DeeThree Exploration Ltd.

Q1

FIRST QUARTER Interim Report for the Three Months Ended March 31, 2012

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HIGHLIGHTS: BY THE NUMBERS

Three Months Ended March 31,	**2012**	2011	Change
(000s, except per share amounts)	*($)*	*($)*	*(%)*
Financial			
Oil and natural gas revenues	**14,277**	1,969	625
Funds from (used in) operations (1)	**5,741**	(833)	789
Per share – basic and diluted (1)	**0.09**	(0.02)	550
Cash flow from (used in) operating activities	**4,064**	(4,863)	184
Net loss	**(3,199)**	(1,991)	(61)
Per share – basic and diluted	**(0.05)**	(0.05)	–
Capital expenditures (2)	**36,715**	129,529	(72)
Working capital (deficit) (3)	**(30,898)**	20,659	(250)
Shareholders' equity	**178,732**	175,423	2
(000s)	*(#)*	*(#)*	*(%)*
Share Data			
At period-end	**66,986**	62,752	7
Weighted average – basic and diluted	**63,321**	36,294	74
			(%)
Operating (4)			
Production			
Natural gas *(mcf/d)*	**8,657**	3,744	131
Crude oil *(bbls/d)*	**1,316**	71	1,754
NGLs *(bbls/d)*	**283**	18	1,472
Total *(boe/d)*	**3,042**	713	327
Average wellhead prices			
Natural gas *($/mcf)*	**2.17**	3.77	(42)
Crude oil and NGLs *($/bbl)*	**85.48**	86.98	(2)
Total *($/boe)*	**51.58**	30.68	68
Netbacks			
Operating netback *($/boe)*	**24.59**	14.92	65
Funds flow netback *($/boe)*	**20.64**	(12.99)	259
Gross (net) wells drilled			
Gas *(#)*	**– (–)**	– (–)	– (–)
Oil *(#)*	**8 (7.1)**	2 (2.0)	300(255)
Standing *(#)*	**2 (2.0)**	– (–)	– (–)
Dry and abandoned *(#)*	**– (–)**	– (–)	– (–)
Total *(#)*	**10 (9.1)**	2 (2.0)	400(355)
Average working interest *(%)*	**91**	100	(9)

(1) Funds from (used in) operations, funds from (used in) operations per share and funds flow netback are not recognized measures under International Financial Reporting Standards ("IFRS"). Refer to the commentary in the Management's Discussion and Analysis under the heading "Non-IFRS Measurements" for further discussion.

(2) Total capital expenditures, including acquisitions and excluding non-cash transactions. Refer to the commentary in the Management's Discussion and Analysis under the heading "Capital Expenditures and Acquisitions" for further information.

(3) Current assets less current liabilities, excluding current derivative financial instruments.

(4) For a description of the boe conversion ratio, refer to the commentary in the Management's Discussion and Analysis under the heading "Other Measurements".

LETTER TO SHAREHOLDERS

DeeThree's first quarter of 2012 was operationally our busiest in Company history. Average production of 3,042 boe/d for the quarter was as budgeted with the majority of the volumes from the Company's active drilling program coming on late in the quarter.

Company Highlights:

- Achieved record production of 3,042 boe/d, resulting in a year over year increase of 327 percent and a 27 percent increase over the last quarter of 2011.
- Increased oil and NGL production by 43 percent over the previous quarter to 1,599 bbls/d compared to 1,118 bbls/d.
- Recorded $5.7 million in funds from operations, respectively a 40 percent and 789 percent increase over the fourth and first quarters of 2011.
- Funds from operations on a per share basis increased to $0.09, up 50 and 550 percent from the fourth and first quarters of 2011 respectively.
- Invested $36.7 million in capital expenditures which included the drilling of 10 (9.1 net) wells.
- Closed a $16.0 million dollar (net of expenses) flow-through financing at a flow through share price of $4.50/share.
- Completed the annual credit review in April, 2012 which resulted in an increase in DeeThree's borrowing base to $60 million from $50 million.

Operational update

In the first quarter, DeeThree rig released 10 gross (9.1 net) wells with an additional 3 gross (2.9 net) wells rig released in April. The majority of the drilling activity in the first quarter was concentrated in two of the Company's three core areas being Lethbridge and Brazeau.

Alberta Bakken Update

Production test results and additional data from the first four Alberta Bakken wells (100% working interest) drilled by DeeThree in 2012 are provided in the following table. The production test results from the recently completed third and fourth wells exceeded expectations averaging 940 bbls/d and 960 bbls/d of oil after a 10 day and 5 day test respectively.

Well Identification	Average Test Rate (bbl/d oil) [1]	End of Test Rate (bbl/d oil) [1]	IP 30 (bbl/d oil)	IP 60 (bbl/d oil)	Current Rate (bbl/d oil)	Oil Cumulative (bbls)
Location #1	765 (4 day)	550	415	370	240	25,000 (70 days)
Location #2	957 (6 day)	800	N/A	N/A	385	12,700 (22 days)
Location #3	940 (10 day)	620	N/A	N/A	N/A	9,800 (10 days)
Location #4	960 (5 day)	650	N/A	N/A	N/A	5,400 (5 days)

(1) Test rates are not necessarily indicative of long-term performance or of ultimate recovery.

DeeThree continues to augment its Alberta Bakken program with modifications to the horizontal well lengths and fracing dynamics. Overall, the Company is very pleased with the continuity of the sand being targeted. Continuous improvement in the flow rates to date has resulted in IP30 and IP60 production results exceeding type curve expectations. The Company currently has two drilling rigs in the area with two additional Alberta Bakken wells anticipated to be completed and tested prior to the end of the second quarter.

The Company has continued to expand its 100% owned oil infrastructure to accommodate anticipated future production volumes. The oil battery has been expanded and pipeline infrastructure has also been constructed to the Company's recently drilled wells to accommodate year round production. DeeThree is in the process of procuring and installing CO_2 removal facilities to process additional solution gas volumes which should be completed by the end of the third quarter.

Lethbridge Commitment Agreement

DeeThree is pleased to announce that it has extended the primary lease term on its Lethbridge property. The primary lease term has been extended for an additional two years to November 30, 2015. In exchange for the lease extension, the Company has surrendered approximately 50,000 acres while still retaining approximately 180,000 acres of what it feels is the most prospective acreage for Bakken reserves. Also as part of this extension, and in place of the twenty well commitment related to the April 13, 2010 agreement, the Company now has a commitment to drill 12 wells over the three-year period (five wells in each of 2012 and 2013 and two wells in 2014), with six of these commitment wells having been drilled to date.

Brazeau Belly River Update

In addition to the 3 (2.9 net) wells drilled in the first quarter of 2012, the Company has continued to drill through the second quarter on its Brazeau Belly River oil play. It is currently drilling the second well of the quarter with one additional well to be drilled prior to the end of June. All three of these wells will be completed as soon as weather permits.

Corporate Summary

The Company's production over the past two weeks has averaged 3,750 boe/d, not including flow rates from the two most recently completed Bakken wells described in the table above. The Company expects as many as 4.0 gross (4.0 net) additional Bakken wells and 3.0 gross (2.9 net) additional Belly River wells to be on production by the end of the second quarter.

Outlook

On March 29, 2012, Deethree announced an increase to its capital budget from $57 million to $82 million and increased guidance on its production targets for 2012, primarily due to the recent success of its drilling program. The Company had the most active quarter in its history investing $36.7 million of its total planned 2012 capital expenditure budget and remains on target to meet its previously announced exit guidance of 5,000 boe/d. The Company's Balance Sheet remains strong as it exited the first quarter with negative working capital of $30.9 million on an increased credit facility of $60 million dollars.

We look forward to providing updates with the results of this very active program as they occur.

On behalf of the Board of Directors,

Martin Cheyne
President & Chief Executive Officer
May 9, 2012

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following Management's Discussion and Analysis ("MD&A") of financial condition and results of operations for DeeThree Exploration Ltd. ("DeeThree" or the "Company") is dated May 8, 2012 and should be read in conjunction with the Company's unaudited interim financial statements and related notes for the three months ended March 31, 2012, as well as the audited financial statements and notes for the year ended December 31, 2011. The interim financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").

Non-IFRS Measurements

This MD&A contains the terms "funds from (used in) operations" and "funds from (used in) operations per share", which should not be considered an alternative to or more meaningful than cash flow from (used in) operating activities as determined in accordance with IFRS. These terms do not have any standardized meaning as prescribed by IFRS. DeeThree's determination of funds from (used in) operations and funds from (used in) operations per share may not be comparable to that reported by other companies. Management uses funds from (used in) operations to analyze operating performance and leverage, and considers funds from (used in) operations to be a key measure as it demonstrates the Company's ability to generate cash necessary to fund future capital investments and to repay debt, if applicable. Funds from (used in) operations is calculated using cash flow from (used in) operating activities as presented in the statement of cash flows before changes in non-cash working capital. DeeThree presents funds from (used in) operations per share whereby per share amounts are calculated using weighted average shares outstanding consistent with the calculation of earnings per share.

The following table reconciles funds from (used in) operations to cash flow from (used in) operating activities, which is the most directly comparable measure calculated in accordance with IFRS:

Three Months Ended March 31,	**2012**	2011
(000s)	*($)*	*($)*
Cash flow from (used in) operating activities	**4,064**	(4,863)
Changes in non-cash working capital	**1,677**	4,030
Funds from (used in) operations	**5,741**	(833)

During the three months ended March 31, 2012, the Company's funds from operations totaled $5,741,000 ($0.09 per basic and diluted share) compared to funds used in operations of $833,000 ($0.02 per basic and diluted share) in 2011.

The Company considers corporate netbacks to be a key measure as they demonstrate DeeThree's profitability relative to current commodity prices. Corporate netbacks are comprised of operating, funds flow and net loss netbacks. Operating netback is calculated as the average sales price of its commodities and then subtracts royalties, operating costs and transportation expenses. Funds flow netback starts with the operating netback and further deducts general and administrative costs, finance expense and adds finance income as well as realized gains on financial instruments. To calculate the net loss netback, DeeThree takes the funds flow netback and deducts share-based compensation expense as well as depletion and depreciation charges, accretion expense, unrealized gains on financial instruments, any impairment or exploration and evaluation expense and deferred income taxes. There is no IFRS measure that is reasonably comparable to netbacks. See the section entitled "Netbacks (per unit)" for the netback calculations.

Net debt and working capital (deficit), which represent current assets less current liabilities, excluding current derivative financial instruments, are used to assess efficiency, liquidity and the general financial strength of the Company. There is no IFRS measure that is reasonably comparable to net debt or working capital (deficit).

Other Measurements

All dollar amounts are referenced in Canadian dollars. Where amounts are expressed on a barrel of oil equivalent ("boe") basis, natural gas volumes have been converted to oil equivalence at six thousand cubic feet of gas to one barrel of oil. This conversion ratio of 6:1 is based on an energy equivalent conversion for the individual products, primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. Such disclosure of boes may be misleading, particularly if used in isolation. Readers should be aware that historical results are not necessarily indicative of future performance.

