

Quetzal Energy Ltd.

Condensed Interim Consolidated Financial Statements

Six Months Ended June 30, 2011 and 2010

(Expressed in U.S. dollars)

Notice to National Instrument 51-102:

The attached unaudited financial statements and notes thereto have been prepared by management and have not been independently audited or reviewed by the auditor of Quetzal Energy Ltd.

Quetzal Energy Ltd.

Condensed Interim Consolidated Statements of Financial Position

As at June 30, 2011, December 31, 2010 and January 1, 2010

(Expressed in U.S. dollars)
(unaudited)

	Note	June 30, 2011	December 31, 2010	January 1, 2010
Assets				
Current assets				
Cash and cash equivalents		22,919,697	3,851,706	5,554,866
Guaranteed investment certificates		-	-	2,930,620
Amounts receivable	8	1,767,042	3,662,300	51,850
Prepaid expenses and deposits		311,096	331,843	132,384
Restricted cash – current	9	949,328	1,219,753	-
		25,947,163	9,065,602	8,669,720
Restricted cash	9	2,451,100	2,250,793	-
Cash call advances	10	793,013	219,551	-
Exploration and evaluation assets	11	37,834,897	31,563,147	16,486,037
Property and equipment	12	457,041	239,190	137,212
		67,483,214	43,338,283	25,292,969
Liabilities				
Current liabilities				
Accounts payable and accrued liabilities		2,310,134	7,486,628	1,932,409
Deposits	21a	103,700	-	-
		2,413,834	7,486,628	1,932,409
Decommissioning liabilities	13	690,374	663,373	221,214
Future income taxes		590,198	600,291	1,306,218
		3,694,406	8,750,292	3,459,841
Shareholders' equity				
Share capital	14b	65,436,174	33,660,673	22,016,454
Warrants	14d	12,214,498	12,372,554	4,751,657
Contributed surplus	14e	4,769,131	3,563,517	2,760,443
Obligation to issue shares		-	-	1,665,081
Deficit		(23,621,686)	(17,201,519)	(9,360,507)
Other comprehensive income		4,990,691	2,192,766	-
		63,788,808	34,587,991	21,883,128
		67,483,214	43,338,283	25,292,969
Going concern	2			
Commitments and contingencies	19			
Subsequent events	21			

Approved on behalf of the Board

Signed: "Stephen W. Austin"

Director

Signed: "Ron MacMicken"

Director

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

Quetzal Energy Ltd.

Condensed Interim Consolidated Statement of Comprehensive Loss
For the six months ended June 30, 2011 and June 30, 2010

(Expressed in U.S. dollars)
(unaudited)

		Three months		Six months	
	Note	2011	2010	2011	2010
Revenue:					
Interest		65,189	15,843	73,554	17,752
		65,189	15,843	73,554	17,752
Expenses:					
General and administrative		1,859,104	1,118,546	3,255,089	2,035,857
Share-based payments		590,319	69,037	1,215,341	255,832
Foreign exchange gain		1,723,477	673,494	1,956,963	1,214,245
Depreciation		36,404	19,131	66,328	20,978
		4,209,304	1,880,208	6,493,721	3,526,912
Net loss before income taxes		(4,144,115)	(1,864,365)	(6,420,167)	(3,509,160)
Future income tax recovery (provision)		-	(519,858)	-	(519,858)
Net loss for the period		(4,144,115)	(2,384,223)	(6,420,167)	(4,029,018)
Foreign currency translation gains		1,570,686	3,732,607	2,797,925	4,824,411
Total comprehensive income (loss)		(2,573,429)	1,348,384	(3,622,242)	795,393
Net loss per common share, basic and diluted		0.007	0.010	0.011	0.019
Weighted average number of common shares used in computing net loss per share, basic and diluted	15	600,764,492	245,920,097	559,557,343	216,847,862

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

Quetzal Energy Ltd.

Condensed Interim Consolidated Statements of Changes in Equity
For the six months ended June 30, 2011 and December 31, 2010

(Expressed in U.S. dollars)
(unaudited)

	Note	Six months ended June 30, 2011	Year ended December 31, 2010	Six months ended June 30, 2010
Share capital				
	14b			
Balance beginning of period		33,660,673	22,016,454	22,016,454
Financing		34,734,600	9,243,579	3,788,966
Settlement of acquisitions		-	2,163,159	1,665,081
Warrants and options exercised		361,298	1,043,296	22,705
Share issue costs		(3,320,397)	(805,815)	(912,887)
Balance, end of period		65,436,174	33,660,673	26,580,319
Obligation to issue shares				
Balance beginning of period		-	1,665,081	1,665,081
Shares issued		-	(1,665,081)	(1,665,081)
Additional obligation to issue shares		-	-	498,078
Balance, end of period		-	-	498,078
Warrants				
	14d			
Balance beginning of period		12,372,554	4,751,657	4,751,657
Exercise of warrants		(158,056)	(309,829)	(13,431)
Issued (net of issue costs)		-	7,930,726	2,465,245
Balance, end of period		12,214,498	12,372,554	7,215,572
Contributed surplus				
	14e			
Balance beginning of period		3,563,517	2,760,443	2,760,443
Share-based payments		1,215,341	949,341	255,832
Impact of change in foreign currency exchange rates		(9,727)	(146,267)	(1,645)
Balance, end of period		4,769,131	3,563,517	3,014,630
Deficit				
Balance beginning of period		(17,201,519)	(9,360,507)	(9,360,507)
Net loss for the period		(6,420,167)	(7,841,012)	(4,029,018)
Balance, end of period		(23,621,686)	(17,201,519)	(13,389,525)
Other comprehensive income				
Balance beginning of period		2,192,766	-	-
Foreign currency translation gains		2,797,925	2,192,766	4,326,333
Balance, end of period		4,990,691	2,192,766	4,326,333
Total equity		63,788,808	34,587,991	28,245,408

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

Quetzal Energy Ltd.

Condensed Interim Consolidated Statements of Cash Flows
For the six months ended June 30, 2011

(Expressed in U.S. dollars)
(unaudited)

	June 30, 2011	June 30, 2010
Cash provided by (used in) the following activities		
Operating activities:		
Net loss for the period	(6,420,167)	(4,029,018)
Adjustments for non-cash items:		
Recovery (provision) for future income taxes	-	519,858
Share-based payments	1,215,341	255,832
Depreciation	66,328	20,978
Unrealized foreign exchange loss	2,798,852	4,916,988
	(2,339,646)	1,684,638
Change in non-cash working capital related to operating activities:		
Accounts receivable	(498,311)	(293,385)
Prepaid expenses and deposits	-	(127,943)
Accounts payable and accrued liabilities	(3,204,249)	3,826,509
Cash flows provided by (used in) operating activities:	(6,042,206)	5,089,819
Investing activities:		
Proceeds from GICs	-	2,930,620
Segregation of restricted cash	70,117	(6,379,774)
Cash call advances	(573,461)	-
Purchase of exploration and evaluation properties	(6,244,750)	(10,070,368)
Purchase of property and equipment	(284,179)	(1,389,675)
	(7,032,273)	(14,909,197)
Change in non-cash working capital related to investing activities:		
Accounts receivable	2,393,569	-
Deposit	103,700	-
Accounts payable and accrued liabilities	(1,972,244)	13,001
Cash flows (used in) investing activities	(6,507,247)	(14,896,196)
Financing activities		
Issuance of shares and warrants, net of costs of \$3,320,397	31,617,445	5,362,699
Cash flows provided from financing activities	31,617,445	5,362,699
Increase in cash and cash equivalents	19,067,991	(4,436,678)
Cash and cash equivalents, beginning of period	3,851,706	5,554,866
Cash and cash equivalents, end of period	22,919,697	1,111,188

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

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

1. Nature of operations

Quetzal Energy Ltd. (the "Company" or "QEL") was incorporated under the laws of the Province of Ontario on October 15, 2004. Pursuant to a resolution passed by shareholders on April 16, 2009, the Company changed its name from Southampton Ventures Inc. to Quetzal Energy Ltd.

The Company's principal business activities are the acquisition, exploration and development of petroleum and natural gas interests in Central and South America. To date, through its subsidiary Quetzal Energy (Bahamas) Ltd. (formerly PetroLatina Corporation), the Company has acquired an 80%-100% interest in two petroleum exploration and development licenses, comprising approximately 402,717 acres in Guatemala. Through its registered branch office in Colombia, the Company has acquired interests ranging from 14% to 35% in four blocks in the Llanos basin in Colombia. The address of the registered office is Suite 1150, 1122 – 4th Street S.W. Calgary, Alberta, T2R 1M1.

The common shares of the Company trade on the TSX Venture Exchange under the symbol "QEI".

These interim consolidated financial statements were approved by the Board of Directors on **August 29, 2011**.

2. Going concern

These condensed interim consolidated financial statements have been prepared on the basis of accounting principles applicable to a going concern, which assume that the Company will continue in operation for the foreseeable future and will be able to realize its assets and discharge its obligations in the normal course of operation.

The Company's ability to maintain its current level of operations is dependent upon its ability to generate sufficient cash to fund its ongoing operations and business plan. The oil market has its inherent fluctuations and the recoverability of amounts recorded as petroleum and natural gas properties is dependent upon the existence and discovery of economically recoverable oil and nature gas reserves, the world demand for oil and the political stability of Guatemala and Colombia. As at June 30, 2011, the Company had not yet achieved profitable operations, has accumulated a deficit of \$23,621,686 (December 31, 2010 - \$17,201,519; January 1, 2010 - \$9,360,507) since its inception, a working capital of \$23,533,328 (December 31, 2010 - \$1,578,975; January 1, 2010 - \$6,737,311) and expects to incur further losses in the development of its business, which is typical of a petroleum and natural gas company in the developmental stage. Until the Company begins earning consistent profits from the sales of its crude oil, it will be dependent upon securing investment funds from equity markets or lenders to continue as a going concern.

