



MESSAGE TO SHAREHOLDERS

The Canadian Oil and Gas industry is currently experiencing the lowest level of gas directed drilling activity in the past four years. This low drilling activity is primarily a result of softening of gas prices and high finding and development costs experienced by producers in 2006. We believe that this creates opportunities as Canadian productivity declines and competition for quality play opportunities improves. We believe that the decline in natural gas directed drilling will have an impact on natural gas supply demand balances leading to higher natural gas prices in the future. Fortress has recognized this as an opportune time to be aggressively investing in natural gas investment opportunities. Fortress has recently completed a very active quarter developing and exploring on its natural gas properties in the Ladyfern area. Its recent drilling success provides the Company with large inventory of future development drilling opportunities.

FIRST QUARTER HIGHLIGHTS

The three months ended March 31, 2007 represents the first quarter Fortress has operated since the acquisition of Marauder where the Company has pursued its "Acquire and Exploit" strategy.

- Fortress drilled 11 development wells, 3 exploration wells, and performed 7 recompletions all operated by Fortress, adding a net 200 boe/d of new production and two new pool discoveries, and has approximately net 200 boe/d that will be brought on stream some time in the third quarter.
- Production averaged 805 boe/d for the quarter, the first full quarter with Marauder, and March average production was 911 boe/d as new wells have been placed on stream.
- Capital expenditures were \$11.8 million which included completion and tie in costs associated with wells drilled in 2006.
- Maintained a strong balance sheet with substantial unutilized borrowing capability. The Company finished the quarter with a net debt of \$3.2 million.
- Fortress strengthened its management team with the addition of Mr. Robert D'Adamo as Vice President, Land and Mr. Darren Jackson as Chief Operating Officer. Both gentlemen bring a wealth of exploration and development experience to Fortress.
- Fortress completed a reorganization of SignalEnergy Inc. ("Signal") on February 20, 2007, with the redemption of 23 million Signal shares at \$1.30 per share, and the exchange of the remaining Signal shares on the basis of one share of Fortress for every five shares of Signal.

UPDATE OF OPERATIONS

Fortress completed a very active quarter having conducted 23 well operations all in the Ladyfern area. Average production for the quarter was 805 boe/d consisting of 4.7 mmcf/d of natural gas and 22 bbl/d of natural gas liquids which is an increase of 54% from the fourth quarter of 2006 during which time the business combination with Marauder took place. The average production for the month of March was 911 boe/d reflecting the increase of production from drilling and tie-in of new wells during the quarter. Fortress experienced production disruptions in the Chigwell and Mearon North areas that relate to third party facilities which reduced first quarter production by approximately 60 boe/d.

Fortress incurred \$11.8 million of Capex which approximately 50% was related to development drilling and re-completions, 30% was exploration drilling activity and 20% was related to pipeline and facility costs. Through its exploration efforts the Company has identified two new gas accumulations at Mearon South and at Square Creek areas. Fortress owns a 50% working interest in the wells and has 26 gross (13 net) sections of land in the area. The Company has identified additional follow-up locations on its lands, which it plans to drill in the 2007/8 winter drilling season.

At Mearon South Fortress owns an interest in 14 gross (4.5 net) sections of land and has recompleted two wells drilled in 2006, one of which tested gas rates of 400 mcf/d, establishing the existence of a new pool. Further drilling in the area is planned in 2008.

The Company owns an interest in 4 gross (2 net) sections of land in the Velma area, and owns a 50% interest in two Blue Sky wells capable of producing approximately 200 boe/d net production. The Company has completed building a pipeline, and is now in the process of installing an amine facility and upgrading the Ladyfern facility with refrigeration, all of which are expected to be completed some time in the third quarter and allowing the Company to commence production from the Velma area.

ADDITIONS TO THE MANAGEMENT TEAM

Fortress is pleased to announce the addition of Darren Jackson, P. Eng as Chief Operating Officer of Fortress Energy Inc. Mr. Jackson was most recently Vice President Operations, Connacher Oil and Gas Ltd. and prior thereto was Director of Production, Canetic Resources, 2002 to 2006.

In addition, Rob D'Adamo has joined the Company as Vice President, Land. Mr. D'Adamo was most recently Senior Land Negotiator for EnCana Corporation and prior thereto Vice President, Business Development, Land and Marketing at NAV Energy Trust. From 1997 to 2003, Mr. D'Adamo was Manager, Land Negotiations at PetroCanada.

The addition of both individuals strengthens the management team by bringing a wealth of operations, engineering and land experience to Fortress.

OUTLOOK

During the quarter we have seen natural gas prices strengthen and we expect prices to remain at these levels into the third and fourth quarters. Activity levels for natural gas projects have declined significantly which has resulted in lower field service costs and improving play quality. Fortress' strong and under leveraged balance sheet will allow the Company to capitalize on opportunities in this environment through property acquisitions and consolidations in its core areas and strategic business combinations.

The acquisition of Marauder in the fourth quarter of 2006 and its large undeveloped land base has provided tremendous exploration and development opportunities for Fortress and a large prospect inventory that will be developed over the next three to four years. The recent management additions will enable the Company to deliver these opportunities.

As a final note, we would like to thank Mr. Norman McIntyre, Chairman of the Board, who will not be standing for re-election at the upcoming annual general meeting. Mr. McIntyre has been a director of the Company since 2004. We would like to thank him for his valuable contribution.

J. Cameron Bailey, President and Chief Executive Officer
On Behalf of the Board of Directors

MANAGEMENT'S DISCUSSION AND ANALYSIS

May 15, 2007

Management's discussion and analysis ("MD&A") should be read in conjunction with the unaudited interim consolidated financial statements of Fortress Energy Inc. ("Fortress" or the "Company", formerly known as SignalEnergy Inc.) for the three months ended March 31, 2007 and the audited consolidated financial statements of Fortress Energy Inc. for the years ended December 31, 2006 and 2005. The interim consolidated financial statements have been prepared in accordance with Canadian Generally Accepted Accounting Principles ("GAAP"). All tabular amounts in the following discussion are in thousands of Canadian dollars unless otherwise noted. Additional information is available on the Company's web site at www.fortressenergy.ca or under the Company's profile at www.sedar.com.

This MD&A provides management's analysis of Fortress' historical financial and operating performance based on information currently available. Actual results will vary from estimates and variances may be significant. Historical results are not indicative of future performance.

Non-GAAP Measurements

Management uses the term "funds from operations" to analyze operating performance and leverage, determined as cash flow from operating activities adjusted for changes in non-cash working capital balances. While widely used in the oil and gas industry, funds from operations does not have any standardized meaning prescribed by GAAP and therefore it may not be comparable to the calculation of similar measures for other entities. The Company considers funds from operations to be a key measure since it demonstrates the Company's ability to generate the cash necessary to fund future growth and repay debt. Funds from operations as presented is not intended to represent operating cash flow or operating profits for the period, nor should it be viewed as an alternative to cash flow from operating activities, net income (loss), or other measures of financial performance calculated in accordance with GAAP.

Management also uses certain key performance indicators ("KPI's") and industry benchmarks such as "operating netbacks" and funds from operations/boe to analyze financial and operating performance. These KPI's and benchmarks as presented do not have any standard meaning prescribed by GAAP and therefore may not be comparable with the calculation of similar measures for other entities.

