Report to Shareholders

Questfire Energy Corp. ("Questfire" or the "Corporation") (TSX Venture: Q.A and Q.B) is pleased to announce its unaudited financial and operating results for the three-month and six-month periods ended June 30, 2012.

Second quarter 2012 Corporate Highlights

- Averaged 69 boepd (93 percent natural gas) with low operating and transportation costs of $9.07/boe and an average royalty rate of 13%.
- Added 6 sections (3,840 acres) of land bringing the Corporation's land base to 29 sections (18,535 acres) all at 100 percent working interest.
- Raised $1,510,000 in unsecured senior convertible debentures.

President's Message

The second quarter of 2012 continued to be a challenging time in a variety of ways for the oil and natural gas industry in Western Canada. Daily spot prices for Alberta natural gas sank to 15-year lows. World oil prices also declined by approximately 20 percent. Along with volatility in commodity prices, equity markets also remain volatile, with investors being averse to risk due in part to continuing economic uncertainty around the world. Consequently, the access to capital for junior oil and natural gas companies has become very limited.

In light of these factors, Questfire continued to be very cautious with respect to capital spending in the second quarter of 2012. The Corporation continued to prospect for light oil drilling opportunities and spent approximately $600,000 in the quarter, with the majority ($383,000) spent on acquiring 6.0 sections (3,840 acres) of Crown lands prospective for light oil drilling. This newly acquired land is held at 100 percent working interest and brings the Corporation's total land base to 29 sections (18,535 acres) all at 100 percent working interest. An additional $94,000 was spent preparing a drilling location at Thorsby for drilling in the third quarter of 2012. Subsequent to the quarter end the well was drilled but unfortunately proved to be unsuccessful and was abandoned.

With this conservative approach no new wells were drilled or production added in the second quarter. Although the Corporation achieved operating and transportation costs of $9.07/boe, which is low for a combined oil and natural gas producer with a small scale of operations, as well as low royalty rate of 13%, production for the quarter averaged a modest 69 boepd (93 percent natural gas). This resulted in modest cash flow from production (revenue less royalties, production and transportation expenses) and a net loss for the quarter.

Going forward, the third quarter should see higher average production and cash flow, with the planned tie-in of the Corporation's liquids-rich gas well drilled and completed in the Thorsby field in the first quarter of 2012. This tie-in is expected to occur in the second half of August with first production in early September. Based on flow test results the well is expected to produce at an initial rate of approximately 0.5 mmscfd with 15 to 20 bbls/d of natural gas liquids or approximately 100 boepd. The corporation will remain conservative in its capital spending while investigating all potential sources of additional capital and funding. The management team at

Questfire continues to prospect for oil-drilling opportunities while evaluating producing oil and natural gas assets that are for sale

We are currently seeing a slow resolution to the North American natural gas oversupply issues, via sharply reduced natural gas drilling, particularly of “dry” gas targets, and increased natural gas consumption for power generation. This is leading to a slow improvement in natural gas pricing, with signs of some stability and investor confidence returning to the equity markets.

In closing, I would like to thank our investors for their continued support and patience, the members of the management team at Questfire for their dedication and hard work and our Board of Directors for their guidance.

On behalf of the Board of Directors,

(Signed) “Richard H. Dahl”

Richard H. Dahl
President and Chief Executive Officer
August 20, 2012

Management’s Discussion and Analysis

This management’s discussion and analysis (MD&A) of financial condition and results of operations is for the three-month and six-month periods ended June 30, 2012, including the 2011 comparative periods, has been prepared in accordance with International Financial Reporting Standards (IFRS) and should be read in conjunction with the unaudited condensed interim financial statements and the notes thereto for the period ended June 30, 2012 and the audited financial statements for the year ended December 31, 2011. These documents, along with other statutory filings, are available on SEDAR at www.sedar.com and at the Corporation’s website at www.questfire.ca.

This document contains forward-looking statements. Forward-looking statements are subject to known and unknown risks, uncertainties and other factors that could influence actual results or events and cause actual results or events to differ materially from those stated, anticipated or implied. Such forward-looking statements necessarily involve risks associated with oil and natural gas exploration, property development, production, marketing and transportation, such as dry holes and non-commercial wells, facility and pipeline damage, loss of markets, volatility of commodity prices, currency fluctuations, imprecision of reserve estimates, environmental risks, competition from other producers and the ability to access sufficient capital from internal and external sources. Readers are cautioned not to place undue reliance on forward-looking statements, as no assurances can be given as to future results, levels of activity or achievements.

