



MIDNIGHT DELIVERS SOLID QUARTER WITH CONSISTENT PRODUCTION AND CASH FLOW AND INCREASED FINANCIAL FLEXIBILITY

SECOND QUARTER 2007 HIGHLIGHTS

CONSISTENT PRODUCTION VOLUMES

- YTD 2007 Production volumes of 2,192 boe/d
 - Flat with first half 2006 production volumes of 2,202 boe/d
- Q2 2007 production volumes of 2,146 boe/d
 - Decreased 4% over Q1 2007 and 15% over Q2 2006
 - ◆ Oil and liquids production averaged 1,185 boe/d
 - Increased 9% over Q1 2007 and 43% over Q2 2006
 - ◆ Natural gas production averaged 5,769 mcf/d
 - Decreased 16% over Q1 2007 and 43% over Q2 2006

CONSISTENT CASH FLOW

- YTD 2007 cash flow of \$11.4 million (\$0.24/diluted share)
 - Decreased 2% from first half 2006 cash flow of \$11.7 million (\$0.29/diluted share)
- Q2 2007 cash flow of \$6.0 million (\$0.13/diluted share)
 - Increased 12% over Q1 2007 and decreased 7% over Q2 2006

MIXED COMMODITY PRICES

- Q2 2007 average prices received of \$56.37/boe for Natural Gas and Oil and NGLs
 - Realized prices increased 4% over Q1 2007 and increased 17% over Q2 2006
 - ◆ Q2 2007 combined Oil & NGLs price of \$66.76/bbl
 - Increased 9% over Q1 2007 and decreased 8% over Q2 2006
 - ◆ Q2 2007 Natural Gas price of \$7.22/mcf
 - Decreased 8% over Q1 2007 and increased 21% over Q2 2006

SLOWED FIELD ACTIVITY

- Due to the wet weather and the resulting prolonged spring break up, capital expenditures for Q2 2007 totalled \$3.4 million
 - Midnight did not drill any wells during Q2 2007

INCREASED FINANCIAL FLEXIBILITY

- During Q2 2007, the Company expanded its bank line to \$35 million from \$30 million and reduced its net debt by \$2.6 million from Q1 2007

PRESIDENT'S MESSAGE

For the first half of 2007, Midnight maintained production volumes and cash flow amid mixed commodity prices and reduced drilling activity. During the second quarter, we focused on controlling our capital and operating costs while expanding our prospect inventory. Following this program, we were able to strengthen our balance sheet with a reduced debt level and expanded borrowing capacity.

Over the past year, Midnight has followed a strategy of restricted capital investment while focusing activities on developing and growing our high value light oil program at Red Earth. During the second quarter, Midnight's oil and liquids production averaged 1,185 bbls/d - up 9% from the prior quarter and 43% over Q2, 2006. Correspondingly, gas production of 5.8 mmcf/d was down 16% from the prior quarter and 43% over Q2, 2006. Our strategy to focus on oil proved prescient as oil production gains and oil price increases more than offset natural gas declines to grow cash flow by 12% over the prior quarter. During the quarter, oil and liquids represented 55% of our overall production base and 65% of our revenues.

During the second quarter, we continued to limit our capital investment in response to both high service costs as well as an early and persistent spring break-up which hampered field access. As a result, Midnight did not drill any wells during the quarter, instead we concentrated our field activities on completions and facility work to bring production on-stream from our 100% successful 2007 first quarter in our light oil core area in Red Earth and in our natural gas core areas in Beaverlodge and Wapiti.

We continue to work and expand our prospect inventory on our high value light oil prospects in Red Earth and Pembina and our natural gas prospects on the Peace River Arch at Beaverlodge and Wapiti. Midnight has a large multi-year prospect portfolio risk-balanced between our light oil development prospects in Red Earth and our high potential natural gas prospects in our multi-zone areas on the Peace River Arch. Midnight is in an enviable position of continuing to build a large prospect inventory of both sweet natural gas and high netback light sweet oil and the ability to efficiently switch its exploration and development focus between commodities depending on the prevailing market conditions.

In the Red Earth area, in addition to enhancing our large light oil exploratory drilling inventory, we focused on upgrading and expanding field facilities and operations including waterflood plans for our west Red Earth production base. At west Red Earth, we have applied for regulatory approvals and Good Production Practice ("GPP") to implement secondary recovery programs which will further add and sustain our sweet oil production from this area.

In the Pembina area, Midnight has a 37.5% working interest in a high impact exploratory oil prospect targeting the highly prolific sour Nisku oil reservoir. The licensee has conducted public consultations and has concluded its public hearing process regarding this location and anticipates receiving regulatory approval during the summer with an anticipated spud date in Q3 2007. This is a high impact exploratory oil prospect that requires significant planning and involves long lead times but if successful would add significantly to our oil production base.

On the Peace River Arch at Beaverlodge, following our first quarter drilling success, Midnight (24% WI) commenced completion and tie-in operations of our Halfway gas discovery which should be on-stream during the third quarter at rates of 1.5 mmcf/d gross. We are very excited by this discovery as it continues to validate our proprietary 3D seismic interpretation techniques. Midnight will be using its 3D seismic interpretation process to drill an exploratory Halfway well in the fourth quarter of this year and will be pursuing regulatory approvals to drill several follow up locations into this Triassic reservoir on our large high working interest land base in this area.

In Wapiti, we tied-in and put on-stream our 100% working interest gas well discovery from last year adding production of approximately 100 boe/d. Also in Wapiti, at Red Rock, our new pool discovery tested at rates of over 1.5 mmcf/d. Midnight is in discussions with area operators to bring our Q1 2007 multi-zone discovery on-stream as soon as

practical. Midnight has accumulated a significant land base through farm-ins in Wapiti and continues to pursue these high potential prospects.

During the second quarter, Midnight, like most other operators in the area, continued to experience high costs in all aspects of its field operations including completions and tie-ins. We responded to these high costs by cautiously pacing our activities and by preparing to accelerate our operations once the market becomes more economically favourable. On top of the high costs, the oil and gas industry continues to reel from the inappropriate attack by the Canadian Government on income trusts in Q4 2006 which consequently softened the capital markets. Notwithstanding these challenges, Midnight's balance sheet remains healthy and our cash flow continues to be strong and with the breadth and depth of our prospect inventory, Midnight is in a very good position to be able to respond quickly to a positive upswing in the market.

Clearly the industry is experiencing a contraction resulting from high service costs and lower natural gas prices compounded by a softening in the capital markets for junior E&P companies. In spite of our confidence in the strength of our team and the potential of our assets and prospect inventory, we intend to approach this time with reasonable prudence and caution. As a result of our restrained activity levels and our commodity price outlook, we are adjusting our annual guidance to remain constant for the balance of the year and to exit at 2,400 to 2,500 boe/d based on a capital program approximately matching cash flows.

At Midnight we have an experienced and proven high-end management and technical team and an excellent risked balanced prospect inventory. We are able to react quickly to changing environments and continue to manage our oil and gas investments in a proficient manner, while staying vigilant to opportunities that may arise in a sensitive and reactive marketplace. We are confident in our abilities to realize success in our areas of expertise and to capitalize on opportunities that bring value to our shareholders and we continue to be very positive about our prospects and potential.

Signed "Fred Woods"

Fred Woods
President and Chief Executive Officer
August 7, 2007

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following Management Discussion and Analysis as provided by the management of Midnight Oil Exploration Ltd. ("Midnight" or the "Company") should be read in conjunction with the unaudited Consolidated Financial Statements and accompanying notes for the three and six months ended June 30, 2007 and 2006 and the audited Consolidated Financial Statements, related notes and Management Discussion and Analysis for the years ended December 31, 2006 and 2005.

Basis of Presentation – The financial data presented below has been prepared in accordance with Canadian Generally Accepted Accounting Principles ("GAAP"). The reporting and measurement currency is the Canadian dollar. For the purpose of calculating unit costs, natural gas is converted to a barrel equivalent ("boe") using six thousand cubic feet of natural gas equal to one barrel of oil unless otherwise stated. The following Management Discussion and Analysis compares the results of the six months ended June 30, 2007 ("YTD 2007") to the six months ended June 30, 2006 ("YTD 2006") and the results of the three months ended June 30, 2007 ("Q2 2007") to the three months ended June 30, 2006 ("Q2 2006") and the results of the three months ended March 31, 2007 ("Q1 2007").

