

**PROBE RESOURCES LTD.**  
MANAGEMENT DISCUSSION AND ANALYSIS  
As of May 31, 2010

This Management Discussion and Analysis was prepared on July 14, 2010.

INDEX	<u>Page</u>
Forward Looking Statements	1
Description of Business	3
Financial Results	7
Financings, Principal Purposes and Milestones	8
Related Party Transactions	11
Liquidity and Solvency	12
Accounting Changes	13
Risks	13
Critical Accounting Estimates	14
Disclosure of Outstanding Share Data	15

This Management Discussion and Analysis (the “MD&A”) should be read in conjunction with the unaudited consolidated financial statements for the nine months ended May 31, 2010 and the year ended August 31, 2009. Natural gas equivalent (“Mcf”) amounts have been calculated using a conversion rate of six thousand cubic feet of natural gas to one barrel of oil (“6:1”) unless otherwise stated. Unless otherwise indicated, the terms “Probe Resources Ltd.,” “Probe” and the “Company” are used interchangeably in this MD&A to refer to Probe Resources Ltd. and its subsidiaries.

The unaudited consolidated financial statements and financial data contained in the MD&A have been prepared in accordance with Canadian generally accepted accounting principles (“Canadian GAAP”) in Canadian currency.

*Forward-Looking Statements*

Certain statements contained in this MD&A may constitute forward-looking statements. These statements relate to future events or the Company's future performance. All statements other than statements of historical fact may be forward-looking statements. Forward-looking statements are often, but not always, identified by the use of words such as “seek”, “anticipate”, “plan”, “continue”, “estimate”, “expect”, “may”, “will”, “project”, “predict”, “potential”, “targeting”, “intend”, “could”, “might”, “should”, “believe” and similar expressions. These statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements. Management believes that the expectations reflected in these forward-looking statements are reasonable but no assurance can be given that these expectations will prove to be correct and such forward-looking statements included in this MD&A should not be unduly relied upon by investors. These statements speak only as of the date of this MD&A and are expressly qualified, in their entirety, by this cautionary statement.

*In particular, this MD&A contains forward-looking statements pertaining to the following:*

- i. capital expenditure programs;
- ii. treatment under governmental regulatory and taxation regimes; and

**PROBE RESOURCES LTD.**  
MANAGEMENT DISCUSSION AND ANALYSIS  
As of May 31, 2010

iii. expectations regarding the Company's ability to raise capital and to continually add to reserves through development.

*With respect to forward-looking statements contained in this MD&A, the Company has made assumptions regarding, among other things:*

iv. the Company's ability to obtain additional financing on satisfactory terms.

*The Company's actual results could differ materially from those anticipated in these forward-looking statements as a result of the risk factors set forth below and elsewhere in this MD&A:*

v. geological, technical, drilling and processing problems;

vi. liabilities and risks, including environmental liabilities and risks, inherent in oil and natural gas operations;

vii. incorrect assessments of the value of acquisitions;

viii. competition for, among other things, capital, acquisitions of reserves, undeveloped lands and skilled personnel; and

ix. the other factors referred to under "Risk Factors".

***The forward-looking statements or information contained in this MD&A are made as of July 14, 2010 and the Company undertakes no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, unless required by applicable securities laws.***

Success in the junior oil and gas sector is measured by a Company's ability to raise funds and the ability to secure properties of merit. Not all of these factors are within management's control. The ability to raise funds is in part dependent on the state of the junior resource stock market, which in turn is dependent on the economic climate, oil and gas prices and perceptions as to which way the market is headed. The ability to secure properties of merit is in large part dependent on management's contacts and the vitality of the sector.

The financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the payment of liabilities in the ordinary course of business. Should the Company be unable to continue as a going concern, it may be unable to realize the carrying value of its assets and to meet its liabilities as they become due.

The Company's ability to continue as a going concern is dependent upon its ability to discover economically recoverable reserves, to bring such reserves into production and attain profitable operations, and to obtain financing sufficient to meet current and future obligations. The financial statements do not reflect the adjustments or reclassification of assets and liabilities which would be necessary if the Company were unable to continue its operations.

The Company is still in the development stage and will require additional capital in the form of debt or equity to continue to execute its business plans.

**PROBE RESOURCES LTD.**  
MANAGEMENT DISCUSSION AND ANALYSIS  
As of May 31, 2010

*Directors and Senior Officers*

Board of Directors

L. Scott Broussard	Chairman and Member of the Reserves Committee
Richard Buski	Chair of the Audit Committee (Independent)
Desmond Balakrishnan	Member of the Audit Committee (Independent)
Bradley Culver	Chair of the Reserves Committee and member of the Audit Committee (Independent)

Senior Officers

L. Scott Broussard	Chief Executive Officer / President / Chairman of the Board
William N. Young III	Chief Operating Officer
Richard FitzGerald	Chief Financial Officer
Roger B. Souders	Vice President, Land
Andre J. Broussard	Vice President, Exploration
Morgan Tincher	Vice President, Finance and Corporate Secretary
Paul A. Diven	Controller
Dan Bomersbach	Operations Manager

*Description of Business*

Probe Resources Ltd. is a public company listed and publicly traded on the TSX Venture Exchange and was incorporated under the British Columbia Business Corporations Act on November 15, 1988. At May 31, 2010, the Company was in the development stage as an oil and natural gas company, owning interests in three oil and natural gas producing properties as well as interests in seven federal oil and natural gas blocks located in the United States Gulf of Mexico.