Forward-Looking Statements

Certain statements contained in this MD&A may constitute forward-looking statements. These statements relate to future events or the Company's future performance. All statements other than statements of historical fact may be forward-looking statements. Forward-looking statements are often, but not always, identified by the use of words such as "seek", "anticipate", "plan", "continue", "estimate", "expect", "may", "will", "project", "predict", "potential", "targeting", "intend", "could", "might", "should", "believe" and similar expressions. These statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements. The Company believes that 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 this MD&A should not be unduly relied upon by investors. These statements speak only as at the date of this MD&A and are expressly qualified, in their entirety, by this cautionary statement. In particular, this MD&A contains forward-looking statements pertaining to the following: projections of market prices and costs, supply and demand for natural gas and crude oil, the quantity of reserves, natural gas and crude oil production levels, capital expenditure programs, treatment under governmental regulatory and taxation regimes, and expectations regarding the Company's ability to raise capital and to continually add to reserves through acquisitions and development.

With respect to forward-looking statements contained in this MD&A, the Company has made assumptions regarding, among other things, the legislative and regulatory environments of the jurisdictions where the Company carries on business or has operations, the impact of increasing competition and the Company's ability to obtain additional financing on satisfactory terms.

The Company's actual results could differ materially from those anticipated in these forward-looking statements as a result of the risk factors included in this MD&A such as: volatility in the market prices for natural gas, crude oil and NGLs; uncertainties associated with estimating reserves; geological, technical, drilling and processing problems; liabilities and risks, including environmental liabilities and risks inherent in natural gas and crude oil operations; incorrect assessments of the value of acquisitions; and, competition for, among other things, capital, acquisitions of reserves, undeveloped lands and skilled personnel. In addition, test results are not necessarily indicative of long-term performance or of ultimate recovery.

This forward-looking information represents the Company's views as at the date of this MD&A and such information should not be relied upon as representing its views as of any date subsequent to the date of this MD&A. DeeThree has attempted to identify important factors that could cause actual results, performance or achievements to vary from those current expectations or estimates expressed or implied by the forward-looking information. However, there may be other factors that cause results, performance or achievements not to be as expected or estimated and that could cause actual results, performance or achievements to differ materially from current expectations. There can be no assurance that forward-looking information will prove to be accurate, as results and future events could differ materially from those expected or estimated in such statements. Accordingly, readers should not place undue reliance on forward-looking information. The Company disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as expressly required by applicable securities legislation.

Description of the Company

DeeThree is a Calgary based resource company actively engaged in natural gas and light crude oil exploration, development and production in key areas of the Western Canadian Sedimentary Basin. DeeThree commenced operations in 2007 as a private company focused on creating long-term shareholder value through prudent operational and financial management.

DeeThree has created a platform for growth through a sound business strategy that includes low risk development, high impact exploration and strategic acquisitions. The Company has three core operating areas: the Peace River Arch area of northwestern Alberta as well as the Brazeau area of west central Alberta, which are prospective for natural gas, light crude oil and natural gas liquids, and the Lethbridge region of southern Alberta, which features shallow gas and prospective Bakken light oil. These three areas have provided the Company with a balanced and diverse production base.

Common shares of DeeThree are listed for trading on the Toronto Stock Exchange under the symbol DTX and the United States OTCQX under the symbol DTHRF.

In late 2008, DeeThree completed its first significant acquisition from a major oil and gas producer of properties in the Lethbridge area of southern Alberta (the "Lethbridge property"). The Lethbridge property was the primary focus of the Company until late in the first quarter of 2011 when DeeThree closed a transformational acquisition of properties in the Peace River Arch and Brazeau areas (the "Peace River Arch and Brazeau properties"). On March 22, 2011 (and effective January 1, 2011), the Company acquired approximately 1,830 boe/d (40 percent light crude oil and NGLS) of primarily high working interest, operated crude oil, natural gas and NGLs production and reserves.

First Quarter 2012 Transactions

In February 2012, the Company received payment of $1,000,000 as proceeds from the default on a farm-out arrangement entered into during 2011. Details of the farm-out are included in the December 31, 2011 MD&A.

On March 27, 2012, the Company issued 3,834,100 flow-through shares at a price of $4.50 per flow-through share for total gross proceeds of $17,253,450 ($16,011,450 net of estimated share issue expenses), including 500,100 flow-through shares ($2,250,450) issued on the exercise in full of the underwriters' over-allotment option. The proceeds of the flow-through share offering will be used to conduct exploration activity on the Company's properties.

Financial and Operating Results

Sales Volumes

Three Months Ended March 31,	**2012**	2011
Sales		
Natural gas *(mcf/d)*	**8,657**	3,744
Crude oil *(bbls/d)*	**1,316**	71
NGLs *(bbls/d)*	**283**	18
Total sales *(boe/d)*	**3,042**	713
	(%)	*(%)*
Production Split		
Natural gas	**47**	88
Crude oil	**43**	10
NGLs	**10**	2
Total	**100**	100

For the first quarter of 2012, the Company's production increased 327 percent to average 3,042 boe/d compared to 713 boe/d in the same period of 2011 (which included 9 days of production from the acquisition of the Peace River Arch and Brazeau properties) and increased 27 percent from the 2,403 boe/d recorded in the fourth quarter of 2011. The year-over-year increase was primarily related to production from the acquisition that closed on March 22, 2011 as well as bringing the successful 2011 and 2012 drills on-stream.

Revenue

Three Months Ended March 31,	**2012**	2011
(000s)	*($)*	*($)*
Natural gas	**1,706**	1,272
Crude oil	**10,595**	600
NGLs	**1,844**	97
Royalty income	**132**	–
Total oil and natural gas revenue	**14,277**	1,969

During the three months ended March 31, 2012, revenue increased 625 percent to $14,277,000 from $1,969,000 in 2011 and rose 20 percent from the $11,873,000 recorded in the fourth quarter of 2011. The year-over-year increase was a result of the March 2011 acquisition, additional production being brought on-stream from 2011 and 2012 drills and higher percentage of crude oil and NGLs production (53 percent compared to 12 percent), resulting in an increase in the corporate average price per boe.

Commodity Prices and Foreign Exchange

Three Months Ended March 31,	**2012**	2011
	($)	*($)*
Benchmark Prices		
Natural gas		
NYMEX *(US$/mmbtu)* (1)	**2.77**	4.14
AECO *(CDN$/GJ)* (2)	**2.03**	3.61
Crude oil		
WTI *(US$/bbl)*	**102.93**	94.10
Edmonton light *(CDN$/boe)*	**92.48**	88.39
Average Realized Prices		
Natural gas *($/mcf)*	**2.17**	3.77
Crude oil *($/bbl)*	**88.45**	94.33
NGLs *($/bbl)*	**71.66**	58.71
Total sales price *($/boe)*	**51.58**	30.68
Foreign Exchange		
CDN$/US$	**1.0012**	0.9860
US$/CDN$	**0.9991**	1.0143

(1) Mmbtu is the abbreviation for millions of British thermal units. One mcf of natural gas is approximately 1.02 mmbtu.
(2) GJ is the abbreviation for gigajoule. One mcf of natural gas is approximately equal to 1.05 GJ.

The Company's financial results are significantly influenced by fluctuations in commodity prices, including price differentials and foreign exchange rates. The Company protects itself from fluctuations in prices by maintaining an appropriate hedging strategy. As at March 31, 2012, DeeThree had six crude oil hedges in place (see "Risk Management" section below for details), five which were entered into during 2011 and one entered into during the first quarter of 2012. Most commodity prices are based on U.S. dollar benchmarks, which result in the Company's realized prices being influenced by the Canadian/U.S. exchange rates. The Company does not sell or transact in foreign currency, but may be impacted by foreign currency exchange rate changes related to commodity prices as outlined above. As at March 31, 2012, DeeThree also had two foreign currency exchange risk management contracts in place to mitigate these risks (see "Risk Management" section below for contract details), both of which were entered into during 2011.

During the three-month period ended March 31, 2012, benchmark natural gas prices in Canada fell 44 percent from the same period last year. In Canada, the benchmark index is the price set at the AECO hub, a major storage site near the TransCanada Energy pipeline exit point from Alberta at Empress. The benchmark index for United States natural gas prices is the market price as established by the New York Mercantile Exchange at Henry Hub ("NYMEX"), a major point of natural gas pipeline intersection in Louisiana. NYMEX is linked to AECO through transportation tariffs from the respective hubs to common markets and through foreign exchange rates. AECO prices averaged $2.03/GJ throughout the first quarter of 2012 compared to $3.61/GJ a year ago. DeeThree's average realized gas price during the three-month period was $2.17/mcf versus $3.77/mcf last year.

Oil prices remained relatively strong in the first quarter of 2012 with West Texas Intermediate ("WTI") averaging $102.93/bbl compared to $94.10/bbl in the same period last year. The benchmark for crude oil prices in North America, and substantially globally, is WTI delivered to Cushing, Oklahoma, again as determined by the NYMEX. Canadian crude prices are based on refiner postings in Canadian dollars at Edmonton, Alberta, and as with natural gas, are linked to WTI through transportation tariffs to common markets and the foreign exchange rate. The average realized price of DeeThree's crude oil was $88.45/bbl for the first quarter of 2012 compared to $94.33/bbl a year ago, while NGLs averaged $71.66/bbl versus $58.71/bbl in 2011. During the quarter, the Company was impacted by widening differentials as growing crude oil supply exhausts pipeline capacities, leading to lower realized prices on this commodity. Information regarding the Company's risk management program can be found in the "Business Risks and Risk Mitigation" section of this MD&A.

Royalties

Three Months Ended March 31,	**2012**	2011
(000s)	*($)*	*($)*
Oil and natural gas revenues	**14,277**	1,969
Total royalties	**2,737**	268
Total royalties *($/boe)*	**9.89**	4.18
Percent of revenue *(%)*	**19**	14

The Lethbridge property attracts primarily freehold royalties, which is a sliding scale royalty determined monthly on a well-by-well basis using a calculation that is based on the New Alberta Crown Royalty 2009 with a cap of 30 percent. The sliding scale varies based on productivity (a higher royalty is payable from wells with higher production rates) and commodity prices (a higher royalty is payable in times of higher natural gas and crude oil prices).

The Peace River Arch and Brazeau properties attract primarily Crown royalties payable to the provincial government and overriding royalties on oil, natural gas and NGLs production. Crown royalties are also sensitive to both production levels and commodity prices; therefore, the Company's royalties will continue to fluctuate with commodity prices, well production rates, production declines of existing wells along with performance and location of new wells drilled. As at March 31, 2012, the Company's product mix was weighted approximately 47 percent natural gas and 53 percent crude oil and NGLs compared to 88 percent and 12 percent, respectively, a year ago.

For the first quarter of 2012, royalties totaled $2,737,000 or 19 percent of revenue compared to $268,000 or 14 percent of revenue last year and $2,452,000 or 21 percent of revenue in the fourth quarter of 2011. The year-over-year royalty rate increase was primarily due to the March 2011 acquisition and new production from the Company's wells brought on-stream during the past year, some of which are subject to a freehold royalty based on the New Alberta Crown Royalty 2009, while others qualify for the 5 percent royalty holiday under the Government of Alberta royalty framework.

