



Q1/10

## MAY 4, 2010 — FAIRBORNE ENERGY LTD. — FIRST QUARTER INTERIM REPORT AND NEWS RELEASE

## HIGHLIGHTS

	Three months ended March 31,		
	2010	2009	CHANGE
<b>Financial</b> ( <i>\$ thousands, except per share amounts</i> )			
Petroleum and natural gas revenue	<b>63,382</b>	68,545	(8%)
Funds generated from operations <sup>(1)</sup>	<b>39,555</b>	32,970	20%
Per share – basic	<b>\$0.39</b>	\$0.38	3%
Per share – diluted	<b>\$0.38</b>	\$0.38	–
Cash flow from operations (including changes in working capital)	<b>43,522</b>	34,782	25%
Per share – basic	<b>\$0.42</b>	\$0.40	5%
Per share – diluted	<b>\$0.42</b>	\$0.40	5%
Net income (loss)	<b>3,809</b>	(4,691)	181%
Per share – basic	<b>\$0.04</b>	\$(0.05)	180%
Per share – diluted	<b>\$0.04</b>	\$(0.05)	180%
Exploration and development expenditures	<b>65,546</b>	52,645	25%
Acquisitions, net of dispositions	<b>1,464</b>	–	–
Working capital deficit	<b>34,611</b>	31,641	9%
Bank indebtedness	<b>102,536</b>	209,925	(51%)
Convertible debentures	<b>96,993</b>	95,024	2%
<b>Operations</b> ( <i>Units as noted</i> )			
Average production			
Natural gas ( <i>Mcf per day</i> )	<b>60,878</b>	67,520	(10%)
Crude oil ( <i>bbls per day</i> )	<b>3,000</b>	3,599	(17%)
Natural gas liquids ( <i>bbls per day</i> )	<b>686</b>	572	20%
Sulphur ( <i>tonnes per day</i> ) <sup>(2),(4)</sup>	<b>54</b>	93	(42%)
Total ( <i>BOE per day</i> )	<b>13,886</b>	15,517	(11%)
Average sales price <sup>(3)</sup>			
Natural gas ( <i>\$ per Mcf</i> )	<b>5.75</b>	6.39	(10%)
Crude oil ( <i>\$ per bbl</i> )	<b>79.24</b>	56.98	39%
Natural gas liquids ( <i>\$ per bbl</i> )	<b>48.71</b>	27.24	79%
Sulphur ( <i>\$ per tonne</i> ) <sup>(4)</sup>	–	185.15	–
Netback per BOE ( <i>\$ per BOE</i> )			
Petroleum and natural gas sales <sup>(3)</sup>	<b>44.97</b>	43.35	4%
Sulphur block revenue	<b>5.57</b>	3.83	45%
Royalties	<b>(4.43)</b>	(5.78)	(23%)
Operating expenses	<b>(8.82)</b>	(12.47)	(29%)
Transportation	<b>(1.03)</b>	(1.14)	(10%)
Operating netback	<b>36.26</b>	27.79	30%
Wells drilled ( <i>gross</i> )	<b>16</b>	16	–
Undeveloped land ( <i>net acres</i> )	<b>229,270</b>	222,936	3%

1) Funds generated from operations is calculated using cash flow from operations as presented in the consolidated statement of cash flows before non-cash working capital and asset retirement expenditures.

2) A BOE conversion ratio has been calculated using a conversion rate of one tonne of sulphur to one barrel.

3) Excludes the change in fair value of derivatives.

4) Excludes the sale of inventory at the West Pembina sulphur block.



*Message to Shareholders***STRATEGIC CAPITAL SPENDING INITIATES PERFORMANCE GROWTH FOR 2010**

In the first quarter of 2010, Fairborne executed a focused capital program which resulted in exit production of 15,500 BOE per day, up 14% from fourth quarter average production of 13,542 BOE per day. First quarter drilling included the development of light crude oil properties at Sinclair and Brazeau and the liquid rich natural gas properties at Harlech and Westerose, as well as the continued successful development of the natural gas Wilrich play in Marlboro. The initial impact of the successful capital program was reflected in first quarter financial and operating results which included:

- Exit production of 15,500 BOE per day at the end of the quarter (68 MMcf per day of natural gas, 4,200 bbls per day of light oil and NGL's);
- First quarter average production of 13,886 BOE per day (61 MMcf per day of natural gas, 3,686 bbls per day of light oil and NGL's), up 3% from fourth quarter 2009 production of 13,542 BOE per day;
- Capital expenditures of \$67 million, including \$11.2 million on land and seismic and \$43.9 million on drilling and completions activities;
- Drilling program of 16 (12.8 net) wells including four (3.6 net) oil wells at Sinclair; three (2.5 net) liquid rich natural gas wells at Harlech; the first (0.9 net) horizontal oil well in Brazeau, two (1.7 net) horizontal gas wells in Marlboro and two (2.0 net) horizontal wells at Westerose;
- Funds generated from operations of \$39.6 million (\$0.39 per share), 20% higher than the first quarter of 2009 (\$33.0 million);
- Operating netback of \$36.26 per BOE with operating costs of \$8.82 per BOE;
- Above-average realized natural gas prices with 42% of first quarter natural gas production hedged at an average price of \$6.59 per Mcf.
- 34% of natural gas production hedged for the balance of 2010 at an average price of \$6.58 per Mcf.
- The Company has received approval from its banking syndicate to maintain its borrowing base at the current level of \$285 million.

**PRODUCTION AND OPERATING RESULTS**

Fairborne's first quarter drilling program resulted in 16 (12.8 net) new wells, the majority of which were brought on production during the month of March for first quarter exit production of 15,500 BOE per day. Current production remains consistent between 15,500 and 16,000 BOE per day, with approximately 68 MMcf per day of natural gas and 4,200 bbls per day of crude oil and natural gas liquids. With the majority of additional production commencing at the end of the quarter, first quarter average production of 13,886 BOE per day was 3% higher than fourth quarter 2009 production of 13,542 BOE per day.

The benefits of cost reduction initiatives which began in 2009 were sustained through the first quarter of 2010 with operating costs of \$8.82 per BOE and an operating netback of \$36.26 per BOE. Funds generated from operations of \$39.6 million were used to partially fund the first quarter capital expenditure program of \$67 million with the balance of spending funded from working capital, leaving \$148 million of available credit (net of working capital) at the end of the quarter. With spring break-up, second quarter capital spending is expected to be approximately \$12 million.

**FOCUSED ASSET DEVELOPMENT**

Fairborne's first quarter capital program was focused on the continued advancement of emerging plays and the development of identified projects within the Company's asset base which could provide the greatest return in light

*Message to Shareholders*

of current market conditions. Based on the continuation of low natural gas prices, a portion of first quarter capital spending was allocated to crude oil and liquid rich natural gas properties to help maintain strong netbacks and stable cash flow.

- **Sinclair:** Ongoing development of the high netback Sinclair oil property through drilling of four wells (3.6 net) and continued implementation of the successful waterflood pilot project. Additional wells and waterflood expansion are planned for the remainder of 2010.
- **Brazeau:** In the Brazeau Belly River Unit 6, Fairborne drilled, completed, and brought on production one (0.9 net) horizontal well during the first quarter. This well has been on production for approximately 30 days and produces at a stabilized rate of 200 barrels per day of 42° API oil. The Company has identified a number of follow up locations in the Unit and Fairborne is planning to drill up to three (2.7 net) additional wells during the remainder of 2010.
- **Marlboro:** Fairborne continued the development of the Wilrich play on its Marlboro property with two (1.7 net) successful horizontal wells drilled and completed prior to spring breakup. A third well was drilling at the end of the first quarter and will be completed in late June or early July 2010. Concurrently, a compression expansion project was completed, and with the first quarter drilling, has resulted in sales gas increasing from 20 MMcf per day (12 MMcf per day net) at the beginning of January 2010 to 31 MMcf per day (21 MMcf per day net). The Company plans to drill up to nine additional Wilrich horizontal wells in the second half of 2010. Fairborne has continued to grow its land position on the Wilrich fairway and currently controls 83.1 (59.2 net) sections.
- **Harlech:** Fairborne continues to develop the Harlech area targeting multizone vertical wells. The zones targeted (Viking, Mannville, Glauconite and Gething) result in liquid rich natural gas and condensate production. During the first quarter, Fairborne drilled three (2.5 net) vertical wells with combined incremental production of 5.1 MMcf per day and 325 bbls per day of condensate and natural gas liquids, providing netbacks in excess of \$30 per BOE. The Company plans to drill up to three additional wells in the second half of 2010.