The management of the Company actively seeks investment and/or joint venture opportunities that are attractive and create long term value for its shareholders.

*Discussion of Gulf of Mexico Operations*

Agreements to Purchase Oil and Gas Rights

On May 22, 2008, the Company's wholly-owned subsidiary Probe Resources US Ltd. ("Probe US") announced it has entered into an agreement (the "Agreement in Principle") with certain arm's length parties (the "Vendors") to purchase 75% working interest rights associated with approximately 26,500 acres on six Federal oil and natural gas lease blocks located in the United States Gulf of Mexico (collectively, the "Concessions"). After completion of the Cutter Transaction, as described below, the Company became the Operator of the Concessions on a 100% working interest basis.

On June 6, 2008, the Company agreed to acquire the remaining 25% working interest rights from Cutter Energy on the Concessions noted above (the "Cutter Transaction"). Cutter Energy is owned by Scott Broussard (President, CEO, and Chairman of Probe) and the acquisition is, therefore, considered to be a non-arm's-length transaction. Total consideration for the Cutter interest rights

**PROBE RESOURCES LTD.**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
As of May 31, 2010

is US\$829,594 cash, and the issue of up to 4,000,000 Common Shares. The Company issued 2,000,000 Common Shares upon closing of the transaction and 666,667 Common shares on March 3, 2009 upon completion of the South Timbalier 214 well. The Company will issue to Cutter the remaining 1,333,333 Common Shares, 666,666 common shares for each occurrence of up to two additional successful wells at distinct leases within 24 months from the date of the agreement. Two wells completed in February 2010 in the East Cameron properties resulted in the issuance of the shares during April 2010.

Pursuant to the terms of the Agreements, the Vendors along with Cutter have delivered to Probe US not less than a 69.5% net revenue interest in each of the Concessions. Probe US paid an aggregate amount of US\$4,250,000 as consideration to the Vendors and US\$829,524 and issued 2,000,000 common shares valued at \$0.50 per share to Cutter. The Agreement provides Probe US the opportunity to conduct a drilling program on the Concessions.

Projects

- A. **High Island 115** – On September 13, 2008, the well’s platform, export line, host platform at High Island 71 and the onshore facilities were all damaged in varying degrees by Hurricane Ike. Production resumed in early 2009 at an average production rate of approximately 7 Million Cubic Feet per Day (“MMcfd”). On July 31, 2009 production again ceased due to the expiration of the lease underlying the High Island 71 host processing facility, as well as the expiration of the “Production Handling Agreement” with the host. The resumption of production at the existing High Island 115 facility entails the reduction of Probe’s interest as consideration for the required construction project. The project included the replacement of the deck on the High Island 115 platform with a processing facility and relocation of the export pipeline which eliminates the need for a separate host platform. Additionally, Probe’s indebtedness of approximately \$860,000 was released as consideration by the project contractor who is a party to the Debt Restructuring Agreement. The well is expected to resume production in July 2010 at an anticipated flow rate of 7-10 MMcfd. Probe is non-operator of the field. Upon resumption of production, Probe will own a 27.50% Working Interest (“WI”) and 22.06% Net Revenue Interest (“NRI”) in the High Island Well.
- B. **South Timbalier 214** – On January 5, 2009 the Company announced the discovery of commercial reserves in the South Timbalier A-6 Sidetrack # 1 well. The well was drilled to 15,825’ measured depth and 14,751’ true vertical depth from a Company owned production platform in the adjacent block which is connected to the NYMEX premium market via a ready for service export pipeline. On January 30, 2009, production commenced from the well. The well is currently producing approximately 3.0 MMcfd and 30 barrels of condensate per day (“BCPD”) and has produced approximately 10.3 billion cubic feet (“BCF”) of gas and 114,000 barrels of condensate to date. The Company holds a 100% WI and 68.5% NRI prior to project payout (“BPPO”) and an 80% WI and 57.7% NRI after project payout (“APPO”).
- C. **East Cameron 36** – On August 25, 2008 the Company announced the discovery of commercial reserves in multiple horizons at its EC 36 A-1 well. The well was spud on August 5, 2008 and was drilled under budget to a total depth of 10,450 feet. Production casing was installed in the well, a caisson was over-driven, and a caisson deck was installed. The well completion was suspended pending financing of the completion costs.

**PROBE RESOURCES LTD.**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
As of May 31, 2010

On April 29, 2009 the Company announced it had entered into a joint venture with Petrodome Energy, LLC and certain other parties for the drilling of its East Cameron 37 prospect. The prospect is adjacent to and was drilled from the same surface location as the East Cameron 36 discovery. The terms of the joint venture consist of the proportionate reimbursement of the Company's sunk costs in the EC 36 A-1 well including prospect acquisition fees, drilling costs and development costs, as well as the joint venture partners' proportionate contribution of well drill out costs and future development costs.