Operating and Transportation Expenses

Three Months Ended March 31,	**2012**	2011
(000s)	*($)*	*($)*
Operating expenses	**4,288**	659
Transportation expenses	**445**	84
Total operating and transportation expenses	**4,733**	743
Operating expenses *($/boe)*	**15.49**	10.27
Transportation expenses *($/boe)*	**1.61**	1.31
Total operating and transportation expenses *($/boe)*	**17.10**	11.58

Operating costs include all costs associated with the production of natural gas and crude oil. The major components of operating costs include charges for contract operating, processing fees, lease rentals, property and pipeline taxes, utilities and well maintenance charges.

Operating expenses for the three months ended March 31, 2012 totaled $4,288,000 or $15.49/boe compared to $659,000 or $10.27/boe in the same period last year and $3,950,000 or $17.87/boe in the fourth quarter of 2011. The year-over-year increase in operating costs is due to the fact that the production acquired in March 2011 attracts a higher operating cost per boe when compared to the Company's historical production.

Transportation expenses for the first quarter of 2012 were $445,000 or $1.61/boe compared to $84,000 or $1.31/boe recorded in the same period last year and $455,000 or $2.06/boe in the fourth quarter of 2011. Transportation expenses reflect NOVA and ATCO transportation costs and fluctuate depending on the proportion of the Company's gas that was flowing on firm service versus interruptible service (interruptible service is slightly more expensive) as well as the proportion of Company volumes on ATCO versus NOVA (ATCO is less expensive). Over the past year, the Company has increased production of both crude oil and NGLs, and the transportation costs associated with those products consist primarily of pipeline tariffs, terminal charges and trucking (crude oil and NGLs attract a higher cost per boe for transportation compared to natural gas).

Risk Management

The Company has elected not to use hedge accounting, and accordingly, the fair value of the financial contracts is recorded at each period-end. The fair value may change substantially from period to period depending on commodity and foreign exchange forward strip prices for the financial contracts outstanding at the balance sheet date. The change in fair value from period-end to period-end is reflected in the earnings for that period. As a result, earnings may fluctuate considerably based on the period ending commodity and foreign exchange forward strip prices.

As at March 31, 2012, the Company had the following crude oil and foreign exchange risk management contracts in place with a total mark-to-market liability value of $2,857,000:

Period	Commodity	Type of Contract	Quantity	Pricing Point	Contract Price
Jan.1/12 – Dec.31/12	Crude oil	Collar	250 bbls/d	WTI – NYMEX	US$95.00/bbl (floor) – US$115.00/bbl (cap) (1)
Jan.1/12 – Dec.31/12	Crude oil	Collar	250 bbls/d	WTI – NYMEX	US$85.00/bbl (floor) – US$112.50/bbl (cap) (2)
Jan.1/12 – Dec.31/12	Crude oil	Collar	250 bbls/d	WTI – NYMEX	US$90.00/bbl (floor) – US$116.60/bbl (cap) (3)
Jan.1/13 – Dec.31/13	Crude oil	Collar	250 bbls/d	WTI – NYMEX	US$85.00/bbl (floor) – US$111.00/bbl (cap) (4)
Jan.1/13 – Dec.31/13	Crude oil	Collar	250 bbls/d	WTI – NYMEX	US$90.00/bbl (floor) – US$113.25/bbl (cap) (5)
Jan.1/13 – Dec.31/13	Crude oil	Collar	250 bbls/d	WTI - NYMEX	US$90.00/bbl (floor) – US$116.25/bbl (cap) (6)

(1) Unless the monthly WTI price averages over US$115.00/bbl every day for the entire month, in which case the cap becomes US$100.00/bbl.
(2) Unless the monthly WTI price averages over US$112.50/bbl every day for the entire month, in which case the cap becomes US$95.00/bbl.
(3) Unless the monthly WTI price averages over US$116.60/bbl every day for the entire month, in which case the cap becomes US$95.00/bbl.
(4) Unless the monthly WTI price averages over US$111.00/bbl every day for the entire month, in which case the cap becomes US$90.00/bbl.
(5) Unless the monthly WTI price averages over US$113.25/bbl every day for the entire month, in which case the cap becomes US$92.00/bbl.
(6) Unless the monthly WTI price averages over US$116.25/bbl every day for the entire month, in which case the cap becomes US$92.00/bbl.

Period	Currency	Type of Contract	Quantity	Pricing Point
Jan.1/12 – Dec. 31/12	US$	Average Rate Participating Forward	US$1,400,000	Strike – $1.0275 Fade In – $0.9300 Participating – $1.0800 (1)
Jan.1/12 – Dec.31/13	US$	Average Rate Range Bonus Accumulator	US$700,000	Target – $1.10 CDN$/US$ + $1,000 bonus/day (2)

(1) If the Bank of Canada average daily noon rate ("average rate") for the month is equal to or greater than the fade in level and equal to or less than the strike, the Company is committed to sell U.S. dollars at the strike price. If the average rate settles greater than the strike and equal to or less than the participating level, no transaction occurs. If the average rate for the month settles above the participating level, the Company is obligated to settle at the strike price and if the average rate settles less than the fade in level, no transaction occurs.
(2) The Company can earn a bonus payout of up to $1,000/day depending on the period in which the exchange rate remains in the applicable range of equal to or greater than $0.9350 and equal to or less than $1.10.

These contracts are considered to be financial instruments and the resulting derivative financial liability has been recorded on the Company's statement of financial position, with the unrealized loss being recorded on the statement of operations and comprehensive loss.

Three Months Ended March 31,	**2012**	2011
(000s)	*($)*	*($)*
Unrealized loss on financial instruments	**1,829**	–
Unrealized loss on financial instruments *($/boe)*	**6.61**	–

During the three months ended March 31, 2012, the Company also realized a gain on these financial instruments as a result of the forward strip prices in relation to the terms of the contracts.

Three Months Ended March 31,	**2012**	2011
(000s)	*($)*	*($)*
Realized gain on financial instruments	**176**	–
Realized gain on financial instruments *($/boe)*	**0.64**	–

G&A Expense

Three Months Ended March 31,	**2012**	2011
(000s)	*($)*	*($)*
Gross G&A expense	**1,642**	2,022
Capitalized G&A (direct)	**(465)**	(118)
Overhead recoveries	**(123)**	(65)
G&A expenses (net)	**1,054**	1,839
Transaction costs	**–**	(1,119)
G&A expense (net)	**1,054**	720
G&A expense (net) *($/boe)*	**3.81**	11.22

Gross G&A expenses totaled $1,642,000 for the three-month period ended March 31, 2012 versus $2,022,000 recorded in the comparable period of 2011 which included $1,119,000 for transaction costs. Net G&A costs were $1,054,000 or $3.81/boe in the first quarter of 2012 compared to $720,000 or $11.22/boe a year ago and $988,000 or $4.47/boe recorded in the fourth quarter of 2011. Year-over-year G&A costs net of transaction costs increased on an absolute basis primarily due to increased staffing costs (including salaries, bonuses and office rent) and consulting charges associated with higher activity levels. Throughout the first three months of 2012, the Company had an average of 18 full-time employees and 4 consultants versus 9 full-time employees and 2 consultants in the same period of 2011.

The Company capitalized direct G&A expenses amounting to $465,000 and had overhead recoveries of $123,000 in the first quarter of 2012 versus $118,000 and $65,000, respectively, in the comparative period of 2011 and $389,000 and $267,000, respectively, in the fourth quarter of 2011.

Share-Based Compensation

Three Months Ended March 31,	**2012**	2011
(000s)	*($)*	*($)*
Gross share-based compensation	**725**	247
Share-based compensation reclassified to operating costs	**(27)**	–
Capitalized share-based compensation	**(281)**	(51)
Share-based compensation expense (net)	**417**	196
Share-based compensation expense (net) *($/boe)*	**1.51**	3.05

The Company has a stock option plan, which is fully described in note 10 of the unaudited interim financial statements. The options have a four-year vesting term, expire five years from the grant date and the fair value of all options granted is estimated at the grant date using the Black-Scholes option pricing model. Share-based compensation expense is a non-cash expense that reflects the amortization over the vesting period of the fair value of stock options granted to the employees, consultants and directors of the Company. For those stock options granted to field employees, their portion of the share-based compensation is reclassified to operating expenses to be consistent with the recognition of their salaries on the statement of operations and comprehensive loss.

For the quarter ended March 31, 2012, the Company incurred a net expense of $417,000 or $1.51/boe versus $196,000 or $3.05/boe in the same period of 2011. The increase was directly attributable to increased staffing.

Depletion and Depreciation ("D&D")

Three Months Ended March 31,	**2012**	2011
(000s)	*($)*	*($)*
D&D provision	**5,952**	871
D&D provision *($/boe)*	**21.50**	13.57

D&D is computed on a unit-of-production basis. Such expense, on a boe basis, fluctuates period to period primarily as a result of changes in the underlying proved plus probable reserves base and in the amount of costs subject to D&D, including future development costs. Such costs are segregated and depleted on an area-by-area basis relative to the respective underlying proved plus probable reserves base.

Depreciation is provided on certain field facilities using the straight-line method over a 20-year useful life and on office assets using the declining balance method at rates between 20 percent and 30 percent.

The Company's D&D expense for the three months ended March 31, 2012 was $5,952,000 or $21.50/boe compared to $871,000 or $13.57/boe a year ago and $5,305,000 or $23.99/boe in the fourth quarter of 2011. The year-over-year increase was attributable to the increased value of the proved plus probable reserves that were acquired in March 2011 and added during 2011 from the Company's drilling program, increased production related to those assets and increased future development costs.

Exploration and Evaluation ("E&E") Expense

Three Months Ended March 31,	**2012**	2011
(000s)	*($)*	*($)*
E&E expense	**1,132**	–
E&E expense *($/boe)*	**4.09**	–

Under IFRS, DeeThree accumulates those costs related to E&E assets in one cost pool, pending determination of technical feasibility and commercial viability. This primarily includes costs for seismic data, undeveloped land and drilling costs until the drilling of the well is complete and results have been evaluated. Costs related to wells that have been determined to be uneconomical as well as cost of undeveloped land lease expiries are expensed as they occur.

During the first quarter of 2012, the Company recorded E&E expense of $1,132,000 or $4.09/boe, which related to lease expiries versus $nil in the same period of 2011.

Finance Income

Three Months Ended March 31,	**2012**	2011
(000s)	*($)*	*($)*
Finance income	–	75
Finance income *($/boe)*	–	1.17

During the first three months of 2012, the Company recorded $nil interest income, compared to $75,000 or $1.17/boe in the same quarter of 2011 which was a result of the Company's positive cash balance during that period.