Non-GAAP Measurements - Within the Management Discussion and Analysis references are made to terms commonly used in the oil and gas industry. Funds from operations, funds from operations per share and netbacks are not defined by GAAP in Canada and are referred to as non-GAAP measures. Funds from operations per share is calculated based on the weighted average number of common shares outstanding consistent with the calculation of net income per share. Netbacks equal total revenue less royalties, operating costs and transportation costs calculated on a boe basis. Management utilizes these measures to analyze operating performance and leverage. Funds from operations is commonly referred to as cash flow by research analysts and is used to value and compare oil and gas companies and is frequently included in published research when providing investment recommendations. Total boes are calculated by multiplying the daily production by the number of days in the period.

The following table reconciles cash provided by operations to funds from operations which is used in the MD&A:

(\$000s)	Q2 2007	Q2 2006	Q1 2007	YTD 2007	YTD 2006
Cash provided by operations	833	8,063	8,044	8,877	13,082
Changes in non-cash working capital	5,199	(1,548)	(2,658)	2,541	(1,380)
Funds from operations	6,032	6,515	5,386	11,418	11,702

Forward Looking Statements - Certain statements contained within the Management Discussion and Analysis, and in certain documents incorporated by reference into this document, constitute forward-looking statements. These statements relate to future events or our future performance. All statements other than statements of historical fact may be forward-looking statements. Forward-looking statements are often, but not always, identified by the use of words such as "seek", "anticipate", "budget", "plan", "continue", "estimate", "expect", "forecast", "may", "will", "project", "predict", "potential", "targeting", "intend", "could", "might", "should", "believe" and similar expressions. These statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements. We believe the expectations reflected in those forward-looking statements are reasonable but no assurance can be given that these expectations will prove to be correct and such forward-looking statements included in, or incorporated by reference into, this Management Discussion and Analysis should not be unduly relied upon. These statements speak only as of the date of this Management Discussion and Analysis or as of the date specified in the documents incorporated by reference into this Management Discussion and Analysis, as the case may be.

In particular, this Management Discussion and Analysis, and the documents incorporated by reference, contain forward-looking statements pertaining to the following:

- *the performance characteristics of our oil and natural gas properties;*
- *oil and natural gas production levels;*
- *the size of the oil and natural gas reserves;*
- *projections of market prices and costs;*
- *supply and demand for oil and natural gas;*
- *expectations regarding the ability to raise capital and to continually add to reserves through acquisitions and development;*

- *treatment under governmental regulatory regimes and tax laws; and*
- *capital expenditures programs.*

The actual results could differ materially from those anticipated in these forward-looking statements as a result of the risk factors set forth below and elsewhere in this Management Discussion and Analysis:

- *volatility in market prices for oil and natural gas;*
- *liabilities inherent in oil and natural gas operations;*
- *uncertainties associated with estimating oil and natural gas reserves;*
- *competition for, among other things, capital, acquisitions of reserves, undeveloped lands and skilled personnel;*
- *incorrect assessments of the value of acquisitions;*
- *geological, technical, drilling and processing problems; and*
- *changes in income tax laws or changes in tax laws and incentive programs relating to the oil and gas industry.*

Statements relating to "reserves" or "resources" are deemed to be forward looking statements, as they involve the implied assessment, based on certain estimates and assumptions, that the resources and reserves described can be profitably produced in the future. Readers are cautioned that the foregoing lists of factors are not exhaustive. The forward looking statements contained in this Management Discussion and Analysis and the documents incorporated by reference herein are expressly qualified by this cautionary statement. We do not undertake any obligation to publicly update or revise any forward-looking statements except as required by securities law.

This Management Discussion and Analysis is dated as of August 7, 2007.

Selected Quarterly Information

Set out below is selected quarterly information for Midnight for the last eight quarters:

Financial (000's, except for per share amounts)	2007		2006				2005	
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
Petroleum and natural gas sales	\$ 11,009	\$ 10,894	\$ 9,410	\$ 10,099	\$ 10,988	\$ 9,191	\$ 8,772	\$ 5,997
Funds from operations	6,032	5,386	4,555	5,445	6,515	5,187	4,991	3,073
Per share								
– Basic	0.13	0.11	0.10	0.13	0.16	0.14	0.16	0.12
– Diluted	0.13	0.11	0.10	0.13	0.16	0.13	0.16	0.12
Net income (loss)	\$ 51	\$ (424)	\$ (565)	\$ 320	\$ 82	\$ 208	\$ 864	\$ 487
Per share								
– Basic	0.00	(0.01)	(0.01)	0.01	0.00	0.01	0.03	0.02
– Diluted	0.00	(0.01)	(0.01)	0.01	0.00	0.01	0.03	0.02
Additions to capital assets	\$ 3,439	\$ 12,582	\$ 8,652	\$ 13,670	\$ 9,945	\$ 29,485	\$ 55,285	\$ 8,175
Net debt	26,577	29,170	21,974	33,579	25,297	41,028	16,730	11,344
Total assets	161,537	159,594	152,833	147,677	138,842	134,452	111,171	54,187
Shares outstanding								
Basic	47,828	47,828	47,828	42,328	42,328	38,328	38,328	26,328
Diluted	53,168	53,001	53,548	45,914	45,903	41,495	41,511	29,360
Operations								
Average daily production								
Natural gas (mcf/d)	5,769	6,891	7,352	7,637	10,091	5,926	4,694	4,885
Oil & NGLs (bbls/d)	1,185	1,090	890	841	830	901	600	270
Combined (boe/d)	2,146	2,239	2,115	2,114	2,512	1,889	1,382	1,084
Netback (\$/boe)	\$ 37.37	\$ 32.45	\$ 29.08	\$ 33.15	\$ 31.68	\$ 33.54	\$ 43.68	\$ 34.21

Midnight has a balanced portfolio of light oil and sweet gas prospects which have delivered solid production and funds from operations. Growth in petroleum and natural gas sales and funds from operations is derived by the combination of increased production and strong commodity prices. Midnight commenced operations in December 2004 with production averaging 723 boe/d for the month. On November 29, 2005, Midnight acquired the Red Earth property increasing our production for Q4 2005 by 303 boe/d. Production growth continued with the drilling of 33

gross (17.2 net) wells in 2006 and 10 gross (3.6 net) wells for the first half of 2007. In the last eight quarters, Oil and NGLs prices have remained robust with sales realized in a range of \$58.25/bbl for Q4 2006 to \$77.01/bbl in Q3 2006 and are currently \$66.76/bbl in the latest quarter. Natural gas prices have been quite volatile with the high of \$11.43/mcf in Q4 2005 to a low of \$5.85/mcf in Q3 2006. During the last eight quarters, Midnight has increased its focus in oil with current production being 55% Oil and NGLs versus only 25% Oil and NGLs in Q3 2005.

Production

The following table outlines our production volumes for the periods indicated:

Production	Q2 2007	Q2 2006	Q1 2007	YTD 2007	YTD 2006
Natural Gas (mcf/d)	5,769	10,091	6,891	6,327	8,020
Oil (bbls/d)	1,008	660	920	964	712
NGLs (bbls/d)	177	170	170	173	153
Total (boe/d)	2,146	2,512	2,239	2,192	2,202

Midnight's Q2 2007 production decreased 15% from Q2 2006 with gas production decreasing 43% and oil and NGLs production increasing 43%. Gas production decreased as Q2 2006 had flush production from our Sheldon property that declined rapidly for the remainder of the year, while our oil production rose with increased production in Red Earth from our ongoing activities. Q2 2007 production remained relatively flat compared to Q1 2007 with a 4% decrease with minimal activity during the quarter. YTD 2007 production is essentially the same as YTD 2006 although our product mix has changed. Oil and liquids make up 52% of our production for YTD 2007 compared to 39% for YTD 2006.

