

Canadian Spirit Resources Inc.

For the nine months ended September 30, 2006

MANAGEMENT DISCUSSION AND ANALYSIS

This management discussion and analysis (“MD&A”) of the financial conditions and results of operations should be read in conjunction with the unaudited interim financial statements for the three and nine month periods ended September 30, 2006 and the audited financial statements and MD&A for the year ended December 31, 2005.

Date

This MD&A includes information up to November 24, 2006.

Reader’s Advisory

The corporate information contained in these pages contains forward-looking forecast information as of November 24, 2006 that may be subject to change after this date. The reader is cautioned that assumptions used in the preparation of such information, although considered reasonable by Canadian Spirit Resources Inc. at the time of preparation, may prove to be incorrect. The actual results achieved during the forecast period will vary from the information provided herein and the variations may be material. Consequently, there is no representation by Canadian Spirit Resources Inc. that actual results achieved during the forecast period will be the same in whole or in part as those forecast.

Corporate Overview

Canadian Spirit Resources Inc. (“CSRI” or the “Company”) is a natural resources exploration company currently focusing on the identification and assembly of unconventional natural gas opportunities in western Canada. Unconventional natural gas includes natural gas produced from coals, shales and tight sands.

The Company also holds a 100% undivided interest, subject to a 10% net profit interest, in thirteen mineral claims covering 2,925 hectares of land in the Iskut River area of the Liard Mining Division, British Columbia (the “Isk Wollastonite Mineral Properties”). The Company determined that this Wollastonite mineral property contains significant reserves which are uneconomic to produce at current prices due to lack of access and infrastructure.

Since May 2002, the Company’s focus has been to evaluate the resource potential of unconventional natural gas exploration properties and is considered to be in its development stage of operations. Although some preliminary evaluation work was performed on unconventional natural gas opportunities prior to May 2002, the decision to change the strategic direction of the Company from evaluation of the Isk Wollastonite Mineral Properties to an evaluation of unconventional natural gas occurred during May 2002. The Company’s strategic advantages are the extensive knowledge and experience of its technical team in unconventional natural gas exploration and development, the highly prospective land base of sixty two sections assembled in the Farrell Creek area of northeastern British Columbia and the energy development experience of its management, employees and directors.

Results of Operations

Farrell Creek, British Columbia:

The focus of the Company’s activities is now on the planning and execution of a pilot production project in the Farrell Creek area of northeastern British Columbia where the Company holds a large, prospective land position. Since 2003, the Company has drilled eight test holes on its lands to evaluate the unconventional natural gas potential. The first test well was drilled, cored, evaluated and suspended in the eastern portion of its land holdings during 2003. The next five test wells were drilled, cored, evaluated and cased to evaluate a contiguous block of thirty sections in the west side of the Farrell Creek area (“West Farrell”) during 2004 and 2005. Two additional wells have been drilled and cased during

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2006. Four of these wells have now been completed in the Gething Formation and are currently being production tested. At September 30, 2006, the Company held an average working interest of 94.23% in 15,988 hectares (39,506 acres) of land in the Farrell Creek area. The Company also holds one section of land in a second area in British Columbia where there is the potential for farm-in and joint venture opportunities.

During the nine months ended September 30, 2006, the Company fracture stimulated the c-83-H and b-92H wells which were drilled and cased in late 2005 and drilled, cased and fracture stimulated the b-03-I well, all in the Gething Formation. These three wells have been production tested for varying periods with natural gas rates ranging from 125 mcf/d to over 300 mcf/d and water production ranging from 10 to 40 barrels per day.

In October 2006, a fourth well in the Company's West Farrell pilot project was drilled and cased. This well, b-02-I, has recently been fracture stimulated and is currently flowing water and natural gas to a temporary facility. By early December, the Company plans to install production tubing and tie-in this well to a more permanent facility which will allow proper measurement of water and natural gas production rates. Capital costs associated with the b-02-I well have been reduced relative to the previous three wells completed for production.