Accretion and Finance Expenses

Three Months Ended March 31,	**2012**	2011
(000s)	*($)*	*($)*
Accretion expense on decommissioning liabilities	**95**	25
Finance expense	**215**	27
Total accretion and finance expenses	**310**	52
Accretion expense on decommissioning liabilities *($/boe)*	**0.34**	0.39
Finance expense *($/boe)*	**0.78**	0.42
Total accretion and finance expenses *($/boe)*	**1.12**	0.81

Accretion expense represents the increase for the reporting period in the present value of the Company's decommissioning liabilities. In the first quarter of 2012, the Company recorded accretion expense of $95,000 or $0.34/boe compared to $25,000 or $0.39/boe in the same period of 2011. The absolute increase was primarily due to the decommissioning liabilities added from the March 2011 acquisition as well as the 2011 and 2012 drills. The underlying liability may increase over time based on new obligations incurred from drilling wells, constructing facilities, acquiring operations, adjusting future estimates of timing or estimated decommissioning costs. The liability can also be reduced as a result of abandonment work actually completed.

During the three months ended March 31, 2012, the Company recorded finance expense of $215,000 or $0.78/boe compared to $27,000 or $0.42/boe a year ago. The Company incurred interest charges and standby fees related to the $50,000,000 credit facility (2011 – $20,000,000), which was drawn to $13,254,000 at the end of the first quarter.

Income Taxes

Three Months Ended March 31,	**2012**	2011
(000s)	($)	($)
Deferred income tax expense (recovery)	**(512)**	66
Deferred income tax expense (recovery) ($/boe)	**(1.85)**	1.03

During the first three months of 2012, the Company recorded a deferred income tax recovery of $512,000 or $1.85/boe compared to an expense of $66,000 or $1.03/boe last year. For 2012, this recovery is a function of the overall net loss adjusted for tax related to the eligible capital expenditures being spent in relation to the March 2011 flow-through share issuance. As these eligible costs are incurred, the Company reverses the flow-through share premium liability and recognizes the deferred income tax expense at that time.

DeeThree does not have current income taxes payable and does not expect to pay current income taxes in 2012 as the Company had estimated tax pools of $217,000,000 available at March 31, 2012.

Funds from (used in) Operations

Three Months Ended March 31,	**2012**	2011
(000s)	*($)*	*($)*
Net loss	**(3,199)**	(1,991)
Non-cash items:		
D&D	**5,952**	871
Accretion	**95**	25
Share-based compensation [1]	**444**	196
Unrealized loss on financial instruments	**1,829**	–
E&E expense	**1,132**	–
Deferred income tax expense	**(512)**	66
Funds from (used in) operations	**5,741**	(833)

(1) The share-based compensation amount included in the calculation of funds from operations has been adjusted for the non-cash portion related to certain field employees that was reclassified to operating expenses for presentation in the statement of operations and comprehensive loss.

During the three months ended March 31, 2012, the Company had funds from operations totaling $5,741,000 or $0.09 per basic and diluted share compared to funds used in operations of $833,000 or $0.02 per basic and diluted share in the comparative period of 2011. This 789 percent absolute increase was primarily due to increased revenue from production offset by increased royalties and operating and transportation costs.

Net Loss

For the three months ended March 31, 2012, the Company recorded a net loss of $3,199,000 or $0.05 per basic and diluted share compared to $1,991,000 or $0.05 per basic and diluted share in the same period of 2011. The year-over-year absolute increase in net loss was primarily due to the E&E expense charge as well as increased depletion recorded during the first quarter of 2012.

Netbacks (per unit)

Three Months Ended March 31,	**2012**	2011
	($/boe)	*($/boe)*
Sales prices	**51.58**	30.68
Royalties	**(9.89)**	(4.18)
Operating	**(15.49)**	(10.27)
Transportation	**(1.61)**	(1.31)
Operating netback [1]	**24.59**	14.92
G&A and other (excludes non-cash items) [2]	**(3.81)**	(28.66)
Realized gain on financial instruments	**0.64**	–
Finance income	**–**	1.17
Finance expenses	**(0.78)**	(0.42)
Funds flow netback [1]	**20.64**	(12.99)
D&D	**(21.50)**	(13.57)
Accretion	**(0.34)**	(0.39)
Share-based compensation	**(1.51)**	(3.05)
Unrealized gain on financial instruments	**(6.61)**	–
E&E expense	**(4.09)**	–
Deferred income tax recovery (expense)	**1.85**	(1.03)
Net loss netback [1]	**(11.56)**	(31.03)

(1) Non-IFRS measure: refer to the commentary at the beginning of this MD&A. Operating netback, funds flow netback and net loss netback are calculated by dividing operating income, funds flow from operations and the net loss by the sales volume in boes for the period then ended. For a description of the boe conversion ratio, refer to the "Other Measurements" commentary at the beginning of this MD&A.

(2) For the period ended March 31, 2011, G&A and other includes transaction costs of $1,119,000 relating to the acquisition of the Peace River Arch and Brazeau properties.

(3) For a description of the boe conversion ratio, refer to the commentary at the beginning of this MD&A.

The operating netback was $24.59/boe for the three months ended March 31, 2012 compared to $14.92/boe in the same period last year and $22.68 in the fourth quarter of 2011. As compared to the prior year, the Company experienced a higher averaged realized price throughout the first quarter of 2012 offset by higher operating costs and royalties. The higher netback was largely the result of a shift to a proportionately higher oil production base, which attracts higher pricing.

Investment and Investment Efficiencies

Capital Expenditures and Acquisitions

Three Months Ended March 31,	**2012**	2011
(000s)(excluding decommissioning liabilities, capitalized share-based compensation)	*($)*	*($)*
Property acquisitions and adjustments	**–**	122,547
Drilling and completions	**30,227**	5,710
Equipment and facilities	**2,398**	42
Land and lease retention	**3,488**	1,145
Geological and geophysical	**122**	(55)
Capitalized G&A and other	**480**	140
Total capital expenditures	**36,715**	129,529
Proceeds from farm-outs	**(1,000)**	–
Total capital expenditures, net proceeds from farm-outs	**35,715**	129,529

During the first three months of 2012, the Company incurred a total of $36,715,000 (2011 – $129,529,000) in capital expenditures, excluding the non-cash decommissioning liabilities and capitalized share-based compensation. Drilling and completion expenditures totaled $30,227,000 during the first quarter of 2012 (2011 – $5,710,000), including the drilling of 10 gross (9.1 net) wells primarily in the Brazeau and Lethbridge areas. In the comparative quarter of 2011, the Company drilled 2 gross (2.0 net) wells, including the horizontal section of the Company's first Bakken well on its Lethbridge property (the vertical section was completed in 2010) and the drilling of the second Bakken location. During the first quarter of 2012, DeeThree spent $2,398,000 (2011 – $42,000) on equipping and tie-ins, which consisted of tying in several of the wells drilled during the fourth quarter of 2011 and the new wells drilled during 2012 as well as installation of the treater in the Lethbridge area. The Company spent $3,488,000 (2011 – $1,145,000) at land sales and $122,000 related to the purchase of 3D seismic data (2011 – a decrease of $55,000 related to credit adjustments on the Company's two seismic programs shot in 2010). The remaining $480,000 (2011 – $140,000) was invested in capitalized G&A and other corporate assets. The Company received $1,000,000 as proceeds from the default on a joint venture agreement entered into during 2011, which was recorded against E&E and partially offset total capital expenditures in the quarter.

Drilling Activity

	Exploration		Development		Total	
	Gross	Net	Gross	Net	Gross	Net
	(#)	*(#)*	*(#)*	*(#)*	*(#)*	*(#)*
Three Months Ended March 31, 2012						
Natural gas	**–**	**–**	**–**	**–**	**–**	**–**
Crude oil and NGLs	**1.0**	**1.0**	**7.0**	**6.1**	**8.0**	**7.1**
Standing	**–**	**–**	**2.0**	**2.0**	**2.0**	**2.0**
Dry and abandoned	**–**	**–**	**–**	**–**	**–**	**–**
Total wells	**1.0**	**1.0**	**9.0**	**8.1**	**10.0**	**9.1**
Success rate *(%)*		**100**		**100**		**100**
Average working interest *(%)*		**100**		**90**		**91**
Three Months Ended March 31, 2011						
Natural gas	–	–	–	–	–	–
Crude oil and NGLs	2	2.0	–	–	2	2.0
Standing	–	–	–	–	–	–
Dry and abandoned	–	–	–	–	–	–
Total wells	2	2.0	–	–	2	2.0
Success rate *(%)*		100		–		100
Average working interest *(%)*		100		–		100

During the first quarter of 2012, DeeThree drilled 10.0 gross (9.1 net) wells (100 percent success rate) that included 1.0 gross (0.3 net) horizontal wells in the Peace River Arch area, 3.0 gross (2.8 net) horizontal oil wells at Brazeau along with 6.0 gross (6.0 net) oil wells in the Lethbridge area. During the three months ended March 31, 2011, the Company drilled 2 gross (2.0 net) wells, which included the horizontal section of the Company's first Bakken location and the second horizontal Bakken well located on its Lethbridge property (100 percent success rate).

Liquidity and Capital Resources

Working Capital

The following table summarizes the change in working capital during the three months ended March 31, 2012 and year ended December 31, 2011:

	Three Months Ended March 31, 2012	Year Ended December 31, 2011
(000s)	*($)*	*($)*
Working capital (deficit) – beginning of period	**(16,901)**	28,505
Abandonment and reclamation costs	**(34)**	(116)
Funds from operations	**5,741**	11,833
Issue of capital stock for cash (net of share issue expenses)	**16,011**	122,434
Capital expenditures	**(36,715)**	(61,578)
Acquisition	**–**	(125,979)
Proceeds from farm-outs	**1,000**	8,000
Working capital deficit – end of period	**(30,898)**	(16,901)

DeeThree entered 2012 with a working capital deficit of $16,901,000. On March 27, 2012, the Company issued 3,834,100 flow-through shares at a price of $4.50 per flow-through share for total gross proceeds of $17,253,450 ($16,011,450 net of estimated share issue expenses), including 500,100 flow-through shares ($2,250,450) issued on the exercise in full of the underwriters' over-allotment option. The proceeds of the flow-through share offering will be used to conduct exploration activity on the Company's properties. During the period, the Company recorded funds from operations of $5,741,000 and invested a total of $36,715,000 in capital expenditures. The Company also received $1,000,000 as proceeds from a default on a farm-out agreement entered into during the second quarter of 2011, which was recorded against E&E and partially offset the total capital expenditures for the period. DeeThree exited the period with a working capital deficit of $30,898,000.

As at March 31, 2012, the Company had a revolving demand credit facility to $50,000,000 with interest charged at the bank's prime rate plus a range of 1.0 percent to 1.25 percent per annum based on the Company's consolidated debt to cash flow ratio. Standby fees associated with this facility range from 0.4 percent to 0.7 percent per annum on the undrawn portion of the facility, again based on the Company's consolidated debt to cash flow ratio. As at March 31, 2012, $13,254,000 was drawn against the facility. Collateral for this facility consists of a general security agreement, providing a security interest over all present and after acquired personal property, and a floating charge on all present and after acquired land interests of the Company. Subsequent to the first quarter, the Company's lender approved an increase to the exisiting facility from $50,000,000 to $60,000,000. The facility is subject to semi-annual reviews by the Company's lender. The next semi-annual review of the credit facility is scheduled for the fall of 2012.

