June 30, 2012, as compared to a deferred tax expense of $1,000 in the six months ended June 30, 2011. The recovery is due in part to a deferred tax asset being recognized upon the acquisition of the Carrot Creek Assets, and the related reversal of the benefit of the tax pools that was not recognized in prior periods. Prior to the acquisition of the Carrot Creek Assets, it had been determined that it was not probable that the tax pools would be recovered. Given the increase in taxable earnings from the Carrot Creek Assets, it is now considered probable that the tax pools will be recovered and a recovery of the benefit of the tax pools was recognized in the first quarter of 2012.

The Company has accumulated approximately $30,182,000 in tax pools at June 30, 2012 (December 31, 2011 – $6,483,000) available for future use as deductions from taxable income. Included in these pools are estimated non-capital loss carry forwards of $4,491,000 (December 31, 2011 – $3,483,000) that expire between the years 2026 and 2032.

EARNINGS (LOSS) AND FUNDS FLOW FROM OPERATIONS

	Three months ended June 30		Six months ended June 30	
	2012	2011	**2012**	2011
($000s, except per boe amounts)				
Earnings (loss)	**(450)**	(53)	**263**	(86)
Adjustments for:				
Share-based payments	**186**	-	**313**	-
Depletion and depreciation	**853**	145	**1,201**	299
Unwinding of the discount on decommissioning liabilities	**10**	1	**16**	2
Deferred tax expense (recovery)	**(79)**	10	**(1,308)**	1
Funds flow from operations	**520**	103	**485**	216
Funds flow from operations ($/boe)	**5.88**	10.97	**3.88**	11.16

In the six months ended June 30, 2012, earnings increased by $349,000 to $263,000 as compared to the six months ended June 30, 2011. This is a function of the acquisition of the Carrot Creek Assets on March 1, 2012, which significantly increased oil and gas sales, royalties, operating expenses, and a significant deferred income tax recovery in the first quarter of 2012. This was offset by increased general and administration expenses, finance expenses, share-based payments, and depletion and depreciation, predominately a result of the increased activity of the Company with the acquisition of the Carrot Creek Assets.

In the three months ended June 30, 2012, Pine Cliff recorded a loss of $450,000 as compared to a loss of $53,000 in the three months ended June 30, 2011. Despite the aforementioned increase in activity of the Company, the non-cash depletion and depreciation of $853,000 (three months ended June 30, 2011 – $145,000) primarily created a loss for the quarter which was not offset by the deferred tax recovery of $79,000 in the second quarter of 2012.

Funds flow from operations, which represents cash flow from operating activities before changes in non-cash working capital and interest payable, was $520,000 and $485,000 in the three and six months ended June 30, 2012, respectively, as compared to $103,000 and $216,000 in the same periods of 2011, respectively. The increase in funds flow from operations in both periods is due to the increase in activity of the Company with the acquisition of the Carrot Creek Assets.

Other comprehensive income

Other comprehensive income relates entirely to the increase in fair value of Pine Cliff's investment in a publicly traded corporation, which was received in the first quarter of 2011 as part of the consideration in the disposal of the South American operations previously owned by Pine Cliff. During the first six months of 2012, the market value of the investment decreased by $87,000, before deferred taxes (June 30, 2011 – $5,000), to $85,000 (December 31, 2011 – $172,000).

SHARE CAPITAL

As at June 30, 2012, a total of 63,564,118 Pine Cliff common shares are issued and outstanding.

Rights offering

Pine Cliff completed a four for one rights offering for all shareholders of record at the close of business on January 11, 2012. Each shareholder received one right for each common shares held. For every four rights, a shareholder was entitled to purchase one Pine Cliff common share at a subscription price of $0.17 per common share. A total of 11,536,423 common shares were issued as part of the rights offering for gross proceeds of $1,961,000.

Private placement

On February 4, 2012, Pine Cliff completed a non-brokered private placement and issued 5,882,000 common shares at a price of $0.17 for gross proceeds of $1,000,000. All of the common shares issued under the placement were subscribed to by Pine Cliff's President and Chief Executive Officer and his associates, and were subject to a four-month holding period from the date of close.

ADDITIONS TO PROPERTY AND EQUIPMENT AND EXPLORATION AND EVALUATION ASSETS

($000s)	**Six months ended June 30, 2012**	Year ended December 31, 2011
Exploration and evaluation assets	**91**	-
Oil and gas assets	**525**	30
Furniture and office equipment	**2**	2
Acquistion of Carrot Creek Assets	**24,463**	-
Capitalized asset retirement costs	**230**	
Total	**25,311**	32

In the six months ended June 30, 2012, Pine Cliff added $25,311,000 in capital assets to its balance sheet as compared to $32,000 in the year ended December 31, 2011. The acquisition of the Carrot Creek Assets included property and equipment of $23,956,000 and exploration and evaluation assets of $507,000. In addition to the purchase of the Carrot Creek Assets, Pine Cliff acquired prospective land at crown land sales, purchased 3-D seismic and attempted to recomplete an existing wellbore. Given the current condition of the wellbore and depressed commodity prices, Pine Cliff has chosen to suspend this recompletion work and revisit the opportunity at a later date.