Pricing

Midnight's natural gas prices are influenced by overall North American supply and demand balance, seasonal changes, storage levels and transportation capacity. Midnight markets its natural gas on a daily spot market basis at various delivery points in Alberta and therefore, the average Alberta spot market price in Canadian dollars per mcf is an appropriate benchmark for our gas prices. We continue to receive a slight premium to the Alberta spot price for our gas sales and expect our future realized price to coincide with the Alberta spot price.

The outlook for natural gas prices is quite mixed in the short term. Current North American natural gas storage levels are at record levels. US drilling of natural gas remains strong and the supply from Liquefied Natural Gas imports continue to expand and act as a counterbalance to the reduced natural gas supply flowing from Canada. The weather remains a key component on the demand side. A sustained hot summer in the Eastern US or an active hurricane season in the Gulf Coast are catalysts required to significantly increase the natural gas prices.

Midnight's realized oil price has a high correlation to the Edmonton Par benchmark price which generally has a strong correlation to the US benchmark West Texas Intermediate at Cushing, Oklahoma ("WTI") price adjusted by the Canadian to US dollar exchange rate. Canadian light oil prices correlate to refinery postings that adjust WTI for the Canadian to US dollar exchange rate as well as transportation costs and quality adjustments. The strengthening of the Canadian dollar relative to the US dollar lowers the effective price received and widens the gap between WTI and Edmonton par. Midnight's oil price is significantly influenced by global supply and demand.

The outlook for crude oil remains positive as the crude fundamentals are unchanged. The world crude supply is declining whereas the physical demand remains firm. As a result, Midnight has increased its exposure to crude over its exposure to the weaker natural gas market.

Prices for NGLs have their own market dynamic. NGLs include condensate, pentane, butane and propane. While prices for condensate and pentane have a relatively strong correlation to oil prices, prices for butane and propane trade at varying discounts due to the market conditions of local supply and demand.

Year-over-year and quarter-over-quarter, Midnight's realized price for commodities has tracked with the appropriate benchmark prices. Midnight did not buy or sell any commodity or currency hedges during the period.

The following table outlines benchmark prices compared to Midnight's realized prices:

Prices and Marketing	Q2 2007	Q2 2006	Q1 2007	YTD 2007	YTD 2006
Benchmark Prices					
Alberta spot (\$/mcf)	\$ 6.94	\$ 5.87	\$ 7.26	\$ 7.10	\$ 6.58
WTI oil (\$US/bbl)	64.95	70.51	58.09	61.58	66.95
Cdn/US average exchange rate	0.911	0.892	0.853	0.882	0.879
Edmonton Par (\$/bbl)	\$ 72.64	\$ 79.06	\$ 67.61	\$ 70.12	\$ 74.16
Midnight's Realized Price					
Natural gas (\$/mcf)	\$ 7.22	\$ 5.98	\$ 7.82	\$ 7.55	\$ 6.50
Oil (\$/bbl)	69.80	75.06	64.04	67.06	69.64
NGLs (\$/bbl)	49.43	61.99	47.07	48.29	61.12
Oil & NGLs (\$/bbl)	66.76	72.38	61.39	64.20	68.13
Total (\$/boe)	\$ 56.37	\$ 48.07	\$ 54.06	\$ 55.20	\$ 50.63

Petroleum and Natural Gas Sales

The following table outlines our production sales by category for the periods indicated below:

Petroleum and Natural Gas Sales (000's)	Q2 2007	Q2 2006	Q1 2007	YTD 2007	YTD 2006
Natural Gas	\$ 3,791	\$ 5,487	\$ 4,851	\$ 8,642	\$ 9,429
Oil	6,403	4,506	5,304	11,707	8,976
NGLs	794	962	721	1,515	1,696
Royalty income	21	33	18	39	78
Total	\$ 11,009	\$ 10,988	\$ 10,894	\$ 21,903	\$ 20,179

Petroleum and natural gas sales totalled \$11.0 million for Q2 2007 and \$21.9 million for YTD 2007. Petroleum and natural gas sales for Q2 2007 were substantially unchanged from Q2 2006 with higher commodity prices offsetting the production declines. Q2 2007 increased 1% from Q1 2007 due to the higher realized commodity prices during the quarter. YTD 2007 sales increased 9% from YTD 2006 with higher realized commodity prices accounting for all of the increase.

Royalties

Royalty payments are made by producers of oil and gas to the owners of the mineral rights on our leases which include provincial governments (Crown) and freehold landowners as well as to other third parties by way of contractual overriding royalties.

In Alberta, royalties on natural gas and NGLs are charged by the government based on an established monthly reference price. The reference price is meant to reflect the average price for gas and NGLs in Alberta. Gas cost allowance, custom processing credits, and other incentive programs reduce the effective royalty rate.

Oil royalty rates are generally a function of production rates on a per well basis and market prices. They may also be subject to certain reductions and incentives. Crown royalties in Alberta are generally satisfied by delivering the required amount of oil to the Crown.

The following tables outline our royalties by type and by commodity:

Royalties by Type (000's)	Q2 2007	Q2 2006	Q1 2007	YTD 2007	YTD 2006
Crown	\$ 1,354	\$ 1,925	\$ 1,854	\$ 3,208	\$ 3,373
Gross overriding & Freehold	264	181	136	400	498
ARTC	-	(137)	-	-	(248)
Total	\$ 1,618	\$ 1,969	\$ 1,990	\$ 3,608	\$ 3,623
\$/boe	\$ 8.29	\$ 8.61	\$ 9.88	\$ 9.09	\$ 9.09
% of revenue	14.7	17.9	18.3	16.5	18.0

Effective January 1, 2007 the Alberta Royalty Tax Credit (ARTC) has been eliminated.

Royalties by Commodity (excluding ARTC)	Q2 2007	Q2 2006	Q1 2007	YTD 2007	YTD 2006
Natural Gas					
000's	\$ 71	\$ 970	\$ 929	\$ 1,000	\$ 2,179
% of revenue	1.9	17.7	19.2	11.6	23.1
Oil					
000's	\$ 1,358	\$ 868	\$ 846	\$ 2,204	\$ 1,216
% of revenue	21.2	19.3	16.0	18.8	13.5
NGLs					
000's	\$ 189	\$ 268	\$ 215	\$ 404	\$ 476
% of revenue	23.8	27.9	29.8	26.7	28.1

For YTD 2007, royalties averaged 16.5% of revenue compared to 18.0% for the corresponding period in 2006. During the quarter Midnight received gas cost allowance ("GCA") adjustments for 2006 and an increase to its current year GCA to total \$767,000 credits for the first half that had a favourable impact on our royalty rates during the period. YTD 2007 natural gas royalties were 11.6% of natural gas revenue compared to 23.1% for YTD 2006. Midnight had applied for a reduction in the useful life for certain facilities which has accelerated the rate in which we will receive our GCA for these areas. Excluding the impact of GCA, gas crown royalties are averaging approximately 20% for 2007 and we expect royalties to continue at this rate, however this will be offset by approximately \$150,000 per month for GCA credits for the remainder of the year. Q2 2007 natural gas royalties were only 1.9% of natural gas revenue due to the GCA credits booked during the period. YTD 2007 oil crown royalties were 18.8% of oil revenue which is an increase from 13.5% for YTD 2006. Q2 2007 oil royalties were 21.2% of oil revenues compared to 16% in Q1 2007 and 19.3% in Q2 2006. Oil royalty rates have increased over Q1 as certain wells that were subject to a Third Tier Royalty Exemption in previous quarters are now subject to royalties and certain new wells that have been brought on stream are subject to higher royalty rates. We expect our oil royalty rates to be over 20% of revenue for the remainder of the year. NGLs royalties for YTD 2007 averaged 26.7% of revenue compared to 28.1% for YTD 2006.