On January 27, 2011, the Company completed a brokered financing pursuant to a short-form prospectus in which it issued 276,000,000 common shares at \$0.125 per share for proceeds of \$31,414,203, net of related costs of \$3,320,397 (note 14b). Management believes that these balances, together with anticipated crude oil sales in 2011, will enable the Company to meet its financial commitments and capital investment program for 2011.

These consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts and classification of liabilities that might be necessary should the Company be unable to continue as a going concern for a reasonable period of time.

3. Basis of presentation

Statement of compliance

The condensed interim consolidated financial statements for the period ended June 30, 2011 have been prepared in accordance with International Accounting Standard 34, *Interim Financial Reporting* ("IAS 34") as issued by the International Accounting Standards Board ("IASB") and using the accounting policies the Company expects to adopt in its annual consolidated financial statements as at and for the year ending December 31, 2011.

These condensed interim consolidated financial statements are the Company's second consolidated financial statements prepared under IFRS. The Company adopted IFRS in accordance with IFRS 1 First-time Adoption of International Financial Reporting Standards ("IFRS 1") with a transition date to IFRS of January 1, 2010. Consequently, the comparative figures for 2010 and the Company's consolidated statement of financial position as

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

at January 1, 2010 have been restated from accounting principles generally accepted in Canada ("Canadian GAAP") to comply with IFRS.

These condensed interim consolidated financial statements should be read in conjunction with the Company's 2010 annual consolidated financial statements prepared in accordance with Canadian GAAP and in consideration of the IFRS transition disclosures included in note 22. In addition, IFRS 1 allows certain exemptions from retrospective application of IFRS in the opening consolidated statement of financial position. Where these have been used they are explained in note 22.

Basis of measurement

These condensed interim consolidated financial statements are stated in U.S. dollars and were prepared on a going concern basis, under the historical cost convention.

Use of estimates and judgments

The preparation of condensed interim consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates. Areas where estimates are significant to the interim consolidated financial statements are disclosed in note 5.

Functional and presentation currency

The Company has determined that its functional currency is the Canadian dollar for its Canadian parent company, Quetzals for the Guatemalan subsidiary and the U.S. dollar for the Colombian branch. The Company has chosen to present its condensed interim consolidated financial statements in U.S. dollars. The change in functional and presentation currency is discussed in note 4b and note 7.

4. Summary of significant accounting policies

The principal accounting policies applied in the preparation of these condensed interim consolidated financial statements are set out below. These policies have been consistently applied by the Company and its subsidiaries to all periods presented.

(a) Basis of consolidation:

Subsidiaries

Subsidiaries are entities controlled by the Company. Control exists when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that currently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Jointly controlled operations and jointly controlled assets

The Company is engaged in oil and gas exploration, development and production through unincorporated joint ventures ("Joint Ventures"). The Company accounts for its share of the results and net assets of these Joint Ventures as jointly controlled assets. The consolidated interim financial statements include the Company's share of these jointly controlled assets and a proportionate share of the relevant revenue and related costs, with the exception of certain current assets and current liabilities where the Company is the operator or has assumed the responsibilities of the operator. In those joint ventures where the Company is the operator or has assumed the responsibilities of the operator, cash, accounts receivable and accounts payable include the entire amount of these balances, being those assets and liabilities for which the Company is responsible.

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

Transactions eliminated on consolidation

Intercompany balances and transactions, and any unrealized gains and losses or income and expenses arising from intercompany transactions are eliminated in preparing the condensed interim consolidated financial statements. Unrealized gains arising from transactions with associates are eliminated to the extent of the Company's interest in the entity. Unrealized losses are eliminated in the same way as unrealized gains, but only to the extent that there is no evidence of impairment.

(b) Foreign currency translation:

Items included in the condensed interim consolidated financial statements of each of the Company's subsidiaries are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transaction. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities not denominated in the functional currency of an entity are recognized in foreign exchange gain or loss.

Assets and liabilities of foreign operations with functional currencies other than U.S. dollars are translated at the period end rates of exchange, and the results of their operations are translated at average rates of exchange for the period. The resulting translation adjustments are included in other comprehensive income in shareholders' equity.

Foreign exchange gains and losses related to intercompany loans forming part of a reporting entity's net investment in a foreign operation are included in foreign currency translation gains. All other foreign exchange gains and losses are recognized in income.

(c) Cash and cash equivalents:

Cash and cash equivalents consist of cash on hand and short-term deposits with original maturities of three months or less.

(d) Restricted cash:

Restricted cash represents cash amounts in trust for future joint venture disbursements and letters of guarantee. The restricted cash related to the letters of guarantee is classified as non-current as the expenditures relating to the guarantees are not expected to occur in 2011.

(e) Non-derivative financial instruments:

Non-derivative financial instruments are recognized when the Company becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership. Non-derivative financial instruments are recognized initially at fair value plus, for instruments not at fair value through profit or loss, any directly attributable transaction costs.

At initial recognition, all financial instruments are classified in one of the following categories depending on the purpose for which the instruments were acquired:

Loans and receivables

Loans and receivables are subsequently measured at amortized cost using the effective interest method, less any impairment losses, with interest expense recognized on an effective yield basis. Assets in this category include accounts receivable.

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss ("FVTPL") are financial assets held for trading or is designated as such by management. Such assets are held for trading if it is acquired principally for the purpose of selling in the short-term. These assets are initially recognized, and subsequently carried, at fair value, with changes

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

recognized in the statement of comprehensive income. Transaction costs are expensed. Assets in this category include cash and cash equivalents and restricted cash.

Other financial liabilities

Other financial liabilities are initially measured at fair value, net of transaction costs, and are subsequently measured at amortized cost using the effective interest method, with interest expense recognized on an effective yield basis. Liabilities in this category include accounts payable and accruals.

Available for sale

Available for sale assets are initially measured at fair value and are subsequently measured at fair market value with changes in value being recognized through other comprehensive income.

Equity instruments

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

(f) Oil and gas exploration and evaluation expenditures:

Exploration and evaluation ("E&E") expenditures incurred prior to acquiring the legal right to explore are charged to expense as incurred.

E&E expenditures incurred subsequent to acquisition of the legal right to explore, including license and property acquisition costs, geological and geophysical expenditures, costs of drilling exploratory wells and directly attributable overhead including salaries and employee benefits, and decommissioning liabilities are initially capitalized as E&E assets.

E&E assets are not depleted and are moved into property and equipment when they are determined to meet certain technical feasibility and commercial viability thresholds as determined by management. Upon transfer to property, plant and equipment, E&E assets are assessed for impairment in addition to regular impairment reviews to ensure they are not carried at amounts above their estimated recoverable values.

As at June 30, 2011, December 31, 2010 and January 1, 2010, all of the petroleum and natural gas assets held by the Company were classified as in the exploration and evaluation stage.

(g) Property and equipment:

Property and equipment includes petroleum properties and other assets.

Petroleum properties

Expenditures on developed petroleum properties such as drilling of development wells, tangible costs of facilities and infrastructure construction are capitalized to petroleum properties when it is probable that a future economic benefit will flow to the Company as a result of the expenditure and the cost can be reliably measured.

The initial cost of an asset comprises its purchase price or construction cost, any costs directly attributable to bringing the asset into operation, the initial estimate of any decommissioning obligation associated with the asset and finance charges on qualifying assets.

Depletion

Petroleum properties are depleted using the unit-of-production method over their reserve life using proven and probable reserves, unless the useful life of the asset is less than the reserve life, in which case the asset is depreciated over its estimated useful life using the straight-line method. Future development costs are included in costs subject to depletion. Reserves and estimated future development costs are determined annually by qualified independent reserve engineers. Changes in factors such as estimates of reserves that affect unit-of-production calculations are dealt with on a prospective basis.

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

Disposals

E&E and development and production assets are derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss on derecognition of the asset, calculated as the difference between the proceeds on disposal, if any, and the carrying value of the asset, is recognized in the consolidated statement of comprehensive income in the period of derecognition.

Other assets

Other assets are carried at cost less accumulated depreciation. Depreciation is charged so as to write-off the cost of these assets less residual value over their estimated useful economic lives, for the following classes of assets:

	Method	Rate
Office furniture and equipment	Declining balance	20%
Computer equipment	Declining balance	30%
Computer software	Straight-line	1 year
Drilling rig	Straight-line	5-8 years
Vehicles	Declining balance	20%
Field equipment	Declining balance	20%

(h) Impairment:

Financial assets

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. Significant financial difficulties of a debtor, probability that the debtor will enter bankruptcy or financial reorganization, and default or delinquency in payments are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognized in the statement of comprehensive income. When a trade receivable is uncollectible, it is written off against the allowance account for trade receivables.

Non-financial assets

At the end of each reporting period, the Company reviews the carrying amounts of its long-lived assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash-generating unit ("CGU") to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual CGU's, or otherwise they are allocated to the smallest group of CGU's for which a reasonable and consistent allocation basis can be identified.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted. If the recoverable amount of an asset or CGU is estimated to be less than its carrying amount, the carrying amount of the asset or CGU is reduced to its recoverable amount. An impairment loss is recognized immediately in income.

Where an impairment loss subsequently reverses for assets with a finite useful life, the carrying amount of the asset or CGU is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset or CGU in prior years. A reversal of an impairment loss is recognized immediately in income.

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

(i) Share-based payments:

The Company operates a number of equity-settled compensation plans under which it receives services from employees, directors, officers, and consultants as consideration for equity instruments of the Company. Share-based compensation expense is recorded in the statement of operations for all options granted with a corresponding increase recorded as contributed surplus.