RELATED PARTY TRANSACTIONS

Related party note payable

On February 28, 2012, the Company's Executive Chairman of the Board and major shareholder (the "Related Party") loaned the Company $7,000,000. The promissory note bears interest at 5% per annum and is repayable on August 31, 2012 or at any time prior to that date, without penalty. Security under the promissory note is over all of the Company's assets and is subordinated to any and all claims in favour of the lender providing a credit facility to the Company. As at June 30, 2012, the full amount of the promissory note was outstanding (December 31, 2011 – nil). Interest paid on this note during the first six months of 2012 was $119,000 (June 30, 2011 – nil). The Company has the option to extend the repayment date of the promissory note up to one year from August 31, 2012 under the same terms and conditions. On August 1, 2012, the Company notified the Related Party that it would be exercising its option to extend the promissory note until August 31, 2013.

Management services agreement

Pine Cliff has a management services agreement with Bonterra, an oil and gas corporation that is publicly traded on the Toronto Stock Exchange with some common directors and management, to provide executive services, technical services, accounting services, oil and gas administration and office administration for Pine Cliff. Total fees for the six months ended June 30, 2012 were $30,000 (June 30, 2011 - $30,000), plus minimal administrative costs. The management services agreement may be cancelled by either party with 90 days notice. As at June 30, 2012, Pine Cliff owed Bonterra $2,800 (December 31, 2011 - $3,800).

Other

Geomark Exploration Ltd. ("Geomark") is a publicly traded company listed on the TSX-Venture with some common directors and some common management with Pine Cliff. As at June 30, 2012, Geomark owns 432,812 common shares of Pine Cliff (December

31, 2011 – 346,250), which represents less than one percent of the total issued and outstanding common shares of Pine Cliff. There were no other transactions between Pine Cliff and Geomark for the periods ended June 30, 2012 and December 31, 2011.

Related party transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of the consideration established and agreed to by the related parties.

LIQUIDITY

Liquidity describes a company's ability to access cash. Companies operating in the upstream oil and gas business, such as Pine Cliff, require sufficient cash to fund exploration and development projects, to increase production and reserves, to acquire strategic oil and gas assets and to repay debt.

The following table highlights Pine Cliff's sources and uses of cash for the three and six months ended June 30, 2012 and 2011:

	Three months ended June 30		Six months ended June 30	
	2012	2011	**2012**	2011
($000s)				
Funds flow (deficiency) from operations	**520**	103	**485**	216
Bank debt proceeds (repayment)	**(694)**	-	**12,096**	-
Related party note payable proceeds	**-**	-	**7,000**	-
Issuance of common shares, net of share issue costs	**-**	-	**2,885**	-
Interest payable	**(7)**	-	**38**	-
Changes in non-cash working capital	**432**	(149)	**443**	(139)
Decrease (increase) in cash	**11**	49	**277**	(68)
Capital expenditures including acquisitions	**262**	3	**23,224**	9

In the first six months of 2012, Pine Cliff raised $2,885,000 (net of share issue costs) through a rights offering and a private placement, set up a revolving demand credit facility and obtained $7,000,000 in short-term financing from a related party. The existing banking arrangements at June 30, 2012 are comprised of a revolving demand credit facility in the amount of $15,000,000, of which $12,096,000 is drawn at June 30, 2012. The current revolving period will end on May 31, 2013 and if the revolving demand credit facility is not renewed it will become payable in full on demand. Funds flow from operations and the unused portion of the credit facility will allow Pine Cliff to meet its short-term financial liabilities, as well as future capital requirements, at a reasonable cost. The Company believes it has sufficient funding and access to capital to meet its obligations as they come due and, if required, will consider additional short-term financing or issuing equity in order to meet its future liabilities.

Working capital is calculated as current assets minus current liabilities and represents the ability of a Company to satisfy both maturing short-term debt and upcoming operational expenses. The capital intensive nature of the oil and gas business may result in working capital deficiencies from time to time. Pine Cliff manages its working capital ratio to ensure that it has sufficient unused funds under its credit facility and access to capital to accommodate such circumstances. Additionally, the revolving demand credit facility requires Pine Cliff to maintain a working capital ratio, excluding both the related party note payable and the current portion of bank debt and inclusive of unused funds under the credit facility, of greater than 1:1. The Company was in compliance with its bank debt covenants during the period ended June 30, 2012 and will take steps to ensure that it remains in compliance with its covenants in future periods. As at June 30, 2012, the Company had a working capital deficiency of $19,453,000 (December 31, 2011 – working capital of $482,000), mainly as a result of the related party note payable of $7,000,000 and revolving demand credit facility of $12,096,000 being considered current liabilities. It is Pine Cliff's intention to repay the related party note payable in the short-term, however, the Company notified the Related Party on August 1, 2012 that it would be exercising its option to extend the repayment date of the related party note payable until August 31, 2013 under the same terms and conditions.