**OUTLOOK**

We are pleased with the results we have achieved in the first four months of 2010. Although natural gas prices continue to remain weak, we have assembled a diverse portfolio of assets that allow us the opportunity to react to market conditions and re-allocate our spending in order to maintain high operating netbacks and achieve strong cash flows. Our success over the past few months has provided a significant increase in production at the end of the first quarter. Moving forward in 2010, cash flow from operations will benefit from increased production levels as well as our risk management program with 34% of natural gas production for the balance of 2010 hedged at an average price of \$6.58 per Mcf. We continue to exercise financial discipline to maintain a strong balance sheet and ensure we have the financial flexibility to take advantage of growth opportunities as they arise.



**Steven R. VanSickle**

President & CEO

May 3, 2010



*Interim Management's Discussion & Analysis***MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following Management Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") was prepared at, and is dated, May 3, 2010. This document is provided by the management of Fairborne Energy Ltd. ("Fairborne" or the "Company") to review first quarter 2010 activities and results as compared to the same period in the previous year, and should be read in conjunction with the unaudited interim consolidated financial statements including selected notes for the three months ended March 31, 2010 and the audited consolidated financial statements including notes for the years ended December 31, 2009 and 2008. The MD&A should be read in conjunction with the Company's MD&A for the year ended December 31, 2009, as disclosure which is unchanged from the December 31, 2009 MD&A has not been duplicated herein. Additional information relating to Fairborne, including Fairborne's annual information form, is available on SEDAR at [www.sedar.com](http://www.sedar.com)

**Nature of Business:** Fairborne is a growth-oriented exploration and production company. The Company maintains its head office in Calgary and is engaged in the business of exploring for, developing, acquiring and producing crude oil and natural gas in Western Canada. Fairborne follows a strategy of balancing risk and reward by focusing on opportunities by geographic area and prospect type. Within the selected areas, the Company develops a portfolio of exploration and development prospects in conjunction with an active acquisition strategy. Fairborne resulted from the reorganization of Fairborne Energy Trust (the "Trust") on December 19, 2007 (the "Reorganization").

**Forward Looking Statements:** This document contains forward-looking statements. Management's assessment of future plans and operations, drilling plans and the timing thereof, plans for the tie in and completion of wells and the timing thereof, budgeted quarterly capital expenditures and 2010 budgeted capital expenditures and the method of funding thereof and the nature of the expenditures may constitute forward-looking statements under applicable securities laws and necessarily involve risks including, without limitation, risks associated with oil and gas exploration, development, exploitation, production, marketing and transportation, loss of markets, volatility of commodity prices, currency fluctuations, imprecision of reserve estimates, environmental risks, competition from other producers, inability to retain drilling rigs and other services, incorrect assessment of the value of acquisitions, failure to realize the anticipated benefits of acquisitions, the inability to fully realize the benefits of the acquisitions, delays resulting from or inability to obtain required regulatory approvals and ability to access sufficient capital from internal and external sources. As a consequence, the Company's actual results may differ materially from those expressed in, or implied by, the forward looking statements. Forward looking statements or information are based on a number of factors and assumptions which have been used to develop such statements and information but which may prove to be incorrect. Although Fairborne believes that the expectations reflected in such forward-looking statements or information are reasonable, undue reliance should not be placed on forward looking statements because the Company can give no assurance that such expectations will prove to be correct. In addition to other factors and assumptions which may be identified in this document and other documents filed by the Company, assumptions have been made regarding, among other things: the impact of increasing competition; the general stability of the economic and political environment in which Fairborne operates; the ability of the Company to obtain qualified staff; equipment and services in a timely and cost efficient manner; drilling results; the ability of the operator of the projects which the Company has an interest in to operate the field in a safe, efficient and effective manner; Fairborne's ability to obtain financing on acceptable terms; field production rates and decline rates; the ability to replace and expand oil and natural gas reserves through acquisition, development or exploration; the timing and costs of pipeline, storage and facility construction and expansion; the ability of the Company to secure adequate product transportation; future oil and natural gas prices; currency, exchange and interest rates; the regulatory framework regarding royalties, taxes and environmental matters in the jurisdictions in which the Company operates; and Fairborne's ability to successfully market its oil and natural gas products. Readers are cautioned that the foregoing list of factors is not exhaustive. Additional information on these and other factors that could affect the Company's operations and financial results are included in reports on file with Canadian securities regulatory authorities and may be accessed through the SEDAR website ([www.sedar.com](http://www.sedar.com)) or at the Company's website ([www.fairborne-energy.com](http://www.fairborne-energy.com)).

Furthermore, the forward looking statements contained in this document are made as at the date of this document and the Company does not undertake any obligation to update publicly or to revise any of the included forward looking statements, whether as a result of new information, future events or otherwise, except as may be required by applicable securities laws.

**Non GAAP Terms:** This document contains the terms "funds generated from operations", "funds generated from operations per share", "cash flow from operations per share", "net debt" and "netbacks" which are non-GAAP terms. The Company uses these measures to help evaluate its performance. The Company uses net debt (bank indebtedness plus negative working capital or less positive working capital) as an alternative measure of outstanding debt. The Company considers corporate netbacks a key measure as it demonstrates its profitability relative to current commodity prices. Netbacks, which have no GAAP equivalent, are calculated on a BOE basis by deducting royalties, operating costs, and transportation from petroleum and natural gas sales and sulphur block sales. The Company considers funds generated from operations a key measure as it demonstrates Fairborne's ability to generate funds necessary to repay debt and to fund future growth through capital investment. Funds generated from operations should not be considered as an alternative to, or more meaningful than, cash flow from operating activities as determined in accordance with Canadian GAAP as an indicator of Fairborne's performance. Fairborne's determination of funds generated from operations may not be comparable to that reported by other companies. The reconciliation between cash flow from operations and funds generated from operations can be found in the statement of cash flows in the consolidated financial statements with funds generated from operations calculated before non-cash working capital and asset retirement expenditures. Fairborne also presents funds generated from operations per share and cash flow from operations per share whereby per share amounts are calculated using weighted average shares outstanding consistent with the calculation of income per share.

**BOE Conversions:** Barrel of oil equivalent ("BOE") amounts may be misleading, particularly if used in isolation. A BOE conversion ratio has been calculated using a conversion rate of one tonne of sulphur to one barrel and six thousand cubic feet of natural gas to one barrel. This conversion ratio of six thousand cubic feet of natural gas to one barrel is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

*Interim Management's Discussion & Analysis***FIRST QUARTER 2010 FINANCIAL RESULTS****Production**

	Three months ended March 31,		
	2010	2009	CHANGE
Natural gas ( <i>Mcf per day</i> )	<b>60,878</b>	67,520	(10%)
Crude oil ( <i>bbls per day</i> )	<b>3,000</b>	3,599	(17%)
Natural gas liquids ( <i>bbls per day</i> )	<b>686</b>	572	20%
Sulphur ( <i>tonnes per day</i> ) <sup>(1),(2)</sup>	<b>54</b>	93	(42%)
Total ( <i>BOE per day</i> )	<b>13,886</b>	15,517	(11%)
Natural gas % of production	<b>73%</b>	73%	–

1) A BOE conversion ratio has been calculated using a conversion rate of one tonne of sulphur to one barrel.

2) Excludes the sale of inventory at the West Pembina sulphur block.

Fairborne's first quarter drilling program resulted in an increase in production to approximately 15,500 BOE per day at the end of the quarter; however the majority of the additional production was not added until late in the first quarter. Fairborne reported average production of 13,886 BOE per day for the first quarter of 2010, a 3% increase from the preceding fourth quarter of 2009 (13,542 BOE per day), and 11% lower than the comparative first quarter of 2009 (15,517 BOE per day).

Natural gas production of 60.9 MMcf per day during the first quarter of 2010 was 3% higher than the preceding fourth quarter of 2009 (59.1 MMcf per day) reflecting the Company's successful drilling program on its Harlech and Marlboro properties in the first quarter of 2010. Compared to the first quarter of 2009, natural gas production decreased 10% as a result of natural declines and property dispositions completed in the second half of 2009.