The test separator deck was installed on the East Cameron 37 caisson on November 14, 2009. A 6" pipeline was installed and tested from the caisson platform to a host platform leased by the Company in Vermilion Block 22. New production facilities were installed and tested on the host platform. A completion rig was moved over the East Cameron 37 caisson deck and the EC 36 A-1 well was successfully completed as a single selective gravel-packed completion in the M7 and M8 Sands on December 24, 2009. The M7 and M8 Sands were cleaned up and flow-tested, ultimately achieving water-free production starting in February 2010 and currently producing 5.5 MMcfd with a condensate rate of 50 BCPD and flowing tubing pressure of 2800 psi. The Company retains a 52% WI and 35.62 NRI BPPO and a 41.6% WI and 30% NRI APPO in the EC 36 A-1 well. The project area consists of East Cameron 36, East Cameron 37, and Vermilion 20 blocks. Probe continues as operator of the project area.

- D. **East Cameron 37** - On June 2, 2009 the Company announced the discovery of commercial gas reserves in its EC 37 A-2 well. The well was spud on May 8, 2009 and directionally drilled under turnkey contract to a total depth of 12,039 feet. Upon completion of drilling activities, production casing was run and the well was suspended pending the financing of the completion costs.

On November 16, 2009 the Company announced that it had secured the necessary funding and had commenced facilities work at East Cameron 37 and the Vermilion 22 host platform, including the construction of an export pipeline from East Cameron 37 to Vermilion 22, and the completion of the EC 37 A-2 well. The completion rig, having completed the EC 36 A-1 well, skidded to the EC 37 A-2 well. The well was successfully completed as a Frac-packed single completion in the Rob L Sand on January 12, 2010. The well was partially cleaned up while the completion rig was on the well. The rig was subsequently released.

The EC 37 A-2 well unexpectedly began producing water upon start-up. Production logs indicated water flow from a deeper, higher pressured horizon behind production casing. A lift boat was mobilized in April 2010 to the East Cameron 37 platform in order to facilitate the pumping of a water blocking treatment on the well. While subsequent production logs indicated a successful operation, the well continues to produce water. The current production rate is 40-50 cubic feet of natural gas per day and 60 barrels of water per day. Assuming no significant change in the current status, the Company plans to plug back to a shallower horizon in the fourth quarter of 2010 to increase production from the well. The well will ultimately be sidetracked to evaluate a deeper seismic amplitude. The Company holds a 52% WI and 35.36% NRI BPPO and a 41.6% WI and 29.79% NRI APPO in the lease.

- E. **East Cameron 246** – On October 30, 2008 the Company announced discovery of commercial reserves in its East Cameron 246 #2 well ("EC 246"). The Company encountered its primary

**PROBE RESOURCES LTD.**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
As of May 31, 2010

objective in the Lentic formation, logging approximately 45 feet of net pay. The expected gross production rate from this formation is 8-12 MMcfd. Upon completion of the drilling activities, production casing was run, and the well was suspended awaiting evaluation of development alternatives.

A letter of intent has been signed with another party to acquire a production platform currently in the Gulf of Mexico. The platform will be moved and installed over the EC 246 well in the fourth quarter of 2010. A pipeline will be laid to a gas transmission line a short distance away. The well will then be completed in the Lentic Sand described above.

The primary term of the East Cameron 246 lease has expired. The lease is currently being held by a Suspension of Operations (“SOP”) through October 31, 2010. The SOP requires certain milestones in order for Probe to retain the lease. Probe has complied with these milestones to date. The Company has farmed out a 10% WI in the lease in July 2010 to assist in financing the development. As a result of the farm out, the Company now holds a 90% WI and 61.65% NRI BPPO and a 72% WI and 51.93% NRI APPO in the lease.

- F. **South Timbalier 198** - In April 2009 Probe acquired the lease underlying its South Timbalier 198 platform. Probe’s geological evaluation indicated significant untapped reserve potential updip to a previously produced well. Subsequent to this evaluation, Probe engaged its independent reserve engineers to confirm the assessment of additional reserve potential. The independent engineering firm has estimated approximately 10 BCF as proved undeveloped reserves, 9 BCF as probable reserves with the potential for additional reserves in other categories. The foregoing approximations are estimates only based on the available technical data and are not contained in a compliant National Instrument 51-101 reserve report and therefore the foregoing should not be relied upon in making any investment decision. As part of its annual fiscal reporting requirement, Probe has engaged its independent engineering firm to complete a National Instrument 51-101 report with respect to the possible additional reserves which will be filed publicly as soon as such report is available. In addition to the risks with respect to the completion of the reserve report, Probe will require significant funding in order to develop any additional reserves. Probe is currently seeking a joint venture partner to facilitate the drilling and completion of a sidetrack of an existing well on the platform to develop these reserves. In the event that Probe is unsuccessful in attracting new financing, whether by debt or equity, no development will take place. Probe is operator and currently holds a 100% WI and 70% NRI in the lease.

Other Interests - Seismic Data

The Company incurred additional seismic data costs of \$791,784 (US\$672,143) during the fiscal year 2009. Total capitalized seismic data costs at May 31, 2010 were \$1,729,163 (US\$1,561,867).

*Independent Reserve Engineers*

As the Company continues to grow and add reserves, it was decided that it will be better served by retaining a globally recognized firm with a greater depth of experience to serve as its independent reserve engineers. Accordingly, the Company appointed Netherland, Sewell and Associates, Inc. on July 20, 2009 to serve as its independent reserve engineers.