Operating Expenses

Operating Expenses (000's)	Q2 2007	Q2 2006	Q1 2007	YTD 2007	YTD 2006
Operating expenses	\$ 2,084	\$ 1,764	\$ 2,346	\$ 4,430	\$ 3,409
Total (\$/boe)	\$ 10.67	\$ 7.72	\$ 11.64	\$ 11.17	\$ 8.55

Operating expenses during Q2 2007 were \$10.67/boe and \$11.17/boe for YTD 2007. Q2 2007 operating costs decreased \$0.97/boe from Q1 2007 and increased \$2.95/boe from the same period in 2006. YTD 2007 operating costs were \$11.17/boe compared to \$8.55/boe for YTD 2006. Operating costs continue to be negatively impacted by industry wide increased cost pressures which has increased the overall operating costs for the Company. Included in operating expenses is the trucking of emulsion. For the first half of 2007, emulsion trucking totalled \$486,000 or \$1.22/boe. Despite the higher cost structure, Midnight's operating costs decreased for the quarter as Q1 2007 costs were impacted by third party charges for maintenance and processing as well as higher than expected water handling and disposal fees. Midnight has reduced the operating expense per boe for the last two quarters and

expects to continue on this trend as new production is brought on stream and as additional oil production in Red Earth is tied-in.

Transportation Expenses

Transportation expenses are defined by the point of legal custody transfer of the commodity and are influenced by the nature of the production, location, availability of transportation and the sales point. The cost of delivering production to the custody transfer point is shown separately as transportation expense. Transportation charges are generally incurred for commodities that are transported through owned or third party infrastructure to an established delivery point such as AECO in Alberta at an agreed tariff and for trucking clean oil.

Transportation charges were \$9,000 for Q2 2007 (\$0.04/boe) and \$28,000 for YTD 2007 (\$0.07/boe). This compares to \$19,000 (\$0.09/boe) in Q1 2007 and \$14,000 (\$0.06/boe) in Q2 2006. Midnight currently incurs minimal transportation charges as most of our natural gas is being sold at the wellhead and most of our oil production is trucked as emulsion which is classified as an operating expense as title does not transfer until it has been processed.

Interest Expense

YTD 2007 interest expense totalled \$765,000. Included in interest expense for the period is \$185,000 of interest accrued on our unspent flow-through share obligation. YTD 2007 interest expense excluding this amount totalled \$580,000 on average bank debt of approximately \$20.6 million representing an effective interest rate of approximately 5.8%. During YTD 2006, interest expense totalled \$405,000 on average bank debt of approximately \$16 million representing an effective interest rate of 5.0%. Q2 2007 interest expense totalled \$426,000 compared to \$235,000 for Q2 2006 as both average debt and interest rates were higher in Q2 2007. Interest expense has increased with an increase in our debt levels and our effective rate has increased with the increase in Canadian interest rates. Our interest in 2007 is expected to fluctuate with the changes in the Bank of Canada rates and our net debt to cash flow ratio along with the additional interest charge from our flow-through share obligation.

General and Administration Expenses

The YTD 2007 cash portion of general and administration ("G&A") expenses totalled \$1,516,000 (\$3.82/boe compared to \$935,000 (\$2.34/boe) for the YTD 2006 period. In 2006, Midnight's general and administration expenses were allocated based on the Administrative and Technical Service Agreement ("TSA") with Daylight Energy Ltd. ("Daylight"). Under this agreement, Daylight had been the employer on behalf of the parties and received payment or reimbursement from Midnight for certain technical and administrative services provided to Midnight. The Company was charged for its direct activities and for its proportionate share of overhead based on production and capital spending. With the termination of the TSA, Midnight is responsible for its own activities with Daylight still providing certain administrative and other non-competitive services through an agreed upon monthly fee. During YTD 2007 Midnight paid \$0.7 million for these direct services. Q2 2007 cash G&A increased to \$803,000 from \$713,000 in Q1 2007 and from \$499,000 in Q2 2006. The increase from Q1 2007 is a result of lower operating recoveries and less capitalized G&A in the quarter as gross G&A decreased slightly quarter over quarter.

Midnight expects cash G&A to be \$3.50 to \$4.50 per boe in 2007 with increased labour costs and additional charges to operate on a stand alone basis.

Stock-Based Compensation

The Company applies the fair value method for valuing stock option grants and warrants. Under this method, compensation costs attributable to all share options granted and warrants issued are measured at fair value at the grant and issuance date and expensed over the vesting period with a corresponding increase to contributed surplus.

The stock-based compensation associated with employee salaries that are capitalized is proportionately capitalized. Midnight recognized stock-based compensation expense of \$440,000 for YTD 2007 and capitalized a corresponding \$188,000. During YTD 2007 284,500 stock options were granted while 664,300 options were forfeited. Midnight's unamortized portion of stock-based compensation is \$2.2 million at June 30, 2007.

The components of general and administration expense are as follows:

General and Administration Expenses (000's)	Q2 2007	Q2 2006	Q1 2007	YTD 2007	YTD 2006
Direct G&A	\$ 1,424	\$ 131	\$ 1,427	\$ 2,851	\$ 274
Technical service fee from Daylight	-	1,083	-	-	2,086
Overhead recoveries	(14)	(180)	(83)	(97)	(308)
Capitalized G&A	(607)	(535)	(631)	(1,238)	(1,117)
Cash G&A	\$ 803	\$ 499	\$ 713	\$ 1,516	\$ 935
Stock-based compensation	154	2	98	252	153
Net G&A	\$ 957	\$ 501	\$ 811	\$ 1,768	\$ 1,088
Cash G&A (\$/boe)	\$ 4.11	\$ 2.18	\$ 3.54	\$ 3.82	\$ 2.34
Stock-based compensation (\$/boe)	0.79	0.01	0.49	0.64	0.38
Net G&A (\$/boe)	\$ 4.90	\$ 2.19	\$ 4.03	\$ 4.46	\$ 2.72

Depletion, Depreciation and Accretion

For YTD 2007, depletion, depreciation and accretion ("DD&A") was \$11.9 million (\$30.10/boe) versus \$11.1 million (\$27.89/boe) for YTD 2006. The increase is a result of a larger capital base being depleted as well as depleting at a higher rate from higher finding and development costs. Q2 2007 DD&A totalled \$6.0 million compared to \$6.5 million in Q2 2006 and \$5.9 million in Q1 2007. The decrease for Q2 2007 from Q2 2006 is a result of lower production during the period.

Taxes

The YTD 2007 tax recovery was \$268,000 versus an expense of \$171,000 for YTD 2006. During the quarter Midnight recognized a recovery of approximately \$150,000 due to the impact of the reduction in tax rates that have been substantively enacted. The difference in the expected rate of 32.1% and the effective rate is primarily from differences relating to stock-based compensation, other non-deductible items and the impact of the reduction in tax rates.

In Q1 2007, Midnight renounced its flow-through share expenditures and accordingly recorded a \$6.2 million future tax liability for the estimated cost of the renounced tax deductions.

Midnight does not expect to become taxable on an income tax basis in 2007 and has approximately \$130 million in tax pools to shelter taxable income in future years.

Funds from Operations and Net Income

For Q2 2007, funds from operations totalled \$6.0 million (\$0.13 per basic and diluted share). Funds from operations totalled \$6.5 million (\$0.16 per basic and diluted share) in Q2 2006 and \$5.4 million (\$0.11 per basic and diluted share) for Q1 2007. For YTD 2007 funds from operations totalled \$11.4 million (\$0.24 per basic and diluted share) compared to YTD 2006 funds from operations of \$11.7 million (\$0.30 per basic and \$0.29 per diluted share).

For YTD 2007 the net loss was \$373,000 compared to net income of \$290,000 for YTD 2006. Net income for Q2 2007 totalled \$51,000 compared to net income of \$82,000 in Q2 2006.

The following table summarizes the net income on a barrel of oil equivalent basis for the periods indicated.

(\$/boe)	Q2 2007	Q2 2006	Q1 2007	YTD 2007	YTD 2006
Sales price	\$ 56.37	\$ 48.07	\$ 54.06	\$ 55.20	\$ 50.63
Royalties	8.29	8.61	9.88	9.09	9.09
Operating expenses	10.67	7.72	11.64	11.17	8.55
Transportation expenses	0.04	0.06	0.09	0.07	0.52
Operating netback	\$ 37.37	\$ 31.68	\$ 32.45	\$ 34.87	\$ 32.47
General and administration	4.11	2.18	3.54	3.82	2.34
Interest	2.18	1.03	1.68	1.93	1.02
Other income	-	(0.04)	-	-	(0.32)
Capital tax	-	(0.07)	-	-	-
Cash flow netback	\$ 31.08	\$ 28.58	\$ 27.23	\$ 29.12	\$ 29.43
Depletion, depreciation and accretion	30.78	28.41	29.45	30.10	27.89
Stock-based compensation	0.79	0.01	0.49	0.63	0.38
Future tax (reduction)	(0.75)	(0.20)	(0.61)	(0.68)	0.43
Net income (loss)	\$ 0.26	\$ 0.36	\$ (2.10)	\$ (0.93)	\$ 0.73

The following table provides reconciliations to the change in funds from operations and net income (loss) for Q2 2007 to Q1 2007 and for Q2 2007 to Q2 2006.