BOE Presentation

Natural gas reserves and volumes recorded in thousand cubic feet are converted to barrels of oil equivalent ("boe") on the basis of six thousand cubic feet ("mcf") of gas to one barrel ("bbl") of oil. The term "barrels of oil equivalent" may be misleading, particularly if used in isolation. A boe conversion ratio of 6 mcf to 1 bbl is based on an energy equivalent conversion method primarily applicable at the burner tip and does not represent a value equivalent at the wellhead.

Forward Looking Statements

Statements in this MD&A may contain forward looking information including expectations of future production, components of cash flow and earnings, expected future events and/or financial results that are forward looking in nature and subject to substantial risks and uncertainties. The reader is cautioned that assumptions used in the preparation of such information may prove to be incorrect. The Company cautions the readers that actual performance will be affected by a number of factors, as many may respond to changes in economic and political circumstances throughout the world. Events or circumstances may cause actual results to differ materially from those predicted, a result of numerous known and unknown risks, uncertainties, and other factors, many of which are beyond the control of the Company. These risks include, but are not limited to: the risks associated with the oil and gas industry, commodity prices and exchange rate changes; industry related risks could include, but are not limited to, operational risks in exploration, development and production, delays or changes in plans; risks associated with the uncertainty of reserve estimates, health and safety risks and the uncertainty of estimates and projections of production, costs and expenses. These external factors beyond the Company's control may affect the marketability of oil and natural gas produced, industry conditions including changes in laws and regulations, changes in income tax regulations, increased competition, fluctuations in commodity prices, interest rates, and variations in the Canadian/United States dollar exchange rate. The reader is cautioned not to place undue reliance on this forward looking information.

Statements throughout this report that are not historical facts may be considered "forward looking statements." These forward looking statements sometimes include words to the effect that management believes or expects a stated condition or result. All estimates and statements that describe the Company's objectives, goals or future plans are forward looking statements. Since forward looking statements address future events and conditions, by their very nature they involve inherent risks and uncertainties. Actual results could differ materially from those currently anticipated due to any number of risks including, but not limited to:

- a. Risks associated with the oil and gas industry and regulatory bodies (e.g. operational risks in exploration, development and production);
- b. Delays or changes in plans with respect to exploration or development projects or capital expenditures;
- c. Uncertainty of estimates and projections relating to recoverable reserves, costs and expenses;
- d. Health, safety and environmental risks; and
- e. Commodity price and exchange rate fluctuations.

SELECTED QUARTERLY INFORMATION

	2007	2006				2005		
	Q1	Q4	Q3	Q2	Q1	Q4	Q3	Q2
Sales volume:								
Natural gas (mcf/d)	4,699	3,010	1,777	1,833	4,366	6,253	5,990	5,100
Oil and NGLs (bbl/d)	22	20	35	69	263	430	242	170
Barrels of oil equivalent (boe)	805	522	331	375	991	1,472	1,240	1,020
Sales price:								
Natural gas (\$/mcf)	7.47	7.19	5.31	6.04	7.86	11.48	9.22	7.25
Oil and NGLs (\$/bbl)	60.56	57.19	65.43	57.08	59.62	65.95	62.88	56.59
Barrels of oil equivalent (boe)	45.48	44.13	35.46	40.08	50.45	68.31	56.82	45.67
Benchmark prices:								
AECO bench (\$/gj)	6.99	6.53	5.39	5.71	7.19	10.84	8.76	6.98
Edmonton Par (\$/bbl)	67.86	65.24	80.26	80.43	68.90	72.18	77.80	65.80
Financial (\$000's):								
Petroleum and natural gas sales	3,296	2,149	1,079	1,362	4,500	9,250	6,483	4,238
Net income (loss)	(308)	(5,635)	(13)	270	13,440	952	536	85
Net income (loss) per share – basic (\$)	(0.02)	(0.07)	(0.00)	0.00	0.19	0.02	0.01	–
Net income (loss) per share – diluted (\$)	(0.02)	(0.07)	(0.00)	0.00	0.19	0.02	0.01	–
Funds from operations	1,558	1,089	821	17	687	4,223	3,141	2,208
Operating costs (\$/boe)	8.82	5.73	8.51	13.13	13.07	12.81	7.20	7.78
Weighted average shares outstanding								
– basic	13,262	81,439	73,266	72,595	70,598	69,195	59,086	47,090
Weighted average shares outstanding								
– diluted	13,262	81,439	73,266	73,316	71,239	69,525	61,240	47,090

Q1 - 2007

Sales volumes increased to 805 boe/d in the first quarter - an increase of 283 boe/d from the prior quarter - reflecting the first full quarter of results from the acquisition of Marauder Resources West Coast Inc. ("Marauder") on November 15, 2006. The Company drilled 14 gross (8 net) wells, tied 8 wells to production facilities (of which 1 well was from the 2006 program), and conducted 7 recompletions of existing well bores, resulting in incremental sales volumes of 200 boe/d in the first quarter of 2007. The Company recorded a net loss of \$308,000 in the quarter compared to a net loss of \$5,635,000 in the prior quarter. The net loss for the fourth quarter of 2006 is the result of a write off of goodwill of \$4.5 million and adjustments to the gain on sale of oil and gas properties to reflect additional capital commitments incurred. Funds from operations for the quarter were \$1,558,000 compared to \$1,089,000 in the prior quarter, reflecting production gains noted and improved operating netbacks.

Q4 - 2006

Sales volumes increased in the quarter to 522 boe/d from 331 boe/d for the prior quarter as a result of the acquisition of Marauder which added additional sales volumes of 450 boe/d from the effective date. Funds from operations increased to \$1,089,000 in the fourth quarter from \$821,000 in the prior quarter, due to the Marauder acquisition and improved natural gas prices realized by the Company which increased by 35.4% to \$7.19/mcf. The Company recorded a net loss of \$5,635,000 in the quarter, as noted previously in this MD&A.

Q3 - 2006

Sales decreased from the prior quarter due to declining commodity prices and sales volumes to \$1,079,000 from \$1,362,000 in the prior quarter. The Company completed workover operations on two wells in the Buick Creek and Bashaw areas in the third quarter of 2006 but was unable to restore production for these wells. Funds from operations improved to \$821,000 in the quarter from \$17,000 in the previous quarter, reflecting lower royalties, operating and general and administrative costs. The Company recorded a net loss of \$13,000 in the quarter primarily as a result of higher depletion and depreciation charges that reflect reserve adjustments for the two wells noted.

Q2 - 2006

Sales volumes declined in the second quarter as a result of the sale of the Company's Redwater, Ferrier, and Carrot Creek properties in the first quarter. A reduction in natural gas prices realized in the quarter of 20.5% contributed to reduced sales revenues. Funds from operations for the second quarter were \$17,000 reflecting lower sales volumes and commodity prices and an increase in operating costs due to an under estimation relating to Redwater in the prior quarter. Incremental legal and advisory costs related to a failed takeover bid for the shares of the Company were recorded in the second quarter. Net income for the quarter was \$270,000 – a significant reduction from the prior quarter which reflects the gain on the sale of oil and gas assets.