Share-based compensation expense is based on the estimated fair values of the options at the time of the grant. The Company uses the Black-Scholes pricing model to estimate the fair value of equity-settled awards at the grant date. The expense is recognized over the vesting period, which is the period over which all of the specified vesting conditions are satisfied. For awards with graded vesting, the fair value of each tranche is recognized over its respective vesting period.

No expense is recognized for awards that do not ultimately vest, except for equity-settled awards where vesting is conditional upon a market or non-vesting condition, which are treated as vesting irrespective of whether or not the market or non-vesting condition is satisfied, provided that all other performance and/or service conditions are satisfied.

(j) Segment Reporting:

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker has been identified as the Executive directors that make strategic decisions.

(k) Provisions:

Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Company expects some or all of the provision to be reimbursed, the expense relating to any provision is presented in the consolidated statement of comprehensive loss net of the reimbursement. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as a finance cost in the consolidated statement of comprehensive income.

Decommissioning liabilities

The Company provides for the costs of decommissioning associated with long-lived assets, which result from the acquisition, construction and development and use of the asset. The best estimate of each asset decommissioning liability is recorded in the period which it is incurred if a reasonable estimate of fair value can be made. The decommissioning liabilities are measured in the consolidated statement of financial position at the fair value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. A corresponding amount is capitalized as part of petroleum and natural gas properties and depleted on a unit-of-production basis. Any further adjustment arising from a reassessment of estimated cost of the decommissioning liabilities also has a corresponding amount capitalized, whilst the charge arising from the accretion of the discount applied to the decommissioning liabilities is capitalized to the carrying value of the asset if in a pre-operating stage, or treated as a component of finance costs in the consolidated statement of comprehensive income once the property has been developed and put into production.

Decommissioning obligations are measured at the present value of management's best estimate of the expenditure required to settle the present obligation as at the statement of financial position date. Subsequent to the initial measurement, the obligation is adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation. The increase in the provision due to the passage of time is recognized as finance costs whereas increases/decreases due to changes in the estimated

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

future cash flows are capitalized. Actual costs incurred upon settlement of the asset retirement obligations are charged against the provision to the extent the provision was established.

(l) Revenue recognition:

Revenues from the sale of petroleum and natural gas are reported as sales revenue when management has determined that the cash generating unit is commercially viable. Revenues from the sale of petroleum and natural gas prior to when a cash generating unit is commercially viable are included in exploration and evaluation, together with the associated operating expenses. Revenues are recognized when the risk and rewards of ownership pass to the purchaser, including delivery of the product, the selling price is fixed or determinable and collectability is reasonably assured.

(m) Income tax:

Income tax expense comprises current and deferred tax. Income tax expense is recognized in profit or loss except to the extent that it relates to items recognized in other comprehensive income or directly in equity.

Current income tax

Current tax expense is based on the results for the period as adjusted for items that are not taxable or not deductible. Current tax is calculated using tax rates and laws that were enacted or substantively enacted at the end of the reporting period. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. Provisions are established where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred tax

Deferred taxes are the taxes expected to be payable or recoverable on unused tax losses, unused tax credits and differences between the carrying amounts of assets in the consolidated statement of financial position and their corresponding tax bases used in the computation of taxable profit, and are accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognized for all taxable temporary differences between the carrying amounts of assets and their corresponding tax bases. Deferred tax assets are recognized to the extent that it is probable that taxable profits will be available against which unused tax losses, unused tax credits and deductible temporary differences can be utilized. Such assets and liabilities are not recognized if the temporary difference arises from the initial recognition of goodwill or from the initial recognition (other than in a business combination) of other assets in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities:

- are generally recognized for all taxable temporary differences;
- are recognized for taxable temporary differences arising on investments in subsidiaries except where the reversal of the temporary difference can be controlled and it is probable that the difference will not reverse in the foreseeable future; and
- are not recognized on temporary differences that arise from goodwill which is not deductible for tax purposes.

Deferred tax assets:

- are recognized to the extent it is probable that taxable profits will be available against which the unused tax losses, unused tax credits and deductible temporary differences can be utilized; and
- are reviewed at the end of the reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

(n) Loss per share:

Basic loss per common share is calculated based on the weighted average number of common shares outstanding during the year. Diluted loss per share is calculated using the treasury stock method, which assumes

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

that the cash that would be received on the exercise of options and warrants is applied to purchase shares at the average price during the period and that the difference between the shares issued upon their exercise and the number of shares obtainable under this computation, on a weighted average basis, is added to the number of shares outstanding. Anti-dilutive amounts are not considered in computing diluted loss per share.

5. Critical judgments and accounting estimates

The preparation of the condensed interim consolidated financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and contingent liabilities at the date of the condensed interim consolidated financial statements and reported amounts of revenues and expenses during the reporting period. Estimates and judgments are continuously evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Actual outcomes can differ from these estimates.

The key sources of estimation uncertainty that have a significant risk of causing material adjustment to the amounts recognized in the condensed interim consolidated financial statements are:

Assessment of commercial reserves

Management is required to assess the level of the Company's commercial reserves together with the future expenditures to access those reserves, which are utilized in determining the depletion charge for the period, assessing whether any impairment charge is required against producing and developed, and the determination of the deferred tax liability. By their nature, these estimates of proved and probable crude oil and natural gas reserves, including the estimates of future prices, costs, related future cash flows and the selection of a pre-tax risked discount rate relevant to the asset in question are subject to measurement uncertainty. The Company employs independent reserves specialists who periodically assess the Company's level of commercial reserves by reference to data sets including geological, geophysical and engineering data together with reports, presentation and financial information pertaining to the contractual and fiscal terms applicable to the Company's assets. Significant judgment is involved when determining whether there have been any significant changes in the Company's crude oil and natural gas reserves.

Impairment of non-financial assets

Impairment exists when the carrying value of an asset or cash generating unit exceeds its recoverable amount, which is the higher of its fair value less costs to sell and its value in use. The fair value less costs to sell calculation is based on available data from binding sales transactions in an arm's length transaction of similar assets or observable market prices less incremental costs for disposing of the asset. The value in use calculation is based on a discounted cash flow model. The cash flows are derived from the budget for the next five years and do not include restructuring activities that the Company is not yet committed to or significant future investments that will enhance the asset's performance of the cash generating unit being tested. The recoverable amount is most sensitive to the discount rate used for the discounted cash flow model as well as the expected future cash inflows and the growth rate used for extrapolation purposes.

Share-based payment transactions

The Company measures the cost of equity-settled transactions with employees by reference to the fair value of the equity instruments at the date at which they are granted. Estimating fair value for share-based payment transactions requires determining the most appropriate valuation model, which is dependent on the terms and conditions of the grant. This estimate also requires determining and making assumptions about the most appropriate inputs to the valuation model including the expected life, volatility and dividend yield of the share option.

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

Decommissioning provisions

Decommissioning provisions consist of asset retirement obligations that are based, in part, on estimates of future costs to settle the obligation, in addition to estimates of the useful life of the underlying assets, the rate of inflation and the risk-free interest rate.

Useful lives of property and equipment

The Company estimates the useful lives of property and equipment based on the period over which the assets are expected to be available for use. The estimated useful lives of property and equipment are reviewed periodically and are updated if expectations differ from previous estimates due to physical wear and tear, technical or commercial obsolescence and legal or other limits on the use of the relevant assets. In addition, the estimation of the useful lives of property and equipment are based on internal technical evaluation and experience with similar assets. It is possible, however, that future results of operations could be materially affected by changes in the estimates brought about by changes in factors mentioned above. The amounts and timing of recorded expenses for any period would be affected by changes in these factors and circumstances. A reduction in the estimated useful lives of the property and equipment would increase the recorded expenses and decrease the non-current assets.

Fair value of financial instruments

The estimated fair value of financial assets and liabilities, by their very nature, are subject to measurement uncertainty.

Taxes

Provisions for taxes are made using the best estimate of the amount expected to be paid based on a qualitative assessment of all relevant factors. The Company reviews the adequacy of these provisions at the end of the reporting period. However, it is possible that at some future date an additional liability could result from audits by taxing authorities. Where the final outcome of these tax-related matters is different from the amounts that were initially recorded, such differences will affect the tax provisions in the period in which such determination is made.

6. Recent accounting pronouncements issued but not yet adopted

Certain new standards, interpretations, amendments and improvements to existing standards were issued by the International Accounting Standards Board ("IASB") or International Financial Reporting Interpretations Committee ("IFRIC") but are not yet effective. The standards impacted that are applicable to the Company are as follows:

- i) IFRS 9, 'Financial Instruments' was issued in November 2009 as the first step in its project to replace IAS 39 'Financial Instruments: Recognition and Measurement'. IFRS 9 introduces new requirements for classifying and measuring financial assets that must be applied starting January 1, 2013, with early adoption permitted. The IASB expanded IFRS 9 during the intervening period to add new requirements for classifying and measuring financial liabilities, derecognition of financial instruments, impairment and hedge accounting. The Company is currently assessing the impact of this standard.
- ii) IFRS 10, 'Consolidated Financial Statements' was issued in May 2011 and will supersede the consolidation requirements in SIC-12 'Consolidation – Special Purpose Entities' and IAS 27 'Consolidated and Separate Financial Statements' effective for annual periods beginning on or after January 1, 2013, with early application permitted. IFRS 10 builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company. The standard also provides additional guidance to assist in the determination of control where this is difficult to assess. The Company is currently assessing the impact of this standard.
- iii) IFRS 11, 'Joint Arrangements' was issued in May 2011 and will supersede existing IAS 31, 'Joint Ventures' effective for the annual period beginning on or after January 1, 2013, with early application permitted. IFRS 11 provides for the accounting of joint arrangements by focusing on the rights and obligations of the arrangement, rather than its legal form (as is currently the case). The standard also eliminates the option to

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

account for jointly controlled entities using the proportionate consolidation method. The Company is currently assessing the impact of this standard.