Change in Funds from Operations and Net Income (000's)	Q2 2007 to Q2 2006		Q2 2007 to Q1 2007	
	Funds from Operations	Net Income	Funds from Operations	Net Income (Loss)
Comparative period	\$ 6,515	\$ 82	\$ 5,386	\$ (424)
Increase (decrease) in revenue:				
Change in production volumes	(1,600)	(1,600)	(336)	(336)
Change in prices	1,621	1,621	451	451
Change in royalties	351	351	372	372
Change in other income	(9)	(9)	-	-
(Increase) decrease in expenses:				
Operating	(320)	(320)	262	262
Transportation	5	5	10	10
Interest	(191)	(191)	(87)	(87)
Cash general and administration	(304)	(304)	(90)	(90)
Stock-based compensation	-	(152)	-	(56)
Depletion, depreciation and accretion	-	484	-	(75)
Taxes	(17)	84	-	24
Abandonment expenditures	(19)	-	64	-
Current period	\$ 6,032	\$ 51	\$ 6,032	\$ 51

Capital Expenditures

The following table highlights the breakdown of expenditures by category for the periods indicated:

Capital Expenditures (000's)	Q2 2007	Q2 2006	Q1 2007	YTD 2007	YTD 2006
Land	\$ 59	\$ 1,013	\$ 68	\$ 127	\$ 4,695
Geological and geophysical	714	931	1,206	1,920	2,024
Drilling	641	3,032	6,093	6,734	16,118
Completions	772	1,283	2,442	3,214	5,896
Facilities, pipelines and equipment	1,253	3,686	2,773	4,026	10,697
Total expenditures	\$ 3,439	\$ 9,945	\$ 12,582	\$ 16,021	\$ 39,430

Due to the wet weather and the resulting prolonged spring break up, capital expenditures for the quarter totalled only \$3.4 million in Q2 2007 versus \$9.9 million in Q2 2006. Midnight did not drill any wells during the second quarter.

During YTD 2007 Midnight drilled 10 gross (3.6 net) wells comprised of 9 gross (2.6 net) natural gas wells and 1 gross (1.0 net) oil well with 100% success. Four (2.2 net) of our natural gas wells were drilled in the Deep Basin and the remaining 5 (0.4 net) were drilled in West Central. Drilling costs accounted for 42% of our capital expenditures in YTD 2007 and Midnight spent an additional \$3.2 million on completion operations and \$4.0 million on facilities, pipelines and equipment. Geological and geophysical expenditures include capitalized G&A and seismic expenditures and totalled \$1.9 million for YTD 2007. Capital expenditures were balanced among our principal properties with 35% spent on our oil properties in Red Earth, 52% on our Deep Basin gas opportunities and 13% on non-operated West Central and minor properties. Capital expenditures for the year are down 60% for the same period in 2006 as our activity has been slower during the year. For YTD 2006, we drilled 23 gross (13.6 net) wells.

In addition to the cash capital expenditures, we capitalized \$188,000 of stock-based compensation and the related future tax liability of \$82,000 consistent with the exploration compensation that we have added to our property base. Midnight had approximately 159,000 net acres of undeveloped land at June 30, 2007.

Equity

During YTD 2007, Midnight issued 284,500 options to employees, 601,800 options that were granted to Daylight employees were forfeited along with 62,500 options to a retired director were forfeited. No options were exercised during 2007. At June 30, 2007 the Company had 3,257,000 options outstanding at an average exercise price of \$2.64. Of these 425,000 have vested and are exercisable at an average price of \$3.50. At August 7, 2007 the Company had 47,827,829 common shares, 3,257,000 stock options and 2,083,333 warrants outstanding.

On November 7, 2006, the Company closed a bought deal financing with a syndicate of underwriters and issued 5.5 million common shares at a price of \$3.05 per common share to raise gross proceeds of approximately \$16.8 million. Management participated in this issue, acquiring 114,000 shares at \$3.05 per share. The offering was done by way of short form prospectus.

On May 17, 2006, Midnight closed a bought deal financing and issued 4 million flow-through common shares at a price of \$5.10 per flow-through common share to raise gross proceeds of \$20.4 million. Management and service providers participated in this issue acquiring 343,000 shares at \$5.10 per flow-through common share. The future tax effect of this issue was recorded in Q1 2007 when the Company renounced the expenditures.

Share Information (000's)	Q2 2007	Q2 2006	Q1 2007	YTD 2007	YTD 2006
Shares outstanding					
Basic	47,828	42,328	47,828	47,828	42,328
Diluted	53,168	45,903	53,001	53,168	45,903
Weighted average shares outstanding					
Basic	47,828	40,262	47,828	47,828	39,300
Diluted	47,828	40,730	47,828	47,828	39,761

Liquidity and Capital Resources

Midnight Oil Exploration Ltd. is listed as a senior issuer on the Toronto Stock Exchange trading under the symbol "MOX". The Company's market capitalization at June 30, 2007 was \$82.3 million.

Trading History on the TSX	Q2 2007	Q2 2006	Q1 2007	YTD 2007	YTD 2006
High	\$ 2.10	\$ 4.25	\$ 2.39	\$ 2.39	\$ 4.70
Low	\$ 1.61	\$ 3.30	\$ 1.35	\$ 1.35	\$ 3.30
Close	\$ 1.72	\$ 3.65	\$ 1.75	\$ 1.72	\$ 3.65
Volume (000's)	7,035	2,328	4,699	11,734	7,301

At June 30, 2007, Midnight had drawn \$27.8 million on its \$35.0 million credit facility and had a working capital surplus of \$1.2 million for a net debt position of \$26.6 million. On May 31, 2007, Midnight increased its credit facility to \$35 million from \$30 million. Midnight's credit facility is available on a revolving basis until May 31, 2008. On this date and at the Company's discretion, the facility is available on a non-revolving basis for a period of 366 days, at which time the facility would be due and payable. Alternatively, the facility may be extended for a further 364-day period at the request of the Company and subject to approval by the bank. The credit facility bears interest at the bank's prime rate or Bankers' Acceptances plus a stamp based on the Company's debt/cash flow ratio, calculated using the two most recent fiscal quarters. The facility is secured by a \$50 million first floating charge debenture and a general securities agreement.

Midnight anticipates that it will have adequate liquidity to fund future working capital and forecasted capital expenditures during 2007 through a combination of cash flow and additional drawing on its existing credit facility. Our 2007 capital budget has been set at \$30 million and our estimated cash flow is approximately \$25 million for the year. Expenditures for our flow-through program should be completed by the end of 2007.

Contractual Obligations

The contractual obligations for which the Company is responsible are as follows:

Contractual Obligations (000's)	Total	Less than 1 Year	1-3 Years	4-5 Years	After 5 Years
Flow through share obligation	\$ 5,924	\$ 5,924	\$ -	\$ -	\$ -
Long-term debt	27,779	-	27,779	-	-
Asset retirement obligations	5,588	194	245	221	4,928
Total Contractual Obligations	\$ 39,291	\$ 6,118	\$ 28,024	\$ 221	\$ 4,928

Midnight enters into many contractual obligations in the course of conducting its day to day business. Material contractual obligations consist of our obligation to expend exploration expenditures pursuant to our flow-through share issue on May 17, 2006 and our long-term debt with a major bank. The payment terms on the asset retirement obligation is based on an estimated timing of expenditures to be made in future periods, actual expenditures and when they may occur may differ materially than presented above. Midnight has not entered into any firm transportation commitments to date.

Financial Instruments

Financial instruments comprise cash and cash equivalents, accounts receivable and accounts payable and accrued liabilities. The fair values of these financial instruments approximate their carrying amounts due to their short-term maturities. The Company's long-term debt bears interest at a floating market rate and accordingly the fair market value approximates the carrying value. Midnight has not identified any embedded derivatives in any of its contracts.