**PROBE RESOURCES LTD.**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
As of May 31, 2010

*Selected Annual Information*

The following financial data are selected information for the Company for the three most recently completed financial years:

	Year ended August 31,		
	2009	2008	2007
Total revenues	\$ 23,918,542	\$ 5,110,861	\$ -
Loss before other items	\$(17,666,205)	\$(4,451,617)	\$(1,154,252)
Basic and diluted loss per share before other item	\$( 0.17)	\$( 0.10)	\$( 0.09)
Net loss	\$(21,626,330)	\$(4,076,271)	\$(1,084,602)
Basic and diluted loss per share	\$( 0.21)	\$( 0.09)	\$( 0.08)
Total assets	\$ 69,086,975	\$46,562,135	\$ 8,195,337
Total long-term liabilities	\$ 4,392,953	\$ 861,510	\$ 531,632
Cash dividends per share	\$ -	\$ -	\$ -

*Results of Operations*

The following table summarizes production volumes, average sales prices and operating revenues for the nine months ended May 31, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Production Volumes		
Oil (Bbl)	26,362	25,993
Natural gas (Mcf)	<u>2,950,246</u>	<u>2,424,521</u>
Natural gas (Mcf)	3,108,421	2,580,479
Natural gas (Mcf/day)	11,428	9,452
Average Sales Price		
Oil	\$74.83	\$52.00
Natural Gas	\$ 4.22	\$ 5.06
Operating Revenue		
Oil	\$ 1,972,614	\$ 1,351,672
Natural Gas	<u>12,442,105</u>	<u>12,265,064</u>
Total	<u>\$14,414,719</u>	<u>\$13,616,736</u>
Lease Operating Expense	\$ 1,334,095	\$ 1,114,991
Lease Operating Expense per Mcfe	\$ 0.43	\$ 0.43

*Summary of Quarterly Results*

The following is a summary of the Company's financial results for the eight most recently completed quarters:

	Q3 May 31 <u>2010</u>	Q2 Feb 28 <u>2010</u>	Q1 Nov 30 <u>2009</u>	Q4 Aug 31, <u>2009</u>	Q3 May 31 <u>2009</u>	Q2 Feb 28 <u>2009</u>	Q1 Nov 30 <u>2008</u>	Q4 Aug 31 <u>2008</u>
Total Revenues	\$2,253,799	\$5,082,117	\$7,078,803	\$10,301,806	\$9,780,116	\$3,764,341	\$72,279	\$1,859,556
Income (loss) before other items:								
Total	\$(4,588,404)	\$(3,030,570)	\$(6,305,769)	\$(14,401,715)	\$570,314	\$(2,184,713)	\$(1,645,389)	\$(2,552,427)
Per share	\$( 0.04)	\$( 0.03)	\$( 0.05)	\$( 0.14)	\$ 0.00	\$( 0.02)	\$( 0.01)	\$( 0.03)
Net Income (loss):								
Total	\$(4,504,963)	\$(2,890,978)	\$(5,256,569)	\$(21,307,717)	\$2,538,541	\$(1,866,819)	\$(990,335)	\$(2,090,181)
Per share	\$( 0.04)	\$( 0.03)	\$( 0.05)	\$( 0.20)	\$ 0.02	\$( 0.02)	\$( 0.01)	\$( 0.02)

**PROBE RESOURCES LTD.**  
MANAGEMENT DISCUSSION AND ANALYSIS  
As of May 31, 2010

*Discussion of Financial Results – May 31, 2010 compared to May 31, 2009*

The Company reported revenues of \$14,414,719 for the nine months ended May 31, 2010 as compared to reported revenues of \$13,616,736 for the nine months ended May 31, 2009. The increase in revenues between periods is primarily a result of higher overall production volumes in the current period from the South Timbalier 214 well (commenced production in February 2009) and the East Cameron properties (the EC 36 A-1 well commenced production in February 2010) offset partially by the High Island 115 well shut in since July, 2009 and overall lower overall natural gas prices between periods. For the previous year's period, the reported production volumes and revenue included the High Island 115 well which was producing for only a portion of the comparable period due to hurricane impacts in September 2008. While the High Island 115 well was back in production in early 2009, the production for the well has been temporarily suspended since July 2009 due to the expiration of the production handling agreement and therefore there have been no production volumes or revenue for the current year period. Operating expenses in the current year (\$2,986,837) increased from the previous year (\$1,883,513) primarily due to the higher lease operating and transportation expenses associated with the increase in production volumes between periods and the additional operating expense of the East Cameron properties which started production in February 2010. Depletion and accretion expense increased in the current year primarily as a result of the increase in production volumes between periods and the higher average depletion rate. General and administrative expense for the nine months ended May 31, 2010 was \$3,671,797 as compared to \$4,740,216 for the May 31, 2009 period. The decrease primarily relates to the wages and benefits expense from the forgiven employee loan expense and stock-based compensation incurred in the previous year, which was offset partially by higher legal fees in the current period resulting from the litigation settlement in the first quarter of fiscal year 2010 and increased legal activities from the Debt Restructuring Agreement and the new credit facilities. Interest expense increased in the current nine month period due to the interest bearing balances associated with the Debt Restructuring Agreement and the related debt instruments, including the new credit facilities in November 2009 and May 2010. The net loss recorded was \$12,652,510 for the nine month period ended May 31, 2010 as compared to a \$318,613 net loss for the May 31, 2009 nine month period. The increase in net loss between periods is from the items indicated above including the increase in depletion and accretion expense from the higher production volumes and overall increase in the average depletion rate. Foreign exchange gain (primarily the difference in exchange rates between the US and Canadian dollars) reflected in the net loss determination was a \$1,272,233 gain for the May 31, 2010 nine month period as compared to a \$2,945,989 gain for the May 31, 2009 nine month period.