Q1 - 2006

In the first quarter of 2006 the Company sold its interest in certain oil and gas assets, as noted previously in this MD&A, for \$91.2 million. The Company used the proceeds to repay its operating loan which had \$28,550,000 drawn at the time of repayment. These oil and gas assets contributed sales volumes of 674 boe/d in the first quarter. Funds from operations declined substantially from the previous quarter due to a 26.1% decline in commodity prices realized by the Company, and an increase in operating costs due to the addition of several wells in the Redwater area that had been tied into production facilities in the first quarter. Net income for the quarter of \$13,440,000 reflects a gain on the sale of oil and gas assets of \$20,087,000.

Q4 - 2005

Sales volumes increased to 1,472 boe/d as a result of the addition of Goose River Resources Ltd. ("Goose River") in August and the Company's capital program which included the drilling of 31 gross (19 net) wells in the last six months of 2005 with a 97% success rate. Funds from operations were \$4,223,000 for the quarter compared to \$3,141,000 in the prior quarter reflecting a 24.5% increase in natural gas prices realized. Net income for the fourth quarter was \$952,000 reflecting substantially improved commodity prices and sales volumes.

Q3 - 2005

In August of 2005, the Company acquired Goose River which contributed sales volumes of 454 boe/d for the quarter from the effective date. The acquisition of Goose River provided a large prospect inventory of drill ready locations which became the focus of the Company's drilling program for the balance of 2005. Funds from operations for the third quarter were \$3,141,000 - an increase of 42.3% from the prior quarter – reflecting a 24.4% increase in commodity prices realized by the Company and increased sales volumes of 220 boe/d over the prior quarter, primarily as a result of the Goose River acquisition. Net income increased to \$536,000 for the quarter from \$85,000 for the second quarter, reflecting improved commodity pricing and higher sales volumes.

Q2 - 2005

The second quarter of 2005 reflects the first full quarter of results from the acquisitions of Predator Exploration Ltd. ("Predator") and a private oil and gas company ("PrivateCo") in January which contributed sales volumes of 748 boe/d. These production gains were reduced by the sale of the Company's Twining property on April 1, 2005 which recorded sales volumes of 170 boe/d in the first quarter of 2005. Funds from operations increased to \$2,208,000 from \$1,361,000 in the first quarter, reflecting a 6.9% increase in commodity prices and lower royalties, as a result of the sale of Twining. Net income for the second quarter of \$85,000 reflects the higher operating netback realized compared to the prior quarter.

REORGANIZATION

A Reorganization (the "Reorganization") of SignalEnergy Inc. ("Signal"), including an arrangement (the "Arrangement") under the Companies Act (Quebec), was approved by the shareholders at a Special General Meeting of Shareholders held on February 15, 2007 and was effective on February 20, 2007.

Under the Arrangement, shareholders of Signal could elect to receive cash, common shares of Fortress, or a combination of both, subject to total cash available of \$30 million. Shareholders representing 63,400,000 common shares of Signal elected to receive cash which resulted in a cash distribution to shareholders of \$30,000,000 to redeem 23,076,923 common shares of Signal at \$1.30 per share. The remaining 66,539,059 common shares of Signal were exchanged for 13,307,815 common shares of Fortress, which was a shell company that was formed for the purposes of completing the Reorganization.

The economic substance of the Reorganization is a transaction whereby the resulting entity is governed under the laws of the Province of Alberta, and not Quebec. Signal was dissolved into Fortress on April 19, 2007.

The balance sheet and share capital presented are of Fortress as a legal entity. The assets, liabilities, and dollar amounts attributed to share capital are those of Signal. The financial position, results of operations and cash flow for all periods prior to the Reorganization are those of Signal.

RESULTS OF OPERATIONS

Sales

	March 31,	
	2007	2006
Petroleum and natural gas sales (\$000's)	3,296	4,500
Sales volume:		
Natural gas (mcf/d)	4,699	4,366
Oil and NGLs (bbl/d)	22	263
Barrels of oil equivalent (boe/d)	805	991
Sales price:		
Natural gas (\$/mcf)	7.47	7.86
Oil and NGLs (\$/bbl)	60.56	59.62
Barrels of oil equivalent (\$/boe)	45.48	50.45

Petroleum and natural gas sales decreased to \$3,296,000 in the first quarter of 2007 compared to \$4,500,000 in the first quarter of the prior year. The decrease is the result of lower sales volumes and lower commodity prices realized by the Company. The first quarter of 2007 reflects the first full quarter of Marauder's operating results which contributed sales volumes of 450 boe/d in the first quarter, excluding the results from the first quarter capital program. In the first quarter of 2006, the Company sold various oil and gas assets, as noted above, which recorded sales volumes of 674 boe/d in that quarter.

The Company's first quarter capital program included the drilling of 14 gross (8 net) wells and 7 recompletions of existing wells. The program added sales volumes of 200 boe/d for the quarter. A total of 8 gross wells were tied into production facilities by the end of the quarter.

Natural gas accounted for 97% of sales volumes for the first quarter of 2007 compared to 74% for the first quarter of 2006. This change in sales mix results from the sale of oil and gas properties in the first quarter of 2006 and the acquisition of Marauder in fourth quarter of 2006. The natural gas price realized by the Company in the first quarter of 2007 decreased to \$7.47/mcf from \$7.86/mcf a year earlier. The average sales price per mcf realized by the Company is consistent with the AECO spot price, adjusted for heat content and transportation costs.

All of the Company's production is marketed in the Alberta spot market and is unhedged.

Royalties

	March 31,	
	2007	2006
Royalties (net of Alberta Royalty Tax Credit) (\$000's)	507	951
\$/boe	6.99	10.66
Percentage of petroleum and natural gas sales	15.3	21.1

Royalties, consisting of crown, gross-overriding and freehold royalties were \$507,000 for the first quarter of 2007, reflecting a decrease of \$444,000 from the first quarter of 2006. This decrease reflects the sale of oil and gas assets in the first quarter of 2006 which carried a substantial freehold and gross override royalty component. In addition, the wells drilled by Marauder in 2006 in the Ladyfern area of British Columbia now qualify for the Ultra-Marginal Royalty Program which reduced the royalty charged by the Crown on these wells to 8.0% of sales.

Operating Expenses

	March 31,	
	2007	2006
Operating expenses (\$000's)	639	1,170
\$/boe	8.82	13.07

The Company's operating expenses decreased to \$639,000 for the first quarter of 2007 from \$1,170,000 for the first quarter of 2006. This decrease is attributed to the sale of oil and gas assets in the first quarter of 2006. On a per boe basis, operating expenses decreased in the first quarter of 2007 to \$8.82/boe, compared to \$13.07/boe in the first quarter of 2006. A substantial portion of this decrease can be attributed to the Redwater property which was sold in March 2006 and which posted higher than average operating costs due to additional costs incurred for compressor and pump jack rentals, trucking, salt water disposal, and oil treating fees at third party facilities.