Petroleum and natural gas volumes are converted to an equivalent measurement basis referred to as a “barrel of oil equivalent” (boe) on the basis of 6,000 cubic feet of natural gas equalling 1 barrel of oil. This is based on an energy equivalency conversion method applicable at the burner tip and does not necessarily represent a value equivalency at the wellhead, which under current commodity prices is greater than 30 mcf to 1 bbl. Readers are cautioned that boe figures may be misleading, particularly if used in isolation.

Questfire’s Board of Directors and Audit Committee have reviewed and approved the June 30, 2012 unaudited condensed interim financial statements, the notes thereto and this MD&A. This MD&A is dated August 20, 2012.

Description of Business

Questfire Energy Corp. (the “Corporation” or “Questfire”) was incorporated on January 15, 2010, and issued one Common Share for a subscription price of $1.00. On November 25, 2010, the Corporation raised $1,895,000 by way of a private placement of Common Shares issued on a “flow-through” basis at $0.20 per share, and on August 18, 2011 the Corporation raised an additional $50,000 by way of a private placement of Common Shares at an issue price of $0.20 per share. On August 24, 2011, the articles of the Corporation were amended to remove the private company restrictions, to reclassify the Common Shares as Class A Shares, and to create Class B shares. On October 18, 2011, the Corporation closed its initial public offering, raising gross proceeds of $6,176,000 and issuing 3,088,000 Class A Shares on a flow-through basis at $0.20 per share, and 555,840 Class B Shares on a flow-through basis at $10.00 per share. On October 26, 2011, the Corporation’s Class A and Class B Shares commenced trading on the TSX Venture Exchange. On June 28, 2012 the Corporation raised $1,510,000 by way of a Private Placement of unsecured senior convertible debentures.

The Corporation is engaged in the acquisition, exploration, development and production of oil and natural gas reserves in Canada. Specifically, the Corporation's focus is to generate and develop its own prospects, acquire oil and natural gas properties directly and/or through farm-in, and participate with joint venturers and other industry partners in oil and natural gas exploration and development in Alberta.

Results of Operations

The Corporation was incorporated on January 15, 2010 and completed its initial public offering on October 18, 2011. As such prior period results available for comparison are limited to exploration and evaluation expenditures, general and administrative expenses, depreciation and finance income or expense.

	Three months ended June 30, 2012 (unaudited)	Three months ended June 30, 2011 (unaudited)	Six months ended June 30, 2012 (unaudited)	Six months ended June 30, 2011 (unaudited)
Revenue				
Oil and natural gas sales	$ **100,018**	$ -	$ **158,044**	$ -
Royalties	**(12,753)**	-	**(21,892)**	-
	87,265	-	**136,152**	-
Expenses				
Production and operating	**(50,949)**	-	**(73,553)**	-
Transportation	**(6,021)**	-	**(8,808)**	-
Exploration and evaluation	**(62,800)**	(24,688)	**(1,124,609)**	(24,688)
General and administrative	**(261,506)**	(66,857)	**(561,011)**	(137,233)
Stock-based compensation	**(27,361)**	-	**(54,722)**	-
Depletion and depreciation	**(63,861)**	(1,900)	**(103,920)**	(3,900)
	(472,498)	(93,445)	**(1,926,623)**	(165,821)
	(385,233)	(93,445)	**(1,790,471)**	(165,821)
Finance income	**335**	3,771	**7,291**	7,885
Finance expense	**(92,815)**	(4,687)	**(180,514)**	(6,583)
Net finance income (expense)	**(92,480)**	(916)	**(173,223)**	1,302
Loss before income taxes	**(477,713)**	(94,361)	**(1,963,694)**	(164,519)
Deferred income tax recovery	**92,728**	-	**396,963**	-
Loss and comprehensive loss	$ **(384,985)**	$ (94,361)	$ **(1,566,731)**	$ (164,519)
Loss and comprehensive loss per share – basic and diluted	$ **(0.03)**	$ (0.01)	$ **(0.12)**	$ (0.02)

Production

Questfire's average production in the second quarter of 2012 was 69 boe per day, compared to nil in the prior year's quarter. Questfire's average production in the first half of the year was 58 boe per day, compared to nil in the first half of 2011. The current production rate is approximately 40 boe per day.