COMMITMENTS AND CONTINGENCIES

In the normal course of business, Pine Cliff has entered into arrangements and incurred obligations that will impact the Company's future operations and liquidity. The maturity dates of the Company's commitments are as follows:

($000s)	Total	< 6 months	6 - 12 months	> 12 months
Trade and other payables	1,833	1,833	-	-
Related party note payable - principal [1]	7,000	-	-	7,000
Related party note payable - future interest	408	175	175	58
Bank loan - principal	12,096	-	12,096	-
Bank loan - future interest	416	227	189	-
	21,753	2,235	12,460	7,058

[1] Subsequent to June 30, 2012, the related party note payable was renewed until August 31, 2013.

Upon disposal of the South American properties in 2010, the Company received a contingent consideration whereby Pine Cliff will be entitled to $200,000 (payable in cash or shares from the purchaser corporation) if by September 24, 2012 the purchaser, or an affiliate to the purchaser, is successful in obtaining a drilling permit followed by the drilling of a well on the Laguna de Piedra concession block in the Rio Negro Province of Argentina or the local permitting authority in the province grants a concession to substitute for the Laguna de Piedra concession and the purchaser or affiliate entity drills a well on the substitute concession. The purchaser has announced they plan to drill on the concession in the second half of 2012. However, collection of this receivable is not determinable at this time and therefore has not been recorded by the Company.

ACCOUNTING POLICY CHANGES

Changes to accounting estimate – property and equipment
On January 1, 2012, the Company prospectively began depleting all of its oil and gas properties and facilities and its decommissioning asset using the Proved plus Probable Method; a change from the Proved Developed Method for oil and gas properties and the straight-line method for production facilities. The change of estimate was due to the Proved plus Probable Method providing a better reflection of the estimated service life of the related assets. For the first six months of 2012, the Company recorded $900,000 less depletion and depreciation under the Proved plus Probable Method, as compared to what would have been recorded using the Proved Developed Method. The Company believes it is not practical to estimate the effect on depletion and depreciation expense for future periods.

New accounting policy – finance income and expense
Finance expenses are comprised of interest expenses and bank charges on borrowings and the unwinding of the discount on provisions. Interest expenses and bank charges are considered operating expenses on the statement of cash flows. Borrowing costs incurred for the construction of qualifying assets are capitalized during the period of time that is required to complete and prepare the assets for their intended use or sale. Qualifying assets are those assets that necessarily take a substantial period of time to get ready for their intended use. All other borrowing costs are recognized in profit or loss. The capitalization rate used to determine the amount of borrowing costs to be capitalized is the weighted average interest rate applicable to the Company's outstanding borrowings during the period.

Interest income is recognized as the interest accrues, using the effective interest method. The effective interest method uses the rate that discounts estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset.

NON-IFRS MEASURES

This MD&A uses the terms "funds flow from operations", "operating netbacks" and "net debt" which are not recognized under IFRS and may not be comparable to similar measures presented by other companies. The Company uses these measures to evaluate its performance, leverage and liquidity, as well as to assess potential acquisitions.

The Company considers funds flow from operations a key performance measure as it demonstrates the Company's ability to generate the funds necessary to repay debt and fund future growth through capital investment. Funds flow from operations and funds flow from operations per share should not be considered as an alternative to, or more meaningful than, cash flow from operating activities as per the statement of cash flows which is considered the most directly comparable measure under IFRS. Funds flow from operations is calculated as cash flow from operating activities before changes in non-cash working capital and changes in interest payable. Funds flow from operations per share is calculated using the same weighted average number of shares outstanding as in the case of the earnings per share calculation for a reporting period.

	Three months ended June 30		Six months ended June 30	
	2012	2011	**2012**	2011
($000s)				
Cash flow from operating activities	**1,198**	69	**867**	217
Less:				
Change in non-cash working capital	**685**	(34)	**344**	1
Change in interest payable	**(7)**	-	**38**	-
Funds flow from operations	**520**	103	**485**	216

The Company considers operating netback to be a key indicator of profitability relative to current commodity prices. Operating netback and operating netback per boe are calculated as oil and gas sales, less royalties and operating expenses on an absolute and a per boe basis, respectively.

Net debt is a term used in the context of liquidity in this MD&A. Net debt is the total of bank debt, related party note payable and trade and other payables, less trade and other receivables and cash. There is no IFRS measure that is reasonably comparable to net debt.

FORWARD-LOOKING INFORMATION

Certain statements contained in this MD&A include statements which contain words such as "anticipate", "could", "should", "expect", "seek", "may", "intend", "likely", "will", "believe" and similar expressions, statements relating to matters that are not historical facts, and such statements of our beliefs, intentions and expectations about development, results and events which will or may occur in the future, constitute "forward-looking information" within the meaning of applicable Canadian securities legislation and are based on certain assumptions and analysis made by us derived from our experience and perceptions. Forward-looking information in this MD&A includes, but is not limited to: expected cash provided by operations; future capital expenditures, including the amount and nature thereof; oil and natural gas prices and demand; expansion and other development trends of the oil and natural gas industry; business strategy and outlook; expansion and growth of our business and operations; maintenance of existing customer, supplier and partner relationships; supply channels; accounting policies; credit risks; and other such matters.