General and Administrative Expenses

	March 31,	
(\$000's)	2007	2006
General and administrative expense	1,198	1,687
General and administrative costs capitalized	(408)	(110)
General and administrative expenses (net)	790	1,577
\$/boe	10.91	17.68

General and administrative expenses decreased to \$1,198,000 in the first quarter of 2007 compared to \$1,687,000 in the first quarter of 2006. This decrease is attributed to severance and retention costs of approximately \$900,000 that were recorded in the first quarter of 2006 attributed to the downsizing that occurred as a result of the sale of oil and gas properties in March. The Company's "acquire and exploit" strategy has resulted in higher levels of administrative staff to integrate the systems and operations of the acquired business than what might otherwise be required.

The Company capitalized general and administrative costs of \$408,000 in the first quarter of 2007 compared to \$110,000 in the first quarter of 2006. This increase is the result of a very active first quarter drilling program as the focus of the program. The focus of the program was on the Company's winter access properties. In the first quarter of 2006, the Company substantially curtailed its exploration and development activities due to the sale of oil and gas properties.

Stock-based Compensation Expense

	March 31,	
	2007	2006
Stock-based compensation expense (\$000's)	110	852
\$/boe	1.52	9.55

Stock-based compensation expense reflects the value attributed to stock options granted to employees, officers, directors and consultants to the Company. During the first quarter of 2007, the Company granted 963,000 stock options. Stock-based compensation expense for the first quarter of 2007 was \$110,000 compared to \$852,000 for the first quarter of 2006. As a result of the sale of oil and gas properties in the first quarter of 2006, all unvested stock options outstanding were vested on March 1, 2006. Stock-based compensation expense for the first quarter of 2006 reflects the early vesting of these options.

Interest Expense

	March 31,	
	2007	2006
Interest expense (\$000's)	18	234
\$/boe	0.25	2.62

Interest expense reflects the interest costs pertaining to the Company's operating line of credit. Interest expense for the first quarter of 2007 was \$18,000 compared to \$234,000 for the first quarter of 2006. Funds drawn on the operating line at March 31, 2007 was \$3,750,000. By comparison, in the first quarter of 2006 the Company repaid its operating line from the sale of oil and gas assets which had \$28,550,000 drawn at that time.

Depletion and Depreciation Expense

	March 31,	
	2007	2006
Depletion and depreciation expense (\$000's)	1,816	1,932
\$/boe	25.05	21.66

Depletion and depreciation expense was \$1,816,000 for the first quarter of 2007 compared to \$1,932,000 for the first quarter of 2006. This decrease is the result of lower sales volumes in the first quarter of 2007 when compared to the first quarter of 2006. The depletion and depreciation rate for the first quarter of 2007 increased to \$25.05/boe from \$21.66/boe for the first quarter of 2006. The increase in rate reflects the mix of properties sold and retained in 2006, reserve adjustments, and estimated future development costs at March 31, 2007 of approximately \$22.4 million.

Accretion of Asset Retirement Obligations

	March 31,	
	2007	2006
Accretion of asset retirement obligations (\$000's)	24	43
\$/boe	0.33	0.48

Accretion expense was \$24,000 for the first quarter of 2007 compared to \$43,000 for the first quarter of 2006. The sale of oil and gas properties in February 2006 resulted in a reduction in asset retirement obligations by \$3,387,000 which were assumed by the purchaser. In addition, the Marauder properties, which are muskeg and accessible in winter months, require less surface reclamation than the sold properties, resulting in a lower retirement obligation on a per well basis.

Income Tax

The Company recorded a future income tax recovery of \$84,000 for the first quarter of 2007 compared to a future income tax expense for the first quarter of 2006 of \$4,527,000. Future income tax reflects the difference between the underlying tax value and carrying value of the Company's assets and liabilities. Future income taxes at March 31, 2006 reflect the sale of oil and gas properties and a reduction of available tax pools.

Operating Netback

<i>(\$/per boe)</i>	March 31,	
	2007	2006
Petroleum and natural gas sales	45.48	50.45
Less: Royalties (net of ARTC)	(6.99)	(10.66)
Operating expenses	(8.82)	(13.07)
Operating netback	29.67	26.72
Funds from operations	21.49	7.70

The operating netback for the first quarter of 2007 increased to \$29.67/boe from \$26.72/boe for the first quarter of 2006. This increase reflects reductions in royalties and operating expenses as a result of the sale of oil and gas properties in the first quarter of 2006.

Funds from operations for the first quarter of 2007 were \$21.49/boe compared to \$7.70/boe for the first quarter of 2006 – an increase of \$13.79/boe. This increase is attributed to the following items: a reduction in general and administrative costs of \$6.77/boe; an increase in the operating netback of \$2.95/boe; an increase in interest revenue of \$1.48/boe; a reduction in interest expense of \$2.37/boe; and decrease in current income taxes of \$0.22/boe.

Net Income

<i>(\$000's except per share amounts)</i>	March 31,	
	2007	2006
Net income/(loss)	(308)	13,440
Net income/(loss) per share – basic	(0.02)	0.19
Net income/(loss) per share – diluted	(0.02)	0.19

The Company recorded a net loss of \$308,000 for the first quarter of 2007 compared to net income of \$13,440,000 for the first quarter of 2006. Net income for the first quarter of 2006 is attributed to the gain on sale of oil and gas assets of \$20,087,000. On a per share basis, after adjusting 2006 per share figures for the reorganization completed by the Company in the first quarter of 2007, the basic and diluted net income (loss) per share for the first quarter of 2007 was (\$0.02) compared to \$0.19 per share for the first quarter of 2006.

Capital Expenditures

<i>(\$000's)</i>	March 31,	
	2007	2006
Land and lease retention	32	104
Geological and geophysical	–	56
Drilling and completions	9,168	908
Facilities and equipment	2,165	1,562
Property acquisitions	–	465
Capitalized overhead costs	408	110
Other	77	–
	11,850	3,205

The Company's drilling program for the first quarter of 2007 focused exclusively on the Company's lands in the Ladyfern, Mearon, Square Creek, and Drake areas. The Company drilled a total of 14 gross (8 net) wells of which 11 gross (6.5 net) were considered to be development wells and 3 gross (1.5 net) were exploratory. In addition, the Company completed 7 recompletion operations existing wells. A total of 8 gross (4.5 net) wells were tied into production facilities in the first quarter of which 1 gross (0.5 net) wells were from Marauder's 2006 drilling program. The wells that were tied to production facilities in the first quarter of 2007 added incremental production of 200 boe/d. The 2007 drilling program also set up an additional 20 development and 6-8 exploratory drilling opportunities for 2008. In the first quarter of 2006, the Company was not actively engaged in exploration or development opportunities due to the sale of oil and gas assets.

As the result of drilling commitments fulfilled under various farm-out arrangements, the Company earned working interests in 2,725 net acres of undeveloped land in the Ladyfern, Mearon, and Square Creek areas.

LIQUIDITY AND CAPITAL RESOURCES

Cash provided by operating activities was \$2,115,000 for the first quarter of 2007 compared to \$2,083,000 for the first quarter of 2006. This increase in cash provided by operating activities is due to an increase in funds provided by operations realized in the first quarter of 2007.

