

**Form 10QSB for AMERICAN ENERGY GROUP LTD**

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**22-Feb-2005****Quarterly Report****ITEM 2- MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION****Forward-Looking Statements**

This report contains statements about the future, sometimes referred to as "forward-looking" statements. Forward-looking statements are typically identified by the use of the words "believe," "may," "will," "should," "expect," "anticipate," "estimate," "project," "propose," "plan," "intend" and similar words and expressions. We intend the forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in Section 27A of the Securities Act and Section 21E of the Exchange Act. Statements that describe our future strategic plans, goals or objectives are also forward-looking statements.

Readers of this report are cautioned that any forward-looking statements, including those regarding the Company or its management's current beliefs, expectations, anticipations, estimations, projections, proposals, plans or intentions, are not guarantees of future performance or results of events and involve risks and uncertainties, such as:

- The future results of drilling individual wells and other exploration and development activities;
- Future variations in well performance as compared to initial test data;
- Future events that may result in the need for additional capital;
- Fluctuations in prices for oil and gas;
- Future drilling and other exploration schedules and sequences for various wells and other activities;

- Uncertainties regarding future political, economic, regulatory, fiscal, taxation and other policies in Pakistan;
- Our future ability to raise necessary operating capital.

The forward-looking information is based on present circumstances and on our predictions respecting events that have not occurred, which may not occur or which may occur with different consequences from those now assumed or anticipated. Actual events or results may differ materially from those discussed in the forward-looking statements as a result of various factors, including the risk factors detailed in this report. The forward-looking statements included in this report are made only as of the date of this report. We are not obligated to update such forward-looking statements to reflect subsequent event or circumstances.

## **Overview**

Prior to the Company's bankruptcy proceedings initiated on June 28, 2002, we were an active oil and gas exploration and development company. The foreclosure of our Fort Bend County, Texas oil and gas leases by the secured creditor in early calendar 2003 resulted in the loss of our only revenue producing asset. We intend to initiate new business activities by prudent management of our Pakistan overriding royalty interest and our Galveston, Texas interests and if we are successful in generating working capital from these investments or from sales of securities, we intend to pursue investment opportunities in the oil and gas business. Drilling of the first well in Pakistan as to which our overriding royalty pertains is scheduled for the first quarter of calendar 2005.

## **Results of Operations**

Our operations for the period ending December 31, 2004 reflected a net loss of \$117,481 attributable to salaries paid to the directors, legal and professional fees, office overhead, administrative expense and interest. There were no revenues from operations. All of our producing oil and gas leases were foreclosed by the first lien lender in early calendar 2003. As a result, the Company is solely dependent upon cash infusion from the sale of securities and loans until business operations which generate an income stream can be developed. Our operating company, The American Energy Operating Corp. did not participate in the bankruptcy proceedings and its accounts payable and accrued liabilities are still carried on our books post-bankruptcy, despite the inactivation of the subsidiary.

As a result of the loss of our cash producing assets through foreclosure, we have purposely omitted a detailed discussion of operational results and their ramifications.

During the bankruptcy proceedings and immediately thereafter, We received \$575,000 in commitments for convertible debt funding from third parties which was authorized under the Second Amended Plan of Reorganization, all of which was collected and converted to Common stock. We have used such funds to finance salaries, legal expenses and nominal administrative overhead.

## **Liquidity and Capital Resources**

Since emerging from bankruptcy, we have been funded solely through the private sale of convertible debt securities totaling \$575,000 pursuant to Second Amended Plan of Reorganization, all of which has been converted to Common stock. Subsequent to the end of the quarter ending December 31, 2004, we obtained

a loan from a private party for \$200,000 for near term operating capital, the terms of which are accrual of interest at Wall Street Prime plus one percent, no prepayment penalty, and a maturity of one year, with the right to extend the maturity for an additional year by the payment of an extension fee of \$20,000. During the quarter ended December 31, 2004, we issued 76,520 shares of restricted Common stock to pay for \$25,416.67 in accounting services through December 31, 2004. On a going forward basis, we believe that we will need additional operating capital and anticipate seeking an infusion of cash through loans, sales of securities, a sale or partial sale of the Galveston County, Texas assets or successful resolution of the Smith Energy litigation. We anticipate that some critical services rendered by third parties during the 2005 calendar year will be paid with Common Stock, instead of cash assets. Successful drilling on the Pakistan Concession by Hydro Tur (Energy) Ltd. will also result in the generation of operating capital once sales into the existing pipeline infrastructure begin. However, there can be no assurance that we will be successful in obtaining sufficient operating capital to meet future needs from any of these potential sources.