- iv) IFRS 12, 'Disclosure of Interests in Other Entities' was issued in May 2011 and is a new and comprehensive standard on disclosure requirements for all forms of interests in other entities, including subsidiaries, joint arrangements, associates and unconsolidated structured entities. IFRS 12 is effective for annual periods beginning on or after January 1, 2013, with earlier application permitted. The Company is currently assessing the impact of this standard.
- v) IFRS 13, "Fair Value Measurement", which provides a common definition of fair value, establishes a framework for measuring fair value under IFRS and enhances the disclosures required for fair value measurements. The standard applies where fair value measurements are required and does not require new fair value measurements. The Company is currently assessing the impact of this standard.

Comment [JF1]: Missing IAS 1 and IAS 19

7. Change in functional and presentation currency

There have been no changes to the presentation currency due to the adoption of IFRS. The Company continues to present condensed interim consolidated financial statements in United States dollars ("US\$").

Effective January 1, 2010, the Company changed the functional currencies of their Colombian subsidiary from Colombian Pesos to US\$ as a significant portion of the subsidiary's revenues, expenses and cash flows are denominated in US\$. In making this change in functional currency, the Company followed the recommendations set out in IAS 21, *The Effects of Change in Foreign Exchange Rates*. In accordance with IAS 21, the financial statements for all years and periods presented have been translated into the existing presentation currency using the temporal method. Under this method, income and expenses for each statement of comprehensive income or separate income statement presented are translated at exchange rates at the dates of the transactions.

All assets and liabilities have been translated using the exchange rate prevailing at the consolidated balance sheets dates. Shareholders' equity transactions have been translated using the rates of exchange in effect as of the dates of the various capital transactions, while shareholders' equity balances from the translation are included as a separate component of other comprehensive income. All resulting exchange differences arising from the translation are included as a separate component of other comprehensive income. All comparative financial information has been re-stated to reflect the Company's subsidiaries' change in functional currency and the effect on the consolidated financial statements resulted in an accumulated and other comprehensive income adjustment of \$2.0 million of which \$2.0 million was adjusted for on transition to IFRS (refer to Note 24) resulting in a nil balance as at January 1, 2010.

8. Amounts receivable

	June 30, 2011	December 31, 2010	January 1, 2010
Oil and gas sales receivable	1,204,091	25,126	26,069
Due from joint venture partners	302,903	3,501,576	-
Income and sales taxes receivable	205,621	116,477	-
Other	54,427	19,121	25,781
	1,767,042	3,662,300	51,850

In determining the recoverable amount of a trade or other receivable, the Company performs a risk analysis considering the type and age of the outstanding receivable and the credit worthiness of the counterparties.

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

9. Restricted cash

	June 30, 2011	December 31, 2010	January 1, 2010
Funds held in trust for joint venture disbursements	845,628	1,219,753	-
Funds held in trust for disposition of Horden Lake mineral property (Note 21a)	103,700	-	-
Restricted cash, current	949,328	1,219,753	-
GICs held as security for the Company's Letters of Guarantee and corporate credit cards	2,451,100	2,250,793	-
	3,400,428	3,470,546	-

The guaranteed investment certificates being held as security for the Company's Letters of Guarantee are prime-linked cashable GICs that mature from July 25, 2011 to November 3, 2011 and bear interest at 0.03% per annum.

10. Cash call advances

The Company may from time to time remit funds to a joint venture operator in anticipation of incurring its share of capital and operating expenses from the joint venture. When the joint venture incurs the cost, the cash call advances will be charged to exploration and evaluation assets or operating expenses.

11. Exploration and evaluation assets

	Balance December 31, 2010	Impact of change in foreign currency exchange rates	Additions, net of capitalized oil revenues	Balance June 30, 2011
Guatemala (i)	16,530,050	325,197	1,701,926	18,557,173
Colombia (ii)	15,033,097	1,338,481	2,906,146	19,277,724
	31,563,147	1,663,678	4,608,073	37,834,897

	Balance January 1, 2010	Impact of change in functional Currency	Additions, net of capitalized oil revenues	Balance December 31, 2010
Guatemala (i)	14,266,336	352,900	2,721,097	17,340,333
Colombia (ii)	2,219,701	278,052	11,725,061	14,222,814
	16,486,037	630,952	14,446,158	31,563,147

	Balance January 1, 2010	Impact of change in functional Currency	Additions, net of capitalized oil revenues	Balance June 30, 2010
Guatemala (i)	14,266,336	358,717	1,367,891	15,992,944
Colombia (ii)	2,219,701	42,005	8,304,463	10,566,169
	16,486,037	400,722	9,672,354	26,559,113

There was no depletion calculation for periods ended June 30, 2011 and June 30, 2010. Although production of crude oil from the Canaguay well in the Canaguaro block, Colombia had commenced during the test phase, management determined that the block was not yet commercially viable.

The Company performed a ceiling test calculation at December 31, 2010 resulting in the discounted cash flows from proved and probable reserves exceeding the carrying value of oil and gas assets.

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

The prices used in the ceiling test evaluation of the Company's oil and gas assets are summarized in the following chart:

	2011	2012	2013	2014	2015	2016
Colombia (\$US/bbl)						
Vasconia oil (25° API)	91.23	91.56	90.58	90.05	90.20	90.74
Guatemala (\$US/bbl)						
WTI oil (40° API)	85.00	87.70	90.50	93.40	96.30	99.40

i) Guatemala

The Company has an 80%-100% interest in two petroleum exploration and development licenses in Guatemala. These licenses were granted for a 25 year period expiring in 2030. Royalties are payable to the Guatemalan government ranging from 5% to 35% based on production and the grade of the crude oil produced.

For the period ended June 30, 2011, the Company capitalized general and administrative expenses of \$527,820 (December 31, 2010 - \$789,103).

ii) Colombia

The Company has interests in four blocks in the Llanos basin in Colombia as follows:

	LLA-21	LLA-27	LLA-36	Canaguaro
Participation interest	35.0%	34.25%	14%	25%
Increased costs assumed	50%	50%	20%	31.25%
Increased participation interest	45.5%	45.275%	18.2%	25%

The Company agreed to assume an increased share of investments, work commitments, costs and expenses for these interests until the cost recovery account for the Company's participating share matches the previous participants' cost contributions. Once the cost recovery amounts are matched, production participation shares will revert to the initial interest percentages. In Canaguaro, the Company assumes 31.25% capital interest of the first \$10 million of the well cost to earn a 25% participating interest. The Company's share of costs in excess of \$10 million is 25% of actual costs.

For the six month period ended June 30, 2011, the Company reduced the exploration and evaluation ("E&E") assets by capitalizing crude oils sales revenues of \$393,971 (June 30, 2010 - \$207,712). Capitalized general and administrative costs ("G&A") were reduced by \$661,206 during this period (June 30, 2011 - G&A capitalized to E&E \$919,794).

12. Property and equipment

	June 30, 2011		
	Cost	Accumulated depreciation	Net book value
Office furniture and equipment	140,794	48,007	92,787
Computer equipment	191,713	73,039	118,674
Computer software	202,947	144,472	58,475
Field equipment / light vehicles	193,191	6,086	187,105
	728,645	271,604	457,041

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

December 31, 2010			
	Cost	Accumulated depreciation	Net book value
Office furniture and equipment	135,944	42,060	93,884
Computer equipment	158,287	53,720	104,567
Computer software	155,663	114,924	40,739
	<u>449,894</u>	<u>210,704</u>	<u>239,190</u>

January 1, 2010			
	Cost	Accumulated depreciation	Net book value
Office furniture and equipment	160,932	86,486	74,446
Computer equipment	130,293	67,527	62,766
Computer software	84,563	84,563	-
	<u>375,788</u>	<u>238,576</u>	<u>137,212</u>

13. Decommissioning liabilities

The Company is legally required to restore its properties to their original condition in both Guatemala and Colombia. Estimated future site restoration costs are based upon engineering estimates of the anticipated method and the extent of site restoration required in accordance with current legislation and industry practices in the various jurisdictions in which the Company has properties.

As at June 30, 2011, the Company estimated the total undiscounted amount of cash flows required to settle its share of the decommissioning liabilities to be \$1,413,000 (December 31, 2010 - \$1,413,000) and \$62,500 (December 31, 2010 - \$62,500) for its wells in Guatemala and Colombia, respectively, which will be incurred in 2019 and 2020.

<i>(\$US)</i>	Six months ended June 30, 2011	Year ended December 31, 2010	Six months ended June 30, 2010
Balance, beginning of period	663,373	221,214	221,214
Change in estimate	-	390,548	-
Additions	-	29,987	-
Unwinding of decommissioning liabilities	27,001	21,624	4,352
Balance, end of period	<u>690,374</u>	<u>663,373</u>	<u>225,566</u>

The following significant assumptions were used to estimate the asset retirement obligation:

	June 30, 2011	December 31, 2010	March 31, 2010
Discount rate	13.25%	13.50%	13.48%
Inflation rate	3.90%	2.00%	2.0%

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

14. Share capital and other equity

a) Authorized

Unlimited number of common shares

Unlimited number of Class A non-voting, non-cumulative, redeemable, retractable preference shares

Unlimited number of Class B voting, non-cumulative, redeemable, retractable preference shares

b) Issued

Common Shares	Number of Shares	Amount
Balance at January 1, 2010	172,831,532	22,016,454
Exercise of warrants (i)	5,477,940	892,136
Exercise of options (ii)	561,000	151,160
Acquisition interests in oil and gas properties (iii)	10,000,000	1,665,081
Acquisition interests in oil and gas properties (iv)	3,000,000	498,078
Issued pursuant to private equity placement (v)	62,933,120	3,788,966
Issued pursuant to private equity placement (vi)	68,337,400	5,454,613
Share issue costs		(805,815)
Balance, December 31, 2010	323,140,992	33,660,673
Financing Jan 27, 2011(vii)	276,000,000	34,734,600
Exercise of warrants (i)	1,623,500	361,298
Share issue costs	-	(3,320,397)
Balance, at June 30, 2011	600,764,492	65,436,174

(i) During the year ended December 31, 2010, 5,477,940 warrants were exercised at prices ranging from \$0.125 and \$0.200 for total proceeds of \$797,675. Pursuant to the exercise of these warrants, \$94,461 was reallocated from warrants to share capital.