Crude oil and NGL production of 3,686 bbls per day for the first quarter of 2010 was consistent with the preceding fourth quarter of 2009 (3,654 BOE per day). The 12% decrease from the comparative first quarter of 2009 (4,171 BOE per day) was primarily attributed to natural declines; however, current oil and NGL production has increased to 4,200 bbls per day.

**Commodity Prices & Risk Management Activities**

	Three months ended March 31,		
	2010	2009	CHANGE
<b>Average prices</b> <sup>(1)</sup>			
Natural gas ( <i>\$ per Mcf</i> )	<b>5.75</b>	6.39	(10%)
Crude oil ( <i>\$ per bbl</i> )	<b>79.24</b>	56.98	39%
Natural gas liquids ( <i>\$ per bbl</i> )	<b>48.71</b>	27.24	79%
Sulphur ( <i>\$ per tonne</i> ) <sup>(2)</sup>	–	185.15	–
BOE ( <i>\$ per BOE</i> )	<b>44.64</b>	43.13	4%
<b>Benchmark prices</b>			
AECO Daily Index ( <i>Cdn\$ per Mcf</i> )	<b>4.95</b>	4.92	1%
AECO Monthly Index ( <i>Cdn\$ per Mcf</i> )	<b>5.36</b>	5.63	(5%)
Edmonton Par ( <i>Cdn\$ per bbl</i> )	<b>80.31</b>	48.23	67%
Nymex Calendar Average ( <i>US\$ per bbl</i> )	<b>78.71</b>	43.08	83%

1) Excludes the change in fair value of derivatives.

2) Excludes revenue from the sale of inventory at the West Pembina sulphur block.



*Interim Management's Discussion & Analysis***Risk Management – Physical Sales Contracts**

Fairborne's risk management strategy is based on the following objectives:

- protect shareholder return on investment;
- reduce risk exposure in budgeted annual funds flow projections; and
- help ensure transaction economics on acquisitions.

**NATURAL GAS**

Although natural gas prices during the first quarter of 2010 were approximately 9% higher than average prices in the fourth quarter of 2009, spot prices were comparable to the first quarter of 2009. Fairborne's first quarter realized prices were 16% higher than the AECO Daily benchmark reference price due to 2010 corporate hedging activities and the higher heat content of Fairborne's production. However, Fairborne's realized natural gas prices were 10% lower than the average price received during the comparative first quarter in the prior year as a result of lower hedge prices in 2010. An average of 25,847 Mcf per day was sold under fixed price physical sales contracts during the first quarter of 2010 representing 42% of the Company's natural gas production. Risk management activities during the first three months of 2010 increased the Company's natural gas revenue by \$3.2 million which had an effect of increasing Fairborne's realized natural gas price by \$0.58 per Mcf to \$5.75 per Mcf.

The following table summarizes the outstanding fixed price physical sales and derivative contracts for natural gas, including contracts outstanding at March 31, 2010 as well as contracts entered into after March 31, 2010:

	2010		
	Q2	Q3	Q4
Swaps			
Volume ( <i>Mcf per day</i> )	21,153	24,754	24,754
Average price ( <i>\$ per Mcf</i> )	6.61	6.57	6.57

*Conversion factor: 1 Mcf = 1.11 GJ*

**CRUDE OIL**

During the first quarter of 2010, Fairborne had an average of 1,500 bbls per day of crude oil under fixed price physical sales contracts representing 50% of crude oil production. Crude oil prices during the first quarter of 2010 showed a significant recovery when compared to the same quarter in 2009. The Company's realized crude oil price of \$79.24 per bbl for the first quarter of 2010 represented an increase of 39% from the same period in 2009, reflecting the overall increase in average market prices.

The following table summarizes the outstanding fixed price physical sales and derivative contracts on crude oil, including contracts outstanding at March 31, 2010 as well as contracts entered into after March 31, 2010:

	2010		
	Q2	Q3	Q4
Collars			
Volume ( <i>bbls per day</i> )	1,500	1,500	1,500
Average floor price ( <i>CDN\$ per bbl</i> )	60.00	60.00	60.00
Average ceiling price ( <i>CDN\$ per bbl</i> )	103.72	103.72	103.72

At March 31, 2010, Fairborne had two crude oil collars that were accounted for as derivative contracts and the combined mark-to-market value of these contracts was recorded as a liability of \$137,000 at March 31, 2010.

*Interim Management's Discussion & Analysis*

## SULPHUR

Sulphur prices significantly decreased during the fourth quarter of 2009 and continued to decrease during the first quarter of 2010. As a result, the Company did not record any revenue on its sulphur production during the first quarter of 2010. Sulphur prices have begun to recover in the second quarter and Fairborne has started receiving revenue for its sulphur production.

**Petroleum and Natural Gas Revenue**

(\$thousands except as noted)	Three months ended March 31,		
	2010	2009	CHANGE
Petroleum and natural gas sales:			
Natural gas	<b>31,495</b>	38,836	(19%)
Crude oil	<b>21,397</b>	18,453	16%
Natural gas liquids	<b>3,005</b>	1,403	114%
Sulphur	<b>(114)</b>	1,545	(107%)
Total	<b>55,783</b>	60,237	(7%)
Per BOE	<b>\$44.64</b>	\$43.13	4%
Other revenue items:			
Sulphur block	<b>6,959</b>	5,353	30%
Change in fair value of derivatives	<b>222</b>	2,643	(92%)
Other income	<b>418</b>	312	34%
Total	<b>7,599</b>	8,308	(9%)
Total petroleum and natural gas revenue	<b>63,382</b>	68,545	(8%)
Per BOE	<b>\$50.72</b>	\$49.08	3%

Fairborne reported petroleum and natural gas revenue of \$63.4 million for the first quarter of 2010, representing a 9% increase from the immediately preceding fourth quarter of 2009 (\$58.3 million) and a 8% decrease from the \$68.5 million reported in the first quarter of 2009. Compared to the preceding fourth quarter of 2009, first quarter 2010 petroleum and natural gas sales reflected stronger commodity prices as well as increased production. When compared to the first quarter of 2009, first quarter 2010 petroleum and natural gas sales reflected comparable natural gas prices and higher crude oil prices but lower production.

During the first quarter of 2010, Fairborne received payments of US\$6.1 million pursuant to the existing contract for the sale of the Company's share of inventory at the West Pembina sulphur block. The sulphur block contract was completed during the first quarter, with no further payments owing to Fairborne. At March 31, 2010, \$3.6 million was recorded as deferred revenue representing the payments received to date in excess of the volumes removed by the purchaser. The Company expects the purchaser to take delivery of the remaining sulphur volumes during the second quarter.

The change in fair value of derivatives represents the change in the mark-to-market value of derivatives during 2010. The \$0.2 million increase recorded in the first quarter of 2010 (2009 – \$2.6 million) reflects both the changes in the unrealized value of existing contracts as well as a reduction for amounts realized on contracts that settled during the period. Fairborne's risk management program, including derivative contracts and physical sales contracts, increased the Company's realized revenue by an estimated \$3.2 million in the first quarter of 2010.



*Interim Management's Discussion & Analysis***Royalties**

<i>(\$thousands except as noted)</i>	Three months ended March 31,		
	<b>2010</b>	2009	CHANGE
Crown	<b>3,636</b>	6,357	(43%)
Freehold and overriding	<b>1,898</b>	1,716	11%
Total	<b>5,534</b>	8,073	(31%)
Crown <i>(% of P&amp;NG sales)</i>	<b>6.5%</b>	10.6%	(39%)
Freehold and overriding <i>(% of P&amp;NG sales)</i>	<b>3.4%</b>	2.8%	21%
Total <i>(% of P&amp;NG sales)</i>	<b>9.9%</b>	13.4%	(26%)
Per BOE	<b>\$4.43</b>	\$5.78	(23%)

Fairborne recorded \$5.5 million of royalties for the first quarter of 2010, representing a royalty rate of 9.9%, a 26% decrease from 13.4% recorded in the first quarter of 2009. Fairborne's risk management program increases natural gas revenues resulting in higher realized prices than the prices utilized in calculating royalties which is reflected in a lower royalty rate for both years. Other factors contributing to the reduced effective royalty rate in 2010 are increased deductions for allowable operating costs and gas cost allowance which began in the second half of 2009.