*Financings, Principal Purposes and Milestones*

On January 22, 2009 the Company entered into a Note Purchase Agreement whereby the Company issued and sold senior secured notes ("Notes") in the aggregate principal amount of US\$10,000,000 (the "Notes") to a Single Holder (the "Holder"). The net proceeds to the Company, as a result of the negotiated discount to face value of the Notes, were CDN\$7,000,000 (US\$5,626,233). The Notes are collateralized by certain oil and natural gas properties. The Notes bear interest at a rate of 15% per annum, fixed and payable monthly in arrears on principal outstanding. The principal was originally scheduled to be paid by monthly payments of US\$200,000. The initial term of the Notes was two years with an extension option at the election of the Company for an additional two years upon payment of an extension fee of US\$300,000 in

**PROBE RESOURCES LTD.**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
As of May 31, 2010

each of the second and third years of the total term. As additional consideration for the Notes, the Holder received, at the time of initial execution, 7,000,000 share purchase warrants exercisable into 7,000,000 common shares of the Company at a price of \$0.20 per share through November 28, 2013. Fees were paid in connection with the issue of the Notes equal to 4% (\$277,272) of the funds raised and 4% (280,000) in warrants of the Company exercisable into common shares at a price of \$0.25 per warrant which expired on February 9, 2010.

On February 19, 2009 the Company entered into a credit facility (“Loan #1”) with an institutional lender in the amount of US\$8,500,000. Loan #1 was initially for a term of six months from the date of advance (the “Maturity Date”). Loan #1 is collateralized by certain of the Company’s oil and natural gas properties. Interest is at an annual rate of 18% payable and compounded monthly on amounts outstanding at month end. In consideration of Loan #1 and its provisions, the Lender received a \$480,000 commitment fee and 7,000,000 share purchase warrants to purchase 7,000,000 common shares of the Company at a price of \$0.25 per share for a four year period expiring February 19, 2013. Finders’ fees were paid in connection with the Loan equal to 4% (\$428,162) of the funds raised by the Company and 4% (280,000) in warrants of the Company exercisable into a common share at a price of \$0.25 per share on or before February 19, 2010. The warrants were not exercised. The Company did not repay Loan #1 within the original six month term and, effective August 31, 2009, Loan #1 was included in the Debt Restructuring Agreement. The interest rate on the balance outstanding remained at the 18% annual rate while monthly debt service payments are determined and made from monthly net restricted cash flow under the Debt Restructuring Agreement arrangement. Certain covenants and reporting requirements of the original Loan #1 Agreement were also modified as part of the Debt Restructuring and Forbearance Agreements. The Forbearance Agreement was executed in conjunction with the Debt Restructuring Agreement where an additional US\$500,000 fee was incurred by the Company and was added to the balance of Loan #1 as of August 31, 2009.

On April 29, 2009, the Company announced that it had entered into a joint venture on its East Cameron 36, East Cameron 37 and Vermillion 20 Blocks. The terms of the arrangement included a proportionate payment at time of the joint venture (received in April 2009) and proportionate contributions in the future for development and production costs by the joint venture participants. The joint venture participants became working interest owners in the prospects, with Probe retaining an overall approximately 52% working interest and approximately 36% net revenue interest before Project Payout and approximately 42% working interest and 30% net revenue interest after Project Payout.

On September 21, 2009 the Company announced that it had entered into a Debt Restructuring Agreement (the “DRA”) which became effective on August 31, 2009. The DRA schedules repayment of the Company’s outstanding past due trade payables and credit agreements in an orderly manner consistent with monthly collected revenues, following deduction for well and lease operating costs, transportation payments and royalty payments as well as general and administrative expenses of the Company. Under the terms of the DRA, repayment will be made to all trade creditors with interest compounded monthly on the outstanding balance at a 10% annual rate. The outstanding credit and note agreements are also included in the DRA. Interest rates on the existing loans and notes at the time of the DRA effective date remained at their original rate. Monthly debt service on the agreements is determined based upon available cash as defined by the DRA and is allocated among the various Creditor classes, including the credit facilities, within the

**PROBE RESOURCES LTD.**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
As of May 31, 2010

provisions of the DRA. The Company also agreed to restrictions on the sale of certain assets and to certain monthly reporting requirements. In the event of a rise (or decline) in the price or sales volume of natural gas, the repayment schedule self adjusts. A Creditors' Committee was formed under the DRA to resolve future issues, and a Creditors' Agent has been selected by the Creditors' Committee to oversee payments by the Company. The DRA was amended in November 2009 and May 2010 for two new credit agreements (outlined below). In the May 2010 amendment, the restricted cash distribution process within the DRA was revised to include a monthly minimum distribution level to the DRA Creditors of US\$75,000. If the minimum distribution level is not met within any of the remaining months of the DRA term, the monthly funding to the Company for its General and Administrative budget from the restricted cash account may be reduced by the shortfall up to a US\$75,000 level. The DRA expires on September 15, 2010 and does not have established renewal or extension provisions for outstanding balances at the time of expiration. The Company and the DRA Creditors' Committee are currently reviewing the expiration date impacts.