Cash used in financing activities for the first quarter of 2007 was \$26,907,000 compared to cash used in financing activities of \$21,411,000 for the first quarter of 2006. The Company sold oil and gas assets in the first quarter of 2006 for net cash proceeds of \$91.2 million. These proceeds were used in the first quarter of 2006 to repay the Company's operating line of credit which had \$28,550,000 drawn at the time of repayment. The balance of these proceeds were used to fund the cash portion of the acquisition of Marauder in the fourth quarter of 2006 and the redemption of common shares as part of the Reorganization whereby the Company redeemed 23 million common shares at a price of \$1.30 per share for proceeds, including reorganization costs, of \$30,471,000. In addition, in the first quarter of 2006, employees and directors exercised stock options which provided additional \$1,564,000 of additional cash to the Company. At March 31, 2007, the Company has drawn on its operating line to \$3,750,000,

Cash used in investing activities for the first quarter of 2007 was \$10,547,000 compared to cash provided by investing activities of \$82,907,000 in the first quarter of 2006. Cash provided by investing activities for the first quarter of 2006 reflects capital expenditures, a reduction in non-cash working capital balances as a result of the substantial decrease in the field activity levels, and the proceeds from the sale of oil and gas properties. Cash used in investing activities for the first quarter of 2007 reflects expenditures related to the Company's drilling program.

Securities Outstanding

Securities outstanding as of the date of this MD&A consist of 13,257,815 issued and outstanding common shares and 970,000 stock options.

Off-balance Sheet Arrangements

The Company has no off-balance sheet arrangements.

Related Party Transactions

The Company has no related party transactions.

Commitments and Contingencies

The Company has no commodity price, interest rate swaps or fixed price contracts in place as of March 31, 2007.

The Company is committed to minimum annual lease payments under operating leases for office premises and office equipment to March, 2013, as follows:

	(\$000's)
Balance of 2007	367
2008	431
2009	430
2010	435
2011	439
2012	439
Thereafter	110
	2,651

Disclosure Controls and Procedures

Disclosure controls and procedures have been designed to ensure that information required to be disclosed by the Company is accumulated and communicated to the Company's management as appropriate to allow timely decisions regarding required disclosure. The Company's Chief Executive Officer and Chief Financial Officer have concluded, based on their evaluation as of the end of the period covered by the annual filings, that the Company's disclosure controls and procedures as of the end of such period are effective to provide reasonable assurance that material information related to the Company, including its consolidated subsidiaries, is made known to them by others within those entities. It should be noted that while the Company's Chief Executive Officer and Chief Financial Officer believe that the Company's disclosure controls and procedures provide a reasonable level of assurance that they are effective, they do not expect that the disclosure controls and procedures will prevent all errors and fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

Internal Controls over Financial Reporting

The discussion and conclusion with respect to the Company's internal controls over financial reporting included in the December 31, 2006 MD&A remain unchanged as at March 31, 2007.

NEW CANADIAN ACCOUNTING PRONOUNCEMENTS

Effective January 1, 2007, the Company adopted five new accounting standards issued by the Canadian Institute of Chartered Accountants ("CICA"): Handbook Section 3855 "Financial Instruments – Recognition and Measurement", Section 3861 "Financial Instruments – Disclosure and Presentation", Section 3865 "Hedges", Section 1506 "Accounting Changes", Section 1530 "Comprehensive Income" and Section 3251 "Equity".

Impact upon adoption of Sections 3855, 3861, 3865, 1506, 1530 and 3251

The adoption of the new standards did not have a significant impact on the Company's financial statements due to the nature of the financial instruments recorded on the balance sheet and the contracts to which the Company is a party.

Financial instruments - recognition and measurement

Section 3855 establishes standards for recognizing and measuring financial assets, financial liabilities, and non-financial derivatives. It requires that financial assets and financial liabilities, including derivatives, be recognized on the balance sheet when the Company becomes a party to the contractual provisions of the financial instrument or non-financial derivative contract. Under this standard, all financial instruments are required to be measured at fair value upon initial recognition except for certain related party transactions. Measurement in subsequent periods depends on whether the financial instrument has been classified as held-for-trading, available-for sale, held-to-maturity, loans or receivables, or other financial liabilities. Financial assets and financial liabilities held for-trading

are measured at fair value with changes in those fair values recognized in net earnings. Financial assets held-to-maturity, loans and receivables, and other financial liabilities are measured at amortized cost using the effective interest method of amortization. Investments in equity instruments classified as available-for-sale that do not have a quoted market price in an active market are measured at cost.

Derivative instruments are recorded on the balance sheet at fair value, including those derivatives that are embedded in financial or non-financial contracts that are not closely related to the host contracts. Changes in the fair values of derivative instruments are recognized in net earnings, with the exception of derivatives designated as effective cash flow hedges and hedges of the foreign currency exposure of a net investment in a self-sustaining foreign operation, which are recognized in other comprehensive income. In addition, Section 3855 requires that an entity must select an accounting policy of either expensing debt issue costs as incurred or applying them against the carrying value of the related asset or liability. The financial instruments recognized on Fortress' balance sheet are deemed to approximate their estimated fair values, therefore no further adjustments were required upon adoption of the new sections. There were no financial assets on the balance sheet which were designated as held-for-trading, held-to-maturity or available-for-sale. All financial assets were classified as loans or receivables and are accounted for on an amortized cost basis. All financial liabilities were classified as other liabilities.

Hedges

Section 3865 provides alternative treatments to Section 3855 for entities which choose to designate qualifying transactions as hedges for accounting purposes. It replaces and expands on Accounting Guideline 13 "Hedging Relationships", and the hedging guidance in Section 1650 "Foreign Currency Translation" by specifying how hedge accounting is applied and what disclosures are necessary when it is applied. The Company does not currently have any hedges in place and therefore the adoption of Section 3865 "Hedges" did not have any impact on the Company's financial statements.

Accounting changes

Section 1506 provides expanded disclosures for changes in accounting policies, accounting estimates and corrections of errors. Under the new standard, accounting changes should be applied retrospectively unless otherwise permitted or where impracticable to determine. As well, voluntary changes in an accounting policy are to be made only when required by a primary source of GAAP or the change results in more relevant and reliable information. The Company did not have any accounting changes in the first quarter of 2007 and therefore was not impacted by this new standard.

Comprehensive income (loss) and accumulated other comprehensive income (loss)

Section 1530 introduces comprehensive income, which consists of net earnings and other comprehensive income ("OCI"). OCI represents changes in shareholder's equity during a period arising from transactions and changes in prices, markets, interest rates, and exchange rates. OCI includes unrealized gains and losses on financial assets classified as available-for-sale, unrealized translation gains and losses arising from self-sustaining foreign operations net of hedging activities and changes in the fair value of the effective portion of cash flow hedging instruments.

The Company has not entered into any transactions which require any amounts to be recorded to other comprehensive income (loss) or accumulated other comprehensive income (loss).