In light of our current lack of revenue-generating business operations and our need to further capitalize future overhead, operations and growth, our viability as a going concern is uncertain. There can be no assurance that we will be successful in our efforts to improve the Company's financial position and to develop its assets.

### **Business Strategy and Prospects**

We believe that there have been positive developments resulting from the bankruptcy proceedings. We have eliminated the Company's debt burden, diminished its labor force and significantly reduced all facets of general and administrative overhead. The cancellation and reissuance of new securities have reduced the outstanding shares from over sixty six million shares to just over twenty three million shares, a number which both permits the issuance of additional securities in the future as needed to obtain strategic assets or funding from investors, and which provides an opportunity for enhanced shareholder value if the current assets become cash generating assets. However, the Company does not currently enjoy a revenue stream from any business operation or asset. We must continue to raise operating capital through other means until a revenue stream is developed, if at all.

### **Pakistan Overriding Royalty**

The Company, through its Hycarbex subsidiary (before the sale of that subsidiary) expended in excess of \$10,000,000.00 on drilling and seismic on the Jacobabad and Yasin concessions in the Republic of Pakistan comprised of over 2,200 square kilometers. The structure, to date, has no Proved Reserves as that term and the calculation for discounted future net cash flows for reporting purposes is mandated by the Financial Accounting Standards Board in Statement of Financial Accounting Standards No. 69, titled "Disclosures About Oil and Natural Gas Producing Activities". While we did not obtain a commercial discovery well in any of our previous Pakistan drilling efforts, we have been encouraged by the technical data derived from the drilling and seismic activities. We believe that the concession acreage contains oil and gas producing physical structures which are worthy of further exploration. If successfully developed, our reserved 18% overriding royalty interest would likely be a good source of cash revenues because the royalty, by its nature, entitles us to share in gross, rather than net, production. These revenues, if any, could be used by the Company for further investment in other revenue generating assets or business activities. The financial risks inherent in oil and gas drilling in Pakistan will no longer be borne by the Company because an overriding royalty interest is not subject to such costs. While successful production and favorable hydrocarbon prices are necessary for the overriding royalty interest to demonstrate real value, we are optimistic that the additional seismic and technical data generated by the Company prior to sale and further expanded and refined after the sale by Hydro Tur (Energy) Ltd. will enhance the chances

of a commercial discovery by Hydro Tur (Energy) Ltd. The drilling of the first well is scheduled during the first quarter of calendar 2005. Absent successful drilling by Hydro Tur (Energy) Ltd., the reserved overriding royalty interest is likely to have little or no value.

### **Galveston County, Texas Leases**

In 1997, we purchased the interests of Luck Petroleum Corporation from its bankruptcy trustee in two oil and gas leases in Galveston County, Texas. The leases are situated in an area which is productive in multiple zones or horizons and the leases themselves have produced commercial quantities of oil and gas from both shallow and mid-range zones. In 1986, Luck Petroleum Corporation assigned these mid-range zones to Smith Energy, reserving for itself an "after-payout" 15% back-in working interest. Luck Petroleum Corporation also limited the depths assigned to Smith Energy, thereby resulting in depths generally greater than 10,000 feet being reserved to Luck Petroleum Corporation. We succeeded to the interests of Luck Petroleum Corporation as a result of the 1997 purchase from the bankruptcy trustee. With regard to the mid-range zones, our research to date has given rise to the belief that "payout" has occurred, as defined in the 1986 conveyance by Luck Petroleum Corporation to Smith Energy. If we are correct, then we are entitled to receive 15% of the monthly working interest production from the existing Smith Energy wells on the leases. As indicated in this report, we have initiated a lawsuit against Smith Energy to establish these rights.

The Smith Energy lawsuit does not pertain to the deep zones under the leases which were acquired from Luck Petroleum Corporation. Based upon our research, we believe that these zones have development potential. We are exploring the various opportunities to realize value from these deep rights, including potential sale. We have not yet determined the best course for these assets. These leases are held in force by third party production and, therefore, the leases do not require development of these rights by a certain date. We believe that we will be able to continue our research and conduct future negotiations toward a development path which best suits our goals and our cash flow position. We are compelled to focus on these efforts for the near term in order to generate additional working capital.