Disclosure and Internal Control Procedures

Disclosure control procedures have been designed to ensure that information required to be disclosed by Midnight is accumulated and communicated to the Company's management as appropriate to allow timely decisions regarding required disclosure. Midnight's Chief Executive Officer and Chief Financial Officer have concluded, based on their

evaluation as of the end of the period covered by the interim filings that the Company's disclosure controls and procedures are effective to provide reasonable assurance that material information related to the issuer is made known to them by others within the Company.

Midnight incorporated new internal controls over financial reporting for 2007. Effective procedures have been designed and implemented over financial reporting in 2007; however, management is aware that there is a lack of segregation of duties due to the limited number of employees dealing with financial matters. Midnight's Chief Executive Officer, Chief Financial Officer and Vice President Finance have been with the Company since its inception and have extensive industry experience. They are aware of and actively involved in the Company's on-going operating activities. While there is an inherent weakness in internal controls over financial reporting due to the limited number of staff and the resultant lack of segregation of incompatible duties, the capabilities and involvement of the Chief Executive Officer, Chief Financial Officer and Vice President Finance serve to mitigate this structural weakness. Their efforts, together with the active involvement of the board of directors, are directed to minimize the risk of a material misstatement in financial reporting. It should be noted that while Midnight's Chief Executive Officer and Chief Financial Officer believe that the Company's disclosure and internal control procedures provide a reasonable level of assurance that they are effective, they do not expect that the disclosure and internal control procedures will prevent all errors and fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

Application of Critical Accounting Estimates

The significant accounting policies used by Midnight are disclosed in note 1 to the audited Consolidated Financial Statements for the years ended December 31, 2006 and 2005 and note 1 to the interim Consolidated Financial Statements for the six months ended June 30, 2007. Certain accounting policies require that management make appropriate decisions with respect to the formulation of estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Management reviews its estimates on a regular basis. The emergence of new information and changed circumstance may result in actual results or changes to estimated amounts that differ materially from current estimates. A detailed discussion of the critical accounting policies and practices of the Company which helps to assess the likelihood of materially different results being reported is disclosed in the 2006 Annual Management and Discussion Analysis.

New Accounting Standards

On January 1, 2007, the Company adopted the new Canadian accounting standards for financial instruments – recognition and measurement, financial instruments – presentations and disclosures, hedging and comprehensive income as disclosed in note 1 to the interim Consolidated Financial Statements for the six months ended June 30, 2007. Adopting these standards did not impact the financial statements.

Risk Factors

There are a number of risk factors facing Companies that participate in the Canadian oil and gas industry. A summary of certain risk factors relating to our business are provided in the Risk Factors Section of our Annual Information Form filed on SEDAR.

Additional Information

Additional information relating to Midnight is filed on SEDAR and can be viewed at www.sedar.com. Information can also be obtained by contacting the Company at Midnight Oil Exploration Ltd., 2100, 144 4th Ave S.W., Calgary, Alberta T2P 3N4 or by email to ir@midnightoil.ca or by accessing our website at www.midnightoil.ca.

Consolidated Balance Sheets

(000's) (unaudited)

	June 30, 2007	December 31, 2006
Assets		
Current assets:		
Accounts receivable	\$ 10,409	\$ 5,928
Deposits and prepaid expenses	294	189
	10,703	6,117
Future taxes	-	391
Petroleum and natural gas assets (note 2)	150,834	146,325
	\$ 161,537	\$ 152,833
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 9,501	\$ 10,153
Long-term debt (note 3)	27,779	17,938
Future taxes	5,645	-
Asset retirement obligations (note 4)	1,955	1,930
Shareholders' equity:		
Share capital (note 5)	113,585	119,807
Warrants (note 5)	42	42
Contributed surplus (note 5)	1,674	1,234
Retained earnings	1,356	1,729
	116,657	122,812
Commitments (note 7)		
	\$ 161,537	\$ 152,833

See accompanying notes to consolidated financial statements.

On behalf of the Board:

Signed *"Tom Medvedic"*
Director

Signed *"Jay Squiers"*
Director

Consolidated Statements of Income (Loss) and Retained Earnings

(000's, except per share amounts) (unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2007	2006	2007	2006
Revenues:				
Petroleum and natural gas sales	\$ 11,009	\$ 10,988	\$ 21,903	\$ 20,179
Royalties	(1,618)	(1,969)	(3,608)	(3,623)
Other income	-	9	-	128
	9,391	9,028	18,295	16,684
Expenses:				
Operating	2,084	1,764	4,430	3,409
Transportation	9	14	28	205
Interest	426	235	765	405
General and administration	957	501	1,768	1,088
Depletion, depreciation and accretion	6,010	6,494	11,945	11,116
	9,486	9,008	18,936	16,223
Income (loss) before taxes	(95)	20	(641)	461
Taxes:				
Capital (recovery)	-	(17)	-	-
Future (reduction)	(146)	(45)	(268)	171
	(146)	(62)	(268)	171
Net income (loss)	51	82	(373)	290
Retained earnings, beginning of period	1,305	1,892	1,729	1,684
Retained earnings, end of period	\$ 1,356	\$ 1,974	\$ 1,356	\$ 1,974
Income (loss) per share: (note 5)				
Basic	\$ 0.00	\$ 0.00	\$ (0.01)	\$ 0.01
Diluted	\$ 0.00	\$ 0.00	\$ (0.01)	\$ 0.01

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

(000's) (unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2007	2006	2007	2006
Cash provided by (used in):				
Operations:				
Net income (loss)	\$ 51	\$ 82	\$ (373)	\$ 290
Items not involving cash:				
Depletion, depreciation and accretion	6,010	6,494	11,945	11,116
Stock-based compensation	154	2	252	153
Future taxes (reduction)	(146)	(45)	(268)	171
Abandonment expenditures	(37)	(18)	(138)	(28)
	6,032	6,515	11,418	11,702
Changes in non-cash working capital	(5,199)	1,548	(2,541)	1,380
	833	8,063	8,877	13,082
Financing:				
Issue of common shares	-	20,400	-	20,400
Share issue costs	-	(1,239)	-	(1,239)
Increase in long-term debt	7,898	3,622	9,841	9,331
Changes in non-cash working capital	-	(74)	(162)	(79)
	7,898	22,709	9,679	28,413
Investments:				
Petroleum and natural gas additions	(3,439)	(9,945)	(16,021)	(39,430)
Changes in non-cash working capital	(5,292)	(20,827)	(2,535)	(2,065)
	(8,731)	(30,772)	(18,556)	(41,495)
Changes in cash	-	-	-	-
Cash, beginning of period	-	-	-	-
Cash, end of period	\$ -	\$ -	\$ -	\$ -
Taxes paid	\$ -	\$ -	\$ -	\$ 88
Interest paid	\$ 285	\$ 265	\$ 601	\$ 465

Cash is defined as cash and cash equivalents.

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

For the three and six months ended June 30, 2007 and 2006
(Tabular amounts are stated in thousands of dollars except share and per share amounts)
(Unaudited)

The interim consolidated financial statements for Midnight Oil Exploration Ltd. ("Midnight" or the "Company") have been prepared in accordance with accounting principles generally accepted in Canada, using the same accounting policies and methods of computation as set out in note 1 to the consolidated financial statements for the year ended December 31, 2006 except as noted below. The disclosures provided below are incremental to those included with the audited consolidated financial statements for the year ended December 31, 2006. The interim financial statements should be read in conjunction with the audited financial statements for the year ended December 31, 2006.

Certain prior year figures have been reclassified to conform with current period presentation.

1. Changes in accounting policy:

On January 1, 2007, the Company adopted the new Canadian accounting standards for financial instruments – recognition and measurement, financial instruments – presentations and disclosures, hedging and comprehensive income. Prior periods have not been restated. Additional disclosure requirements for financial instruments have been approved by the Canadian Institute of Chartered Accountants and will be required disclosure beginning January 1, 2008.