Realized Prices

For the second quarter, the Corporation's average realized price was $1.97 per mcf for natural gas and $72.76 per bbl for crude oil and natural gas liquids (NGL). For the first half, the

Corporation's average realized price was $2.00 per mcf for natural gas and $73.26 per bbl for crude oil and NGL. All of the Corporation's production was marketed by a second-party marketer and no commodity hedges were entered into during the quarter or subsequently.

Revenue

Revenue in the second quarter was $100,018, consisting of natural gas revenue, oil and NGL revenue, and represented the first full quarter of revenue for the Corporation. Revenue for the six months ended June 30, 2012 was $158,044.

Royalties

Royalty expense in the second quarter was $12,753, or 13 percent of revenues and royalty expense for the first half was $21,892 or 14 percent of revenues, representing freehold royalties applicable on the Corporation's revenue.

Production and Operating Expense

Production and operating expense for the second quarter was $50,949 or $8.11 per boe. For the first half production and operating expense was $73,553 or $7.01 per boe. Operating expense is largely comprised of custom processing fees and equipment rentals and the Corporation expects to maintain operating costs at this level for the duration of the year.

Transportation Expense

Transportation expense for the first quarter was $6,021 or $0.96 per boe. For the first half transportation expense was $8,808 or $0.84 per boe.

Exploration and Evaluation (E&E) Expenditures

The Corporation recorded E&E expenditures of $62,800 for the second quarter compared to $24,688 for the respective period in 2011. For the six months ended June 30, 2012 the Corporation recorded E&E expenditures of $1,124,609, compared to $24,688 for the respective period in 2011. The increases in both periods are due to the start of geological salaries being paid in July 2011 and a $999,309 E&E impairment recorded in 2012.

General and Administrative (G&A) Expense

G&A expense amounted to $261,506 in the second quarter of 2012, compared to $66,857 in the second quarter of 2011. G&A expense amounted to $561,011 in the first six months of 2012, compared to $137,233 for the period ending June 30, 2011. Increases over 2011 are mainly due to executive officers being paid a salary starting in July 2011 and increased office activity in 2012 related to commencing operations.

Stock-Based Compensation

Stock-based compensation expense was calculated using the Black-Scholes option pricing model to estimate the fair value of each option granted. The Corporation recorded stock-based compensation expense of $27,361 for the quarter and $54,722 for the six-month period ended June 30, 2012, compared to $nil for the same periods in 2011. The current period's increase over the prior periods is a result of stock options being issued in October 2011. The Corporation records an expense each period with a corresponding charge to contributed surplus. This expense was recognized for the options granted to directors, officers, employees and consultants.

The Corporation granted a total of 1,281,000 options in the year ended December 31, 2011 at a price of $0.20 per option, and has recorded a total stock-based compensation expense since inception of $80,049. The remaining expense of $121,651, calculated under the Black-Scholes option pricing model, will be expensed over the vesting periods of the options. There were no options outstanding prior to these grants, and no options are currently exercisable.

Depletion, Depreciation and Accretion

The Corporation recorded depletion, depreciation and accretion expense of $63,861 in the second quarter and $103,920 in the six months ended June 30, 2012, compared to $1,900 and $3,900 in the respective periods in 2011. The current periods' increases from the prior year's periods is a result of the Corporation's first discovery well commencing production in the first quarter of 2012 and thus beginning to incur depletion charges.

Finance Income

The Corporation earned finance income of $335 in the second quarter and $7,291 in the first six months of 2012, compared to $3,771 and $7,885 in the respective periods of 2011. The Corporation raised its initial equity in November 2010 and completed its initial public offering in October 2011. The decreases in finance income are a result of higher average cash balances in 2011 than in 2012. The Corporation's cash balances earned a yield of approximately 1.1 percent per annum.

Finance Expense

Finance expense (composed of Part XII.6 tax, accretion on the Class B Share liability and accretion on the Corporation's decommissioning liability) was $92,815 in the second quarter and $180,514 in the first six months of 2012 compared to $4,687 and $6,583 in the respective periods of 2011. The increase is mainly due to Part XII.6 tax being accrued related to the unspent portion of the flow-through share renunciations and accretion on the Class B Share liability starting in October 2011.