Landowner approval has been received for the right-of-way of the Company's planned pipeline connecting the proposed field processing facilities with the Duke Energy sales pipeline. This approval will allow the "hot-tap" of the Duke Energy pipeline to proceed enabling future gas delivered to this pipeline. The Company has retained Polaris Engineering Ltd. to lead the design and construction of the field facilities, pipeline and gathering system required to tie-in the West Farrell pilot project. Subject to the performance of the pilot project and natural gas prices, the Company's goal is to have these facilities in place and natural gas flowing to market by the third quarter of 2007.

A Scheme Application for Farrell Creek is being prepared and will be submitted to the B.C. Oil & Gas Commission for approval. Regulatory approval of the Scheme Application will facilitate the timely development of the pilot project and extend the confidentiality period for certain technical information.

Bittern Lake, Alberta:

In the third and fourth quarters of 2005, the Company drilled four Horseshoe Canyon wells on one section of joint venture lands in Alberta at minimal cost to the Company. Two wells were completed with positive initial indications but were shut-in pending further evaluation of formation water production. Due to the inability to acquire a sizable land base for development on reasonable terms, the Company and its joint venture partner are evaluating disposition or farmout opportunities of these lands.

Isk Wollastonite, British Columbia:

No field work was conducted at the Isk Wollastonite mine site during the first nine months of 2006. Due to expressions of interest to evaluate these claims for other mineral deposits, the Company will continue to seek annual extensions to all claims prior to their expiry dates. Annual extensions are available to the Company for the next nine years. The Company will continue to pursue farming these claims out to third parties.

Revenue

Revenues represent interest on surplus cash deposits and, during the first quarter of 2006 and the last half of 2005, management fees earned under a joint venture agreement. Revenues earned from management

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fees during the three and nine month periods ended September 30, 2006 were \$Nil and \$45,000 respectively (2005: \$45,000 and \$45,000). The Company does not have any producing properties at this time.

General and Administration Expenses

	Three months ended Sept. 30		Nine months ended Sept. 30	
	2006	2005	2006	2005
Consulting fees	\$ 54,399	\$ 42,782	\$ 172,459	\$ 187,228
Salaries and benefits	221,237	212,713	709,788	565,469
Other general administration	116,794	115,325	462,061	365,913
	<u>392,430</u>	<u>370,820</u>	<u>1,344,308</u>	<u>1,118,610</u>
Less: Capitalized costs	<u>(132,864)</u>	<u>(143,910)</u>	<u>(454,480)</u>	<u>(427,541)</u>
	259,566	226,910	889,828	691,069
Stock-based compensation	<u>(431,560)</u>	<u>448,558</u>	<u>18,353</u>	<u>1,934,904</u>
	<u>\$ (171,994)</u>	<u>\$ 675,468</u>	<u>\$ 908,181</u>	<u>\$ 2,625,973</u>

During the nine month period ended September 30, 2006, consulting fees decreased 8% from the prior year period due to less consulting work in the areas of land, geology and engineering offset in part by recruiting costs in the second and third quarter of 2006. During the same comparative nine month periods, the Company capitalized consulting fees related to land, geology and engineering of \$Nil in 2006 versus \$76,128 in 2005.

Salaries and benefits rose 4% during the three month period and 26% during the nine month period ended September 30, 2006 compared to the corresponding periods in 2005. The nine month increase is attributed to the retention of geological, land and administrative staff in the second and third quarters of 2005 and to salary increases to employees effective January 2006. The smaller period over period increase for the three months ended September 30, 2006 reflects staff reductions that occurred in the second and third quarters of 2006. The Company capitalizes salaries and benefits associated with staff directly related to exploration activities. During the three and nine month periods ended September 30, 2006, the Company capitalized \$120,632 and \$420,323 respectively of salary and benefits compared to \$126,708 and \$322,299 during the same period in 2005. The increase in capitalized costs in the nine month period is due to the addition of technical staff, salary increases and the related benefits.