(a) Financial instruments – recognition and measurement:

This new standard requires all financial instruments within its scope, including all derivatives, to be recognized on the balance sheet initially at fair value. Subsequent measurement of all financial assets and liabilities except those held-for-trading and available for sale are measured at amortized cost determined using the effective interest rate method. Held-for-trading financial assets are measured at fair value with changes in fair value recognized in earnings. Available-for-sale financial assets are measured at fair value with changes in fair value recognized in comprehensive income and reclassified to earnings when derecognized or impaired. There were no changes to the measurement of existing financial assets and liabilities at the date of adoption.

(b) Derivatives:

The Company may use various types of derivative financial instruments to manage risks associated with crude oil and natural gas price fluctuations. These instruments are not used for trading or speculative purposes. Proceeds and costs realized from holding the related contracts are recognized in petroleum and natural gas revenues at the time that each transaction under a contract is settled. For the unrealized portion of such contracts, the Company utilizes the fair value method of accounting. The fair value is based on an estimate of the amounts that would have been paid to or received from counterparts to settle these instruments given future market prices and other relevant factors. The method requires the fair value of the derivative financial instruments to be recorded at each balance sheet date with unrealized gains or losses on those contracts recorded through net earnings.

The Company has elected to account for its commodity sales and other non-financial contracts, which were entered into and continue to be held for the purpose of receipt or delivery of non-financial items in accordance with its expected purchase, sale or usage requirements as executory contracts on an accrual basis rather than as non-financial derivatives. Prior to adoption of the new standards, physical receipt and delivery contracts did not fall within the scope of the definition of a financial instrument and were also accounted for as executory contracts.

(c) Embedded derivatives:

On adoption, the Company elected to recognize, as separate assets and liabilities, only for those embedded derivatives in hybrid instruments issued, acquired or substantively modified after January 1, 2003. The Company did not identify any material embedded derivatives which required separate recognition and measurement.

(d) Other comprehensive income:

The new standards establish a new statement of comprehensive income, which is comprised of net earnings and other comprehensive income. As the Company currently has no other comprehensive income items requiring disclosure this statement of comprehensive income is not required.

2. Petroleum and natural gas assets:

	June 30, 2007	December 31, 2006
Cost	\$ 192,951	\$ 176,594
Accumulated depletion and depreciation	(42,117)	(30,269)
	\$ 150,834	\$ 146,325

During the six months ended June 30, 2007, the Company capitalized \$1,425,000 (2006 – \$1,288,000) of general and administration expenses related to exploration and development activities. Included in this amount is the non-cash related stock-based compensation of \$188,000 (2006 - \$171,000). The future tax liability of \$82,000 (2006 - \$77,000) associated with the capitalized stock-based compensation has also been capitalized.

The cost of unproven properties at June 30, 2007 of \$25,819,000 (2006 - \$30,411,000) has been excluded from the depletion and depreciation calculation. Future development costs of proven reserves of \$4,869,000 (2006 - \$5,696,000) have been included in the depletion and depreciation calculation.

3. Long-term debt:

Midnight has a revolving term credit facility available for up to \$35 million with a Canadian chartered bank. The facility is available on a revolving basis until May 31, 2008. On May 31, 2008, at the Company's discretion, the facility is available on a non-revolving basis for a period of 366 days, at which time the facility would be due and payable. Alternatively, the facility may be extended for a further 364-day period at the request of the Company and subject to approval by the bank. The credit facility bears interest at the bank's prime rate or at Bankers' Acceptance rates plus a stamping fee based on the Company's debt to cash flow ratio, calculated using the two most recent fiscal quarters. The facility is secured by a \$50 million first floating charge debenture and a general securities agreement. At June 30, 2007, \$27,779,000 was drawn on this facility. The effective interest rate for the bank debt was 5.8% for the six months ended June 30, 2007. The \$35 million borrowing base is subject to a semi-annual and annual review by the bank.

4. Asset retirement obligations:

The Company's asset retirement obligations result from net ownership interests in petroleum and natural gas assets including well sites, gathering systems and processing facilities. The Company estimates the total undiscounted amount of cash flow required to settle its asset retirement obligations is approximately \$5.6 million which will be incurred from 2007 to 2054. The majority of the costs will be incurred between 2010 and 2025. An inflation factor of 2% has been applied to the estimated asset retirement cost at June 30, 2007 and December 31, 2006. A credit-adjusted risk-free rate of 8% was used to calculate the fair value of the asset retirement obligations at June 30, 2007 and December 31, 2006.

A reconciliation of the asset retirement obligations is provided below:

	June 30, 2007	December 31, 2006
Balance, beginning of period	\$ 1,930	\$ 1,416
Liabilities incurred	66	679
Liabilities settled	(138)	(297)
Accretion expense	97	132
Balance, end of period	\$ 1,955	\$ 1,930

5. Share capital

(a) Authorized:

The authorized share capital consists of an unlimited number of common shares without par value.

(b) Issued and outstanding:

	Number of Shares	Amount
Common shares:		
Balance, December 31, 2005	38,327,829	\$ 84,262
Issued pursuant to private placement	4,000,000	20,400
Issued pursuant to short form prospectus	5,500,000	16,775
Share issue costs (net of tax of \$739)	-	(1,630)
Balance, December 31, 2006	47,827,829	\$ 119,807
Tax effect of flow-through shares issued in 2006	-	(6,222)
Balance, June 30, 2007	47,827,829	\$ 113,585

On May 17, 2006 the Company issued 4,000,000 flow-through Common Shares at a price of \$5.10 per share. The proceeds, net of share issue costs of \$1.3 million (\$0.9 million net of tax), were \$19.1 million.

On November 7, 2006 the Company issued 5,500,000 Common Shares at a price of \$3.05 per share. The proceeds, net of share issue cost of \$1.1 million (\$0.7 million net of tax), were \$15.7 million.

Pursuant to the flow-through Common Share offering, the Company renounced \$20.4 million of qualifying oil and natural gas expenditures effective December 31, 2006. The future income tax effect and reduction to share capital was recorded in the first quarter of 2007, the period in which the Company filed the renouncement documents with the tax authorities.

(c) Per share amounts:

The following summarizes the common shares used in calculating the per share amounts:

	Three months ended June 30,		Six months ended June 30,	
	2007	2006	2007	2006
Weighted average shares outstanding:				
Basic	47,827,829	40,261,895	47,827,829	39,300,205
Diluted	47,827,829	40,730,194	47,827,829	39,761,308

The reconciling items between basic and diluted average common shares outstanding are stock options and warrants. For the three and six months ended June 30, 2007 there were 3,257,000 options that were anti-dilutive (2006 – 1,491,800) and 2,083,333 warrants that were anti-dilutive (2006 – nil).

(d) Stock options:

The Company has reserved 4,782,783 common shares for granting under option to employees, directors and other persons who provide ongoing management or consulting services to the Company. Stock options are granted for a term up to five years and vest over three years from the date granted. The exercise price of each option equals the market price of the Company's common shares on the date of the grant.

The summary of stock option activity is presented below:

	Number of options	Weighted average exercise price
Balance, December 31, 2005	1,099,800	\$ 3.50
Granted	2,590,000	2.56
Forfeited	(53,000)	3.49
Balance, December 31, 2006	3,636,800	\$ 2.83
Granted	284,500	1.91
Forfeited	(664,300)	3.37
Balance, June 30, 2007	3,257,000	\$ 2.64
Exercisable at June 30, 2007	425,000	\$ 3.50

(e) Warrants:

	Number of Warrants	Amount
Warrants:		
Balance December 31, 2006 and June 30, 2007	2,083,333	\$ 42

Each warrant is exercisable into one common share of the Company at a price of \$3.00 per share. The warrants vest equally over three years and expire on November 29, 2008. Two thirds of the warrants have vested and are exercisable at June 30, 2007.

(f) Stock-based compensation:

Midnight accounts for its stock-based compensation plan using the fair value method. Under this method, a compensation cost is charged over the vesting period for warrants and options granted to employees, officers, directors and other service providers.

Midnight has not incorporated an estimated forfeiture rate for stock options that will not vest, rather the Company accounts for actual forfeitures as they occur.