**Operating Costs**

<i>(\$thousands except as noted)</i>	Three months ended March 31,		
	<b>2010</b>	2009	CHANGE
Operating costs			
Natural gas	<b>8,173</b>	12,472	(34%)
Oil and NGLs	<b>2,852</b>	4,932	(42%)
Total	<b>11,025</b>	17,404	(37%)
Per BOE	<b>\$8.82</b>	\$12.47	(29%)

Fairborne recorded operating costs of \$11.0 million (\$8.82 per BOE) during the first quarter of 2010, consistent with the preceding fourth quarter of 2009 (\$8.75 per BOE). Operating costs of \$8.82 per BOE in 2010 have decreased 29% from \$12.47 per BOE in the first quarter of 2009 as a result of cost reduction initiatives implemented later in 2009 on the Company's Wild River and Sinclair properties.

**Transportation Expenses**

	Three months ended March 31,		
	<b>2010</b>	2009	CHANGE
Transportation <i>(\$thousands)</i>	<b>1,291</b>	1,594	(19%)
Per BOE	<b>\$1.03</b>	\$1.14	(10%)

Transportation costs of \$1.3 million (\$1.03 per BOE) for the first quarter of 2010 includes clean oil trucking, trucking of natural gas liquids, certain third party fuel charges and transportation and fuel costs associated with the usage of natural gas pipelines. Compared to the first quarter of 2009, transportation costs in the first quarter of 2010 are lower as a result of decreased transportation costs on the Company's Sinclair and Harlech properties.

*Interim Management's Discussion & Analysis***Operating Netbacks**

(\$ per BOE)	Three months ended March 31,		
	2010	2009	CHANGE
Petroleum and natural gas sales <sup>(1)</sup>	<b>44.64</b>	43.13	4%
Sulphur block revenue	<b>5.57</b>	3.83	45%
Other income <sup>(1)</sup>	<b>0.33</b>	0.22	50%
Royalties	<b>(4.43)</b>	(5.78)	(23%)
Operating costs	<b>(8.82)</b>	(12.47)	(29%)
Transportation	<b>(1.03)</b>	(1.14)	(10%)
Operating netback	<b>36.26</b>	27.79	30%

1) Excludes the change in fair value of derivatives

Fairborne's operating netback of \$36.26 per BOE was consistent with the fourth quarter of 2009 (\$36.85 per BOE) and 30% higher when compared to the first quarter of 2009 (\$27.79 per BOE). The increase in the operating netback in 2010 reflects stronger crude oil prices, increased sulphur block revenue and lower operating costs.

**General and Administrative ("G&A") Expenses**

(\$thousands except as noted)	Three months ended March 31,		
	2010	2009	CHANGE
G&A expenses, net of recoveries	<b>2,338</b>	2,151	9%
Compensation costs	<b>2,275</b>	2,670	(15%)
Total G&A expenses	<b>4,613</b>	4,821	(4%)
G&A expenses, net of recoveries, per BOE	<b>\$1.87</b>	\$1.54	21%
Compensation costs, per BOE	<b>\$1.82</b>	\$1.91	(5%)

Fairborne recorded \$2.3 million (\$1.87 per BOE) of G&A expenses, net of recoveries, in the first quarter of 2010, a 9% increase when compared to \$2.2 million (\$1.54 per BOE) in the first quarter of 2009 which was reduced by an accrual adjustment for the 2008 employee bonus program.

Compensation expense of \$2.3 million in the first quarter of 2010 was 15% lower than the \$2.7 million recorded during the first quarter of 2009. Compensation expense recorded during the first quarter of 2010 included \$2.2 million related to the stock option plan and \$0.1 million related to the vesting of the remaining Restricted Units and Performance Units held by senior officers and directors. Compensation expense recorded during the first quarter of 2009 included \$3.0 million related to the stock option plan and \$0.1 million representing the amortization of the remaining Restricted Units and Performance Units, partially offset by a \$0.5 million recovery of compensation expense related to the retention award program. As at March 31, 2010, the intrinsic value of the retention award plan, being the difference between Fairborne's share price at the end of the period and the exercise price of the award, was zero.

**Interest**

(\$thousands except as noted)	Three months ended March 31,		
	2010	2009	CHANGE
Interest expense	<b>2,993</b>	3,559	(16%)
Accretion of convertible debentures	<b>483</b>	502	(4%)
Total interest	<b>3,476</b>	4,061	(14%)
Per BOE	<b>\$2.78</b>	\$2.91	(4%)



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Fairborne recorded \$3.0 million in interest expense in the first quarter of 2010, a decrease of 12% from the preceding quarter (Q4 2009 – \$3.4 million) and a decrease of 16% from \$3.6 million recorded in the first quarter of 2009. The decrease in interest expense from the fourth quarter of 2009 is consistent with lower debt levels maintained during the first three months of 2010. Compared to the first quarter of 2009, net debt has decreased substantially but the interest savings have been partially offset by higher borrowing margins and stamping fees initiated by the Company's lenders. Also included in interest expense is the accretion of convertible debentures. The costs associated with the debenture offering along with the amount allocated to the conversion feature are included in interest expense over the term of the debentures.

**Depletion, Depreciation and Accretion (DD&A)**

	Three months ended March 31,		
	2010	2009	CHANGE
Depletion, depreciation and accretion ( <i>\$thousands</i> )	<b>31,149</b>	37,541	(17%)
Per BOE	<b>\$24.92</b>	\$26.88	(7%)

Fairborne recorded \$31.1 million in depletion and depreciation of capital assets and accretion of asset retirement obligations during the first quarter of 2010. On a BOE basis, the 2010 first quarter DD&A rate of \$24.92 per BOE was 6% lower than the average DD&A rate for the prior year (\$26.45 per BOE) and 7% lower than the first quarter 2009 (\$26.88 per BOE) as a result of reserve additions associated with the Company's first quarter capital expenditure program.

**Taxes**

	Three months ended March 31,		
	2010	2009	CHANGE
Future tax expense (reduction) ( <i>\$thousands</i> )	<b>2,485</b>	(258)	–
Per BOE	<b>\$1.99</b>	\$(0.18)	–

Fairborne recorded a future tax expense of \$2.5 million in the first quarter of 2010 compared to a future tax recovery of \$0.3 million recorded during the first quarter of 2009, both of which reflect a provision for future tax at tax rates expected to apply when the related temporary differences reverse. The increase in tax expense is consistent with the net earnings before taxes.

**Net Income (Loss) and Funds Generated from Operations**

<i>(\$thousands except as noted)</i>	Three months ended March 31,		
	2010	2009	CHANGE
Funds generated from operations	<b>39,555</b>	32,970	20%
Per share – basic	<b>\$0.39</b>	\$0.38	3%
Per share – diluted	<b>\$0.38</b>	\$0.38	–
Cash flow from operations (including changes in working capital)	<b>43,522</b>	34,782	25%
Per share – basic	<b>\$0.42</b>	\$0.40	5%
Per share – diluted	<b>\$0.42</b>	\$0.40	5%
Net income (loss)	<b>3,809</b>	(4,691)	181%
Per share – basic	<b>\$0.04</b>	\$(0.05)	180%
Per share – diluted	<b>\$0.04</b>	\$(0.05)	180%

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The following table provides a reconciliation between cash flow from operations and funds generated from operations:

(\$thousands)	Three months ended March 31,	
	2010	2009
Cash flow from operations	<b>43,522</b>	34,782
Change in non-cash working capital	<b>(4,278)</b>	(2,311)
Asset retirement expenditures	<b>311</b>	499
Funds generated from operations	<b>39,555</b>	32,970