Deferred Income Tax

Deferred income tax recovery was $92,728 in the second quarter and $396,963 in the first six months of 2012 compared to $nil in the respective periods of 2011, relating primarily to the loss incurred for the period.

Loss

The Corporation incurred a loss of $384,985 ($0.03 per share basic and diluted) in the second quarter and a loss of $1,566,731 ($0.12 per share basic and diluted) in the six months ended June 30, 2012, compared to a loss of $94,361 ($0.01 per share basic and diluted) and $164,519 ($0.02 per share basic and diluted) for the respective periods of 2011.

Supplemental Quarterly Information

The following tables summarize key financial and operating information for the periods indicated:

	Three months ended			
	September 30, 2011	December 31, 2011	March 31, 2012	June 30, 2012
Net loss	$ (264,558)	$ (418,647)	$ (1,181,746)	$ (384,985)
Per share, basic	(0.03)	(0.03)	(0.09)	(0.03)
Capital expenditures	258,669	2,986,024	1,115,759	600,202
Total assets (end of period)	$ 1,796,508	$ 8,643,419	$ 5,596,977	$ 6,913,099

	Three months ended			
	September 30, 2010	December 31, 2010	March 31, 2011	June 30, 2011
Net loss	$ (922)	$ (36,213)	$ (70,158)	$ (94,361)
Per share, basic	(922)	(0.01)	(0.01)	(0.01)
Capital expenditures	-	362,195	-	275,694
Total assets (end of period)	$ 1	$ 1,873,185	$ 1,781,495	$ 1,699,712

Capital Expenditures

	Three months ended June 30, 2012	Six months ended June 30, 2012
Land	$ 382,748	$ 415,532
Geological and geophysical	84,313	87,193
Drilling and completions	93,799	823,446
Production equipment and facilities	39,342	325,035
Workovers and recompletions	-	64,755
Administrative capital	-	-
	$ 600,202	$ 1,715,961

For the three-month period ended June 30, 2012 Questfire made expenditures of $600,202. The Corporation acquired 6 sections of land and incurred initial costs associated with the drilling of the Corporation's fourth well, all in the W4 and W5 exploration areas.

For the six-month period ended June 30, 2012 Questfire made expenditures of $1,715,961. The Corporation acquired 8 sections of land, placed two wells on production as well as incurred costs associated with the Corporation's third and fourth wells, all in the W4 and W5 exploration areas.

Overall at June 30, 2012 the Corporation had E&E assets of $2,088,457. These included 17,415 acres of undeveloped land, 3.9 km^2 of 3D seismic data in the Richdale area and 21 km^2

of 3D seismic data in the Thorsby area. There were also costs incurred and capitalized for surveying and licensing of certain wells to be drilled in 2012.

At June 30, 2012 the Corporation had Property & Equipment of $2,611,608. These included 1,120 acres of land and costs associated with the three wells drilled to date. As well, $6,026 and $30,856 were incurred and capitalized in 2011 and 2010, respectively, to purchase computer systems and printers for use by management to evaluate potential oil and natural gas prospects.

Share Capital and Option Activity

As at June 30, 2012 and as of this date the Corporation has 12,813,001 Class A Shares and 555,840 Class B Shares outstanding.

There were 1,281,000 options to acquire Class A Shares outstanding at June 30, 2012 and as of this date at an average exercise price of $0.20 per share, which were granted to directors, officers, employees and consultants of the Corporation pursuant to its stock option plan. Nil options are exercisable as at June 30, 2012 and as of this date.

Liquidity and Capital Resources

At June 30, 2012 the Corporation had working capital of $1,810,104 (excluding the flow-through share premium), but has $4,342,987 of flow through share expenditures to incur by no later than December 31, 2012. The Corporation has indemnified flow-through share subscribers for their income taxes payable as a result of any deficiency in flow-through share renouncements ultimately made by the Corporation. The Corporation's ability to continue as a going concern and to meet its flow-through share obligations depends upon its ability to attain profitable operations and to generate funds therefrom and/or financing from external parties sufficient to meet future obligations. The Corporation successfully raised $1,510,000 through the issuance of convertible debentures during the three months ended June 30, 2012 however there is no assurance that debt and future equity financings will be available on acceptable terms to meet the Corporation's ongoing capital requirements.