On November 10, 2009 the Company entered into a new credit agreement ("Loan #2") with an institutional lender for US\$9,250,000. Loan #2 is collateralized by certain of the Company's oil and natural gas properties. Loan #2 bears interest at 18% compounded monthly over a primary loan term of one year. Approximately US\$1,000,000 of the proceeds were used for related loan fees to the institutional lender. The fees incurred were deferred and are being expensed over the expected one year loan period. Debt service on Loan #2 is generated from the two wells of the East Cameron development project which came on production in February 2010. The Debt Restructuring Agreement was amended as a result of the Loan #2 agreement and the restricted cash flow to determine the monthly debt service is governed by the amended Debt Restructuring Agreement, while it remains in effect.

On May 27, 2010 the Company entered into a new term credit agreement ("Loan #3") with an institutional lender primarily for the planned East Cameron 246 development project. The initial funding of Loan #3 was US\$1,750,000 primarily for required bonding, legal fees and deposits. Initial Loan #3 funding has an associated original issue discount of US\$175,000, which was included in the overall initial borrowing amount of US\$1,750,000. The initial Loan #3 funding bears interest at an annual rate of 18% compounded monthly on amounts outstanding at month end and the primary loan term is through May 19, 2012. The Company and the institutional lender are evaluating the development and completion of the East Cameron 246 project and the expected funding requirements. Debt service will be generated from net production payments from the EC 246 well development project as the project moves forward. The Debt Restructuring Agreement was again amended to incorporate the new loan while the restricted cash flow to determine the monthly debt service is also to be governed by the amended Debt Restructuring Agreement, while it remains in effect.

*Capital Resources*

The Company's first three producing wells from the May 22, 2008 purchase agreements described above have been funded by a combination of the proceeds of the brokered private placement closed in July 2008, debt, operating cash flow, and joint ventures. The Company anticipates that current and future development and completion activities will be funded by a combination of debt, operating cash flow, and joint ventures. The actual number of wells drilled may vary depending upon various factors, including the availability and cost of drilling rigs, success of existing wells,

**PROBE RESOURCES LTD.**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
As of May 31, 2010

weather delays, regulatory issues and other factors. The Company may not be able to obtain the funding described above on terms that would be acceptable. If the Company cannot obtain adequate funding, it may be required to limit or defer planned drilling programs.

*Off Balance Sheet Arrangements*

There are no off-balance sheet arrangements to which the Company is committed.

*Commitments*

Contractual Obligations:

Operating Leases

The Company has a non-cancelable operating lease for its office facility. The lease has scheduled increases requiring the Company to pay its share of operating costs, and expires in December 2013. Future minimum payments under the operating lease are as follows:

May 31, 2011	\$369,543
May 31, 2012	\$376,088
May 31, 2013	\$376,088
December 31, 2013	\$219,384

*Contingency*

Probe reached a settlement of all claims and dismissal of a lawsuit, which had alleged the use of confidential information related to certain properties previously acquired by Probe. As a condition of the settlement, the Company paid US\$1.25 million in November 2009 and the Litigation Settlement counterparty also received small overriding royalties prospectively (starting with November 2009 production) on certain Probe properties. Probe and management vigorously deny any wrongdoing with respect to all of the matters alleged and the settlement specifically acknowledges that there is no admission of liability on either party's part. The settlement amount was included in the August 31, 2009 financial results for the Company where the Company recorded a provision of \$1,472,625 (US\$1,250,000). The settlement amount was paid in November 2009.

*Related Party Transactions*

In the course of regular business activities, the Company enters into transactions with related parties from time to time. During the nine months ended May 31, 2010 and 2009, the Company incurred the following fees charged by directors of the Company or by entities of which a director is a partner or entities with directors in common with the Company:

	<u>2010</u>	<u>2009</u>
Directors' fees	\$ 75,602	\$ 61,000
Legal fees	129,921	606,179
Wages and benefits	115,991	117,047
	<u>\$ 321,514</u>	<u>\$ 784,226</u>

**PROBE RESOURCES LTD.**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
As of May 31, 2010

These charges were measured by the exchange amount which is the amount agreed upon by the transacting parties.

At May 31, 2010, and August 31, 2009, accounts payable and accrued liabilities include \$296,772 and \$337,627 respectively, due to directors of the Company or to private entities with directors in common with the Company.

During the year ended August 31, 2008 the Company acquired an interest in certain oil and natural gas properties from a private company controlled by an officer/director.

On September 2, 2008, the Company advanced USD\$750,000 to an officer of the Company as a relocation/home ownership loan. The advance bore interest at 5% and was repayable on the earlier of January 1, 2010, or immediately in the case of the borrower's termination of the employment agreement dated February 12, 2008. The loan was to be forgiven as to 50% after one year and the remaining 50% after the second year unless the employment was terminated. The first 50% of the loan was forgiven on January 1, 2009 and the second 50% was forgiven on January 1, 2010.