All such forward-looking information is based on certain assumptions and analyses made by us in light of our experience and perception of historical trends, current conditions and expected future developments, as well as other factors we believe are appropriate in the circumstances. The risks, uncertainties, and assumptions are difficult to predict and may affect operations, and may include, without limitation: foreign exchange fluctuations; equipment and labour shortages and inflationary costs; general economic conditions; industry conditions; changes in applicable environmental, taxation and other laws and regulations as well as how such laws and regulations are interpreted and enforced; the ability of oil and natural gas companies to raise capital; the effect of weather conditions on operations and facilities; the existence of operating risks; volatility of oil and natural gas prices; oil and gas product supply and demand; risks inherent in the ability to generate sufficient cash flow from operations to meet current and future obligations; increased competition; stock market volatility; opportunities available to or pursued by us; and other factors, many of which are beyond our control. The foregoing factors are not exhaustive.

Actual results, performance or achievements could differ materially from those expressed in, or implied by, this forward-looking information and, accordingly, no assurance can be given that any of the events anticipated by the forward-looking information will transpire or occur, or if any of them do, what benefits will be derived there from. Except as required by law, Pine Cliff disclaims any intention or obligation to update or revise any forward-looking information, whether as a result of new information, future events or otherwise.

The forward-looking information contained in this MD&A is expressly qualified by this cautionary statement.

The information provided in this report, including the financial statements, is the responsibility of management. In the preparation of these statements, estimates are sometimes necessary to make a determination of future values for certain assets or liabilities. Management believes such estimates have been based on careful judgments and have been properly reflected in the accompanying financial statements.

Management maintains a system of internal controls to provide reasonable assurance that the Company's assets are safeguarded and to facilitate the preparation of relevant and timely information.

The audit committee has reviewed these financial statements with management and has reported to the Board of Directors. The Board of Directors have approved the financial statements as presented in this interim report.

CONDENSED STATEMENTS OF FINANCIAL POSITION
(Canadian dollars, 000s)
(unaudited)

	Note	**As at June 30, 2012**	As at December 31, 2011
ASSETS			
Current assets			
Cash		**-**	277
Trade and other receivables		**1,316**	109
Prepaid expenses and deposits		**75**	23
Investment		**85**	172
		1,476	581
Exploration and evaluation assets	4	**598**	-
Property and equipment	5	**25,318**	1,806
Deferred taxes	6	**1,639**	-
Total assets		**29,031**	2,387
LIABILITIES			
Current liabilities			
Trade and other payables		**1,833**	99
Related party note payable	7	**7,000**	-
Bank debt	8	**12,096**	-
		20,929	99
Decommissioning liabilities		**2,511**	82
Total liabilities		**23,440**	181
SHAREHOLDERS' EQUITY			
Share capital	9	**17,704**	14,819
Contributed surplus		**1,079**	766
Accumulated other comprehensive loss		**(213)**	(137)
Deficit		**(12,979)**	(13,242)
Total shareholders' equity		**5,591**	2,206
Total liabilities and shareholders' equity		**29,031**	2,387

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

CONDENSED STATEMENTS OF EARNINGS (LOSS)
(Canadian dollars, 000s except per share data)
(unaudited)

	Note	Three months ended June 30		Six months ended June 30	
		2012	2011	**2012**	2011
Oil and gas sales		**2,130**	236	**3,031**	482
Royalties		**(395)**	(6)	**(546)**	(21)
REVENUE		**1,735**	230	**2,485**	461
EXPENSES					
Operating		**695**	67	**966**	135
General and administration		**317**	60	**724**	110
Depletion and depreciation	5	**853**	145	**1,201**	299
Share-based payments	9	**186**	-	**313**	-
Finance expenses	10	**213**	1	**326**	2
Total expenses		**2,264**	273	**3,530**	546
Loss before income taxes		**(529)**	(43)	**(1,045)**	(85)
Deferred tax expense (recovery)	6	**(79)**	10	**(1,308)**	1
EARNINGS (LOSS) FOR THE PERIOD		**(450)**	(53)	**263**	(86)
Earnings (loss) per share ($)	9				
Basic		**(0.01)**	(0.00)	**0.00**	(0.00)
Diluted		**(0.01)**	(0.00)	**0.00**	(0.00)

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

CONDENSED STATEMENTS OF COMPREHENSIVE EARNINGS (LOSS)
(Canadian dollars, 000s)
(unaudited)

	Note	Three months ended June 30		Six months ended June 30	
		2012	2011	**2012**	2011
Earnings (loss) for the period		**(450)**	(53)	**263**	(86)
OTHER COMPREHENSIVE EARNINGS					
Unrealized loss on investment		**(162)**	(71)	**(87)**	(5)
Deferred taxes on unrealized loss on investment		**21**	10	**11**	1
COMPREHENSIVE EARNINGS (LOSS) FOR THE PERIOD		**(591)**	(114)	**187**	(90)

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

CONDENSED STATEMENTS OF CASH FLOWS
(Canadian dollars, 000s)
(unaudited)