Off-Balance-Sheet Arrangements

The Corporation does not have any special-purpose entities nor is it a party to any arrangements that would be excluded from the balance sheet.

Commitments

Pursuant to its initial public offering completed on October 18, 2011, the Corporation is committed to expending $6,176,000 by December 31, 2012 on activities that will qualify as Canadian exploration expenses (CEE) for income tax purposes. To June 30, 2012, the Corporation had incurred approximately $1,833,013 of eligible expenditures.

The Corporation is committed under a software licence agreement expiring January 1, 2014 to making future minimum payments estimated at $29,339 for 2012 and $58,677 for 2013.

The Corporation entered into a lease for office space that runs to August 31, 2013. The estimated remaining amounts due under the lease, exclusive of estimated related operating expenses and taxes, are $34,110 for 2012 and $45,480 for 2013.

Related-Party Transactions

During the three and six month periods ended June 30, 2012, the Corporation incurred $43,300 and $50,770 respectively (2011 - $nil and $nil) of legal fees to Davis LLP, of which a partner is also a director of Questfire. Of these amounts, $34,000 and $34,000 respectively (2011 - $nil and $nil) was charged to issuance costs and $9,300 and $16,770 respectively (2011 - $nil and $nil) was charged to general and administrative expenses. As at June 30, 2012, $48,521 (2011 - $nil) of the amount above was included in accounts payable.

Hedging

The Corporation had no hedges in place as at June 30, 2012 and does not anticipate hedging in the immediate future.

Risks and Uncertainties

The oil and natural gas industry is subject to numerous risks that can affect cash flow from operating activities and the ability to grow. Further discussion can be found under "Risk Factors" in the Corporation's Prospectus dated September 30, 2011.

Critical Accounting Estimates

The Corporation's accounting policies are described in note 3 to the audited financial statements for the year ended December 31, 2011. Certain accounting policies are identified as critical accounting policies because they require management to make judgments and estimates based on conditions and assumptions that are inherently uncertain. Critical estimates and judgments are outlined in note 2 to the audited financial statements for the year ended December 31, 2011. The use of these accounting policies, estimates and judgments could result in materially different results should the underlying conditions change or the assumptions prove incorrect.

Management's assumptions are based on factors that, in management's opinion, are relevant and appropriate. Management's assumptions may change over time as operating conditions change. The key areas subject to judgment and estimation are described below.

Assessment of commercial reserves

Amounts recorded for depletion and depreciation and amounts used for impairment testing are based on estimates of proved and probable petroleum and natural gas reserves, production rates, commodity prices, future costs and other relevant assumptions. The impact of changes in such estimates on the financial statements of future periods could be material. The Company's reserve estimates are evaluated annually by an independent qualified reservoir engineering firm pursuant to National Instrument 51-101 *Standards of Disclosure for Oil & Gas Activities*.

Impairment

The Corporation monitors internal and external indicators of impairment relating to its intangible and tangible assets, which could indicate that the carrying value of the assets might not be recoverable. The assessment of impairment indicators involves judgment.

E&E assets are reviewed for impairment whenever events or changes in circumstances indicate the carrying value may not be recoverable. Oil and natural gas properties are reviewed for impairment at least annually and whenever events or changes in circumstances indicate that the carrying value of an asset might not be recoverable. The assessment of impairment depends on estimates of reserves, production rates, future prices, future costs and other relevant assumptions.

Decommissioning provision

Amounts recorded as decommissioning provision and the related accretion expense require the use of estimates with respect to the amount and timing of decommissioning and restoration costs. Revisions to the estimated timing of funds flows or to the original estimated undiscounted cost could result in an increase or decrease to the obligation.

Share-based payments

Estimating the fair value of the options granted requires the input of several variables including estimated volatility of the issuer's stock price over the life of the option, future interest rates, and the estimated life of the option. Changes in these estimates would alter the option's fair value and the related expense as determined by the valuation model.

Valuation of E&E assets

The value of E&E assets depends on the discovery of economically recoverable reserves, which in turn depends on future oil and natural gas prices, future capital expenditures and environmental and regulatory restrictions.

Valuation of accounts receivable

The valuation of accounts receivable is based on management's best estimate of the provision for doubtful accounts.