DeeThree expects to fund future capital expenditures with its current working capital, funds flow from operations and the unused demand credit facility.

Related Party Transactions and Off-Balance Sheet Transactions

As at March 31, 2012, the Company had the following related party transactions:

The Company has retained a law firm to provide legal services. The Corporate Secretary of DeeThree is a partner of this firm. During the period ended March 31, 2012, the Company incurred $161,000 in costs with the firm (period ended March 31, 2011 – $177,000), which have been included in G&A expenses and share issue costs, and $94,000 remained in accounts payable at March 31, 2012 (March 31, 2011 – $59,000). Services provided related to advice and counsel primarily in the areas of general legal, corporate governance and banking matters. The Company expects to continue using the services of this firm throughout the balance of 2012.

All related party transactions were in the normal course of operations and have been measured at exchange amounts established and agreed to by the related parties and which are similar to those that the Company would expect to have negotiated with third parties in similar circumstances.

There were no off-balance sheet transactions entered into during the period nor were there any outstanding as at the date of this MD&A.

Contractual Obligations and Commitments

Years Ended December 31,	2012	2013	2014	2015+	Total
(000s)	*($)*	*($)*	*($)*	*($)*	*($)*
Operating lease – office	447	640	640	800	2,527
Operating lease – equipment	201	111	41	–	353
Exploration expenditures (flow-through)	2,353	17,253	–	–	19,606
Drilling contracts	5,543	5,037	–	–	10,580
Bank debt	13,254	–	–	–	13,254
Total	21,798	23,041	681	800	46,320

As at March 31, 2012, the Company had contractual obligations for its office lease totaling approximately $2,527,000 to March 2016. The head office lease obligations are comprised of the lease and includes parking and an estimate of occupancy costs of the Company's head office space. The Company also had contractual obligations for several vehicles totaling approximately $353,000 to the end of 2014.

In connection with the issuance of flow-through shares by the Company during the first quarter of 2012, DeeThree is required to spend $17,253,450 of eligible exploration expenditures by December 31, 2013. As at March 31, 2012, none of these eligible exploration expenditures had been incurred. These expenditures will be renounced to shareholders in January 2013 effective December 31, 2012.

In connection with the issuance of flow-through shares by the Company during the first quarter of 2011, DeeThree is required to spend $15,450,000 of eligible exploration expenditures by December 31, 2012. As at March 31, 2012, approximately $13,097,000 of the eligible exploration expenditures had been incurred. These expenditures were renounced to shareholders in January 2012 effective December 31, 2011. The remaining expenditures of $2,353,000 will be incurred during 2012.

During 2011, DeeThree entered into contracts for drilling rig services, and as at March 31, 2012, the Company had committed to using services totaling $10,580,000 extending into 2013.

At March 31, 2012, the Company also had the obligation to repay the amount outstanding on the revolving demand credit facility, which was drawn to $13,254,000 at period-end.

In connection with the acquisition of the Lethbridge property in November 2008, the Company had an operational commitment to drill 30 wells in the area covered in the agreement over a three-year period commencing November 14, 2008 (ten wells per year). In addition, DeeThree had committed to shoot four townships of seismic data over the same period (one township in year one, two townships in year two and one township in year three). As at March 31, 2012, the Company had fulfilled the drilling commitment, having drilled 38 wells, including those drilled as part of the farm-out agreements, as well as the seismic data acquisition commitment.

On April 13, 2010 and effective March 1, 2010, the Company executed a two-year extension to its amended lease agreement, which is part of a lease issuance, seismic and drilling commitment agreement. This extension involves a commitment to drill an additional 20 wells over the two-year period (ten wells per year) into the Mississippian horizon and expires on November 15, 2013. At the conclusion of the five-year term of the commitment agreement, the applicable areas of the Lethbridge property, which do not have a well located thereon, revert to the Lethbridge property vendor subject to the right of DeeThree to extend the term in respect of an additional five or ten sections of Lethbridge property land by committing to drill an additional five or ten wells, respectively, on such sections of land. Unless cured within a 45-day period, a default by the Company of its obligations under the commitment agreement may result in the applicable areas of the Lethbridge property, which do not have a well located thereon, reverting to the Lethbridge property vendor.

Share Capital

As at May 8, 2012, the Company had 66,986,191 common shares outstanding and 5,566,000 stock options outstanding.

Selected Quarterly Information [1]

Three Months Ended	**Mar.31, 2012**	Dec.31, 2011	Sep.30, 2011	Jun.30, 2011	Mar.31, 2011	Dec.31, 2010	Sep.30, 2010	Jun.30, 2010
(000s, except per share amounts)	*($)*	*($)*	*($)*	*($)*	*($)*	*($)*	*($)*	*($)*
Oil and natural gas revenues	**14,277**	11,873	9,440	9,465	1,969	1,483	1,618	1,679
Funds from (used in) operations	**5,741**	4,094	3,795	4,777	(833)	8	462	372
Per share – basic and diluted	**0.09**	0.06	0.06	0.08	(0.02)	–	0.02	0.02
Cash flow from (used in) operating activities	**4,064**	754	8,910	2,299	(4,863)	(23)	687	407
Net loss	**(3,199)**	(9,330)	(353)	(899)	(1,991)	(5,738)	(6,664)	(2,079)
Per share – basic and diluted	**(0.05)**	(0.15)	(0.01)	(0.01)	(0.05)	(0.23)	(0.29)	(0.10)
Total assets	**240,124**	213,239	206,885	195,267	192,682	65,334	52,336	38,691
Capital expenditures [2]	**36,715**	20,529	25,009	12,490	129,529	7,532	3,572	4,012
Working capital (deficit) [3]	**(30,898)**	(16,901)	(3,356)	17,871	20,659	28,505	20,668	3,133
Shareholders' equity	**178,732**	167,568	176,346	174,850	175,423	55,126	47,479	32,880
Production								
Natural gas *(mcf/d)*	**8,657**	7,714	8,167	8,214	3,744	3,691	3,958	4,191
Crude oil *(bbls/d)*	**1,316**	957	597	609	71	18	17	14
NGLs *(bbls/d)*	**283**	161	177	189	18	1	1	1
Total *(boe/d)*	**3,042**	2,403	2,135	2,167	713	635	678	714

(1) The selected quarterly information has been prepared in accordance with the accounting principles as contained in the notes to the unaudited interim financial statements, except for funds from (used in) operations, which is a non-prescribed measure under IFRS.
(2) Total capital expenditures, including acquisitions.
(3) Current assets less current liabilities, excluding current derivative financial instruments.

Factors That Have Caused Variations over the Quarters

During the first quarter of 2011, DeeThree completed a transformational acquisition that significantly increased the Company's revenues, funds from operations and cash flow in subsequent periods. DeeThree's production also increased significantly and shifted from an approximate 98 percent natural gas focus to approximately 63 percent natural gas and 37 percent crude oil and NGLs for the year ended December 31, 2011.

Please refer to the "Financial and Operating Results" section and other sections of this MD&A for detailed discussions on variations during the comparative quarters and to DeeThree's previously issued interim and annual MD&A for changes in prior quarters.

Subsequent Events

In April 2012, the Company's lender approved an increase to the Company's existing credit facility from $50,000,000 to $60,000,000.

Subsequent to the quarter end, in May 2012, DeeThree extended the primary lease terms on its Lethbridge property for an additional two year term to November 30, 2015. In exchange for the lease extension, the Company has surrendered approximately 50,000 acres while still retaining approximately 180,000 acres of what it feels is the most prospective acreage for Bakken reserves. DeeThree will retain all wells purchased under the original agreement on the surrendered lands and retain existing corresponding leases for producing/capable formations only. Also as part of this extension, and in place of the 20 well commitment from the April 13, 2010 agreement, the Company now has a commitment to drill 12 wells over the three year period (five wells in each of 2012 and 2013 and two wells in 2014). To the date of this MD&A the Company has drilled six of the new commitment wells.

Critical Estimates

The preparation of the Company's financial statements requires management to adopt accounting policies that involve the use of significant estimates and assumptions. These estimates and assumptions are developed based on the best available information and are believed by management to be reasonable under the existing circumstances. New events or additional information may result in the revision of these estimates over time. The following discussion outlines some of the accounting policies and practices that are critical to determining DeeThree's financial results and a summary of the critical estimates and judgements used by DeeThree can be found in note 2 to the December 31, 2011 audited annual financial statements.

Reserves Determination

The proved natural gas, crude oil and NGLs reserves that are used in determining DeeThree's depletion rates, the magnitude of the borrowing base available to the Company from its lender and the ceiling test are based on management's best estimates, and are subject to uncertainty. Through the use of geological, geophysical and engineering data, the reservoirs and deposits of natural gas, crude oil and NGLs are examined to determine quantities available for future production, given existing operations and economic conditions and technology. The evaluation of recoverable reserves is an ongoing process impacted by current production, continuing development activities and changing economic conditions as reflected in natural gas and crude oil prices. Consequently, the reserves are estimated, which are subject to variability. To assist with the reserves evaluation process, the Company employs the services of independent oil and gas reservoir engineers.

Income Taxes

The determination of DeeThree's income and other tax liability requires interpretation of complex laws and regulations often involving multiple jurisdictions. All tax filings are subject to audit and potential reassessment after lapse of considerable time. Accordingly, the actual income tax liability may differ significantly from the liability estimated or recorded.

Other Estimates

The accrual method of accounting will require management to incorporate certain estimates, including revenues, royalties, production costs and capital expenditures as at a specific reporting date but for which actual revenue and royalties have not yet been received, and estimates on capital projects that are in progress or recently completed where actual costs have not been received at a specific reporting date.

Controls and Procedures

Disclosure Controls

Disclosure controls and procedures are designed to ensure that information required to be disclosed by the Company is accumulated and communicated to management (including the Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO")) to allow timely decisions regarding required disclosure.

DeeThree's CEO and CFO 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. Based on their evaluation, DeeThree's CEO and CFO have concluded that, as of March 31, 2012, the Company's internal controls and procedures over financial reporting were effective. DeeThree is required to disclose herein any change in the design of the Company's internal control over financial reporting that occurred during the period ended March 31, 2012 that has materially affected, or is reasonably likely to materially affect, DeeThree's internal control over financial reporting. DeeThree confirms that no such changes were made to its internal controls over financial reporting during the period.

Internal Controls over Financial Reporting

DeeThree is required to comply with Multilateral Instrument 52-109 – "Certification of Disclosure in Issuers' Annual and Interim Filings". The certificate of interim filings for the period ended March 31, 2012 requires that DeeThree disclose in the interim MD&A any changes in the Company's internal control over financial reporting that occurred during the period that has materially affected, or is reasonably likely to materially affect DeeThree's internal control over financial reporting. DeeThree confirms that no such changes were made to internal controls over financial reporting during the period.