	Note	Three months ended June 30 **2012**	2011	Six months ended June 30 **2012**	2011
CASH PROVIDED BY (USED IN):					
OPERATING ACTIVITIES					
Earnings (loss) for the period		**(450)**	(53)	**263**	(86)
Items not affecting cash:					
Share-based payments		**186**	-	**313**	-
Depletion and depreciation		**853**	145	**1,201**	299
Finance expenses		**213**	1	**326**	2
Deferred tax expense (recovery)		**(79)**	10	**(1,308)**	1
Changes in non-cash working capital	11	**685**	(34)	**344**	1
Interest paid		**(210)**	-	**(272)**	-
Cash provided by operating activities		**1,198**	69	**867**	217
INVESTING ACTIVITIES					
Expenditures on property and equipment	5	**(172)**	(3)	**(525)**	(9)
Expenditures on exploration and evaluation assets	4	**-**	-	**(91)**	-
Acquisitions	3	**(90)**	-	**(22,608)**	-
Changes in non-cash working capital	11	**(253)**	(115)	**99**	(140)
Cash used in investing activities		**(515)**	(118)	**(23,125)**	(149)
FINANCING ACTIVITIES					
Issuance of common shares, net of share issue costs		**-**	-	**2,885**	-
Related party note payable	7	**-**	-	**7,000**	-
Bank debt	8	**(694)**	-	**12,096**	-
Cash provided by (used in) financing activities		**(694)**	-	**21,981**	-
Increase (decrease) in cash		**(11)**	(49)	**(277)**	68
Cash - beginning of period		**11**	225	**277**	108
CASH - END OF PERIOD		**-**	176	**-**	176

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

CONDENSED STATEMENTS OF CHANGES IN EQUITY
(Canadian dollars, 000s)
(unaudited)

	Note	Share capital	Contributed surplus	Accumulated other comprehensive loss	Deficit	Total equity
BALANCE AT JANUARY 1, 2011		14,819	766	-	(13,035)	2,550
Comprehensive loss for the period		-	-	(4)	(86)	(90)
BALANCE AT JUNE 30, 2011		**14,819**	**766**	**(4)**	**(13,121)**	**2,460**
Comprehensive loss for the period		-	-	(133)	(121)	(254)
BALANCE AT DECEMBER 31, 2011		14,819	766	(137)	(13,242)	2,206
Shares issued pursuant to a rights offering	9	1,961	-	-	-	1,961
Shares issued pursuant to a private placement	9	1,000	-	-	-	1,000
Share issue costs	9	(76)	-	-	-	(76)
Comprehensive earnings (loss) for the period		-	-	(76)	263	187
Share-based payments	9	-	313	-	-	313
BALANCE AT JUNE 30, 2012		**17,704**	**1,079**	**(213)**	**(12,979)**	**5,591**

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

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS
As at June 30, 2012 and December 31, 2011 and for the three and six month periods ended June 30, 2012 and 2011 (unaudited)
(all tabular amounts in Canadian dollars 000s, unless otherwise indicated)

1. NATURE OF BUSINESS

Pine Cliff Energy Ltd. ("Pine Cliff" or the "Company") is a public company listed on the TSX Venture Exchange and incorporated under the Business Corporations Act (Alberta). The address of the Company's registered office is Suite 901, 1015 4th Street SW, Calgary, Alberta, T2R 1J4.

Pine Cliff is engaged in the exploration for, and development and production of, oil and natural gas in the Western Canadian Sedimentary Basin and conducts many of its activities jointly with others; these condensed interim financial statements (the "financial statements") reflect only the Company's proportionate interest in such activities.

2. BASIS OF PREPARATION

a) Statement of Compliance
The financial statements have been prepared in accordance with IAS 34 – *Interim Financial Reporting* using accounting policies consistent with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board.

The accounting policies and method of computation followed in the preparation of the financial statements are the same as those followed in the preparation of Pine Cliff's annual consolidated financial statements for the year ended December 31, 2011, except as described below. The financial statements do not include all of the information required for annual financial statements and should be read in conjunction with the Company's annual consolidated financial statements for the year ended December 31, 2011.

These financial statements were authorized for issue by the Company's Board of Directors on August 14, 2012.

b) Changes to Accounting Estimate
Property and equipment
On January 1, 2012, the Company prospectively began depleting all of its oil and gas properties and facilities and its decommissioning asset using the unit-of-production method over their proved plus probable reserve life ("Proved plus Probable Method"); a change from the unit–of-production method over their proved developed reserve life ("Proved Developed Method") for oil and gas properties and the straight-line method for production facilities. The change of estimate was due to the Proved plus Probable Method providing a better reflection of the estimated service life of the related assets. For the first six months of 2012, the Company recorded $900,000 less depletion and depreciation under the Proved plus Probable Method, as compared to what would have been recorded using the Proved Developed Method. The Company believes it is not practical to estimate the effect on depletion and depreciation expense for future periods.

c) New Accounting Policy
Finance income and expense
Finance expenses are comprised of interest expenses and bank charges on borrowings and the unwinding of the discount on provisions. Interest expenses and bank charges are considered operating expenses on the statement of cash flows. Borrowing costs incurred for the construction of qualifying assets are capitalized during the period of time that is required to complete and prepare the assets for their intended use or sale. Qualifying assets are those assets that necessarily take a substantial period of time to get ready for their intended use. All other borrowing costs are recognized in profit or loss. The capitalization rate used to determine the amount of borrowing costs to be capitalized is the weighted average interest rate applicable to the Company's outstanding borrowings during the period.