Income taxes

The amounts recorded for deferred income taxes are based on estimates as to the timing of the reversal of temporary differences and tax rates substantively enacted. They are also based on estimates of the probability of the Corporation utilizing certain tax pools and assets which, in turn, depends on estimates of proved and probable reserves, production rates, future petroleum and natural gas prices and changes in legislation, tax rates and interpretations by taxation authorities. The availability of tax pools is subject to audit and interpretation by taxation authorities.

Share capital, flow-through share premium, convertible debentures and convertible Class B Shares

The amounts recorded as share capital, flow-through share premium, convertible debentures and convertible Class B Shares are based on factors including estimated value of Class A Shares on issuance date excluding the flow-through provision, estimated interest rates at which the Corporation would be able to borrow funds, and other relevant assumptions.

Changes in Accounting Policies

The following pronouncements by the International Accounting Standards Board (IASB) will become effective for financial reporting periods beginning on or after January 1, 2013 (after January 1, 2015 for IFRS 9) and have not yet been adopted by the Corporation. All of these new or revised standards permit early adoption with transitional arrangements, depending upon the date of initial application:

IFRS 9 – “Financial Instruments” addresses the classification and measurement of financial assets.

IFRS 10 – “Consolidated Financial Statements” builds on existing principles and standards and identifies the concept of control as the determining factor in whether an entity should be included in the consolidated financial statements of the parent company.

IFRS 11 – “Joint Arrangements” establishes the principles for financial reporting by entities when they have an interest in arrangements that are jointly controlled.

IFRS 12 – “Disclosure of Interests in Other Entities” provides the disclosure requirements for interests held in other entities, including joint arrangements, associates, special-purpose entities and other off-balance-sheet entities.

IFRS 13 – “Fair Value Measurement” defines fair value, requires disclosure about fair value measurements and provides a framework for measuring fair value when it is required or permitted within the IFRS standards.

International Accounting Standard (IAS) 1 – “Presentation of Financial Statements” requires corporations to group items presented within other comprehensive income based on whether they may be subsequently reclassified to profit or loss.

IAS 19 – “Employee Benefits” revises the recognition, presentation and disclosure requirements for defined benefit plans.

IAS 27 – “Separate Financial Statements” revises the standard which addresses the presentation of parent-company financial statements that are not consolidated financial statements.

IAS 28 – “Investments in Associates and Joint Ventures” revises the existing standard, prescribes the accounting for investments and sets out the requirements for the application of the equity method when accounting for investments in associates and joint ventures.

The Corporation has not completed its evaluation of the effect of adopting these standards on its financial statements.

Additional Information

Additional information regarding the Corporation is available on SEDAR at www.sedar.com or can be obtained by contacting the Corporation at Questfire Energy Corp., Suite 400, 703 – 6th Ave S.W., Calgary, Alberta, T2P 0T9.

Corporate Information

BOARD OF DIRECTORS

RICHARD DAHL [(1)(3)]
President & CEO,
Questfire Energy Corp.
Calgary, Alberta

NEIL DELL [(1)(2)(3)]
Independent Businessman
Calgary, Alberta

ROGER MACLEOD [(1)(2)]
Partner
Davis LLP
Calgary, Alberta

JOHN RAMESCU [(2)(3)]
Vice President, Land
Questfire Energy Corp.
Calgary, Alberta

Notes:
(1) Audit Committee
(2) Corporate Governance and Compensation Committee
(3) Reserves Committee

OFFICERS AND KEY PERSONNEL

RICHARD DAHL
President & Chief Executive Officer

DARREN KISSER
Vice President, Engineering and Operations

FRED LAUDEL
Vice President, Exploration

JOHN RAMESCU
Vice President, Land

BRUCE SHEPARD
Vice President, Exploitation

RONALD WILLIAMS
Vice President, Finance & Chief Financial Officer

RODNEY KELLER
Project Manager

MICHAEL DER
Corporate Secretary

GRAHAM NORRIS
Assistant Corporate Secretary

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LEGAL COUNSEL
Davis LLP
Calgary, Alberta

TRANSFER AGENT
Olympia Trust Company
Calgary, Alberta

STOCK EXCHANGE LISTING
The TSX Venture Exchange
Symbols: Q.A and Q.B