**BOE ANALYSIS**

	Three months ended March 31,			
	2010		2009	
	(\$thousands)	(\$ per BOE)	(\$thousands)	(\$ per BOE)
Petroleum and natural gas revenue <sup>(1)</sup>	<b>63,382</b>	<b>50.72</b>	68,545	49.08
Royalties	<b>(5,534)</b>	<b>(4.43)</b>	(8,073)	(5.78)
Operating expenses	<b>(11,025)</b>	<b>(8.82)</b>	(17,404)	(12.47)
Transportation	<b>(1,291)</b>	<b>(1.03)</b>	(1,594)	(1.14)
Change in fair value of derivatives	<b>(222)</b>	<b>(0.18)</b>	(2,643)	(1.89)
General & administrative <sup>(2)</sup>	<b>(2,338)</b>	<b>(1.87)</b>	(2,151)	(1.54)
Compensation expense <sup>(3)</sup>	<b>(424)</b>	<b>(0.34)</b>	(151)	(0.11)
Interest expense <sup>(4)</sup>	<b>(2,993)</b>	<b>(2.39)</b>	(3,559)	(2.55)
Funds generated from operations	<b>39,555</b>	<b>31.66</b>	32,970	23.60
Change in fair value of derivatives	<b>222</b>	<b>0.18</b>	2,643	1.89
Compensation expense – non-cash	<b>(1,851)</b>	<b>(1.48)</b>	(2,519)	(1.80)
Accretion of convertible debentures	<b>(483)</b>	<b>(0.39)</b>	(502)	(0.36)
Depletion, depreciation and accretion	<b>(31,149)</b>	<b>(24.92)</b>	(37,541)	(26.88)
Future tax reduction (expense)	<b>(2,485)</b>	<b>(1.99)</b>	258	0.18
Net income (loss)	<b>3,809</b>	<b>3.06</b>	(4,691)	(3.37)

1) Including the change in fair value of derivatives (non-cash) and revenue from the sale of inventory at the West Pembina sulphur block.

2) Net of compensation expense (non-cash).

3) Cash component of compensation expense which resulted from the cash settlement of Restricted Units and Performance Units.

4) Net of accretion on convertible debentures (non-cash).

Fairborne reported funds generated from operations of \$39.6 million (\$31.66 per BOE) for the first quarter of 2010, an increase of 4% from the preceding fourth quarter of 2009 (\$37.9 million) and 20% higher than the first quarter of 2009 (\$33.0 million). The increase in funds generated from operations reflected lower operating costs and interest expense in 2010. The net income of \$3.8 million (\$3.06 per BOE) for the first quarter of 2010 reflected the impact of increased cash flows and a lower depletion rate, partially offset by the future tax expense recorded during the quarter.



*Interim Management's Discussion & Analysis***LIQUIDITY AND CAPITAL RESOURCES****Capital Expenditures**

<i>(\$thousands)</i>	Three months ended March 31,	
	2010	2009
Exploration and development		
Land and lease acquisitions	7,829	3,810
Geological and geophysical	3,321	84
Drilling, completions and workovers	43,882	39,370
Well equipment and facilities	10,509	9,292
Corporate assets	5	89
	<b>65,546</b>	52,645
Property acquisitions	1,464	–
Total	<b>67,010</b>	52,645

During the first quarter of 2010, Fairborne's exploration and development expenditures totaled \$65.5 million with capital expenditures financed through funds generated from operations as well as working capital. Land and lease acquisitions of \$7.8 million during the quarter were primarily focused in the Harlech, Marlboro and Sinclair areas where \$6.8 million was utilized to acquire additional acreage at provincial land sales. Property acquisitions of \$1.5 million included acquiring additional working interests in the Marlboro and West Pembina areas.

Fairborne spent \$43.9 million on drilling and completion activities in the first quarter of 2010 with a total of 16 (12.8 net) wells drilled resulting in nine (7.7 net) natural gas wells and seven (5.1 net) oil wells. First quarter drilling activities were focused on Fairborne's Sinclair, Harlech, Brazeau, Marlboro and Westerosé properties, with four (3.6 net) wells drilled in Sinclair, three (2.5 net) wells drilled on the Company's Harlech property, one (0.9 net) horizontal well drilled at Brazeau, two (1.7 net) horizontal wells drilled in Marlboro and two (2.0 net) horizontal wells at Westerosé.

Tangible capital expenditures during the three months ended March 31, 2010 included the tie-in of various wells in the Harlech, Sinclair and Marlboro areas as well as a significant gathering system expansion in the Marlboro area.

**Working Capital and Bank Indebtedness**

At March 31, 2010, Fairborne had drawn \$102.5 million (December 31, 2009 – \$103.7 million) against its credit facilities and had a working capital deficit of \$34.6 million (December 31, 2009 – \$6.4 million). With continued volatility in commodity and capital markets into 2010, Fairborne intends to limit its 2010 capital expenditure program to a level which it anticipates will be able to be funded from its annual 2010 funds generated from operations. The annual capital expenditure budget was more heavily weighted to the first quarter of 2010 with drilling activities planned prior to spring break-up. As such, the Company utilized working capital in the first quarter to finance capital expenditures in excess of funds generated from operations. On an annualized basis, Fairborne anticipates capital expenditures to be financed from funds generated from operations.

Fairborne's credit facilities at March 31, 2010 included a \$270 million extendible revolving term credit facility and a \$15 million demand operating credit facility for a total available facility of \$285 million. The extendible revolving term facility is available on a revolving basis until May 28, 2010 and, if not renewed at this date, repayment of the amounts drawn will be required on May 30, 2011. The facilities continue to be subject to semi-annual reviews.

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Subsequent to March 31, 2010, the lending syndicate borrowing base was extended to May 27, 2011 at \$285 million on substantially the same terms.

**Shareholders' Equity**

The Company is authorized to issue an unlimited number of common shares and an unlimited number of preferred shares, issuable in series.

During the first quarter of 2010 15,183 common shares were issued on the exercise of 15,582 RTU's and PTU's and 107,166 RTU's and PTU's were settled for cash. In addition, 2,204 common shares were issued on the exercise of stock options.

As a result of the 2009 flow-through financing, Fairborne has a commitment to spend \$20.0 million on qualifying Canadian exploration expenditures prior to December 31, 2010. As at March 31, 2010, \$10.0 million of qualifying exploration expenditures have been incurred.

The following table provides a summary of outstanding common shares, warrants, convertible debentures and shares under incentive plans including stock options, at the dates indicated:

	<b>April 30 2010</b>	<b>March 31 2010</b>	December 31 2009
<i>(thousands)</i>			
Common shares	<b>102,482</b>	<b>102,479</b>	102,462
Warrants <sup>(1)</sup>	<b>4,406</b>	<b>4,406</b>	4,406
Convertible debentures <sup>(2)</sup>	<b>\$100,000</b>	<b>\$100,000</b>	\$100,000
Incentive plans			
Restricted Units <sup>(3)</sup>	–	–	30
Performance Units <sup>(4)</sup>	–	–	92
Stock options	<b>6,797</b>	<b>6,885</b>	5,235
Weighted average common shares <sup>(5)</sup>			
Basic	<b>n/a</b>	<b>102,465</b>	90,609
Diluted	<b>n/a</b>	<b>103,255</b>	90,609

1) Each warrant entitles the holder to acquire 0.39 of a common share at an exercise price of \$8.13 per common share, exercisable until June 1, 2010.

2) The convertible debentures are convertible into common shares at a conversion price of \$13.50 per share.

3) At December 31, 2009, the Restricted Units entitled the holders to acquire an aggregate of 35,125 common shares of the Company, subject to vesting in accordance with the restricted unit and performance unit incentive plan (the "Incentive Plan").

4) At December 31, 2009, the Performance Units entitled the holders to acquire an aggregate of 84,714 common shares of the Company, subject to vesting in accordance with the Incentive Plan.

5) Weighted average common shares are for the twelve months ended December 31, 2009 and for the three months ended March 31, 2010.



*Interim Management's Discussion & Analysis***BUSINESS ENVIRONMENT AND RISK**

The business risks the Company is exposed to are those inherent in the oil and gas industry as well as those governed by the individual nature of Fairborne's operations. Geological and engineering risks, the uncertainty of discovering commercial quantities of new reserves, commodity prices, interest rate and foreign exchange risks, competition and government regulations – all of these govern the businesses and influence the controls and management at the Company. Fairborne manages these risks by:

- attracting and retaining a team of highly qualified and motivated professionals who have a vested interest in the success of the Company;
- operating properties in order to maximize opportunities;
- employing risk management instruments to minimize exposure to volatility of commodity prices, interest rate and foreign exchange rates;
- maintaining a strong financial position; and
- maintaining strict environmental, safety and health practices.