Interest income is recognized as the interest accrues, using the effective interest method. The effective interest method uses the rate that discounts estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset.

3. ACQUISITION

Carrot Creek Assets
On March 1, 2012, Pine Cliff acquired certain oil and natural gas assets in the Carrot Creek area of Alberta (the "Carrot Creek Assets") for cash consideration of $22,608,000. The results of the Carrot Creek Assets have been included in the financial statements since that date. The Carrot Creek Assets contributed oil and gas sales, net of royalties, of $2,289,000 and operating expenses of $850,000 for the period from March 1, 2012 to June 30, 2012. If the acquisition had occurred on January 1, 2012, total oil and gas sales, net of royalties, would have been approximately $3,978,000 and total operating expenses would have been

approximately $1,529,000 for the six months ended June 30, 2012. Pine Cliff does not believe it is practical to estimate the effect on future periods.

The acquisition has been accounted for using the acquisition method, and the purchase price was allocated to the assets acquired and the liabilities assumed as follows:

Net assets acquired:	
Property and equipment	23,956
Exploration and evaluation assets	507
Decommissioning provision	(2,182)
Working capital	26
Deferred income tax asset	301
Total net assets acquired	22,608

Consideration:	
Cash	22,608
Total purchase price	22,608

4. EXPLORATION AND EVALUATION ASSETS

The following table reconciles Pine Cliff's exploration and evaluation assets:

Cost:	
Balance at December 31, 2011	-
Additions	91
Acquisitions	507
Balance at June 30, 2012	**598**

5. PROPERTY AND EQUIPMENT

The following table reconciles Pine Cliff's property and equipment assets:

Cost:	Oil and gas properties	Office equipment	Total
Balance at December 31, 2011	4,600	2	4,602
Additions	755	2	757
Acquisitions	23,956	-	23,956
Balance at June 30, 2012	**29,311**	**4**	**29,315**

Accumulated depletion and depreciation:	Oil and gas properties	Office equipment	Total
Balance at December 31, 2011	(2,796)	-	(2,796)
Depletion and depreciation for the period	(1,201)	-	(1,201)
Balance at June 30, 2012	**(3,997)**	**-**	**(3,997)**

Carrying value at:	Oil and gas properties	Office equipment	Total
December 31, 2011	1,804	2	1,806
June 30, 2012	**25,314**	**4**	**25,318**

Impairment
The impairment of property and equipment assets and any subsequent reversal of such impairment losses are recognized in the statement of earnings (loss). There were no impairment losses or reversals recorded in the statement of earnings (loss) for the three or six months ended June 30, 2012 and 2011.

6. DEFERRED TAXES

The Company has recorded a deferred tax asset related to the benefit of tax pools, as it is probable that they will be recovered.

	June 30, 2012	December 31, 2011
Deferred income tax assets (liabilities):		
Share issue costs	**18**	-
Investment	**30**	20
Decommissioning provision	**627**	20
Property and equipment	-	91
Capital loss carry forward	**100**	104
Non-capital losses carry forward	**1,607**	871
Unrecorded benefit of tax pools	**-**	(1,106)
Exploration and evaluation assets	**(150)**	-
Property, plant and equipment	**(593)**	-
Net deferred income tax asset	**1,639**	-

Deferred income tax recovery varies from the amount that would be computed by applying federal and provincial income tax rates as follows:

	Six months ended June 30	
	2012	2011
Loss before income taxes	**(1,045)**	(85)
Corporate income tax rate	**25.0%**	26.5%
Computed income tax recovery	**(261)**	(23)
Increase (decrease) resulting from:		
Non-deductible compensation expense	**78**	-
Changes in the unrecorded benefit of tax pools	**(1,106)**	20
Changes in tax rates and other	**(19)**	4
Deferred income tax expense (recovery)	**(1,308)**	1

Pine Cliff has approximately $30,182,000 in tax pools at June 30, 2012 (December 31, 2011 – $6,483,000) available for future use as deductions from taxable income. Included in these pools are estimated non-capital loss carry forwards of $4,491,000 (December 31, 2011 – $3,483,000) that expire between the years 2026 and 2032.

7. TRANSACTIONS WITH RELATED PARTIES

Related party note payable

On February 28, 2012, the Company's Executive Chairman of the Board and major shareholder loaned the Company $7,000,000. The promissory note bears interest at 5% per annum and is repayable on August 31, 2012 or at any time prior to that without penalty. Security under the promissory note is over all of the Company's assets and is subordinated to any and all claims in favour of the lender providing a credit facility to the Company. As at June 30, 2012, the full amount of the promissory note was outstanding (December 31, 2011 – nil). Interest paid on this note during the three and six months ended June 30, 2012 was $87,000 and $119,000, respectively (June 30, 2011 – nil).