*Liquidity and Solvency*

At May 31, 2010, the Company had a net working capital deficiency of \$(34,628,865) and had not yet achieved profitable operations and expects to incur further losses in the near-term development of its business, which casts substantial doubt about the Company's ability to continue as a going concern. The Company's ability to continue as a going concern is dependent upon its ability to generate future profitable operations and cash flow, to re-negotiate or otherwise settle the Debt Restructuring Agreement, and/or to obtain the necessary financing to meet its current obligations and growth opportunity program and repay its liabilities arising from normal business operations when they come due. The Company also entered into a Debt Restructuring Agreement effective August 31, 2009 (amended for Loan #2 and Loan #3), which addresses the payment of outstanding trade payables and its debt service obligation based upon its monthly cash flow from operations. As of May 31, 2010, the DRA creditors' balances were US\$37,428,906, consisting of accounts payables balance of US\$11,579,293 and debt balances of US\$25,849,613.

Listed below are three significant factors that have contributed to the Company's current negative working capital position:

1. ***Capital Markets:*** The economic climate was changing rapidly during the Company's last equity offering in July 2008. While the Company attained its minimum goal for the offering, \$10 to \$15 million in commitments to the offering were withdrawn prior to closing. The economic climate continued to worsen in late 2008 and the Company has not been able to replace the shortage with a subsequent offering.
2. ***Commodity Prices:*** Although the Company executed a rig contract in August 2008 when natural gas prices were over \$10/Mcf, the Company experienced an unavoidable six month rig delay to drill the South Timbalier 214 Well during which time prices declined below \$5/Mcf. The original schedule was to drill this well in June 2008, but the drilling was delayed until November 2008; first by the rig owner, then by Hurricanes Gustav and Ike. The South Timbalier 214 Well initially produced approximately 1,000,000 Mcfe per

**PROBE RESOURCES LTD.**  
MANAGEMENT DISCUSSION AND ANALYSIS  
As of May 31, 2010

month, but the commodity price decline reduced anticipated cash flow by \$5 million per month, or \$30 million year to date. Natural Gas prices continued to be depressed in the 2009 fiscal year and the lower overall average between years negatively impacted the working capital balance.

3. ***Production Delays:*** The Company experienced a mechanical equipment failure on the ST 214 Well in March 2009. Not only did the repair cost approximately \$2 million, but \$2.5 million of revenue was also delayed by the resulting shut in for repair. Hurricane Ike also damaged certain onshore facilities which host the Company's High Island 115 well. As a result, this well did not produce from September 2008 until February 2009, with production again ceasing on July 30, 2009 due to the expiration of the lease underlying the High Island 71 host processing facility, as well as the expiration of the "Production Handling Agreement" with the host. Resumption of production is expected in July 2010. The mechanical issue on the recently completed EC 37 has also unfavorably impacted the Company's cash flow during the remediation process.

*Adoption of New Accounting Standards*

International Financial Reporting Standards ("IFRS")

In 2006, the Canadian Accounting Standards Board ("AcSB") published a new strategic plan that will significantly affect financial reporting requirements for Canadian companies. The AcSB strategic plan outlines the convergence of Canadian GAAP and IFRS over an expected five year transitional period. In February 2008 the AcSB announced that 2011 is the changeover date for publicly-listed companies to use IFRS, replacing Canada's own GAAP. The date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. The transition date of January 1, 2011 will therefore require the restatement for comparative purposes of amounts reported by the Company for the year ended August 31, 2011. While the Company has begun assessing the adoption of IFRS for 2011, the financial reporting impact of the transition to IFRS has not been determined at this time.

*Risks*

A number of factors could cause the Company's results to differ materially from its expectations. Readers should carefully review the following factors, and all information contained on SEDAR. Exploration for oil and natural gas and foreign offshore operations involves many risks, which even a combination of experience, knowledge and careful evaluation may not be able to overcome. There is no assurance that commercial quantities of oil and natural gas will continue to be discovered by the Company. Risk factors include: risks associated with the exploration for and development of oil and natural gas reserves; operational risks and liabilities that are not covered by insurance; volatility in market prices for oil, NGLs and natural gas; the ability of the Company to fund its substantial capital requirements and operations; risks associated with ensuring title to the Company's properties; changes in environmental or other legislation applicable to the Company's operations and the Company's ability to comply with current and future environmental and other laws; the accuracy of oil and gas reserve and resource estimates and estimated production levels as they are affected by the Company's exploration and development drilling and estimated decline rates; the Company's success at acquisition, exploration,

**PROBE RESOURCES LTD.**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
As of May 31, 2010

exploitation and development of reserves and resources; the Company's reliance on key operational and management personnel; the ability of the Company to obtain and maintain all of its required permits and licenses; competition for, among other things, capital, drilling equipment, acquisitions of reserves, undeveloped lands and skilled personnel; changes in general economic, market and business conditions in Canada, the U.S., and worldwide; actions by governmental or regulatory authorities including changes in income tax laws or changes in tax laws, royalty rates and incentive programs relating to the oil and gas industry; adverse regulatory rulings, orders and decisions.

Current volatility in the economies of the U.S. and worldwide may impact the Company's future performance. Declines in the prices of natural gas and oil in the U.S. may lessen cash flows. Falling demand for rigs and other services and equipment may have a positive impact on future drilling costs. Less equity capital and debt availability may slow development projects and may require more reliance on internally generated cash flow. Industry practices of sharing risk with the formation of joint ventures may require a tightening and more restricted selection of joint venture partners.