**CHANGE IN ACCOUNTING POLICIES AND RECENT ACCOUNTING PRONOUNCEMENTS****International Financial Reporting Standards ("IFRS")**

Effective January 1, 2011, Canadian public companies are required to adopt International Financial Reporting Standards ("IFRS"). In the time leading up to the conversion date, some existing Canadian standards will change to converge with IFRS. Fairborne's financial statements up to and including the December 31, 2010 financial statements will continue to be reported in accordance with Canadian GAAP as it exists on each reporting date. Financial statements for the quarter ended March 31, 2011, including comparative amounts, will be prepared on an IFRS basis.

In order to transition to IFRS, management has formed an executive steering committee which oversees the project team. A transition plan is in place to convert the financial statements to IFRS. Training has been provided to key employees and the Company continues to assess the effect of the transition on information systems, internal controls over financial reporting and disclosure controls and procedures. Systems and controls are being updated as IFRS accounting processes are implemented. Analysis and quantification of differences between IFRS and Fairborne's current accounting policies is continuing. Some accounting policies may change on adoption of IFRS even though Fairborne's current accounting policies are acceptable under IFRS. Changes in accounting policy may materially impact the financial statements.

There are several significant accounting policy changes anticipated on adoption of IFRS. Changes in IFRS prior to adoption may result in other accounting policy changes which could significantly impact the financial statements. Numerous accounting policy changes will be made under IFRS, with the most significant changes expected to include accounting for petroleum and natural gas assets and equipment ("P&NG assets"), accounting for business combinations and accounting for deferred taxes. The anticipated changes were described in more detail in our December 31, 2009 MD&A. The impact of these changes has not yet been quantified. In accordance with Fairborne's IFRS project plan and as a result of the 2009 year end reporting requirements, no further progress was completed on the Company's IFRS project in the first quarter of 2010.

*Interim Management's Discussion & Analysis***CONTROLS AND PROCEDURES****Disclosure Controls and Procedures**

Fairborne's Chief Executive Officer and Chief Financial Officer have designed or caused to be designed under their supervision, disclosure controls and procedures to provide reasonable assurance that (i) material information relating to the Company is made known to Fairborne's Chief Executive Officer and Chief Financial Officer by others, particularly during the period in which the annual and interim filings are being prepared; and (ii) information required to be disclosed by the Company in its annual filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time period specified in securities legislation.

**Internal Controls over Financial Reporting**

Fairborne's Chief Executive Officer and Chief Financial Officer have designed or caused to be designed under their supervision, internal controls over financial reporting to provide reasonable assurance regarding the reliability of the Company's financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP.

No material changes in Fairborne's internal controls over financial reporting were identified during the three months ended March 31, 2010, that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

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



*Interim Management's Discussion & Analysis***QUARTERLY FINANCIAL INFORMATION**

The following is a summary of select financial information for the quarterly periods indicated:

	2010	2009		
	Q1	Q4	Q3	Q2
<b>Financial</b> ( <i>\$thousands, except per share amounts</i> )				
Petroleum and natural gas revenue	<b>63,382</b>	58,338	55,244	58,430
Funds generated from operations	<b>39,555</b>	37,863	37,236	35,742
Per share – basic	<b>\$0.39</b>	\$0.37	\$0.43	\$0.41
Per share – diluted	<b>\$0.38</b>	\$0.37	\$0.43	\$0.41
Cash flow from operations (including changes in working capital)	<b>43,522</b>	38,750	40,048	27,653
Per share – basic	<b>\$0.42</b>	\$0.38	\$0.46	\$0.32
Per share – diluted	<b>\$0.42</b>	\$0.38	\$0.46	\$0.32
Net income (loss)	<b>3,809</b>	(3,124)	(497)	(17,333)
Per share – basic	<b>\$0.04</b>	\$(0.02)	\$(0.01)	\$(0.20)
Per share – diluted	<b>\$0.04</b>	\$(0.02)	\$(0.01)	\$(0.20)
Total assets	<b>976,138</b>	940,443	961,920	1,001,840
Working capital deficit (surplus)	<b>34,611</b>	6,370	(1,539)	(7,227)
Bank indebtedness	<b>102,536</b>	103,738	204,046	232,184
Convertible debentures	<b>96,993</b>	96,510	96,027	95,525
<b>Operations</b>				
Average production				
Natural gas ( <i>Mcf per day</i> )	<b>60,878</b>	59,132	56,797	66,744
Crude oil ( <i>bbls per day</i> )	<b>3,000</b>	3,037	3,292	3,552
Natural gas liquids ( <i>bbls per day</i> )	<b>686</b>	617	563	632
Sulphur ( <i>tonnes per day</i> ) <sup>(1)</sup>	<b>54</b>	33	100	64
Total ( <i>BOE per day</i> )	<b>13,886</b>	13,542	13,421	15,372

1) Excludes the sale of inventory at the West Pembina sulphur block.

*Interim Management's Discussion & Analysis*

	2009	2008		
	Q1	Q4	Q3	Q2
<b>Financial</b> ( <i>\$thousands, except per share amounts</i> )				
Petroleum and natural gas revenue	68,545	85,165	97,489	85,670
Funds generated from operations	32,970	40,309	55,307	51,458
Per share – basic	\$0.38	\$0.46	\$0.64	\$0.60
Per share – diluted	\$0.38	\$0.46	\$0.63	\$0.60
Cash flow from operations (including changes in working capital)	34,782	37,693	65,598	41,650
Per share – basic	\$0.40	\$0.43	\$0.76	\$0.49
Per share – diluted	\$0.40	\$0.43	\$0.76	\$0.48
Net income (loss)	(4,691)	11,657	19,182	3,717
Per share – basic	(\$0.05)	\$0.14	\$0.22	\$0.04
Per share – diluted	(\$0.05)	\$0.14	\$0.22	\$0.04
Total assets	1,023,526	1,013,177	999,065	946,025
Working capital deficit	31,641	27,917	64,814	7,363
Bank indebtedness	209,925	196,282	161,302	180,977
Convertible debentures	95,024	94,522	94,020	93,499
<b>Operations</b>				
Average production				
Natural gas ( <i>Mcf per day</i> )	67,520	69,460	62,601	59,529
Crude oil ( <i>bbls per day</i> )	3,599	4,086	3,312	2,506
Natural gas liquids ( <i>bbls per day</i> )	572	657	580	610
Sulphur ( <i>tonnes per day</i> ) <sup>(1)</sup>	93	138	129	106
Total ( <i>BOE per day</i> )	15,517	16,458	14,454	13,143

1) Excludes the sale of inventory at the West Pembina sulphur block.



*Interim Consolidated Financial Statements***INTERIM CONSOLIDATED BALANCE SHEETS**

(Unaudited)

<i>(\$thousands)</i>	<b>March 31, 2010</b>	December 31, 2009
<b>Assets</b>		
Current assets		
Cash and cash equivalents	\$ 194	\$ 147
Accounts receivable	34,923	35,155
Prepaid expenses and deposits	7,667	8,079
	<b>42,784</b>	43,381
Petroleum and natural gas properties and equipment <i>(Note 1)</i>	<b>917,184</b>	880,892
Goodwill	<b>16,170</b>	16,170
	<b>\$ 976,138</b>	\$ 940,443
<b>Liabilities</b>		
Current liabilities		
Accounts payable and accrued liabilities	\$ 73,706	\$ 44,602
Derivative liability <i>(Note 7)</i>	137	359
Current portion of compensation plans	—	505
Deferred revenue	3,552	4,285
	<b>77,395</b>	49,751
Bank indebtedness <i>(Note 2)</i>	<b>102,536</b>	103,738
Convertible debentures <i>(Note 3)</i>	<b>96,993</b>	96,510
Asset retirement obligation <i>(Note 4)</i>	<b>11,320</b>	11,200
Future income taxes	<b>97,452</b>	89,919
<b>Shareholders' Equity</b>		
Common shares <i>(Note 5)</i>	<b>531,886</b>	536,789
Warrants	<b>2,721</b>	2,721
Equity component of convertible debentures <i>(Note 3)</i>	<b>5,581</b>	5,581
Contributed surplus <i>(Note 5)</i>	<b>27,038</b>	24,827
Retained earnings	<b>23,216</b>	19,407
	<b>590,442</b>	589,325
	<b>\$ 976,138</b>	\$ 940,443