The Company has the option to extend the repayment date of the promissory note up to one year from August 31, 2012 under the same terms and conditions (See Note 13).

Management services agreement

Pine Cliff has a management services agreement with Bonterra Energy Corp. ("Bonterra"), an oil and gas corporation that is publicly traded on the Toronto Stock Exchange with some common directors and management, to provide executive services, technical services, accounting services, oil and gas administration and office administration for Pine Cliff. Total fees for the three and six months ended June 30, 2012 and 2011 were $15,000 and $30,000, respectively, plus minimal administrative costs. The management services agreement may be cancelled by either party with 90 days notice. As at June 30, 2012, Pine Cliff owed Bonterra $2,800 (December 31, 2011 – $3,800).

Other
Geomark Exploration Ltd. ("Geomark") is a publicly traded company listed on the TSX-Venture with some common directors at June 30, 2012 and some common management with Pine Cliff. As at June 30, 2012, Geomark owns 432,812 common shares of Pine Cliff (December 31, 2011 – 346,250), which represents less than one percent of the total issued and outstanding common shares of Pine Cliff. There were no other transactions between Pine Cliff and Geomark for the periods ended June 30, 2012 and December 31, 2011.

Related party transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of the consideration established and agreed to by the related parties.

8. BANK DEBT

On March 1, 2012, Pine Cliff set up a $15,000,000 revolving demand credit facility with a Canadian chartered bank, of which $12,096,000 is drawn at June 30, 2012. The revolving demand credit facility is considered a current liability at June 30, 2012 as the current revolving period will end on May 31, 2013 and if the revolving demand credit facility is not renewed it will become payable in full on demand. Amounts drawn under this facility are in the form of Canadian prime lending rate based loans, guaranteed notes or letters of credit. The facility bears interest at the prime lending rate plus 0.75% per annum. Pine Cliff realized an effective interest rate of 3.75% for the six months ended June 30, 2012. The facility is secured by a first priority security interest on all present and after acquired property of the Company.

The revolving demand credit facility requires Pine Cliff to maintain a working capital ratio, excluding the related party note payable and the current portion of the bank debt and inclusive of unused funds under the credit facility, of greater than 1:1. The Company was in compliance with its bank debt covenants during the period ended June 30, 2012.

9. SHARE CAPITAL

Authorized
The Company is authorized to issue an unlimited number of Common Shares without nominal or par value. The Company is also authorized to issue, in one or more series, an unlimited number of Class B Preferred Shares without nominal or par value.

Issued

Issued and outstanding share capital continuity:	Common shares (000s)	Share capital
Balance at December 31, 2011	46,146	14,819
Shares issued pursuant to a rights offering	11,536	1,961
Shares issued pursuant to a private placement	5,882	1,000
Share issue costs	-	(76)
Balance at June 30, 2012	**63,564**	**17,704**

The shares issued pursuant to a private placement in the six months ended June 30, 2012 were issued to the President and Chief Executive Officer and his associates.

The average market value of the Company's shares for the purposes of calculating the dilutive effect of share options was based on quoted market prices for the period that the options were outstanding. In calculating the weighted average number of diluted shares outstanding for the six months ended June 30, 2012, the Company excluded 345,000 options, as their effect is anti-dilutive. For the three months ended June 30, 2012 and the three and six month periods ended June 30, 2011, all options were excluded as there was a loss in the periods then ended.

Loss per share calculation:	Three months ended June 30 **2012**	2011	Six months ended June 30 **2012**	2011
Numerator				
Earnings (loss) for the period	**(450)**	(53)	**263**	(86)
Denominator (000s)				
Weighted-average common shares outstanding - basic	**63,564**	46,146	**60,406**	46,146
Effect of options outstanding	**-**	-	**1,743**	-
Weighted-average common shares outstanding - diluted	**63,564**	46,146	**62,149**	46,146
Earnings (loss) per share - basic ($)	**(0.01)**	(0.00)	**0.00**	(0.00)
Earnings (loss) per share - diluted ($)	**(0.01)**	(0.00)	**0.00**	(0.00)

Share-based payments

The Company provides an equity settled stock option plan (the "Option Plan") for its directors, employees and consultants. Under the Option Plan, the Company may grant options for up to 10% of outstanding common shares at June 30, 2012 (December 31, 2011 – fixed amount of 4,527,569). The term and vesting period of the options granted are determined at the discretion of the Board of Directors. The exercise price of each option granted equals the market price of the Company's stock based on the market price immediately preceding the date of grant and the option's maximum term is five years.