Stock-based compensation charges were significantly impacted by the volatility in the Company's share price during 2006 compared to 2005 and by the cancellation of certain unvested stock options. The compensation cost charged against earnings for stock options granted for the three and nine month periods ended September 30, 2006 was (\$3,246) and \$500,667 respectively (2005: \$352,559 and \$1,521,904). The decrease is due to the cancellation of unvested stock options and the reduced number of options granted in the current period compared to the prior period. Total compensation expense (recovery) for share appreciation rights for the three and nine month periods ended September 30, 2006 was (\$432,000) and (\$486,000) respectively (2005: \$96,000 and \$413,000) based on a closing price \$1.63 per share on the TSX Venture Exchange on September 29, 2006. The Company has reduced the accrual of a long term liability from \$1,122,000 at June 30, 2006 to \$690,000 at September 30, 2006 relating to share appreciation rights.

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Other General and Administration Costs

Other general and administrative costs increased 27% during the first nine months of 2006 compared to 2005 but were approximately equal to 2005 for the third quarter of 2006 as indicated in the following table:

	Three months ended Sept. 30		Nine months ended Sept. 30	
	2006	2005	2006	2005
Professional fees	\$ 5,923	\$ 21,973	\$ 67,055	\$ 63,728
Investor relations & filing fees	42,343	6,648	130,871	71,703
Office premises & insurance	24,472	49,302	133,730	116,883
Office supplies	25,040	25,053	71,449	70,023
Staffing costs	17,097	11,169	29,654	25,614
Other	1,919	1,180	29,302	17,962
	<u>116,794</u>	<u>115,325</u>	<u>462,061</u>	<u>365,913</u>
Less: Capitalized costs	<u>(12,232)</u>	<u>(10,309)</u>	<u>(34,157)</u>	<u>(29,114)</u>
	<u>\$ 104,562</u>	<u>\$ 105,016</u>	<u>\$ 427,904</u>	<u>\$ 336,799</u>

Professional fees for legal and audit were of similar amounts in 2006 compared to 2005. The increase of professional fee expenses in 2006 was due to reservoir engineering activity to update the Company's contingent resource estimates. Investor relations and filing fees increased in 2006 over the comparable period in 2005 due to the retention of an investor relations firm in 2006; due to increased filing and transfer agent fees associated with the higher number of common shares outstanding; and due to a greater number of investor presentations. Office premises and insurance costs increased due to the higher rental costs for the Company's new offices compared to the prior period. Office supply costs for 2006 and 2005 include the licensing costs for a computer mapping program and related exploration mapping costs of which \$21,925 (2005: \$18,805) were capitalized to natural gas properties. Other costs for 2006 include interest of \$15,971 on Part XII.6 tax due to the Company not incurring exploration expenditures in the time periods required under flow-through share look-back rules.

Summary of Quarterly Results

The Company has had no operating revenue in its history. Net losses prior to income taxes, including the income tax benefit recorded for flow-through shares issued during December 2004, for the prior eleven quarters were:

	2006		2005		2004	
	Amount	Per Share	Amount	Per Share	Amount	Per Share
Net loss by quarter						
First Quarter	\$ (975,817)	\$ (0.04)	\$ (1,094,574)	\$ (0.05)	\$ (264,063)	\$ (0.02)
Second Quarter	31,536	-	(745,055)	(0.03)	(383,367)	(0.02)
Third Quarter	174,092	0.01	(469,598)	(0.02)	(561,720)	(0.03)
Fourth Quarter	-	-	<u>(1,497,189)</u>	<u>(0.06)</u>	<u>(868,870)</u>	<u>(0.05)</u>
Loss before income taxes	(770,189)	(0.03)	(3,806,416)	(0.16)	(2,078,020)	(0.12)
Future income tax recovery	-	-	-	-	336,200	0.02
Net loss after tax	<u>\$ (770,189)</u>	<u>\$ (0.03)</u>	<u>\$ (3,806,416)</u>	<u>\$ (0.16)</u>	<u>\$ (1,741,820)</u>	<u>\$ (0.10)</u>