It should be noted that while DeeThree's CEO and CFO believe that the Company's internal controls and procedures provide a reasonable level of assurance and are effective, they do not expect that these controls will prevent all errors or 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.

Accounting Standards Issued But Not Yet Applied

IFRS 9 – "Financial Instruments" was issued by the IASB in November 2009 and was the first step to replace IAS 39 – "Financial Instruments: Recognition and Measurement". In October 2010, the requirements for classifying and measuring financial liabilities were added to IFRS 9. Under this guidance, entities would be required to reverse the portion of the fair value change due to a company's own credit risk out of earnings and recognize the change in other comprehensive income. IFRS 9 is effective for the Company on January 1, 2015. DeeThree is currently evaluating the impact of IFRS 9 on its financial statements and believes there will be no significant impact to the Company upon implementation of the standard.

IAS 12 – "Income Taxes" was amended on December 20, 2010 to remove subjectivity in determining on which basis an entity measures the deferred tax relating to an asset. The amendment introduces a presumption that an entity will assess whether the carrying value of an asset will be recovered through the sale of the asset. The amendment to IAS 12 is effective for reporting periods beginning on or after January 1, 2012. The Company is currently evaluating the impact of this amendment to IAS 12 on its financial statements.

IFRS 10 – "Consolidated Financial Statements" replaces IAS 27 – "Consolidated Separate Financial Statements". IFRS 10 introduces a single control model to assess whether to consolidate an investee. The standard was issued as part of a new suite of consolidation and related standards replacing existing requirements for joint ventures (now joint arrangements) and making limited amendments in relation to associates. The new requirements are effective in annual periods beginning on or after January 1, 2013. The Company is currently evaluating the impact of IFRS 10 and believes the standard will not be applicable to the preparation of its financial statements.

IFRS 11 and IAS 28 – "Joint Arrangements and Investments in Subsidiaries" were issued as part of its new suite of consolidation and related standards, replacing existing requirements for subsidiaries. Under IFRS 11 and IAS 28, classification of the joint arrangement depends on whether parties have rights to, and obligations for, underlying assets and liabilities; joint ventures are no longer allowed to use proportionate consolidation and must use equity accounting. The new requirements are effective in annual periods beginning on or after January 1, 2013. The Company is currently evaluating the impact of IFRS 9 and IAS 28 and believes the standard will not be applicable to the preparation of its financial statements.

IFRS 12 – "Disclosure of Interests in Other Entities" is a new standard, which combines all of the disclosure requirements for subsidiaries, associates and joint arrangements, as well as unconsolidated structured entities. The new requirements are effective in annual periods beginning on or after January 1, 2013. The Company is currently evaluating the impact of IFRS 12 and believes the standard will not be applicable to the preparation of its financial statements.

IFRS 13 – "Fair Value Measurement" is a new standard meant to clarify the definition of fair value, provide guidance on measuring fair value and improve disclosure requirements related to fair value measurement. DeeThree is currently evaluating the impact of IFRS 13 on its financial statements and believes there will be no significant impact to the Company upon implementation of the standard.

In June 2011, the IASB published amendments to IAS 1 – "Presentation of Financial Statements: Presentation of Items of Other Comprehensive Income", which are effective for annual periods beginning on or after July 1, 2012 and are to be applied retrospectively. Early adoption is permitted. The amendments require that an entity present separately the items of other comprehensive income that may be reclassified to profit or loss in the future from those that would never be reclassified to profit or loss. The Company intends to adopt the amendments in its financial statements for the annual period beginning on January 1, 2013. As the amendments only require changes in the presentation of items in other comprehensive income, the Company does not expect the amendments to IAS 1 to have a material impact on the financial statements.

Business Risks and Risk Mitigation

DeeThree's exploration and production activities are concentrated in the Western Canadian Sedimentary Basin where the industry is very competitive. There are a number of risks facing participants in the oil and gas industry, some of which are common to all businesses, while others are specific to the sector. Such risks include finding and developing oil and natural gas reserves economically, estimating amounts of recoverable reserves, producing the reserves in commercial quantities, finding a suitable market at attractive commodity prices, financial and liquidity risks, and environmental and safety risks.

DeeThree mitigates these risks by utilizing a team of highly qualified professionals with expertise and experience in these areas. DeeThree attempts to maximize drilling success by exploring areas that have multi-zone horizons, targeting deeper horizons with uphole potential, continuously assessing new acquisition opportunities to complement existing activities and balancing higher risk exploratory drilling with lower risk development drilling.

Beyond exploration risk, there is the potential that the Company's natural gas and crude oil reserves may not be economically produced at prevailing prices. DeeThree minimizes this risk by generating exploration prospects internally, targeting high quality projects, attempting to operate the project by accessing sales markets through Company owned infrastructure or mid-stream operators.

DeeThree has retained an independent engineering consulting firm that assists the Company in evaluating recoverable amounts of oil and natural gas reserves. Values of recoverable reserves are based on a number of variable factors and assumptions such as commodity prices, projected production, future production costs and governmental regulation. Consequently, estimates could vary from actual results.

DeeThree is exposed to commodity price risk whereby the fair value of future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for petroleum and natural gas are impacted by not only the relationship between the Canadian and United States dollars, but also global economic events that dictate the levels of supply and demand. The Company protects itself from fluctuations in prices by maintaining an appropriate hedging strategy. As at March 31, 2012, DeeThree has six crude oil hedges in place (see "Commodity Prices and Foreign Exchange" section). Most commodity prices are based on U.S. dollar benchmarks, which result in the Company's realized prices being influenced by the Canadian/U.S. exchange rates. The Company does not sell or transact in foreign currency, but may be impacted by foreign currency exchange rate changes related to commodity prices as outlined above. At March 31, 2012, DeeThree had two foreign currency exchange risk management contracts in place.

Credit risks arise from a counterparty failing to meet its obligations in accordance with the agreed upon terms. The Company may be exposed to third party credit risk through its contractual arrangements with its current or future joint venture partners, marketers of its commodities and other parties. DeeThree makes every effort to sell its commodities to major companies with excellent credit ratings.

The oil and natural gas industry is a very capital intensive industry, and in order to fully realize the Company's strategic goals and business plans, DeeThree will rely on equity markets as a source of new capital in addition to bank financing and internally generated cash flow to fund its ongoing capital investments. DeeThree's ability to raise additional capital will depend on a number of factors such as general economic and market conditions that are beyond the Company's control. Internally generated funds will also fluctuate with changing commodity prices. DeeThree anticipates it will continue to have adequate liquidity to fund its financial liabilities through its future funds from operations and available bank credit. DeeThree is committed to maintaining a strong balance sheet along with an adaptable capital expenditures program that can be adjusted to capitalize on, or reflect, acquisition opportunities and, if necessary, a tightening of liquidity sources. DeeThree has had no defaults or breaches on its bank debt or any of its financial liabilities.

There are numerous environmental risks associated with oil and natural gas exploration and production. Some of these risks can involve pollution of the environment and destruction of natural habitat as well as safety risks such as personal injury. DeeThree has established an Environmental, Health and Safety Program and has updated its operational emergency response plan and operational safety manual to address these operational issues. In addition, a comprehensive insurance program is maintained to mitigate risks and protect against significant losses where possible. DeeThree operates in accordance with all applicable environmental legislation and strives to maintain compliance with such regulations.

In addition, DeeThree is also subject to other risks and uncertainties which are described in the Company's Annual Information Form dated March 28, 2012.

Outlook

On March 29, 2012, DeeThree announced an increase to its capital budget from $57,000,000 to $82,000,000 and increased guidance on its production targets for 2012, primarily due to the recent success of its drilling program. The Company had the most active quarter in its history investing $36,700,000 of its total planned 2012 capital expenditure budget and remains on target to meet its previously announced exit guidance of 5,000 boe/d. The Company's balance sheet remains strong as it exited the first quarter with negative working capital of $30,898,000 on an increased credit facility of $60,000,000.

STATEMENTS OF FINANCIAL POSITION

As at	March 31, 2012	December 31, 2011
(000s)(unaudited)	*($)*	*($)*
Assets		
Current assets		
Accounts receivable	**13,462**	15,906
Deposits and prepaid expenses	**396**	500
	13,858	16,406
Non-current assets		
Exploration and evaluation assets *(note 5)*	**25,189**	18,631
Property and equipment *(note 6)*	**199,206**	176,562
Deferred tax asset	**1,871**	1,640
Total assets	**240,124**	213,239
Liabilities		
Current liabilities		
Bank debt *(note 7)*	**13,254**	8,521
Accounts payable and accrued liabilities	**31,502**	24,786
Derivative financial instruments	**1,350**	383
	46,106	33,690
Non-current liabilities		
Decommissioning liabilities *(note 8)*	**10,713**	10,363
Flow-through share premium liabilities *(note 9)*	**3,066**	973
Long-term derivative financial instruments	**1,507**	645
Total liabilities	**61,392**	45,671
Shareholders' equity		
Share capital *(note 9)*	**210,539**	196,901
Contributed surplus	**3,476**	2,751
Deficit	**(35,283)**	(32,084)
Total shareholders' equity	**178,732**	167,568
Total liabilities and shareholders' equity	**240,124**	213,239

Commitments *(note 13)*

Subsequent events *(note 14)*

See accompanying notes to the financial statements.

STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS

Three Months Ended March 31,	**2012**	2011
(000s, except per share amounts)(unaudited)	*($)*	*($)*
Revenue		
Oil and natural gas revenues	**14,277**	1,969
Royalties	**(2,737)**	(268)
Oil and natural gas revenues, net of royalties	**11,540**	1,701
Expenses		
Operating and transportation	**4,733**	743
General and administrative	**1,054**	1,839
Depletion and depreciation *(note 6)*	**5,952**	871
Share-based compensation *(note 10)*	**417**	196
Exploration and evaluation expense *(note 5)*	**1,132**	–
	13,288	3,649
Unrealized loss on financial instruments	**1,829**	–
Realized gain on financial instruments	**(176)**	–
Accretion and finance expenses *(note 8)*	**310**	52
Finance income	**–**	(75)
	15,251	3,626
Loss before income tax	**(3,711)**	(1,925)
Taxes		
Deferred income tax expense (recovery)	**(512)**	66
Net loss and comprehensive loss for the period	**(3,199)**	(1,991)
Deficit – beginning of period	**(32,084)**	(19,511)
Deficit – end of period	**(35,283)**	(21,502)
Net loss per share *(note 9)*		
Basic and diluted	**(0.05)**	(0.05)

See accompanying notes to the financial statements.

STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

	Share Capital	Contributed Surplus	Deficit	Total Equity
(000s)(unaudited)	*($)*	*($)*	*($)*	*($)*
Balance – January 1, 2012	**196,901**	**2,751**	**(32,084)**	**167,568**
Flow-through shares issued	**17,253**	**–**	**–**	**17,253**
Share issue costs	**(1,242)**	**–**	**–**	**(1,242)**
Tax benefit of share issue costs	**311**	**–**	**–**	**311**
Premium on flow-through shares	**(2,684)**	**–**	**–**	**(2,684)**
Share-based compensation	**–**	**725**	**–**	**725**
Net loss	**–**	**–**	**(3,199)**	**(3,199)**
Balance – March 31, 2012	**210,539**	**3,476**	**(35,283)**	**178,732**
Balance – January 1, 2011	73,530	1,107	(19,511)	55,126
Common shares issued	115,219	–	–	115,219
Flow-through shares issued	15,450	–	–	15,450
Share issue costs	(8,200)	–	–	(8,200)
Tax benefit of share issue costs	2,074	–	–	2,074
Premium on flow-through shares	(2,550)	–	–	(2,550)
Share-based compensation	–	247	–	247
Exercise of options	58	(10)	–	48
Net loss	–	–	(1,991)	(1,991)
Balance – March 31, 2011	195,581	1,344	(21,502)	175,423

See accompanying notes to the financial statements.

STATEMENTS OF CASH FLOWS

Three Months Ended March 31,	**2012**	2011
(000s)(unaudited)	*($)*	*($)*
Cash flow from (used in):		
Operating activities		
Net loss for the period	**(3,199)**	(1,991)
Adjustments for:		
Depletion and depreciation	**5,952**	871
Share-based compensation	**444**	196
Accretion *(note 8)*	**95**	25
Unrealized loss on financial instruments	**1,829**	–
Exploration and evaluation expense	**1,132**	–
Deferred income tax expense (recovery)	**(512)**	66
Change in non-cash working capital *(note 11)*	**(1,677)**	(4,030)
	4,064	(4,863)
Financing activities		
Increase in bank debt	**4,733**	–
Issuance of share capital	**17,253**	130,717
Share issue expenses	**(1,242)**	(8,200)
Changes in non-cash working capital *(note 11)*	**98**	–
	20,842	122,517
Investing activities		
Property and equipment expenditures	**(28,206)**	1,326
Exploration and evaluation expenditures *(note 5)*	**(8,509)**	(8,308)
Proceeds from farm-out *(note 5)*	**1,000**	–
Property acquisitions *(note 4)*	**–**	(122,547)
Changes in non-cash working capital *(note 11)*	**10,809**	311
	(24,906)	(129,218)
Change in cash and cash equivalents	**–**	(11,564)
Cash and cash equivalents – beginning of period	**–**	32,994
Cash and cash equivalents – end of period	**–**	21,430

See accompanying notes to the financial statements.

NOTES TO THE FINANCIAL STATEMENTS

As at and for the period ended March 31, 2012
(unaudited)

1. Reporting Entity

DeeThree Exploration Ltd. ("DeeThree" or the "Company") is a publicly traded company incorporated under the laws of Alberta. The Company is principally engaged in the exploration for and exploitation, development and production of oil and natural gas, and conducts many of its activities jointly with others. These interim financial statements reflect only the Company's interests in such activities. DeeThree is registered and domiciled in Canada. The address of its main office is Suite 2200, 520 Third Avenue S.W., Calgary, Alberta.

2. Basis of Presentation

(a) Statement of Compliance

These interim financial statements for the three months ended March 31, 2012 are unaudited and have been prepared in accordance with International Accounting Standard ("IAS") 34 – "Interim Financial Reporting" using accounting policies consistent with IFRS.

The interim financial statements should be read in conjunction with the Company's annual audited financial statements for the year ended December 31, 2011.

The interim financial statements were authorized for issue by the Board of Directors on May 8, 2012.

3. Significant Accounting Policies

The Company's accounting policies are described in Note 3 to the December 31, 2011 audited annual financial statements. Those accounting policies have been applied consistently to all periods presented in these interim financial statements.

4. Acquisitions

During the first quarter of 2011, the Company acquired oil and gas assets principally located in the Peace River Arch area of northern Alberta and the Brazeau area of central Alberta for total cash consideration of $123,185,000. The property acquisition closed on March 22, 2011 and was accounted for as a business combination under IFRS 3 – "Business Combinations". Acquisition costs of $1,125,000 were charged to general and administrative expense on the statement of income and comprehensive income. Had the acquisition closed January 1, 2011, for the year ended December 31, 2011, the Company estimates that its pro forma revenue and net loss would have been approximately $39,200,000 and $13,064,000, respectively.

(000s)	*($)*
Net assets acquired	
Petroleum and natural gas assets	122,081
E&E assets	7,773
Adjustments related to January 1 to March 22, 2011 period	(1,815)
Decommissioning liabilities	(4,854)
	123,185
Consideration	
Total cash consideration	123,185

5. Exploration and Evaluation Assets

	Three Months Ended March 31, 2012	Year Ended December 31, 2011
(000s)	*($)*	*($)*
Balance – beginning of period	**18,631**	11,052
Additions	**34,313**	57,010
Proceeds from farm-out	**(1,000)**	(8,000)
Acquisitions through business combinations	**–**	8,249
Transfers to property and equipment	**(25,623)**	(41,693)
E&E expenses	**–**	(7,474)
Lease expiries	**(1,132)**	(513)
Balance – end of period	**25,189**	18,631

During the period ended March 31, 2012, an expense of $1,132,000 was recorded to recognize lease expiries on undeveloped land that occurred during the period (year ended December 31, 2011 – $513,000).

6. Property and Equipment

	Oil and Natural Gas Properties	Office Equipment	Total
(000s)	*($)*	*($)*	*($)*
Cost or deemed cost			
Balance – January 1, 2011	37,692	59	37,751
Acquisitions through business combinations	122,883	–	122,883
Additions	8,926	194	9,120
Transfers from E&E assets	41,693	–	41,693
Balance – December 31, 2011	211,194	253	211,447
Additions	2,958	15	2,973
Transfers from E&E assets	25,623	–	25,623
Balance – March 31, 2012	**239,775**	**268**	**240,043**
Accumulated depletion and depreciation			
Balance – January 1, 2011	19,970	23	19,993
Depletion and depreciation for the year	14,871	21	14,892
Balance – December 31, 2011	34,841	44	34,885
Depletion and depreciation for the period	5,941	11	5,952
Balance – March 31, 2012	**40,782**	**55**	**40,837**
Net book value			
December 31, 2011	176,353	209	176,562
March 31, 2012	**198,993**	**213**	**199,206**

(a) Capitalization of General and Administrative and Share-Based Compensation Expenses

During the period ended March 31, 2012, approximately $465,000 of directly attributable general and administrative expense and $281,000 of directly attributable share-based compensation expense were capitalized as expenditures on property and equipment (December 31, 2011 – $884,000 and $576,000, respectively).

(b) Amortization and Impairment Charges

For the period ended March 31, 2012, management performed an impairment test and determined that no impairment was required.

(c) Future Development Costs and Salvage Value

During the three months ended March 31, 2012, an estimated $22,430,000 of future development costs associated with proved plus probable undeveloped reserves was included in the calculation of depletion and depreciation expense and an estimated $2,817,000 of salvage value of production equipment was excluded (December 31, 2011 – $44,747,000 and $2,791,000, respectively).

7. Bank Debt

At March 31, 2012, the Company had a revolving demand credit facility with an authorized borrowing base of $50,000,000 with interest charged at the bank's prime rate plus a range of 1.0 percent to 1.25 percent per annum based on the Company's consolidated debt to cash flow ratio. Standby fees associated with this facility range from 0.4 percent to 0.7 percent per annum on the undrawn portion of the facility, again based on the Company's consolidated debt to cash flow ratio. At March 31, 2012, $13,254,000 (December 31, 2011 – $8,521,000) was drawn against the revolving demand credit facility. Please refer to Note 14 "Subsequent Events" for details on the Company's credit facility increase subsequent to the quarter end. The next semi-annual review of the credit facility is scheduled for the fall of 2012. The amount of the facility is subject to a borrowing base test performed on a periodic basis by the lenders, based primarily on reserves and using commodity prices estimated by the lenders as well as other factors. A decrease in the borrowing base could result in a reduction to the credit facility. Collateral for this facility consists of a general security agreement, providing a security interest over all present and after acquired personal property and a floating charge on all present and after acquired land interests of the Company.

8. Decommissioning Liabilities

The Company has estimated the net present value of decommissioning obligations to be $10,713,000 as at March 31, 2012 (December 31, 2011 – $10,363,000) based on an undiscounted total future liability of $15,352,000 (December 31, 2011 – $14,398,000). These payments are expected to be incurred over a period of one to 20 years with the majority of costs to be incurred between 2013 and 2026. At March 31, 2012, a risk-free rate of 3.5 percent (December 31, 2011 – 3.5 percent) and an inflation rate of 2 percent (December 31, 2011 – 2 percent) were used to calculate the net present value of the decommissioning liabilities.

	Three Months Ended March 31, 2012	Year Ended December 31, 2011
(000s)	*($)*	*($)*
Balance – beginning of period	**10,363**	2,498
Liabilities incurred	**256**	538
Liabilities acquired	**–**	5,154
Revisions	**33**	2,055
Settlements	**(34)**	(116)
Accretion of decommissioning liabilities	**95**	234
Balance – end of period	**10,713**	10,363

9. Share Capital

(a) Authorized

Unlimited number of common voting shares, no par value.
Unlimited number of preferred shares, no par value, issuable in series.

(b) Issued – Common Shares

	Three Months Ended March 31, 2012		Year Ended December 31, 2011	
	Shares	Amount	Shares	Amount
	(#)	*($000s)*	*(#)*	*($000s)*
Balance – beginning of period	**63,152,091**	**196,901**	32,937,091	73,530
Common shares issued *(i)*	**–**	**–**	27,195,000	116,602
Flow-through shares issued *(ii)*	**3,834,100**	**17,253**	3,000,000	15,450
Premium on flow-through shares *(ii)*	**–**	**(2,684)**	–	(2,550)
Exercise of options *(iii)*	**–**	**–**	20,000	58
Share issue costs	**–**	**(1,242)**	–	(8,283)
Tax benefit of share issue costs	**–**	**311**	–	2,094
Balance – end of period	**66,986,191**	**210,539**	63,152,091	196,901

(i) Private Placements

In July 2011, DeeThree issued 400,000 common shares at a price of $3.46 per common share in exchange for approximately 12,800 net acres of undeveloped land located primarily in the Peace River Arch area of Alberta. Share issue expenses of approximately $7,000 were recorded in relation to this transaction and the value of the acquired land has been included in the Company's E&E balance at December 31, 2011.

In March 2011, DeeThree issued 26,795,000 common shares at a price of $4.30 per common share for total gross proceeds of $115,219,000 ($107,934,000 net of share issue expenses), including 3,495,000 common shares ($15,029,000) issued on the exercise in full of the underwriters' over-allotment option.

(ii) Flow-Through Shares

In March 2012, DeeThree issued 3,834,100 flow-through shares at a price of $4.50 per flow-through share for total gross proceeds of $17,253,450 ($16,011,450 net of estimated share issue expenses), including 500,100 flow-through shares ($2,250,450) issued on the exercise in full of the underwriters' over-allotment option. The implied premium on the flow through shares of $0.70 per share or $2,683,870 was recorded as a liability on the statement of financial position at March 31, 2012 and the Company is committed to spend the $17,253,450 on qualified exploration and development expenditures by December 31, 2013.