A summary of the status of the Company's stock option plan as at June 30, 2012 and changes during the six month period then ended is presented as follows:

Stock options issued and outstanding:	Options (000s)	Weighted-average exercise price ($ per share)
Outstanding at December 31, 2011	-	-
Granted	3,575	0.42
Forfeited	(110)	0.38
Outstanding at June 30, 2012	**3,465**	**0.42**
Exercisable at June 30, 2012	**-**	**-**

The following table summarizes information about stock options outstanding at June 30, 2012:

Exercise price:	Stock options outstanding (000s)	Weighted-average remaining term (years)	Stock options exercisable (000s)	Weighted-average remaining term (years)
$0.38	2,865	3.6	-	-
$0.50	255	3.5	-	-
$0.67 - $0.68	345	3.0	-	-
	3,465	3.6	-	-

The Company records share-based payment expense over the vesting period, which ranges between one to three years, based on the fair value of the options granted to employees, directors and consultants. In the six months ended June 30, 2012, the Company granted 3,575,000 stock options with an estimated fair value of $1,251,000 or $0.35 per option using the Black-Scholes option pricing model with the following key assumptions (weighted-average):

Assumptions:	Six months ended June 30, 2012
Exercise price ($)	0.42
Estimated volatility of underlying common shares (%)	128
Weighted average expected life (years)	3.9
Risk-free rate (%)	1.2
Forfeiture rate (%)	0.0
Expected dividend yield (%)	0.0

10. FINANCE EXPENSES

Finance expenses are comprised of:

Finance expenses:	Three months ended June 30 **2012**	2011	Six months ended June 30 **2012**	2011
Interest and bank charges	**203**	-	**310**	-
Unwinding of the discount on decommissioning liabilities	**10**	1	**16**	2
	213	1	**326**	2

11. SUPPLEMENTAL CASH FLOW INFORMATION

	Three months ended June 30 **2012**	2011	Six months ended June 30 **2012**	2011
Operating activities				
Changes in non-cash working capital:				
Trade and other receivables	**(273)**	(2)	**(1,208)**	66
Prepaid expenses and deposits	**(6)**	6	**(52)**	2
Trade and other payables and accrued liabilities	**964**	(38)	**1,604**	(67)
	685	(34)	**344**	1
Investing activities				
Changes in non-cash working capital:				
Trade and other receivables	**-**	6	**-**	11
Trade and other payables and accrued liabilities	**(253)**	(121)	**99**	(151)
	(253)	(115)	**99**	(140)

12. FINANCIAL INSTRUMENTS

Financial instruments and fair value measurement

Financial instruments of the Company consist of cash, trade and other receivables, investment, trade and other payables, related party note payable and bank debt. The carrying values of the financial instruments presented in the financial statements approximate their respective fair values.

The following table sets out the Company's classification, carrying value and fair value of financial assets and liabilities as at June 30, 2012 and December 31, 2011:

Description: [1]	Level	**June 30, 2012** **Carrying value**	**Fair value**	December 31, 2011 Carrying value	Fair value
Cash	1	**-**	**-**	277	277
Trade and other receivables		**1,316**	**1,316**	109	109
Investment	1	**85**	**85**	172	172
Trade and other payables		**(1,833)**	**(1,833)**	(99)	(99)
Related party note payable		**(7,000)**	**(7,000)**	-	-
Bank debt		**(12,096)**	**(12,096)**	-	-

[1] Cash is classified as fair-value through profit or loss. Trade and other receivables are classified as loans and receivables which are measured at amortized cost. The investment is classified as available-for-sale which is measured at fair value and any gains or losses are recognized in other comprehensive earnings (loss) in the period they occur. Trade and other payables, related party note payable and bank debt are classified as financial liabilities and are measured at amortized cost.

Commitments

The Company believes it has sufficient funding and access to capital to meet its obligations as they come due. The maturity dates of the Company's financial liabilities are as follows:

Maturity dates of financial liabilities	Recognized in Financial Statements	Total	< 6 months	6 - 12 months	> 12 months
Trade and other payables	Yes - Liability	1,833	1,833	-	-
Related party note payable - principal [1]	Yes - Liability	7,000	-	-	7,000
Related party note payable - future interest	No	408	175	175	58
Bank loan - principal	Yes - Liability	12,096	-	12,096	-
Bank loan - future interest	No	416	227	189	-
		21,753	2,235	12,460	7,058

[1] The related party note payable was renewed until August 31, 2013 subsequent to June 30, 2012. See Note 13.

13. SUBSEQUENT EVENT

On August 1, 2012, the Company notified the related party that it would be exercising its option to extend the promissory note until August 31, 2013.

BOARD OF DIRECTORS

Gary J. Drummond
George F. Fink
Philip B. Hodge
Randy M. Jarock
Carl R. Jonsson
F. William Woodward

OFFICERS

George F. Fink
Executive Chairman of the Board

Philip B. Hodge
President and Chief Executive Officer

Robb D. Thompson
Chief Financial Officer and Secretary

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REGISTRAR AND TRANSFER AGENT

Olympia Trust Company
Calgary, Alberta

AUDITORS

Deloitte & Touche LLP
Calgary, Alberta

SOLICITORS

Borden Ladner Gervais LLP
Calgary, Alberta

BANKERS

Alberta Treasury Branch
Calgary, Alberta

STOCK EXCHANGE LISTING

TSX Venture Exchange
Trading Symbol: PNE

WEBSITE

www.pinecliffenergy.com