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For the each period up to and including September 30, 2006, the existence of stock options and warrants affects the calculation of loss per share on a Diluted basis. As the effect of this dilution is to reduce the reported loss per share, Diluted loss per share information has not been shown. For the second and third quarters of 2006, the per share figures are the same for both Basic and Diluted amounts.

Stock-based compensation expense for stock option grants and SARs contributed significantly to the Company's losses and volatility of losses during the last eleven quarters. Excluding the effects of stock-based compensation, the Company's pre-tax losses by quarter would have been:

Net loss by quarter prior to stock-based compensation expense

	2006	2005	2004
First Quarter	\$ (216,771)	\$ (174,539)	\$ (124,615)
Second Quarter	(277,597)	(178,745)	(204,315)
Third Quarter	(257,468)	(21,039)	(178,968)
Fourth Quarter	-	(1,256,242)	(32,197)
Loss before income taxes	<u>\$ (751,836)</u>	<u>\$ (1,630,565)</u>	<u>\$ (540,095)</u>

The quarterly results include impairment charges of \$21,783, \$14,982 and \$14,979 for the first, second and third quarters of 2006 and \$1,121,164 for the fourth quarter of 2005, relating to completion work on the Bluesky Formation at Farrell Creek that proved to be uneconomic.

Liquidity and Capital Resources

The Company's capital program for the three and nine month periods ended September 30 is detailed in the following table:

	Three months ended Sept. 30		Nine months ended Sept. 30	
	2006	2005	2006	2005
Lease acquisitions and retentions	\$ 43,141	\$ 2,142,684	\$ 70,399	\$ 2,207,650
Geological and geophysical	14,249	49,140	17,593	81,561
Drilling and completion	3,839,067	2,286,168	7,972,259	2,545,840
Capitalized overhead	132,864	153,910	454,480	416,848
Total petroleum and natural gas	4,029,321	4,631,902	8,514,731	5,251,899
Office equipment and furnishings	10,985	5,850	15,640	67,745
Total capital expenditures	<u>\$ 4,040,306</u>	<u>\$ 4,637,752</u>	<u>\$ 8,530,371</u>	<u>\$ 5,319,644</u>

The Company's budget is reviewed and approved by the Board of Directors on a quarterly basis. The base budget for 2006 is \$10.3 million including \$0.1 million for land acquisition and retention, \$9.6 million for drilling, completion and production activities and \$0.6 million for capitalized overhead.

Cash administration expenses (G&A excluding stock based compensation) for 2006 are expected to be approximately \$1.72 million before capitalization of exploration related overhead and recoveries; a \$105,000 increase from 2005. The net increase can be attributed to: an increase in salaries, benefits and staffing costs of \$67,000 due to salary increases for existing staff; a reduction of consulting and professional fees of \$121,000; an increase of approximately \$34,000 due to a new lease on the

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Company's offices and insurance; an increase of \$75,000 due to increased investor relations activities and filing fees associated with a larger capital base; and a general increase of \$50,000 due to costs associated with increased staffing and activity. The Company expects that interest and other income will decrease to approximately \$238,000 from \$319,000 in 2005 due to lower cash balances and less recovery from joint venture participants during 2006. This will reduce the net cash administration expense requirements from \$1.7 million to \$1.5 million. The Company has not budgeted for any cash flow from operations during 2006.

The Company is in strong financial condition at September 30, 2006 with working capital of \$5.0 million, consisting of cash in the amount of \$7.7 million, accounts receivable and prepaid expenses of \$0.3 million, net of accounts payable and accrued trade liabilities of \$3.0 million. The Company has no bank indebtedness and has no credit agreements to borrow money in place at this time.