During the first quarter ended March 31, 2011, 1,623,500 warrants were exercised at \$0.125 for total proceeds of \$203,242. Pursuant to the exercise of these warrants, \$158,056 was reallocated from warrants to share capital.

(ii) During the year ended December 31, 2010, 561,000 stock options were exercised at \$0.175 for total proceeds of \$95,610. Pursuant to the exercise of these stock options \$55,550 in contributed surplus was reallocated to share capital.

(iii) On February 1, 2010, the Company issued 10,000,000 common shares in settlement of its acquisition of petroleum and natural gas interests in Colombia. The shares have been valued at \$1,665,081 as at the date of the related participation agreements.

(iv) On July 26, 2010, the Company issued 3,000,000 common shares in settlement of its acquisition of petroleum and natural gas interests in Colombia. The value of the shares was \$498,078 based on a share been valued of \$0.166 per share (\$0.17 per share) which was the trading price of the shares when the Company entered into the agreement.

(v) On March 18, 2010, the Company completed a private equity placement raising gross proceeds of \$8,078,777 for the issuance of 58,816,000 units at \$0.14 per unit. The agents received 4,117,120 units, representing 7% of the units issued in lieu of a cash paid commission. In total 62,933,120 units were issued. Each unit consists of one common share and one common share purchase warrant exercisable at a price of \$0.20 and expires on October 26, 2011. The share purchase warrants attached to the issued units were valued at \$4,610,597.

The agent units were assigned a value of \$310,786 which was allocated between share capital and warrants of \$139,986 and \$170,800 and issuance costs, respectively. Issuance costs of \$238,867 were allocated at \$107,490 for the common shares and \$131,377 for the warrants.

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

(vi) On September 9, 2010, the Company completed a private equity placement raising gross proceeds of \$9,256,312 (\$C9,567,236) for the issuance of 68,337,400 units at \$C0.14 per unit. Each unit consists of one common share and one common share purchase warrant. Each warrant entitles the holder to acquire one common share of the Company at a price of \$C0.20 until October 26, 2011. The share purchase warrants attached to the issued units were valued at \$3,801,695. Total issue costs of \$953,121 were allocated as \$558,364 for the common shares and \$394,757 for the warrants.

(vii) On January 27, 2011, the Company completed an equity placement pursuant to a short-form prospectus raising gross proceeds of \$34,734,600 (\$C34,500,000) for the issuance of 276,000,000 common shares at \$C0.125 per common share. Total issue costs were \$3,320,397 (\$C3,301,493).

c) Stock options

A summary of the status of the Company's stock options and changes during the periods then ended is shown below:

	Six months ended June 30, 2011		Year ended December 31, 2010	
	Number of options outstanding	Weighted Average exercise price (\$C)	Number of options outstanding	Weighted Average exercise price (\$C)
Outstanding at beginning of year	18,190,000	0.214	9,140,000	0.294
Granted	14,850,000	0.125	10,600,000	0.143
Exercised	-	-	(561,000)	0.175
Forfeited, cancelled, expired	(500,000)	(0.185)	(989,000)	0.207
	32,540,000	0.174	18,190,000	0.214

The following stock options were outstanding on March 31, 2011:

Exercise Price (\$C)	Number of Options Outstanding	Remaining Contractual Life (years)	Number of Options Vested
0.750	200,000	1.00	200,000
3.100	225,000	1.22	225,000
0.750	400,000	1.22	400,000
0.200	2,265,000	3.20	1,698,750
0.170	1,000,000	3.87	750,000
0.200	300,000	3.87	225,000
0.135	8,800,000	4.48	4,400,000
0.175	4,500,000	3.59	2,250,000
0.125	14,850,000	4.95	3,712,500
	32,540,000	4.37	13,861,250

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

d) Warrants

The schedule of warrant activity during the period ended June 30, 2011 is as follows:

	Number of Warrants	Weighted average exercise price (\$C)	Value (\$US)
Balance, January 1, 2010	125,959,257	0.196	4,751,657
Issued pursuant to private placement	62,933,120	0.200	4,610,597
Compensation warrants issued	4,117,120	0.140	352,531
Issued pursuant to private placement	68,337,400	0.200	3,801,695
Compensation warrants issued	4,783,618	0.140	323,970
Exercised	(5,477,940)	0.151	(309,829)
Issued on exercise of warrants	3,040,440	0.200	215,368
Issue costs incurred	-	-	(1,373,435)
Balance, December 31, 2010	263,693,015	0.197	\$12,372,554
Exercised	(1,623,500)	0.097	(158,056)
Balance, June 30, 2011	262,069,515	0.197	\$12,214,498

e) Contributed surplus

	(\$US)
Balance, January 1, 2010	2,760,443
Share-based payments	949,341
Reallocation to common share capital on exercise of options	(55,550)
Impact of foreign exchange	(90,717)
Balance, December 31, 2010	3,563,517
Share-based payments	1,215,341
Impact of foreign exchange	(9,727)
	\$ 4,769,131

15. Net loss per common share

The weighted average number of common shares outstanding during the three months ended June 30, 2011 was 600,764,492 (June 30, 2010 – 256,920,789) and during the six months ended June 30, 2011 was 559,557,343 (2010 - 216,847,862). All outstanding warrants and stock options have been excluded from the computation of diluted loss per share as their effect would be anti-dilutive.

16. Capital management

The Company's objectives when managing capital is to safeguard the Company's ability to continue as a going concern, so that it can continue to provide benefits for stakeholders. The Company sets the amount of capital in proportion to risk. Methods employed to adjust the Company's capital structure could include any, all, or a combination of the following actions: repurchase shares pursuant to a normal course issuer bid; issue new shares through a public offering or private placement; or obtain debt financing. The Company manages its capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. The Company's ability to raise future capital through equity financing and debt financing is subject to uncertainty and the inability to raise such capital may have an adverse impact over the Company's ability to continue as a going concern (note 2).

The Company defines its capital as total equity plus long-term debt. Total equity is comprised of share capital and all issued stock options and warrants. Currently, neither the Company nor its subsidiaries has any short or long-

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

term debt. Neither the Company nor its subsidiaries are subject to any externally imposed capital requirements such as loan covenants or capital ratios.

17. Financial instruments

The Company has classified its financial instruments under the following classifications:

- (i) Cash and restricted cash is classified as financial assets held for trading;
- (ii) Trade and other receivables are classified as loans and receivables; and,
- (iii) Accounts payable and accrued liabilities are classified as other financial liabilities.

The carrying value and fair value of the Company's financial instruments as at June 30, 2011 and June 30, 2010 are as follows:

Financial instrument classification	June 30, 2011 Carrying Value \$	June 30, 2011 Fair value \$	June 30, 2010 Carrying Value \$	June 30, 2010 Fair Value \$
Assets held for trading:				
Cash and cash equivalents	22,919,697	22,919,697	1,111,188	1,111,188
Restricted cash, current	949,328	949,328	1,486,058	1,486,058
Restricted cash, non-current	2,451,100	2,451,100	4,893,716	4,893,716
Loans and receivables:				
Accounts receivable	1,767,042	1,767,042	345,235	345,235
Other financial liabilities:				
Accounts payable and accrued liabilities	(2,310,134)	(2,310,134)	(5,771,919)	(5,771,919)

Fair value represents the price at which a financial instrument could be exchanged in an orderly market, in an arm's length transaction between knowledgeable and willing parties who are under no compulsion to act. The Company's financial instruments consist of cash and cash equivalents, restricted cash, accounts receivable and accounts payable and accrued liabilities. The fair values of these financial instruments approximate their carrying value due to their short-term to maturity.

The Company's financial assets and liabilities recorded at fair value have been classified according to the following hierarchy based on the amount of observable inputs used to value the instruments.

- Level 1 – Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.
- Level 2 – Pricing inputs are other than quoted prices in active markets included in Level 1. Prices in Level 2 are either directly or indirectly observable as of the reporting date. Level 2 valuations are based on inputs, including quoted forward prices for commodities, time value and volatility factors, which can be substantially observed or corroborated in the market place.
- Level 3 – Valuations in this level are those with inputs for the assets or liabilities that are not based on observable market data.

The Company's cash and restricted cash have been assessed on the fair value hierarchy described above; cash and restricted cash are classified as Level 1.

18. Financial risk management

The Company's risk management policies are established by the Board of Directors to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, to monitor risks of market conditions, and adherence to the Company's policy.

Credit risk

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its commercial obligations.

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

Virtually all of the Company's accounts receivable are with companies in the petroleum and natural gas industry and are subject to normal industry credit risks. The Company generally extends unsecured credit to these companies and therefore, the collection of accounts receivable may be affected by changes in economic or other conditions. Management monitors the financial conditions of its customers on an on-going basis and believes that there are other buyers in the marketplace that would purchase the production under the same financial terms.