*See accompanying notes to the interim consolidated financial statements.*

*Interim Consolidated Financial Statements***INTERIM CONSOLIDATED STATEMENTS OF OPERATIONS AND RETAINED EARNINGS**

(Unaudited)

<i>(\$thousands except per share amounts)</i>	For the three months ended March 31,	
	2010	2009
<b>Revenue</b>		
Petroleum and natural gas	\$ 63,382	\$ 68,545
Royalties	(5,534)	(8,073)
	<b>57,848</b>	60,472
<b>Expenses</b>		
Operating	11,025	17,404
Transportation	1,291	1,594
General and administrative	4,613	4,821
Interest	3,476	4,061
Depletion, depreciation and accretion	31,149	37,541
	<b>51,554</b>	65,421
<b>Income (loss) before taxes</b>	<b>6,294</b>	(4,949)
Future taxes (reduction)	2,485	(258)
<b>Net income (loss) and comprehensive income (loss)</b>	<b>3,809</b>	(4,691)
Retained earnings, beginning of period	19,407	45,052
<b>Retained earnings, end of period</b>	<b>\$ 23,216</b>	\$ 40,361
<b>Net income (loss) per share</b> <i>(Note 5)</i>		
Basic	\$ 0.04	\$ (0.05)
Diluted	\$ 0.04	\$ (0.05)

See accompanying notes to the interim consolidated financial statements.



*Interim Consolidated Financial Statements***INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Unaudited)

<i>(\$thousands)</i>	For the three months ended March 31,	
	<b>2010</b>	2009
<b>Cash provided by (used in):</b>		
<b>Operating activities</b>		
Net income (loss)	\$ 3,809	\$ (4,691)
Items not involving cash:		
Depletion, depreciation and accretion	31,149	37,541
Compensation expense	1,851	2,519
Future taxes (reduction)	2,485	(258)
Accretion of convertible debentures	483	502
Change in fair value of derivatives	(222)	(2,643)
Asset retirement expenditures	(311)	(499)
	<b>39,244</b>	<b>32,471</b>
Change in non-cash working capital	4,278	2,311
	<b>43,522</b>	<b>34,782</b>
<b>Financing activities</b>		
Bank indebtedness	(1,202)	13,643
<b>Investing activities</b>		
Expenditures on petroleum and natural gas properties	(65,546)	(52,645)
Acquisition of petroleum and natural gas properties	(1,464)	—
Change in non-cash working capital	24,737	4,218
	<b>(42,273)</b>	<b>(48,427)</b>
Change in cash and cash equivalents	47	(2)
Cash and cash equivalents, beginning of period	147	126
<b>Cash and cash equivalents, end of period</b>	<b>\$ 194</b>	<b>\$ 124</b>
Interest paid	<b>\$ 816</b>	<b>\$ 2,437</b>

*See accompanying notes to the interim consolidated financial statements.*

*Interim Consolidated Financial Statements***SELECTED NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

For the three months ended March 31, 2010 (unaudited)

*(tabular amounts are stated in thousands and thousands of dollars except per share amounts)*

The interim consolidated financial statements of Fairborne Energy Ltd. (the “Company” or “Fairborne”) have been prepared by management in accordance with accounting principles generally accepted in Canada. The interim consolidated financial statements have been prepared following the same accounting policies and methods of computation as the consolidated financial statements for the year ended December 31, 2009. The disclosure which follows is incremental to the disclosure included with the annual financial statements. These interim consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2009.

**1. PETROLEUM AND NATURAL GAS PROPERTIES AND EQUIPMENT**

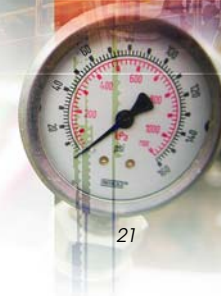
	<b>March 31, 2010</b>	December 31, 2009
Petroleum and natural gas properties and equipment	<b>\$ 1,502,476</b>	\$ 1,435,282
Accumulated depletion and depreciation	<b>(587,130)</b>	(556,289)
Corporate assets	<b>4,312</b>	4,307
Accumulated depreciation	<b>(2,474)</b>	(2,408)
	<b>\$ 917,184</b>	\$ 880,892

As at March 31, 2010, future development costs of \$201.1 million (December 31, 2009 – \$193.8 million) were included in the depletion calculation and costs of acquiring unproved properties in the amount of \$53.9 million (December 31, 2009 – \$48.2 million) were excluded from the depletion calculation.

**2. BANK INDEBTEDNESS**

At March 31, 2010 the Company had a \$270 million extendible revolving term credit facility and a \$15 million demand operating credit facility available from a syndicate of Canadian chartered banks, subject to the banks’ semi-annual valuation of Fairborne’s petroleum and natural gas properties. The extendible revolving term facility is available on a revolving basis until May 28, 2010 (364 day facility) at which time it may be extended, at the lenders option. If the revolving period is not extended, the undrawn portion of the facility will be cancelled and the amount outstanding will convert to a 365 day non-revolving term facility. The amounts outstanding under the non-revolving term facility are required to be repaid at the end of the term facility being May 28, 2011. Interest payable on amounts drawn under the facilities is at the prevailing bankers’ acceptance rates plus stamping fees, lenders’ prime rate or LIBOR rates plus applicable margins, depending on the form of borrowing by the Company. The margins and stamping fees vary from 0.75 to 4.25% depending on financial statement ratios and the form of borrowing. The credit facilities are secured by a general security agreement and a first ranking floating charge on the assets of the Company. At March 31, 2010 letters of credit totaling \$0.5 million were outstanding.

Subsequent to March 31, 2010, the lending syndicate borrowing base was extended to May 27, 2011 at \$285 million on substantially the same terms.



*Interim Consolidated Financial Statements***3. CONVERTIBLE DEBENTURES**

The following table sets forth a reconciliation of the convertible debentures for the three months ended March 31, 2010:

	Number of debentures	Debt component	Equity component
Balance, beginning of period	100,000	\$ 96,510	\$ 5,581
Accretion	–	483	–
<b>Balance, end of period</b>	<b>100,000</b>	<b>\$ 96,993</b>	<b>\$ 5,581</b>

**4. ASSET RETIREMENT OBLIGATION**

The following table sets forth a reconciliation of the asset retirement obligation for the three months ended March 31, 2010:

Balance, beginning of period	\$ 11,200
Liabilities incurred	189
Liabilities settled	(311)
Accretion expense	242
<b>Balance, end of period</b>	<b>\$ 11,320</b>

**5. SHAREHOLDERS' EQUITY**

The Company is authorized to issue an unlimited number of common shares and an unlimited number of preferred shares, issuable in series.

**a) Common Shares**

The following table sets forth a reconciliation of the common shares issued and outstanding for the three months ended March 31, 2010:

	Number of shares	Amount
Balance, beginning of period	102,462	\$ 536,789
Issued on vesting of Restricted Units and Performance Units	15	140
Issued on exercise of stock options	2	5
Tax effect of flow through shares issued in 2009	–	(5,048)
<b>Balance, end of period</b>	<b>102,479</b>	<b>\$ 531,886</b>

As a result of the 2009 flow-through financing, Fairborne has a commitment to spend \$20.0 million on qualifying Canadian exploration expenditures. As at March 31, 2010, \$10.0 million of qualifying exploration expenditures have been incurred.

*Interim Consolidated Financial Statements***b) Per share amounts**

The following table summarizes the weighted average common shares used in calculating net income (loss) per share:

	Three months ended March 31,	
	2010	2009
Numerator		
Net income (loss) – basic and diluted	\$ 3,809	\$ (4,691)
Denominator		
Weighted average shares – basic	102,465	86,964
Options	790	–
Denominator for diluted net income (loss) per share	103,255	86,964
Basic net income (loss) per share	\$ 0.04	\$ (0.05)
Diluted net income (loss) per share	\$ 0.04	\$ (0.05)

Excluded from the diluted number of shares for the three months ended March 31, 2010 is the effect of convertible debentures (7.4 million shares), warrants (1.7 million shares) and 3.6 million stock options as they are out of the money. Excluded from the diluted number of shares for the three months ended March 31, 2009 is the effect of convertible debentures (7.4 million shares), warrants (1.7 million shares) and 8.6 million stock options.