On August 11, 2006, the Company issued 3,200,000 Units at \$2.05 per Unit pursuant to a brokered private placement. Each Unit consisted of one common share and one share purchase warrant. Each warrant entitles the holder to purchase one share for one year at an exercise price of \$2.50 per share. Net proceeds of the issue were \$6.1 million.

On September 19, 2006, the Company granted stock options to four non-executive employees entitling them to acquire a total of 41,000 shares in the Company at an exercise price of \$2.05 per share. The Company's practice is to set the exercise price of stock options at the greater of market price or the price at which shares were issued to the public within the previous ninety days. On the same date, the Company re-priced 195,000 previously granted stock options reducing the exercise price to \$2.05 per share without any change to the original expiry date. All the re-priced options are held by non-executive employees. This step was taken to re-establish the incentive element of the stock option component of employee compensation in a very competitive market.

The Company has raised a total of \$38.8 million, after share issue costs, through a number of private placements and the exercise of warrants and options during the past three years. At September 30, 2006 there were 3,200,000 warrants outstanding with an exercise price of \$2.50 per share that expire on August 11, 2007.

Business Risks

The principal operating risks facing the Company are the productive capabilities of the Gething Formation on the Company's lands; the volatility of natural gas prices; the uncertainty of further land acquisitions due to the intense competition for prospective opportunities; the availability of drilling and service equipment in a timely and cost effective manner; and the Company's ability to economically extract hydrocarbons from its lands.

Government incentives, regulations and taxation of the oil and gas industry in Canada have been significant factors affecting industry profitability. The regulatory environment has been relatively stable for several years. However CSRI is unable to predict or control the direction of future public policy. Regulations regarding safety and the environment are strictly adhered to and CSRI sets a high standard of operating practice in order to minimize risks to employees and the environment.

The Company's ability to continue its operations, develop its assets and realize their carrying values is dependent upon continued support of its shareholders, favorable capital market conditions and commodity

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prices; obtaining additional equity financing and, ultimately, generating revenues sufficient to cover operating costs and capital requirements.

Related Party Transactions

During the first nine months of 2006 and 2005, the Company had transactions with directors of the Company, persons related to them or companies controlled by them in the normal course of business as follows:

For the nine month periods ended September 30	2006	2005
Consulting fees	\$ 63,900	\$ 58,400
Salaries and benefits	\$ 87,395	\$ 70,500

Consulting fees in the nine month period ended September 30, 2006 included \$63,900 (2005: \$58,400) paid or payable to a director and senior officer of the Company. Accounts payable includes \$13,362 (2005: \$5,816) due to a director for consulting fees earned during the period.

Salaries and benefits of \$87,395 (2005: \$70,500) was the compensation paid to a director and senior officer of the Company during nine month period ended September 30, 2006.

Transactions with related parties are recorded at cost, which represents exchange amounts for services provided. In addition during the first nine months of 2005, certain directors, relatives of directors, or companies controlled by directors subscribed for 14,354 (2006: Nil) for shares or units in private placement offerings of the Company under the same terms as to other investors.

Since September 30, 2006 to the date of this report, the Company has continued to employ a director as a salaried employee and has continued to contract with another director to provide services as a consultant.

Share Capital

The Company has authorized share capital of an unlimited number of common shares of no par value. Since September 30, 2006 to the date of this report, the Company has not issued any common shares. The issued share capital as at November 24, 2006 consists of 25,633,082 common shares. On this same date, the Company has 3,200,000 warrants outstanding and 2,401,000 stock options outstanding. Since September 30, 2006, the Company has committed to grant 100,000 stock options to a new employee at the time he commences his employment.

Corporate Information

Additional information regarding the Company is available on SEDAR at www.sedar.com or the Company's website at www.csri.ca.