All of the Company's cash and cash equivalents and guaranteed investment certificates are on deposit with well known and established financial institutions. As such, management considers credit risk related to these financial assets to be minimal.

The Company's maximum credit risk exposure is limited to the carrying value of its cash and cash equivalents, guaranteed investment certificates and accounts receivable. At June 30, 2011, the Company had no material accounts receivable deemed to be uncollectible.

Commodity price risk

Commodity price risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in commodity prices. The nature of the Company's operations will result in exposure to fluctuations in commodity prices. The Company is currently in its development stage and as such the exposure to fluctuations in commodity prices are not actively managed. In the future, the Company may use commodity price contracts to manage exposure to fluctuations in pricing.

Interest rate risk

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The Company does not have a material exposure to this risk as there are no outstanding debt facilities and all investments have a short-term to maturity.

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they come due. The Company ensures, as far as possible, that it will have sufficient liquidity to meet its liabilities when due, without incurring unacceptable losses or harm to the Company's reputation.

The Company prepares annual capital expenditure budgets which are regularly monitored and updated as necessary. The Company also utilizes authorization for expenditures to further manage capital expenditures and attempts to match its payment cycle with collection of petroleum and natural gas revenues. Accounts payable and accrued liabilities at June 30, 2011, all have contractual maturities of less than 90 days and are subject to normal trade terms.

Foreign currency risk

The reporting currency of the Company is U.S. dollars. The Company enters into transactions denominated in Canadian dollars, Colombian pesos and Quetzals for which the related expenses and accounts payable balances are subject to exchange rate fluctuations. The Company's cash and cash equivalents are also denominated in foreign currencies. The Company does not specifically hedge its exposure to foreign currency risk. The Company's management monitors the exchange rate fluctuations on a regular basis. The Company does not use currency derivative instruments to manage its exposure to foreign currency fluctuations.

19. Commitments and contingencies

a) Operating leases

The Company is committed under long-term leases for premises through 2015. One rented premise in Toronto, Canada has been sublet to an arm's-length company at an annual amount of \$39,457 from January 1, 2009 to April 30, 2013.

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

Minimum annual rentals, in aggregate and for each of the next five years, are approximately as follows:

\$US	Canada	Colombia	Guatemala	Total
2011	93,006	95,434	31,249	219,689
2012	89,405	95,434	13,021	197,860
2013	33,200	95,434	-	128,634
2014	-	95,434	-	95,434
2015	-	23,532	-	23,532
	215,611	405,268	44,270	665,149

b) Licenses

Guatemala

The Company is committed to meeting all of the conditions of its Guatemalan licenses including annual license fees, costs of mandatory training and submission of annual work plans for approval by the Ministry of Energy and Mines in Guatemala ("MEM"). Annual fees for the Guatemalan licenses and mandatory training are estimated at \$81,500 and \$62,500 per annum respectively for the next five years and over the full terms of the licenses which expire in 2019 and 2030.

Colombia

The Company is committed to meeting all of the conditions of its Colombian interests. To hold these interests, the Agencia Nacional de Hidrocarburos ("ANH") required the Company to post security in the form of letters of guarantee. The Company has fulfilled its responsibility through the issuance of five letters of guarantee that total \$7,158,883 and expire from July 4, 2012 to July 4, 2013. These letters of guarantee are secured by \$2,293,000 of guaranteed investment certificates held by the Company's bank, and by \$4,866,000 in guarantees provided by the Export Development Corporation, an agency of the Federal Government of Canada.

c) Oil distribution agreement

Quetzal Energy (Bahamas) Ltd. (formerly PetroLatina Corporation), has engaged the services of another corporation for the distribution and sale of oil and its derivatives and products. The fee for this service is 0.50 Quetzal for every gallon of these products.

d) Contingency

Immediately prior to the Company's acquisition of Quetzal Energy (Bahamas) Ltd., certain amounts due by Quetzal Energy (Bahamas) Ltd. to its former parent company were settled for no consideration. Although management has been advised that the settlement was structured so as to not incur a Guatemalan income tax liability there remains a possibility that the transaction could be challenged by the Guatemalan government. The liability is \$5.4 million. Management is of the opinion that this liability is no likely to occur, and because it cannot assess the likelihood or the amount of the liability no amount has been accrued in these condensed consolidated interim financial statements.

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

20. Segmented information

The Company operates in one segment, the oil and gas business, and has operations in Guatemala and Colombia with its head office in Canada. The geographical segmentation of the Company's assets and revenues are as follows:

As at June 30, 2011				
	Canada	Colombia	Guatemala	Total
Current assets	22,263,896	2,603,487	1,079,781	25,947,164
Restricted cash	2,451,100	-	-	2,451,100
Cash call advances	793,012	-	-	793,012
Exploration and evaluation assets	-	18,384,188	19,450,709	37,834,897
Property and equipment	273,520	178,792	4,729	457,041
Total assets	25,781,528	21,166,467	20,535,219	67,483,214
For the six months ended June 30, 2011				
Interest	57,100	14,208	2,046	73,354
Net loss	2,778,268	2,926,568	715,330	6,420,165
As at December 31, 2010				
	Canada	Colombia	Guatemala	Total
Current assets	3,004,434	4,544,131	1,517,037	9,065,602
Restricted cash	2,250,793	-	-	2,250,793
Cash call advances	-	219,551	-	219,551
Exploration and evaluation assets	-	17,340,333	14,222,814	31,563,147
Property and equipment	122,231	108,758	8,201	239,190
Total assets	5,377,458	22,212,773	15,748,052	43,338,283
For the twelve months ended December 31, 2010				
Interest	1,740	37,856	8,100	47,696
Net loss	6,088,645	681,877	1,070,490	7,841,012
As at June 30, 2010				
	Canada	Colombia	Guatemala	Total
Current assets	1,250,502	1,671,087	281,219	3,202,808
Restricted cash	4,893,716	-	-	4,893,716
Cash call advances	-	-	-	-
Exploration and evaluation assets	-	10,557,506	16,001,607	26,559,113
Other property and equipment	239,214	198,589	1,068,106	1,505,909
Total assets	6,383,432	12,427,182	17,350,932	36,161,546
For the six months ended June 30, 2010				
Interest	240	16,906	606	17,752
Net loss	2,851,568	616,731	560,719	4,029,018

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

21. Subsequent events

- a) On May 12, 2011, Quetzal announced that it had entered into a binding Letter Agreement with El Condor Minerals Inc. (TSX VENTURE: LCO) ("El Condor"), to sell Quetzal's 95% interest in its non-core Horden Lake Property, a copper-nickel property with precious metal credits located in the Province of Quebec, approximately 200 kilometers north of Mattagami, Quebec.

Under the terms of the Letter Agreement, El Condor will purchase Quetzal's 95% interest in the Horden Lake Property for a purchase price of \$5 million, comprised of \$3 million in cash including a \$100,000 non-refundable deposit that was paid on May 24, 2011, and \$2 million in common shares of El Condor. The agreement stipulates that El Condor must complete the acquisition by November 6, 2011.

- b) On May 16, 2011 Quetzal proposed a plan to distribute its Guatemalan oil and gas interests, held through a wholly-owned subsidiary, to its shareholders, subject to, among other things, TSX Venture Exchange, court, shareholder and other regulatory approvals. The plan would have resulted in the creation of a new, publicly traded company, RealPetrol Ltd. ("RealPetrol"), which would indirectly hold the Guatemalan assets. A special shareholders' meeting was held on July 19, 2011 in Calgary, Alberta to vote on the proposal, however the proposal failed to receive the number of votes required to pass. More information about this proposal is contained in the Management Information Circular that was mailed to the shareholders and posted on the Canadian Securities Administrators' website at www.sedar.com, "Sedar" on May 31, 2011.

22. First time adoption of IFRS

The Company has adopted IFRS effective January 1, 2010 (the "transition date") and has prepared its opening IFRS balance sheet as at that date. Prior to the adoption of IFRS the Company prepared its financial statements in accordance with Canadian Generally Accepted Accounting Principles ("Canadian GAAP"). The Company's consolidated financial statements for the year ending December 31, 2011 will be the first annual financial statements that comply with IFRS.

As stated in Note 2, these condensed interim consolidated financial statements represent the Company's initial presentation of the financial results of operations and financial position under IFRS for the period ended June 30, 2011 in conjunction with the Company's first annual audited consolidated financial statements to be issued under IFRS as at and for the year ended December 31, 2011 and are in accordance with IFRS 1, "First-time Adoption of International Financial Reporting Standards" and with IAS 34, "Interim Financial Reporting" as issued by the IASB.

The Company will ultimately prepare its opening IFRS balance sheet by applying existing IFRS with an effective date of December 31, 2011 or prior. Accordingly, the opening IFRS balance sheet and the December 31, 2010 comparative balance sheet presented in the consolidated financial statements for the year ending December 31, 2011 may differ from those presented at this time.

IFRS 1 requires the presentation of comparative information as at the January 1, 2010 transition date and subsequent comparative periods as well as the consistent and retrospective application of IFRS accounting policies. To assist with the transition, the provisions of IFRS 1 allow for certain mandatory and optional exemptions for first-time adopters to alleviate the retrospective application of all IFRSs. Accordingly, these condensed interim consolidated financial statements were prepared using the accounting policies stated in Note 4 and were retrospectively and consistently applied except where specific IFRS 1 optional and mandatory exemptions permitted an alternative treatment upon transition to IFRS for first-time adopters. The significant exemptions applied under IFRS 1 in preparing these condensed interim consolidated financial statements are set out below.