Future accounting changes

On December 1, 2006, the CICA issued three new accounting standards: Handbook Section 1535, *Capital Disclosures*, Handbook Section 3862, *Financial Instruments – Disclosures*, and Handbook Section 3863, *Financial Instruments – Presentation*. These new standards are effective January 1, 2008. Section 1535 specifies the disclosure of (i) an

entity's objectives, policies and processes for managing capital; (ii) quantitative data about what the entity regards as capital; (iii) whether the entity has complied with any capital requirements; and (iv) if it has not complied, the consequences of such non-compliance. The new Sections 3862 and 3863 replace Handbook Section 3861, *Financial Instruments – Disclosure and Presentation*, revising and enhancing its disclosure requirements, and carrying forward unchanged its presentation requirements. These new sections place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks. We are currently assessing the impact of these new standards on our financial statements.

BUSINESS RISKS AND UNCERTAINTIES

Fortress' production and exploration activities are concentrated in the Western Canadian Sedimentary Basin, where activity is highly competitive and includes a variety of different sized companies ranging from smaller junior producers to the much larger integrated petroleum companies. Fortress is subject to the various types of business risks and uncertainties including:

- finding and developing oil and natural gas reserves at economic costs;
- production of oil and natural gas in commercial quantities; and
- marketability of oil and natural gas produced.

In order to reduce exploration risk, the Company strives to employ highly qualified and motivated professional employees with a demonstrated ability to generate quality proprietary geological and geophysical prospects. To help maximize drilling success, Fortress combines exploration in areas that afford multi-zone prospect potential, targeting a range of low to moderate risk prospects with some exposure to select high-risk with high-reward opportunities. The Company explores in areas where the Company has drilling experience.

The Company mitigates its risk related to producing hydrocarbons through the utilization of the most appropriate technology and information systems. In addition, the Company seeks to maintain operational control of its prospects.

Oil and gas exploration and production can involve environmental risks such as pollution of the environment and destruction of natural habitat, as well as safety risks such as personal injury. In order to mitigate such risks, Fortress conducts its operations at high standards and follows safety procedures intended to reduce the potential for personal injury to employees, contractors and the public at large. The Company maintains current insurance coverage for general and comprehensive liability as well as limited pollution liability. The amount and terms of this insurance are reviewed on an ongoing basis and adjusted as necessary to reflect changing corporate requirements, as well as industry standards and government regulations. Fortress may periodically use financial or physical delivery hedges to reduce its exposure against the potential adverse impact of commodity price volatility, as governed by formal policies approved by senior management subject to controls established by the Board of Directors.

CONSOLIDATED BALANCE SHEETS

As at (in thousands) (unaudited)	March 31, 2007	December 31, 2006
ASSETS <i>(note 2)</i>		
Current		
Cash and cash equivalents	\$ 1,417	\$ 36,756
Accounts receivable	10,214	7,951
Prepaid expenses	413	368
	12,044	45,075
Property, plant and equipment <i>(note 4)</i>	80,772	70,579
	\$ 92,816	\$ 115,654
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Accounts payable and accrued liabilities	\$ 11,531	\$ 7,080
Income taxes payable	-	283
Revolving operating loan <i>(note 5)</i>	3,750	-
	15,281	7,363
Asset retirement obligations <i>(note 6)</i>	1,860	1,678
Future income tax liability	4,968	5,052
	22,109	14,093
Shareholders' Equity		
Share capital <i>(note 8)</i>	116,696	157,508
Contributed surplus <i>(note 8)</i>	12,045	1,779
Deficit	(58,034)	(57,726)
	70,707	101,561
	\$ 92,816	\$ 115,654

See accompanying notes to the consolidated financial statements

CONSOLIDATED STATEMENTS OF OPERATIONS, COMPREHENSIVE INCOME (LOSS) AND DEFICIT

For the three months ended March 31

(in thousands, except per share amounts) (unaudited)

	2007	2006
REVENUE		
Petroleum and natural gas	\$ 3,296	\$ 4,500
Royalties (net of Alberta Royalty Tax Credit)	(507)	(951)
	2,789	3,549
Interest income	216	139
	3,005	3,688
EXPENSES		
Operating	639	1,170
General and administrative	790	1,577
Stock-based compensation (note 9)	110	852
Interest	18	234
Depletion and depreciation	1,816	1,932
Accretion of asset retirement obligations (note 6)	24	43
	3,397	5,808
Loss before the following	(392)	(2,120)
OTHER		
Gain on sale of oil and gas property, plant and equipment	-	20,087
Income (loss) before income taxes	(392)	17,967
Income tax expense (recovery) (note 7)		
Current	-	20
Future	(84)	4,507
	(84)	4,527
Net income (loss) and comprehensive income (loss) for the period	(308)	13,440
Deficit, beginning of period	(57,726)	(65,814)
Deficit, end of period	\$ (58,034)	\$ (52,374)
Net income (loss) and comprehensive income (loss) per share (note 8)		
Basic	\$ (0.02)	\$ 0.19
Diluted	\$ (0.02)	\$ 0.19

See accompanying notes to the consolidated financial statements

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the three months ended March 31
(in thousands) (unaudited)

	2007	2006
CASH PROVIDED BY (USED IN):		
OPERATING ACTIVITIES		
Net income (loss) for the period	\$ (308)	\$ 13,440
Items not affecting cash flows:		
Stock-based compensation	110	852
Depletion and depreciation	1,816	1,932
Accretion of asset retirement obligations	24	43
Gain on sale of oil and gas property, plant and equipment	-	(20,087)
Future income tax expense (recovery)	(84)	4,507
Funds from operations	1,558	687
Change in non-cash operating working capital <i>(note 10)</i>	557	1,396
	2,115	2,083
FINANCING ACTIVITIES		
Change in revolving operating loan	3,750	(22,975)
Issuance of common shares on exercise of stock options	-	1,564
Redemption of common shares <i>(note 8)</i>	(30,471)	-
Purchase of common shares <i>(note 8)</i>	(186)	-
	(26,907)	(21,411)
INVESTING ACTIVITIES		
Property, plant and equipment expenditures	(11,850)	(3,205)
Sale of property and equipment, net of transaction costs	-	95,477
Deferred costs	-	(175)
Change in non-cash investing working capital <i>(note 10)</i>	1,303	(9,190)
	(10,547)	82,907
Net change in cash	(35,339)	63,579
Cash and cash equivalents – beginning of period	36,756	61
Cash and cash equivalents – end of period	\$ 1,417	\$ 63,640
Supplemental cash flow information:		
Interest paid	\$ 18	\$ 234
Income taxes paid	-	-

See accompanying notes to the consolidated financial statements

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2007 (Tabular figures are in thousands of dollars unless otherwise indicated)(unaudited)

1. NATURE OF OPERATIONS

Fortress Energy Inc. ("Fortress" or the "Company" formerly SignalEnergy Inc.) is a Calgary-based junior oil and gas exploration and development company. All activity is conducted in Western Canada and comprises a single operating segment.

Effective February 20, 2007, SignalEnergy Inc. ("Signal") completed a reorganization whereby all of its assets were transferred to Fortress and a significant number of Signal shares were redeemed for cash. This transaction is further described in notes 2 and 8.

2. SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of presentation

Except as noted below, the unaudited interim consolidated financial statements of the Company have been prepared by management in accordance with Canadian generally accepted accounting principles using the same accounting policies as set out in note 2 to the audited consolidated financial statements for the year ended December 31, 2006. Certain information or disclosures normally required to be included in notes to annual audited financial statements have been condensed or omitted. The unaudited interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements for the year ended December 31, 2006.