In March 2011, DeeThree issued 3,000,000 flow-through shares at a price of $5.15 per flow-through share for total gross proceeds of $15,450,000 ($14,460,000 net of share issue expenses) and $0.85 per share or $2,550,000 was determined to be the implied premium on the flow-through shares. As at March 31, 2012, $382,000 of the flow-through share premium remains on the statement of financial position as a liability and the Company is committed to spending an additional $2,353,000 on qualified exploration and development expenditures by December 31, 2012.

(iii) On January 6, 2011, 10,000 options were exercised at a weighted average price of $2.45 per share and on March 16, 2011, 10,000 options were exercised at a weighted average price of $2.29 per share for total cash proceeds of $48,000 and previously recognized share-based compensation expense of $10,000.

(c) Per Share Amounts

Per share amounts have been calculated on the weighted average number of shares outstanding. The basic and diluted shares outstanding were as follows:

Three Months Ended March 31,	**2012**	2011
(000s, except share and per share amounts)	*($)*	*($)*
Loss for the period	**(3,199)**	(1,991)
	(#)	*(#)*
Weighted average number of common shares – basic and diluted	**63,320,623**	36,294,258
	($)	*($)*
Net loss per weighted average common share – basic and diluted	**(0.05)**	(0.05)

10. Share-Based Compensation

The Company has an option program that entitles officers, directors, employees and certain consultants to purchase shares in the Company. Options are granted based on the five-day volume weighted average prior to the date of grant, vest 20 percent after six months and then 20 percent on the first, second, third and fourth anniversaries from the grant date and expire five years from the grant date.

The number and weighted average exercise prices of stock options are as follows:

	Three Months Ended March 31, 2012		Year Ended December 31, 2011	
	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price
	(#)	*($)*	*(#)*	*($)*
Outstanding – January 1	**4,382,200**	**2.89**	1,885,000	2.26
Issued	**1,130,000**	**3.74**	2,603,000	3.35
Exercised	**–**	**–**	(20,000)	2.37
Forfeited	**(1,200)**	**4.22**	(85,800)	3.00
Outstanding – end of period	**5,511,000**	**3.06**	4,382,200	2.89
Exercisable – end of period	**1,226,900**	**2.62**	1,177,900	2.57

The fair value of the common share purchase options granted was estimated as at the date of grant using the Black-Scholes option pricing model and the following weighted average assumptions:

Weighted Average Exercise Price	Options Outstanding	Weighted Average Contractual Life	Options Exercisable
($)	*(#)*	*(years)*	*(#)*
As at March 31, 2012			
1.20 – 1.99	**200,000**	**1.17**	**150,000**
2.00 – 2.99	**2,970,000**	**3.67**	**776,000**
3.00 – 3.99	**1,102,500**	**4.82**	**20,500**
4.00 – 4.45	**1,238,500**	**4.09**	**280,400**
	5,511,000	**3.90**	**1,226,900**

The fair value of the common share purchase options granted was estimated as at the date of grant using the Black-Scholes option pricing model and the following weighted average assumptions:

As at	**March 31, 2012**	December 31, 2011
Risk-free interest rate *(%)*	**1.17**	1.48
Expected life *(years)*	**3.10**	2.1
Expected volatility *(%)*	**78**	77
Expected dividend yield *(%)*	**–**	–
Fair value of options granted during the year *($/share)*	**1.89**	1.39

A forfeiture rate of 0 percent for those options granted during the three months ended March 31, 2012 (year ended December 31, 2011 – 0 percent) was used when recording share-based compensation expense. This estimate is adjusted to the actual forfeiture rate. Share-based compensation cost of $417,000 was expensed during the three months ended March 31, 2012 (year ended December 31, 2011 – $1,030,000).

11. Supplemented Cash Flow Information

Changes in non-cash working capital is comprised of:

Three Months Ended March 31,	**2012**	2011
(000s)	*($)*	*($)*
Accounts receivable	**2,444**	(4,227)
Prepaid expenses and other	**104**	28
Accounts payable and accrued liabilities	**6,716**	480
Abandonment and reclamation costs	**(34)**	–
	9,230	(3,719)
Related to operating activities	**(1,677)**	(4,030)
Related to financing activities	**98**	–
Related to investing activities	**10,809**	311
	9,230	(3,719)

12. Financial Risk Management

The Company has exposure to credit, liquidity and market risk. The Company's risk management policies are established to identify and analyze the risks faced by the Company, set appropriate limits and controls, and to monitor risks and adherence to market conditions and the Company's activities.

(a) Capital Management

The Company manages its capital to maintain its ability to continue as a going concern and to provide returns to shareholders and benefits to other stakeholders. The capital structure of the Company consists of cash and cash equivalents, bank debt and equity comprising of issued share capital, contributed surplus and deficit.

The following is a breakdown of the Company's capital structure:

As at	**March 31, 2012**	December 31, 2011
(000s)	*($)*	*($)*
Cash and cash equivalents	**–**	–
Bank debt	**13,254**	8,521
Shareholders' equity	**178,732**	167,568

The Company manages its capital structure and makes adjustments to it in light of economic conditions. In order to maintain or adjust capital structure, DeeThree may issue new common shares, issue new debt, adjust exploration and development capital expenditures or acquire or dispose of assets. During the first quarter of 2012, the Company issued 3,834,100 flow-through shares at a price of $4.50 per flow-through share, including 500,100 flow-through shares issued on the exercise in full of the underwriters' over-allotment option. During the first quarter of 2011, the Company issued 26,795,000 common shares at a price of $4.30 per share as well as 3,000,000 flow-through shares at a price of $5.15 per share. During the third quarter, the Company issued 400,000 common shares at a price of $3.46 per share in exchange for approximately 12,800 net acres of undeveloped land. In the fourth quarter of 2011, the Company increased its revolving demand credit facility to an authorized borrowing base of $50,000,000 and subsequent to March 31, 2012, increased the facility again to an authorized borrowing base of $60,000,000. The Company, upon approval from its Board of Directors, will balance its overall capital structure through new share issues, the issue of debt or by undertaking other activities as deemed appropriate under the specific circumstances.

DeeThree does not have any externally imposed financial covenants governing its capital structure. The current credit facility has no financial ratio covenants; however, there are certain covenants in the agreement with respect to restrictions to significantly altering the Company's capital structure without the approval of the lender.

The Company's overall strategy with respect to capital risk management remains unchanged from the year ended December 31, 2011.

13. Commitments

Years Ended December 31,	2012	2013	2014	2015+	Total
(000s)	*($)*	*($)*	*($)*	*($)*	*($)*
Operating lease – office	447	640	640	800	2,527
Operating lease – equipment	201	111	41	–	353
Exploration expenditures (flow-through)	2,353	17,253	–	–	19,606
Drilling contracts	5,543	5,037	–	–	10,580
Bank debt	13,254	–	–	–	13,254
Total	21,798	23,041	681	800	46,320

In connection with the issuance of flow-through shares by the Company during the first quarter of 2012, DeeThree is required to spend $17,253,450 of eligible exploration expenditures by December 31, 2013. As at March 31, 2012, none of these eligible exploration expenditures had been incurred. These expenditures will be renounced to shareholders in January 2013 effective December 31, 2012.

In connection with the issuance of flow-through shares by the Company during the first quarter of 2011, DeeThree is required to spend $15,450,000 of eligible exploration expenditures by December 31, 2012. As at March 31, 2012, approximately $13,097,000 of the eligible exploration expenditures had been incurred. These expenditures were renounced to shareholders in January 2012 effective December 31, 2011. The remaining expenditures of $2,353,000 will be incurred during 2012.

At March 31, 2012, the Company also had the obligation to repay the amount outstanding on the revolving demand credit facility, which was drawn to $13,254,000 at period-end.

14. Subsequent Events

In April 2012, the Company's lender approved an increase to the Company's existing credit facility from $50,000,000 to $60,000,000. Refer to Note 7 "Bank Debt" for additional details regarding the credit facility.

Subsequent to the quarter end, in May 2012, DeeThree extended the primary lease terms on its Lethbridge property for an additional two year term to November 30th, 2015. In exchange for the lease extension, the Company has surrendered approximately 50,000 acres while still retaining approximately 180,000 acres of what it feels is the most prospective acreage for Bakken reserves. DeeThree will retain all wells purchased under the original agreement on the surrendered lands and retain existing corresponding leases for producing/capable formations only. Also as part of this extension, and in place of the 20 well commitment from the April 13, 2010 agreement, the Company now has a commitment to drill 12 wells over the three year period (five wells in each of 2012 and 2013 and two wells in 2014). To the date of this MD&A the Company has drilled six of the new commitment wells.

CORPORATE INFORMATION

Board of Directors

Michael Kabanuk
Executive Chairman
DeeThree Exploration Ltd.

Brendan Carrigy
Independent Businessman

Martin Cheyne
President & Chief Executive Officer
DeeThree Exploration Ltd.

Henry Hamm (1)(2)(3)
Independent Businessman

Dennis Nerland (1)(2)(3)
Partner
Shea Nerland Calnan LLP

Brad Porter (1)(2)(3)
Independent Businessman

(1) Audit Committee Member
(2) Reserves Committee Member
(3) Corporate Governance & Compensation Committee Member

Officers

Martin Cheyne
President & Chief Executive Officer

Gail Hannon
Chief Financial Officer

Trevor Murray
Vice President, Land

Clayton Thatcher
Vice President, Exploration

Daniel Kenney
Corporate Secretary

Head Office

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Website: www.deethree.ca

Auditors

KPMG LLP
Calgary, Alberta

Banker

Canadian Imperial Bank of Commerce
Calgary, Alberta

Evaluation Engineers

Sproule Associates Limited
Calgary, Alberta

Legal Counsel

Davis LLP
Calgary, Alberta

Registrar and Transfer Agent

Olympia Trust Company
Calgary, Alberta

Stock Trading

Toronto Stock Exchange
Trading Symbol: DTX
OTCQX
Trading Symbol: DTHRF

Abbreviations

bbls	barrels
boe	barrels of oil equivalent
GJ	gigajoules
/d	per day
mbbls	thousand barrels
mboe	thousand barrels of oil equivalent
mcf	thousand cubic feet
mm	million
mmbtu	million British thermal units
mmcf	million cubic feet
NGLs	natural gas liquids

Conversion of Units

1,0 mcf	=	1.02 mmbtu
1.0 mcf	=	1.05 GJ
1.0 acre	=	0.40 hectares
2.5 acres	=	1.0 hectare
1.0 bbl	=	0.159 cubic metres
6.29 bbls	=	1.0 cubic metre
1.0 foot	=	0.3048 metres
3.281 feet	=	1.0 metre
1.0 mcf	=	28.2 cubic metres
0.035 mcf	=	1.0 cubic metre
1.0 mile	=	1.61 kilometres
0.62 miles	=	1.0 kilometre

Natural gas is equated to oil on the basis of 6 mcf : 1 bbl

DeeThree Exploration Ltd.

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