Deemed cost election for oil and gas properties

Under Canadian GAAP, the Company followed the "full cost accounting" method of accounting for oil and gas activities in which all costs directly associated with the acquisition of, the exploration for, and the development of oil and natural gas reserves were capitalized on a country-by-country cost centre basis ("Upstream Activities"). Costs accumulated within each country cost centre were to be depleted using the unit-of-production method

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

based on proved reserves determined using estimated future prices and costs after commercial production commenced.

Upon transition to IFRS, the Company was required to adopt new accounting policies for Upstream Activities, including exploration and evaluation costs and development costs. Under IFRS, exploration and evaluation costs are those expenditures for an area where technical feasibility and commercial viability has not yet been determined, are presented separately on the statement of financial position as exploration and evaluation assets and may or may not be amortized based on the Company's accounting policy. Development costs include those expenditures for areas where technical feasibility and commercial viability has been determined, are presented as a part of property, plant and equipment on the statement of financial position and are depleted and depreciated on an area-by-area level.

The Company adopted the IFRS 1 exemption whereby the Company deemed its January 1, 2010 IFRS upstream asset costs to be equal to its Canadian GAAP historical upstream property, plant and equipment net book value. Accordingly, exploration and evaluation costs were deemed equal to the petroleum and natural gas properties reported as at January 1, 2010, after taking into account adjustments required by IFRS for capitalized share-based payments, decommissioning liabilities and foreign currency translation.

IAS 37, Provisions, Contingent Liabilities and Contingent Assets

The Company has elected to measure decommissioning liabilities as at the Transition Date in accordance with IAS 37, "Provisions, Contingent Liabilities and Contingent Assets" ("IAS 37") and recognize directly in exploration and evaluation assets the difference between that amount and the carrying amount of those liabilities at the date of transition determined under Canadian GAAP. It is the Company's policy to capitalize the accretion associated with decommissioning liabilities.

IFRIC 4, Determining whether an Arrangement contains a Lease

The Company has elected not to reassess whether an arrangement contains a lease under IFRIC 4, "Determining whether an Arrangement contains a Lease", for contracts that were assessed under previous GAAP.

IFRS 2, Share-Based Payment

This standard has not been applied to equity settled share-based payment transactions where equity instruments were granted after November 7, 2002 but vested before January 1, 2010, the Company's transition date.

IFRS 3, Business combinations

The Company has applied the business combinations exemption in IFRS 1, such that IFRS 3, "Business Combinations" ("IFRS 3"), will not apply retrospectively to past business combinations. Accordingly, the Company has not restated business combinations that took place prior to the transition date.

IAS 21, The Effects of Changes in Foreign Exchange Rates

This standard has not been applied retrospectively with regards to calculating the foreign currency cumulative translation reserve. The foreign currency cumulative translation reserve has been set to zero on the transition date and therefore a gain or loss on subsequent disposal of a foreign operation will only include foreign exchange differences that arose subsequent to the transition date.

Estimates

The remaining IFRS 1 exceptions and exemptions were not applicable or material to the preparation of the Company's Consolidated Statement of Financial Position at the date of transition on January 1, 2010.

The following reconciliations present the adjustments made to the Company's Canadian GAAP financial results of operations and financial position to comply with IFRS 1. A summary of the significant accounting policy changes and applicable exemptions are discussed following the reconciliations. Reconciliations include the Company's consolidated statement of financial positions as at January 1, 2010, June 30, 2010 and December 31, 2010, and

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

consolidated statements of comprehensive loss, changes in Shareholders' equity and cash flows for the three months ended March 31, 2010 and for the twelve months ended December 31, 2011.

Reconciliation of the consolidated statement of financial position as at January 1, 2010

(\$US)	Note	Canadian GAAP	IFRS 1 - OCI	Share based payments	Decommission- ing liabilities	Foreign currency	IFRS
ASSETS							
Current assets							
Cash and cash equivalents		5,553,206	-	-	-	1,660	5,554,866
Guaranteed investment certificates		2,930,542	-	-	-	78	2,930,620
Amounts receivables		40,175	-	-	-	11,675	51,850
Prepaid expenses and deposits		143,768	-	-	-	(11,384)	132,384
Restricted cash - current		-	-	-	-	-	-
		8,667,691	-	-	-	2,029	8,669,720
Non-current assets							
Restricted cash		-	-	-	-	-	-
Exploration and evaluation assets	A,D,E	-	21,057,701	(2,438)	(1,624,003)	(2,945,223)	16,486,037
Petroleum and natural gas properties	A	21,057,701	(21,057,701)	-	-	-	-
Property and equipment		138,903	-	-	-	(1,691)	137,212
Total assets		29,864,295	-	(2,438)	(1,624,003)	(2,944,885)	25,292,969
LIABILITIES							
Current liabilities							
Accounts payable and accrued liabilities		1,928,262	-	-	-	4,147	1,932,409
Decommissioning liabilities	E	1,961,194	-	-	(1,624,003)	(115,977)	221,214
Deferred tax	F	1,362,000	-	-	-	(55,782)	1,306,218
		5,251,456	-	-	(1,624,003)	(167,613)	3,459,840
SHAREHOLDERS' EQUITY							
Share capital		22,016,455	-	-	-	(1)	22,016,454
Warrants		4,751,657	-	-	-	-	1,665,081
Contributed surplus	D	2,724,443	-	(30,700)	-	-	4,751,657
Obligation to issue shares		1,665,081	-	-	-	-	2,693,743
Deficit	C, D	(8,605,117)	2,060,320	28,262	-	(2,777,272)	(9,293,807)
Accumulated other comprehensive income	C	2,060,320	(2,060,320)	-	-	-	-
		24,612,839	-	(2,438)	-	(2,777,272)	21,833,128
Total Liabilities and Shareholders' Equity		29,864,295	-	(2,438)	(1,624,003)	(2,944,886)	25,292,969

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

Reconciliation of the consolidated statement of financial position as at June 30, 2010

(\$US)	Note	Canadian GAAP	IFRS 1 - OCI	Share based payments	Decommissioning liabilities	Foreign currency	IFRS
ASSETS							
Current assets							
Cash and cash equivalents		1,111,190	-	-	-	-	1,111,190
Amounts receivables		374,519	-	-	-	(29,286)	345,235
Prepaid expenses and deposits		230,984	-	-	-	29,343	260,327
		1,716,693	-	-	-	57	1,716,750
Non-current assets							
Restricted cash		4,893,716	-	-	-	-	4,893,716
Cash call advances		1,487,102	-	-	-	(1,044)	1,486,058
Exploration and evaluation assets	A,D,E	-	31,781,741	(8,856)	(1,758,802)	(3,454,969)	26,559,113
Petroleum and natural gas properties	A	32,836,833	(32,836,833)	-	-	-	-
Property and equipment		351,878	1,055,092	-	-	98,939	1,505,909
Total assets		41,286,222	-	(8,856)	(1,758,802)	(3,357,018)	36,161,546
LIABILITIES							
Current liabilities							
Accounts payable and accrued liabilities		5,445,712	-	-	-	326,207	5,771,919
Decommissioning liabilities	E	2,044,623	-	-	(1,758,802)	(60,254)	225,567
Future income tax	F	3,047,923	-	-	-	(1,129,271)	1,918,652
		10,538,258	-	-	(1,758,802)	(863,318)	7,916,138
SHAREHOLDERS' EQUITY							
Share capital		29,029,719	-	-	-	(2,449,400)	26,580,319
Warrants		7,215,572	-	-	-	-	7,215,572
Contributed surplus	D	3,133,417	-	(112,543)	-	(6,244)	3,014,630
Obligation to issue shares		498,078	-	-	-	-	498,078
Deficit	C, D	(10,698,237)	2,060,320	103,687	-	(4,855,294)	(13,389,524)
Accumulated other comprehensive income	C	1,569,414	(2,060,320)	-	-	4,817,239	4,326,333
		30,747,963	-	(8,856)	-	(2,493,699)	28,245,408
Total Liabilities and Shareholders' Equity		41,286,222	-	(8,856)	(1,758,802)	(3,357,018)	36,161,546

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

Reconciliation of the consolidated statement of financial position as at December 31, 2010

(\$US)	Note	Canadian GAAP	IFRS 1 - OCI	Share-based payments	Decommissi- -oning liabilities	Foreign currency	IFRS
ASSETS							
Current assets							
Cash and cash equivalents		3,861,000	-	-	-	(9,294)	3,851,706
Guaranteed investment certificates		-	-	-	-	-	-
Amounts receivables		3,724,175	-	-	-	(61,876)	3,662,300
Prepaid expenses and deposits		324,581	-	-	-	7,263	331,843
Restricted cash - current		1,234,829	-	-	-	(15,076)	1,219,753
		9,144,585	-	-	-	(78,983)	9,065,602
Non-current assets							
Restricted cash		2,323,166	-	-	-	(72,373)	2,250,793
Cash call advances		222,265	-	-	-	(2,714)	219,551
Exploration and evaluation assets	A,D,E	-	36,033,641	(8,838)	(354,999)	(4,106,657)	31,563,147
Petroleum and natural gas properties	A	36,033,641	(36,033,641)	-	-	-	-
Property and equipment		239,170	-	-	-	20	239,190
Total assets		47,962,827	-	(8,838)	(354,999)	(4,260,707)	43,338,283
LIABILITIES							
Current liabilities							
Accounts payable and accrued liabilities		7,553,844	-	-	-	(67,216)	7,486,628
Decommissioning liabilities	E	1,018,372	-	-	(354,999)	-	663,373
Deferred tax	F	597,460	-	-	-	2,831	600,291
		9,169,676	-	-	(354,999)	(64,385)	8,750,292
SHAREHOLDERS' EQUITY							
Share capital		33,660,649	-	-	-	24	33,660,673
Warrants		12,372,554	-	-	-	-	12,372,554
Contributed surplus	D	3,827,170	-	(263,652)	-	(1)	3,563,517
Deficit	C, D	(14,225,381)	2,060,320	254,814	-	(5,064,720)	(17,201,519)
Accumulated other comprehensive income	C	3,158,159	(2,060,320)	-	-	1,094,927	2,192,766
		38,793,151	-	(8,838)	-	4,196,323	34,587,991
Total Liabilities and Shareholders' Equity		47,962,827	-	(8,838)	(354,999)	(4,260,707)	43,338,283