The Company's operations are located in the US and the Company's financial statements are denominated in Canadian dollars. The Company's financial results will fluctuate based on the exchange rate between Canadian and U.S. dollars.

*Critical Accounting Estimates*

a) Oil and Natural Gas Properties

The Company follows the full cost method of accounting for oil and natural gas operations whereby all costs of exploring for and developing oil and natural gas reserves are initially capitalized. Such costs include land acquisition costs, lease rentals, geological and geophysical expenses, carrying charges on non-producing properties, costs of drilling and overhead charges directly related to acquisition and exploration activities.

Costs capitalized, together with the costs of production equipment and pipeline, are depleted and amortized on the unit-of-production method based on the estimated Company net proved reserves as determined and estimated by independent petroleum engineers. Petroleum products and reserves are converted to a common unit of measure, using 6 MCF of natural gas to one barrel of oil.

Costs of acquiring and evaluating unproved properties are initially excluded from depletion calculations. These unevaluated properties are assessed periodically to ascertain whether impairment has occurred. When proved reserves are assigned or the property is considered to be impaired, the cost of the property or the amount of the impairment is added to costs subject to depletion calculations.

Proceeds from a sale of oil and natural gas properties are applied against the capitalized costs, with no gain or loss recognized, unless such a sale would significantly alter the rate of depletion and amortization.

**PROBE RESOURCES LTD.**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
As of May 31, 2010

In applying the full cost method, the Company utilizes a ceiling test whereby the carrying value of oil and natural gas properties is compared to the sum of the undiscounted cash flows expected to result from the proved reserves and the lower of cost and market of unproved properties.

The recoverability of amounts shown for unproven properties is dependent upon the discovery of economically recoverable reserves, the ability of the Company to obtain necessary financing to complete the development of the properties and upon future profitable production or proceeds from the disposition thereof.

b) Asset Retirement Obligations

The fair value of obligations associated with the retirement of tangible long-lived assets are recorded in the period in which it is incurred and a reasonable estimate of the fair value can be made, with a corresponding increase to the carrying amount of the related asset. The obligations recognized are statutory, contractual or legal obligations. The liability is accreted over time for changes in the fair value of the liability through charges to accretion. The costs capitalized to the related assets are amortized in a manner consistent with the depreciation, depletion and amortization of the related asset.

c) Stock-based Compensation

The fair value of all share purchase options granted is expensed over their vesting period, with a corresponding increase to contributed surplus. Upon exercise of share purchase options, the consideration paid by the option holder, together with the amount previously recognized in contributed surplus, is recorded as an increase to share capital.

The Company uses the Black-Scholes option valuation model to calculate the fair value of share purchase options at the date of grant. Option pricing models require the input of highly subjective assumptions, including the expected price volatility. Changes in these assumptions can materially affect the fair value estimate.

*Disclosure of Outstanding Share Data*

As at July 14, 2010, authorized share capital for the Company was unlimited common and preferred shares without par value. While no preferred shares have been issued, a total of 106,383,200 common shares have been issued as follows:

**PROBE RESOURCES LTD.**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
As of May 31, 2010

	Share Capital		
	<u>Number of Shares</u>	<u>Amount</u>	<u>Contributed Surplus</u>
Balance, September 1, 2008	104,383,200	\$42,623,302	\$3,789,693
Issued for lease acquisition	666,666	100,000	-
Less: share issue costs	-	(11,022)	-
Finders' fee warrants	-	-	33,600
Share purchase options	-	-	<u>1,100,981</u>
Balance, August 31, 2009	<u>105,049,866</u>	<u>\$42,712,280</u>	<u>\$4,924,274</u>
Issued for lease acquisition	1,333,334	120,000	-
Share purchase options	-	-	<u>144,462</u>
Balance, July 14, 2010	<u>106,383,200</u>	<u>\$42,832,280</u>	<u>\$5,068,736</u>

Share purchase warrants outstanding at July 14, 2010 are as follows:

<u>Number of Warrants</u>	<u>Exercise Price</u>	<u>Expiry Date</u>
7,000,000	\$0.20	November 28, 2013
<u>7,000,000</u>	\$0.25	February 19, 2013
<u>14,000,000</u>		

Share purchase options outstanding at July 14, 2010 are as follows:

<u>Number of Options</u>	<u>Exercise Price</u>	<u>Expiry Date</u>
563,910	\$0.67	July 26, 2012
100,000	\$0.49	October 26, 2012
250,000	\$0.60	November 22, 2012
3,799,000	\$0.40	March 5, 2013
70,000	\$0.40	October 2, 2013
857,826	\$0.19	February 10, 2014
2,033,923	\$0.20	June 1, 2014
300,000	\$0.15	July 29, 2014
400,000	\$0.15	September 20, 2014
<u>400,000</u>	\$0.25	September 20, 2014
<u>8,774,659</u>		

**PROBE RESOURCES LTD.**  
MANAGEMENT DISCUSSION AND ANALYSIS  
As of May 31, 2010

*Financial Instruments*

The carrying value of cash and cash equivalents and accounts payable and accrued liabilities approximate their fair value because of the short-term maturity of those instruments.

For further information, please contact the Company.

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