The fair value of options and warrants granted were estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions and resulting values:

	2007	2006
Fair value of options granted	\$ 0.71	\$ 0.95
Risk free interest	4.1%	4.0%
Estimated hold period prior to exercise	4 years	4 years
Expected volatility	40%	40%
Dividend per share	\$ 0.00	\$ 0.00

(g) Contributed surplus:

The following table reconciles Midnight's contributed surplus:

	June 30, 2007	December 31, 2006
Balance, beginning of period	\$ 1,234	\$ 469
Stock-based compensation	440	765
Balance, end of period	\$ 1,674	\$ 1,234

6. Related party:

Prior to December 31, 2006, Midnight's general and administration expenses were allocated based on the Administrative and Technical Service Agreement ("TSA") with Daylight Energy Ltd. ("Daylight"). Under this agreement, Daylight had been the employer on behalf of the parties and received payment or reimbursement from Midnight for certain technical and administrative services provided to Midnight. The Company was charged for its direct activities and for its proportionate share of overhead based on production and capital spending. With the termination of the TSA on December 31, 2006, Midnight is responsible for its own activities with Daylight still providing certain administrative and other non-competitive services through an agreed upon monthly fee. For the six months ended June 30, 2007 Midnight paid \$0.7 million for these direct services. For the six months ended June 30, 2006, Midnight was charged \$1.0 million for general and administration expenses and \$1.1 million for capital expenditures relating to the TSA. Payment terms to Daylight are in accordance with normal industry standards.

7. Commitments

The Company renounced \$20.4 million of qualifying oil and natural gas expenditures effective December 31, 2006 pursuant to the flow-through share offering which closed on May 17, 2006. By June 30, 2007 the Company incurred \$14.5 million of qualifying expenditures and has an additional commitment to expend \$5.9 million on qualifying expenditures by December 31, 2007.

Quarterly Information

Financial (000's, except for per share amounts)	2007		2006				2005			
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Petroleum and natural gas sales	\$ 11,009	\$ 10,894	\$ 9,410	\$ 10,099	\$ 10,988	\$ 9,191	\$ 8,772	\$ 5,997	\$ 5,050	\$ 3,170
Royalties	1,618	1,990	1,462	1,966	1,969	1,654	2,172	1,678	1,401	702
Operating expenses	2,084	2,346	2,239	1,657	1,764	1,645	1,044	902	969	782
Transportation expenses	9	19	49	28	14	191	3	5	-	3
Netback	\$ 7,298	\$ 6,539	\$ 5,660	\$ 6,448	\$ 7,241	\$ 5,701	\$ 5,553	\$ 3,412	\$ 2,680	\$ 1,683
G&A – cash charge	803	713	580	645	499	436	491	278	292	141
Net interest (income)	426	339	290	324	235	170	(68)	58	4	(18)
Abandonment expenditures	37	101	235	34	18	10	51	3	10	31
Other income	-	-	-	-	(9)	(119)	-	-	-	-
Capital tax	-	-	-	-	(17)	17	88	-	-	-
Funds from operations	\$ 6,032	\$ 5,386	\$ 4,555	\$ 5,445	\$ 6,515	\$ 5,187	\$ 4,991	\$ 3,073	\$ 2,374	\$ 1,529
Per share – Basic	0.13	0.11	0.10	0.13	0.16	0.14	0.16	0.12	0.09	0.06
– Diluted	0.13	0.11	0.10	0.13	0.16	0.13	0.16	0.12	0.09	0.06
Net income (loss)	\$ 51	\$ (424)	\$ (565)	\$ 320	\$ 82	\$ 208	\$ 864	\$ 487	\$ 158	\$ 160
Per share – Basic	0.00	(0.01)	(0.01)	0.01	0.00	0.01	0.03	0.02	0.01	0.01
– Diluted	0.00	(0.01)	(0.01)	0.01	0.00	0.01	0.03	0.02	0.01	0.01
Additions to capital assets	\$ 3,439	\$ 12,582	\$ 8,652	\$ 13,670	\$ 9,945	\$ 29,485	\$ 55,285	\$ 8,175	\$ 4,482	\$ 8,565
Net debt	26,577	29,170	21,974	33,579	25,297	41,028	16,730	11,344	6,242	4,134
Total assets	161,537	159,594	152,833	147,677	138,842	134,452	111,171	54,187	47,350	45,106
Shares outstanding										
Basic	47,828	47,828	47,828	42,328	42,328	38,328	38,328	26,328	26,328	26,328
Diluted	53,168	53,001	53,548	45,914	45,903	41,495	41,511	29,360	29,393	28,821
Operations										
Average daily production										
Natural gas (mcf/d)	5,769	6,891	7,352	7,637	10,091	5,926	4,694	4,885	5,151	3,924
Oil & NGLs (bbls/d)	1,185	1,090	890	841	830	901	600	270	297	135
Combined (boe/d)	2,146	2,239	2,115	2,114	2,512	1,889	1,382	1,084	1,156	788
Average prices received										
Natural gas (\$/mcf)	\$ 7.22	\$ 7.82	\$ 6.84	\$ 5.85	\$ 5.98	\$ 7.39	\$ 11.73	\$ 9.70	\$ 7.62	\$ 6.92
Oil & NGLs (\$/bbl)	66.76	61.39	58.25	77.01	72.38	64.17	66.19	64.97	53.64	58.96
Combined (\$/boe)	\$ 56.37	\$ 54.06	\$ 48.35	\$ 51.92	\$ 48.07	\$ 54.07	\$ 69.02	\$ 60.13	\$ 48.01	\$ 44.68
Royalties	8.29	9.88	7.51	10.11	8.61	9.73	17.09	16.82	13.33	9.89
Operating expenses	10.67	11.64	11.51	8.52	7.72	9.68	8.22	9.05	9.20	11.03
Transportation expenses	0.04	0.09	0.25	0.14	0.06	1.12	0.03	0.05	-	0.04
Netback received (\$/boe)	\$ 37.37	\$ 32.45	\$ 29.08	\$ 33.15	\$ 31.68	\$ 33.54	\$ 43.68	\$ 34.21	\$ 25.48	\$ 23.72

Corporate Information

DIRECTORS

Frederick N. Woods

President and Chief Executive Officer
Midnight Oil Exploration Ltd.
Calgary, Alberta

Peter T. Harrison ^{1, 2, 3, 4}

Senior Vice-President
Montrusco Bolton Investment Inc.
Montreal, Quebec

Anthony M. Lambert

President and Chief Executive Officer
Daylight Resources Trust
Calgary, Alberta

Tom J. Medvedic ^{1, 2, 3, 4}

Vice President, Finance and Chief Financial Officer
Calfrac Well Services Ltd.
Calgary, Alberta

Jay D. Squiers ^{1, 2, 3, 4}

Independent Businessman
Dallas, Texas
United States

Members of the following Committees

1 Audit

2 Compensation

3 Reserves

4 Corporate Governance

ABBREVIATIONS

/d	per day
bbl(s)	barrel(s)
mbbls	thousand barrels
mcf	thousand cubic feet
mmcf	million cubic feet
bcf	billion cubic feet
boe	barrels of oil equivalent
mboe	thousand barrels of oil equivalent
mmbtu	millions of British thermal units
ARTC	Alberta Royalty Tax Credit
WTI	West Texas Intermediate crude oil
NGLs	natural gas liquids
Cdn	Canadian
US	United States

CORPORATE OFFICE

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OFFICERS

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Executive Vice-President and Chief Financial Officer

Thomas F. Moslow

Senior Vice-President, Exploration

Andrew D. Weldon

Vice-President, Business Development

Chad L. Kalmakoff

Vice-President, Finance

C. Donald Leitch

Vice-President, Operations

Peter R. O'Leary

Vice-President, Geology

E. Martin Saizew

Vice-President, Engineering

Chris von Vegesack, Corporate Secretary

Partner
Burnet, Duckworth & Palmer LLP
Calgary, Alberta

Banker

Canadian Imperial Bank of Commerce
Calgary, Alberta

Legal Counsel

Burnet, Duckworth & Palmer LLP
Calgary, Alberta

Auditors

KPMG LLP
Chartered Accountants
Calgary, Alberta

Evaluation Engineers

GLJ Petroleum Consultants
Calgary, Alberta

Registrar and Transfer Agent

Valiant Trust Company
Calgary, Alberta

TSX Symbol: MOX