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

Reconciliation of the consolidated statement of comprehensive loss for the three months ended June 30, 2010

(\$US)	Note	Canadian GAAP	Share based payments	Foreign Currency	IFRS
Revenue					
Interest		17,164	-	(1,321)	15,843
		17,164	-	(1,321)	15,843
Expenses					
General and administrative		1,142,016	-	(23,470)	1,118,546
Share-based payments	D	153,686	(31,356)	(53,293)	69,037
Foreign exchange gain		(73,104)	-	746,598	673,494
Depreciation		14,719	-	4,412	19,131
		1,237,317	(31,356)	674,247	1,880,208
Net loss before income tax		(1,220,153)	31,356	(675,568)	(1,864,365)
Recovery of future income taxes	F	269,723	-	(789,581)	(519,858)
Net loss for the period		(950,430)	31,356	(1,465,149)	(2,384,223)
Other comprehensive income		(1,259,233)	-	4,991,840	3,732,607
Comprehensive income (loss)		(2,209,663)	31,356	3,526,691	1,348,384

Reconciliation of the consolidated statement of comprehensive loss for the six months ended June 30, 2010

(\$US)	Note	Canadian GAAP	Share based payments	Foreign Currency	IFRS
Revenue					
Interest		18,989	-	(1,237)	17,752
		18,989	-	(1,237)	17,752
Expenses					
General and administrative		2,004,104	-	31,753	2,035,857
Share-based payments	D	374,031	(75,425)	(42,774)	255,832
Foreign exchange gain		(17,912)	-	1,232,157	1,214,245
Depreciation		21,609	-	(631)	20,978
		2,381,832	(75,425)	1,220,505	3,526,912
Net loss before income tax		(2,362,843)	75,425	(1,221,742)	(3,509,160)
Recovery of future income taxes	F	269,723	-	(789,581)	(519,858)
Net loss for the period		(2,093,120)	75,425	(2,011,323)	(4,029,018)
Unrealized foreign currency translation loss on translation to presentation currency		(490,906)	-	5,315,317	4,824,411
Comprehensive income (loss)		(2,584,026)	75,425	3,303,994	795,393

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

Reconciliation of the consolidated statement of comprehensive loss for the year ended December 31, 2010

(\$US)	Note	Canadian GAAP	Share based payments	Foreign Currency	IFRS
Revenue					
Interest		67,045	-	(19,349)	47,696
Expenses					
General and administrative		5,762,744	-	673,827	6,436,571
Share-based payments	D	1,139,190	(226,552)	36,702	949,340
Foreign exchange gain		(498,579)	-	1,680,677	1,182,098
Depreciation		70,739	-	(13,500)	57,239
		6,474,094	(226,552)	2,377,706	8,625,248
Net loss before income tax		(6,407,049)	226,552	(2,397,055)	(8,557,552)
Recovery of future income taxes	F	786,785	-	(50,245)	736,540
Net loss for the period		(5,620,264)	226,552	(2,447,300)	(7,841,012)
Unrealized foreign currency translation loss on translation to presentation currency		1,097,839	-	1,097,839	2,192,766
Comprehensive loss		(4,522,425)	226,552	(1,352,373)	(5,648,246)

Restatement of the consolidated statement of cash flows for the periods ended June 30, 2010 and December 31, 2010

The restatement from Canadian GAAP to IFRS had no significant effect on the reported cash flows generated by the Company. The reconciling items between Canadian GAAP presentation and IFRS have no effect on the cash flows generated.

IFRS Adjustments

The following discussions explain the significant differences between the Company's Canadian GAAP accounting policies and those applied by the Company under IFRS. IFRS policies have been retrospectively and consistently applied, except where specific IFRS 1 optional and mandatory exemptions permitted an alternative treatment upon transition to IFRS for first-time adopters. The descriptive note captions below correspond to the adjustments presented in the preceding reconciliations.

A. Exploration and evaluation assets

As explained above under "Deemed cost election for oil and gas properties", the company reclassified \$21,057,701, \$32,836,833 and \$36,033,641 to exploration and evaluation assets at January 1, 2010, June 30, 2010 and December 31, 2010, respectively, based on the deemed carrying amounts representing unproved properties balance as determined under previous GAAP.

Impairment

Under Canadian GAAP, capitalized costs of oil and gas properties were tested for impairment separately as explained below. Under IFRS, capitalized costs of oil and gas properties are allocated to cash-generating units ("CGU") for the purpose of impairment test as explained below.

Under Canadian GAAP, oil and gas properties impairment was recognized if the carrying amount exceeded the undiscounted cash flows from proved reserves for a country cost centre. Impairment was measured as the amount by which the carrying value exceeded the sum of the fair value of the proved and probable reserves

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

and the costs of unproved properties. The Company did not report any impairment under Canadian GAAP for the year ended December 31, 2010.

Under IFRS, impairment is recognized if the carrying value exceeds the recoverable amount for a CGU. A CGU is defined as the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or group of assets. If the carrying value of the CGU exceeds the recoverable amount, the CGU is written down with an impairment recognized in income. Recoverable amount is determined as higher of value in use and fair value less cost to sell where value in use is the present value of the future cash flows expected to be derived from a CGU and fair value less cost to sell is the estimated amount obtainable from the sale of the CGU in an arm's length transaction between knowledgeable willing parties, less cost of disposal.

The Company did not report any impairment as a result of the application of IFRS as at January 1, 2010.

B. Asset and Liabilities Held For Sale ("AHFS") and disposition of Oil and Gas Properties

Under Canadian GAAP, proceeds from disposition of oil and gas properties were deducted from the full cost pool without recognition of a gain or loss and the accounting standard for classification of AHFS was not applicable to the disposition of oil and gas properties unless the deduction resulted in a change to the country cost centre depletion rate of 20 percent or greater, in which case a gain or loss was recorded and assets and liabilities were classified as held for sale.

Under IFRS, gains or losses are recorded on dispositions and calculated as the difference between the proceeds and the net book value of the asset disposed and the requirements of the classification of AHFS are applicable to all oil and gas properties. No adjustment was reported from the conversion to IFRS.

C. Foreign Currency

In accordance with IFRS 1, the Company has elected to deem all foreign currency translation differences that arose prior to the transition date in respect of foreign operations and the company's share of associate's translation differences to be nil and reclassified amounts recorded in other comprehensive loss as determined in accordance with previous GAAP to retained earnings. As a result, accumulated other comprehensive income was decreased by \$2,060,320 with a corresponding decrease to the deficit as at January 1, 2010.

D. Compensation

Share-based payments

In accordance with IFRS 1, the Company has elected to apply the requirements of IFRS 2 "share-based payment" to those equity instruments that were issued after November 7, 2002 but that had not vested as of January 1, 2010 and liabilities awards that will be settled after the Transition Date. The Company currently has one equity compensation plan.

Employee Stock Option Plan

Canadian GAAP allowed the Company to choose an accounting policy of recording the estimate of forfeiture either on the date of the grant or by recording in a period when the forfeiture actually occurs. The Company had the accounting policy of recording forfeitures in the period when they occur. IFRS requires entities to measure the estimate of forfeiture at the time of grant. As a result, share-based compensation expense and property and equipment were decreased with a corresponding decrease to contributed surplus.

E. Provisions

Under Canadian GAAP, the decommissioning liability was measured at the estimated fair value of the retirement and decommissioning expenditures expected to be incurred. Liabilities were not recalculated to reflect period end discount rates. Under IFRS, the decommissioning liability is measured as the best estimate of the expenditure to be incurred and requires that the liability be re-measured at each reporting period using the period end discount rate.

Quetzal Energy Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
For the period ended June 30, 2011

(Expressed in U.S. dollars, unless otherwise noted)

In conjunction with the IFRS 1 exemption regarding oil and gas properties discussed above, the Company was required to re-measure its decommissioning liability upon transition to IFRS and recognize the difference in deficit. The application of this exemption resulted in a \$1,624,003 decrease to the decommissioning liability on the Company's consolidated statement of financial position as at January 1, 2010 and a corresponding reduction to the exploration and evaluation assets. Subsequent IFRS remeasurements of the obligation are recorded through property and equipment with an offsetting adjustment to the decommissioning liability. As at June 30, 2010 and December 31, 2010, the Company's decommissioning liability decreased by \$1,758,802 and \$354,999, respectively

F. Taxes

The Company recorded the following differences to the amounts reported as deferred tax under Canadian GAAP compared to IFRS.

IFRS provides an exemption whereby deferred tax on temporary differences is not required to be recorded for an item which is not a business combination, and at the time of the transaction, neither affects accounting or taxable income. The Company elected to use this exemption and accordingly, reversed the previously recognized deferred income tax asset and liability with respect to the above items with corresponding reductions to deficit.

Inter-company capital losses

An adjustment to recognize the deferred tax benefit on an intercompany capital loss was recorded under IFRS which was not permitted under Canadian GAAP, net of any unrealized foreign exchange gain or loss on long-term debt.

Current vs. Non-current classification

Under IFRS, all deferred taxes are classified as non-current, irrespective of the classification of the underlying assets or liabilities to which they relate, or the expected reversal of the temporary difference.

G. Loss per share

Basic and diluted loss per share under IFRS was impacted by the IFRS loss adjustments discussed above.