**c) Equity and liability based compensation plans****i) INCENTIVE PLAN**

The following table sets forth a reconciliation of the restricted and performance incentive plan activity for the three months ended March 31, 2010:

	Number of Performance Units	Number of Restricted Units	Total
Balance, beginning of period	30	92	122
Exercised	(30)	(92)	(122)
Balance, end of period	–	–	–

During the quarter ended March 31, 2010, all remaining restricted and performance units vested and were settled with either cash or common shares. As such, no liability remains at March 31, 2010.



*Interim Consolidated Financial Statements*

## ii) STOCK OPTION PLAN

The following table sets forth a reconciliation of the stock option plan activity for the three months ended March 31, 2010:

	Number of options	Weighted average exercise price
Balance, beginning of period	5,235	\$ 4.25
Granted	1,681	4.16
Exercised	(6)	2.53
Forfeited	(25)	6.31
Balance, end of period	<b>6,885</b>	<b>\$ 4.22</b>
Exercisable, end of period	<b>1,679</b>	<b>\$ 4.37</b>

The weighted average fair value of options granted during the three months ended March 31, 2010 was \$1.63 per option using the Black-Scholes option pricing model with the following assumptions: risk free interest rate of two percent, expected volatility of 64 percent, average expected life of three years and dividend rate of nil. An estimated forfeiture rate of two percent has been applied to the compensation costs recognized.

The following table summarizes stock options outstanding at March 31, 2010:

Exercise Price	Options outstanding	Remaining term (years)
\$ 2.00 – \$ 4.99	6,692	4.5
\$ 5.00 – \$ 7.99	55	4.1
\$ 8.00 – \$ 10.99	58	3.5
\$ 11.00 – \$ 13.99	80	3.3
	<b>6,885</b>	<b>4.5</b>

## iii) RETENTION AWARD PLAN

The following table sets forth a reconciliation of the retention award plan activity for the three months ended March 31, 2010:

	Number of awards	Weighted average exercise price
Balance, beginning of period	1,390	\$ 5.74
Forfeited	(85)	5.75
Balance, end of period	<b>1,305</b>	<b>\$ 5.74</b>
Exercisable, end of period	<b>850</b>	<b>\$ 5.74</b>

*Interim Consolidated Financial Statements***d) Contributed Surplus**

The following table sets forth a reconciliation of the contributed surplus for the three months ended March 31, 2010:

Balance, beginning of period	\$ 24,827
Equity based compensation	2,216
Stock options exercised	(5)
Balance, end of period	<b>\$ 27,038</b>

**6. FINANCIAL INSTRUMENTS**

As at March 31, 2010, the Company's accounts receivable is aged as follows:

Current (less than 90 days)	\$ 30,352
Past due (more than 90 days)	4,571
Total	<b>\$ 34,923</b>

**Fair value of financial instruments:**

The carrying value of Fairborne's financial instruments, other than bank indebtedness and convertible debentures, approximate their fair value due to their short maturity. The fair value of the bank indebtedness approximates its carrying value as it bears interest at a floating rate. The fair value of the convertible debentures at March 31, 2010 was \$101.9 million (December 31, 2009 – \$100.3 million).

**7. COMMODITY CONTRACTS**

Fairborne has a risk management program whereby the Company sells forward a portion of its future production through fixed price sales contracts with customers.

**a) Commodity Contracts Recorded at Fair Value:**

At March 31, 2010 certain contracts have been recorded on the balance sheet at their estimated fair value as a \$0.1 million liability (December 31, 2009 – \$0.4 million). The change in the fair value has been recorded in petroleum and natural gas sales for the three months ended March 31, 2010.

**Oil:**

	Volume <i>(bbls per day)</i>	Price <i>(US\$ per bbl)</i>	Settlement Index
Collars			
Apr 1, 2010 – Dec 31, 2010	500	55.00 – 108.00	WTI
Apr 1, 2010 – Dec 31, 2010	500	70.00 – 100.15	WTI



*Interim Consolidated Financial Statements***b) Commodity Contracts not Recorded at Fair Value:**

The following oil and natural gas fixed price physical sales contracts outstanding at March 31, 2010 have been entered into for the purpose of physical delivery of a non-financial item; therefore, the physical delivery contracts are not fair valued. Settlements on these contracts are included in petroleum and natural gas revenue as they occur.

**Oil:**

	Volume (bbls per day)	Price (US\$ per bbl)	Settlement Index
Collars			
Apr 1, 2010 – Dec 31, 2010	500	55.00 – 103.00	WTI

**Natural Gas:**

	Volume (GJs per day)	Price (CDN\$ per GJ)	Settlement Index
AECO Swaps			
Apr 1, 2010 – Dec 31, 2010	5,000	5.86	AECO C Monthly
Apr 1, 2010 – Dec 31, 2010	2,500	5.67	AECO C Monthly
Apr 1, 2010 – Dec 31, 2010	1,500	5.90	AECO C Monthly
Apr 1, 2010 – Dec 31, 2010	1,500	5.86	AECO C Monthly
Apr 1, 2010 – Dec 31, 2010	1,500	5.88	AECO C Monthly
Apr 1, 2010 – Dec 31, 2010	1,500	6.00	AECO C Monthly
Apr 1, 2010 – Dec 31, 2010	4,000	6.00	AECO C Monthly
Apr 1, 2010 – Dec 31, 2010	2,000	6.13	AECO C Monthly
Apr 1, 2010 – Dec 31, 2010	2,000	6.15	AECO C Monthly
Apr 1, 2010 – Dec 31, 2010	2,000	6.16	AECO C Monthly
Jul 1, 2010 – Dec 31, 2010	4,000	5.72	AECO C Monthly

*Corporate Directory***FAIRBORNE ENERGY LTD.**

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 Calgary, Alberta T2P 5H1  
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**AUDITORS****KPMG LLP****RESERVE EVALUATORS****GLJ Petroleum Consultants Ltd.****BANKERS**

**Royal Bank of Canada**  
**National Bank of Canada**  
**Canadian Imperial Bank of Commerce**  
**Alberta Treasury Branch**

**LEGAL COUNSEL**

**Burnet, Duckworth & Palmer LLP**  
**McCarthy Tetrault LLP**

**STOCK EXCHANGE LISTING**

**The Toronto Stock Exchange**  
 Trading Symbol: **FEL**  
 Convertible Debentures: **FEL.DB**

**CORPORATE GOVERNANCE**

A system of corporate governance for Fairborne has been established to provide the Board of Directors, management and shareholders of the Company with effective governance. A more detailed discussion of corporate governance is available in the Information Circular for the Annual Meeting of Shareholders.

**DIRECTORS**

**Greg Bay**  
 President and CEO  
 Cypress Capital Management Ltd.

**Robert B. Hodgins**  
 Investor and Corporate Director

**Johannes J. Nieuwenburg**  
 General Partner  
 KERN Partners Ltd.

**Carl J. Tricoli**  
 Founder and Managing Partner  
 Denham Capital Management LP

**Steven R. VanSickle**  
 President and CEO  
 Fairborne Energy Ltd.

**Richard A. Walls**  
 President and  
 Chief Executive Officer  
 C & C Energy Canada Ltd.

**Rodney D. Wimer**  
 President  
 Mazama Capital Partners

**GENERAL INFORMATION**

Shareholders and interested investors are encouraged to visit our web site:

*<http://www.fairborne-energy.com>*

Historical public documents, corporate information, latest presentation material and press releases are all available. Filings also available at: [www.sedar.com](http://www.sedar.com)

**OFFICERS**

**Steven R. VanSickle**  
 President  
 and Chief Executive Officer

**David L. Summers**  
 Chief Operating Officer

**Aaron G. Grandberg**  
 Chief Financial Officer

**Jackie M. Cugnet**  
 Vice President  
 Finance

**David S. Cymbalisky**  
 Vice President  
 Engineering

**Scott W. Hadley**  
 Vice President  
 Exploration

**F. Tom Park**  
 Vice President  
 Marketing

**Gary M. Poirier**  
 Vice President  
 Production

**David E.T. Pyke**  
 Vice President  
 Land and Contracts

**ANNUAL MEETING**

The Annual Meeting of the Shareholders of Fairborne Energy Ltd. will be held at 3:00 pm, on May 26th, 2010 in the Grand Lecture Room at the Metropolitan Conference Centre, 333 – 4th Avenue S.W. Calgary, Alberta.





**FAIRBORNE  
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