On February 20, 2007, Signal and Fortress reorganized, as follows (refer to note 8 for a continuity of Fortress' and Signal's share capital):

- (i) Signal redeemed 23,076,923 common shares for cash at a price of \$1.30 per share;
- (ii) Fortress issued 13,307,815 common shares from treasury to Signal's shareholders in exchange for all of Signal's outstanding shares;
- (iii) Out-of-pocket transaction costs of \$471,000.

The economic substance of the Reorganization is a transaction whereby the resulting entity is governed under the laws of the Province of Alberta, and not Quebec. Signal was dissolved into Fortress on April 19, 2007.

The balance sheet and share capital as presented are of Fortress as a legal entity. The assets, liabilities, and dollar amounts attributed to share capital are those of Signal. The financial position, results of operations and cash flow for all periods prior to the Reorganization are those of Signal.

(b) Comparative figures

Certain comparative figures have been reclassified to conform to the presentation adopted in the current period.

3. CHANGES IN ACCOUNTING POLICIES

Effective January 1, 2007, the Company adopted five new accounting standards issued by the Canadian Institute of Chartered Accountants ("CICA"): Handbook Section 3855 "Financial Instruments – Recognition and Measurement", Section 3861 "Financial Instruments – Disclosure and Presentation", Section 3865 "Hedges", Section 1506 "Accounting Changes", Section 1530 "Comprehensive Income" and Section 3251 "Equity".

Impact upon adoption of Sections 3855, 3861, 3865, 1506, 1530 and 3251

The adoption of the new standards did not have a significant impact on the Company's financial statements due to the nature of the financial instruments recorded on the balance sheet and the contracts to which the Company is a party.

Financial instruments - recognition and measurement

Section 3855 establishes standards for recognizing and measuring financial assets, financial liabilities, and non-financial derivatives. It requires that financial assets and financial liabilities, including derivatives, be recognized on the balance sheet when the Company becomes a party to the contractual provisions of the financial instrument or non-financial derivative contract. Under this standard, all financial instruments are required to be measured at fair value upon initial recognition except for certain related party transactions. Measurement in subsequent periods depends on whether the financial instrument has been classified as held-for-trading, available-for sale, held-to-maturity, loans or receivables, or other financial liabilities. Financial assets and financial liabilities held-for-trading are measured at fair value with changes in those fair values recognized in net earnings. Financial assets held-to-maturity, loans and receivables, and other financial liabilities are

March 31, 2007 (Tabular figures are in thousands of dollars unless otherwise indicated)

measured at amortized cost using the effective interest method of amortization. Investments in equity instruments classified as available-for-sale that do not have a quoted market price in an active market are measured at cost.

Derivative instruments are recorded on the balance sheet at fair value, including those derivatives that are embedded in financial or non-financial contracts that are not closely related to the host contracts. Changes in the fair values of derivative instruments are recognized in net earnings, with the exception of derivatives designated as effective cash flow hedges and hedges of the foreign currency exposure of a net investment in a self-sustaining foreign operation, which are recognized in other comprehensive income. In addition, Section 3855 requires that an entity must select an accounting policy of either expensing debt issue costs as incurred or applying them against the carrying value of the related asset or liability. The financial instruments recognized on Fortress' balance sheet are deemed to approximate their estimated fair values, therefore no further adjustments were required upon adoption of the new sections. There were no financial assets on the balance sheet which were designated as held-for-trading, held-to-maturity or available-for-sale. All financial assets were classified as loans or receivables and are accounted for on an amortized cost basis. All financial liabilities were classified as other liabilities.

Hedges

Section 3865 provides alternative treatments to Section 3855 for entities which choose to designate qualifying transactions as hedges for accounting purposes. It replaces and expands on Accounting Guideline 13 "Hedging Relationships", and the hedging guidance in Section 1650 "Foreign Currency Translation" by specifying how hedge accounting is applied and what disclosures are necessary when it is applied. The Company does not currently have any hedges in place and therefore the adoption of Section 3865 "Hedges" did not have any impact on the Company's financial statements.

Accounting changes

Section 1506 provides expanded disclosures for changes in accounting policies, accounting estimates and corrections of errors. Under the new standard, accounting changes should be applied retrospectively unless otherwise permitted or where impracticable to determine. As well, voluntary changes in an accounting policy are to be made only when required by a primary source of GAAP or the change results in more relevant and reliable information. The Company did not have any accounting changes in the first quarter of 2007 and therefore was not impacted by this new standard.

Comprehensive income (loss) and accumulated other comprehensive income (loss)

Section 1530 introduces comprehensive income, which consists of net earnings and other comprehensive income ("OCI"). OCI represents changes in shareholder's equity during a period arising from transactions and changes in prices, markets, interest rates, and exchange rates. OCI includes unrealized gains and losses on financial assets classified as available-for-sale, unrealized translation gains and losses arising from self-sustaining foreign operations net of hedging activities and changes in the fair value of the effective portion of cash flow hedging instruments.

The Company has not entered into any transactions which require any amounts to be recorded to other comprehensive income (loss) or accumulated other comprehensive income (loss).

Future accounting changes

On December 1, 2006, the CICA issued three new accounting standards: Handbook Section 1535, *Capital Disclosures*, Handbook Section 3862, *Financial Instruments – Disclosures*, and Handbook Section 3863, *Financial Instruments – Presentation*. These new standards are effective January 1, 2008. Section 1535 specifies the disclosure of (i) an entity's objectives, policies and processes for managing capital; (ii) quantitative data about what the entity regards as capital; (iii) whether the entity has complied with any capital requirements; and (iv) if it has not complied, the consequences of such non-compliance. The new Sections 3862 and 3863 replace Handbook Section 3861, *Financial Instruments – Disclosure and Presentation*, revising and enhancing its disclosure requirements, and carrying forward unchanged its presentation requirements. These new sections place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks. We are currently assessing the impact of these new standards on our financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

March 31, 2007 (Tabular figures are in thousands of dollars unless otherwise indicated)

4. PROPERTY, PLANT AND EQUIPMENT

	March 31, 2007 \$	December 31, 2006 \$
Oil and gas properties	89,185	77,194
Other	164	146
	89,349	77,340
Accumulated depletion and depreciation	(8,577)	(6,761)
Net book value	80,772	70,579

For the three months ended March 31, 2007, the Company capitalized general and administrative expenses of \$408,000 (March 31, 2006 - \$110,000) directly attributable to exploration and development activities.

Estimated future development costs of \$22.4 million (March 31, 2006 - \$nil) were included in the calculation of depletion expense for the quarter ended March 31, 2007. As at March 31, 2007, undeveloped land costs of \$3.9 million (March 31, 2006 - \$1.2 million) were excluded from assets subject to depletion.

5. BANK FACILITIES

The Company has an operating loan facility with its bank (the "Bank") to a maximum of \$7 million. The loan bears interest at the Bank's prime lending rate plus 0.25% and is secured by an interest over all present and after acquired property and a floating charge on all lands of a subsidiary company.

6. ASSET RETIREMENT OBLIGATIONS

The Company's asset retirement obligations result from net ownership interests in oil and gas assets including well sites, gathering systems and processing facilities. The Company estimates the net present value of its total asset retirement obligations at March 31, 2007 to be \$1.9 million based on a total future liability of \$3.3 million which will be primarily incurred between 2007 and 2029. An inflation rate of 2.0% (2006 - 3.0%) and a credit-adjusted risk-free rate of 6.5% were used to calculate the fair value of the asset retirement obligations.

Asset Retirement Obligations	\$
Balance, December 31, 2006	1,678
Liabilities incurred	158
Accretion expense	24
Balance, March 31, 2007	1,860

7. INCOME TAXES

The provision for income tax expense (recovery) recorded in the consolidated statement of operations differs from the amount that would be obtained by applying the statutory income tax rate to the income (loss) before tax as follows:

	March 31, 2007 \$	March 31, 2006 \$
Income (loss) before tax	(392)	17,967
Expected tax expense (recovery) at 32.12% (2006 - 34.50%)	(126)	6,041
Add (deduct) income tax effect of:		
Non-deductible crown charges	-	77
Resource allowance	-	(46)
Stock-based compensation	35	287
Flow-through share renouncement	-	(1,022)
Non-deductible expenses and other permanent differences	7	9
Large Corporations Tax	-	20
Rate adjustments	-	(839)
Income tax expense (recovery)	(84)	4,527

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

March 31, 2007 (Tabular figures are in thousands of dollars unless otherwise indicated)

8. SHARE CAPITAL

(a) Authorized:

Unlimited number of voting common shares without par value.

Unlimited number of non-voting, non-retractable, non-redeemable preferred shares without par value to be issued in series as determined by the Company.

(b) Common shares issued and outstanding:

(i) SignalEnergy Inc.

	Number of Common Shares	\$
Balance, December 31, 2006	89,615,982	157,508
Redemption of common shares ⁽ⁱⁱⁱ⁾	(23,076,923)	(40,374)
Exchanged for common shares of Fortress ⁽ⁱⁱⁱ⁾	(66,539,059)	(117,134)
Balance, March 31, 2007	-	-

(ii) Fortress Energy Inc.

	Number of Common Shares	\$
Balance, December 31, 2006	-	-
Issued in exchange for shares of Signal ⁽ⁱⁱⁱ⁾	13,307,815	117,134
Normal course issuer bid ^(iv)	(50,000)	(438)
Balance, March 31, 2007	13,257,815	116,696

(iii) A Reorganization (the "Reorganization") of SignalEnergy Inc. ("Signal"), including an arrangement (the "Arrangement") under the Companies Act (Quebec), was approved by the shareholders at a Special General Meeting of Shareholders held on February 15, 2007 and was effective on February 20, 2007.

Under the Arrangement, shareholders of Signal could elect to receive cash, common shares of Fortress, or a combination of both, subject to total cash available of \$30 million. Shareholders representing 63,400,000 common shares of Signal elected to receive cash which resulted in a cash distribution to shareholders of \$30,000,000 to redeem 23,076,923 common shares of Signal at \$1.30 per share. The historical value of these shares of \$40,374,000 was removed from share capital and the excess over the redemption price and reorganization costs of \$9,904,000 was recorded as an increase in contributed surplus. The remaining 66,539,059 common shares of Signal were exchanged for common shares of Fortress on a basis of one common share of Fortress for every five common shares of Signal, resulting in the issuance of 13,307,815 common shares of Fortress.

Fortress was a shell company that was formed for the purposes of completing the Reorganization of Signal.

(iv) On December 13, 2006, the Company initiated a normal course issuer bid process whereby a maximum of 896,160 common shares (as adjusted for the Reorganization) could be repurchased beginning December 15, 2006 and terminating December 14, 2007. As at March 31, 2007, the Company had purchased 50,000 common shares at an average price of \$3.71 per share or \$186,000. The historical value of these shares of \$438,000 was removed from share capital and the excess over the purchase price of \$252,000 was recorded as an increase in contributed surplus.

(c) Contributed surplus:

	\$
Balance, December 31, 2006	1,779
Share redemption	9,904
Normal course issuer bid	252
Stock-based compensation expense	110
Balance, March 31, 2007	12,045

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

March 31, 2007 (Tabular figures are in thousands of dollars unless otherwise indicated)

(d) Stock option plan:

consultants of the Company pursuant to an incentive plan (the "Plan"). Under the Plan, the exercise price of options granted cannot be less than the closing market price for the Company's common shares on the date of grant. Options typically vest over a four-year period and expire five years from the date of grant.

The following table summarizes stock option transactions:

	Number	Weighted average exercise price \$
Outstanding, beginning of period	22,000	20.75
Granted	963,000	4.65
Cancelled	(15,000)	4.75
Outstanding, end of period	970,000	5.09
Exercisable, end of period	22,000	20.75

The Company has the following stock options outstanding at March 31, 2007:

Exercise Price \$	Outstanding		Exercise Price \$	Exercisable	
	Number	Weighted average years to expiry		Number exercisable	Exercise Price \$
3.00 - 4.00	15,000	5.0	3.11	-	-
4.00 - 5.00	933,000	4.8	4.65	-	-
19.50 - 50.00	22,000	2.1	20.75	22,000	20.75
Outstanding, March 31, 2007	970,000	4.7	5.09	22,000	20.75

(e) Per share amounts:

The weighted average number of common shares outstanding for the three months ended March 31, 2007 and 2006 are as follows:

	March 31, 2007	March 31, 2006
Weighted average - basic	13,262,135	70,598,169
Weighted average - diluted	13,262,135	71,239,284

The weighted average number of common shares outstanding reflects the effects of the Reorganization on February 20, 2007. The dilutive effect of the Company's issuable securities at March 31, 2007, which consist of 970,000 (March 31, 2006 - 2,610,500) stock options to issue common shares, was nil shares (March 31, 2006 - 641,115 shares).

9. STOCK-BASED COMPENSATION

The Company records compensation costs on the granting of stock options using the fair value method. Compensation expense is calculated using the Black-Scholes option pricing model with the following weighted average assumptions:

	March 31, 2007	March 31, 2006
Risk-free interest rate (%)	3.75	3.51
Expected life (years)	5.0	5.0
Expected volatility (%)	50.0	60.0
Expected dividend yield (%)	-	-

The estimated fair value of stock options of \$2.26 per share (March 31, 2006 - \$3.55) is amortized to expense over the vesting period on a straight-line basis. For the three months ended March 31, 2007, the Company recorded compensation expense of \$110,000 related to stock options (March 31, 2006 - \$852,000).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

March 31, 2007 (Tabular figures are in thousands of dollars unless otherwise indicated)

10. CHANGE IN NON-CASH WORKING CAPITAL

Changes in non-cash working capital balances are comprised of the following:

	March 31, 2007	March 31, 2006
	\$	\$
Accounts receivable	(2,263)	3,362
Prepaid expenses	(45)	60
Accounts payable and accrued liabilities	4,451	(11,236)
Income taxes payable	(283)	20
	1,860	(7,794)
Attributable to operating activities	557	1,396
Attributable to investing activities	1,303	(9,190)

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