

TALISMAN

E N E R G Y

INTERIM MANAGEMENT'S DISCUSSION AND ANALYSIS

JULY 29, 2009

Management's Discussion and Analysis (MD&A)

(July 29, 2009)

This discussion and analysis should be read in conjunction with the unaudited Interim Consolidated Financial Statements of Talisman Energy Inc. ("Talisman" or the "Company") as at and for the three and six month periods ended June 30, 2009 and 2008, the December 31, 2008 MD&A and audited Consolidated Financial Statements and the MD&A and unaudited Interim Consolidated Financial Statements as at and for the three months ended March 31, 2009 and 2008. The Company's Consolidated Financial Statements and the financial data included in the MD&A have been prepared in accordance with accounting principles generally accepted in Canada (Canadian GAAP). All comparisons are between the quarters ended June 30, 2009 and 2008, unless stated otherwise. All amounts are in Canadian dollars unless otherwise indicated. Abbreviations used in this MD&A are listed on the page headed 'Abbreviations'.

Second Quarter Results Summary

- Cash provided by operating activities during the quarter was \$1.1 billion, a decrease from \$1.5 billion a year ago, primarily due to lower prices. Year to date cash provided by operating activities was \$2.2 billion.
- Net income was \$63 million, down from \$426 million a year earlier, also driven by lower prices.
- Production averaged 424,000 boe/d, 2% below the second quarter of 2008. Year to date, production from continuing operations has averaged 426,000 boe/d, 6% above last year.
- Netbacks were down 55% from a year earlier, averaging \$27.41/boe with both oil and natural gas prices significantly lower due to the global economic slowdown.
- Talisman has continued to strengthen its balance sheet. Long-term debt net of cash and cash equivalents and bank indebtedness at quarter end was \$2 billion, down from \$3.9 billion at December 31, 2008.
- The Company closed the sale of non-core midstream assets in Alberta and non-strategic properties in Southeast Saskatchewan and Trinidad and Tobago in the second quarter, with total proceeds of \$1.3 billion.
- Talisman has made exploration discoveries at Huron-1 (Colombia), Grevling (Norway) and Shaw (UK).
- The Company is currently producing 30 mmcf/d from the Marcellus Shale play and has increased its 2009 drilling program to approximately 50 wells.

Highlights

June 30,	Three months ended		Six months ended	
	2009	2008	2009	2008
Financial (millions of C\$ unless otherwise stated)				
Net income (loss) from continuing operations	(433)	249	(526)	665
Net income from discontinued operations	496	177	1,044	227
Net income	63	426	518	892
C\$ per common share				
Net income – Basic	0.06	0.42	0.51	0.88
– Diluted	0.06	0.41	0.51	0.86
Net income (loss) from continuing operations				
– Basic	(0.43)	0.24	(0.52)	0.65
– Diluted	(0.43)	0.24	(0.52)	0.64
Production (daily average)				
Oil and liquids (bbls/d)	204,023	203,332	212,639	201,220
Natural gas (mmcf/d)	1,270	1,226	1,278	1,192
Continuing operations (mboe/d)	416	408	426	401
Discontinued operations (mboe/d)	8	24	11	25
Total mboe/d (6 mcf = 1 boe)	424	432	437	426

Higher oil and liquids and natural gas volumes from continuing operations were driven by increased production in Southeast Asia. The Company's net income was impacted by the decline in global commodity prices. The increase in income from discontinued operations was a result of gains arising on three transactions that closed during the second quarter of 2009 (See 'Discontinued Operations' section of this MD&A).

Daily Average Production, Before Royalties

June 30,	Three months ended			Six months ended		
	2009	2009 vs 2008 (%)	2008	2009	2009 vs 2008 (%)	2008
Continuing operations						
Oil and liquids (bbls/d)						
North America	31,602	(5)	33,136	31,869	(4)	33,203
UK	89,936	-	89,886	96,277	12	86,089
Scandinavia	31,165	5	29,709	33,009	8	30,451
Southeast Asia	38,094	6	35,847	37,719	3	36,537
Other	13,226	(10)	14,754	13,765	(8)	14,940
	204,023	-	203,332	212,639	6	201,220
Natural gas (mmcf/d)						
North America	806	(6)	857	815	(3)	836
UK	21	11	19	25	56	16
Scandinavia	43	115	20	47	147	19
Southeast Asia	400	21	330	391	22	321
	1,270	4	1,226	1,278	7	1,192
Continuing operations (mboe/d)						
	416	2	408	426	6	401
Discontinued operations						
North America	5		12	7		12
UK	-		4	-		5
Scandinavia	-		3	-		2
Other	3		5	4		6
Discontinued operations (mboe/d)	8	(67)	24	11	(56)	25
Total mboe/d (6 mcf = 1 boe)	424	(2)	432	437	3	426

Production from continuing operations increased by 2% over the previous year due principally to increased natural gas volumes in Southeast Asia. On a year-to-date basis, production from continuing operations increased by 6% as a result of higher liquids production in the UK and increased natural gas volumes in Southeast Asia.

Natural gas production from continuing operations in North America decreased by 51 mmcf/d due principally to natural declines and the Edson plant turnaround, partially offset by successful development in the Montney core, Marcellus and Outer Foothills.

In the UK, oil and liquids production from continuing operations remained unchanged relative to the second quarter of 2008 since increased production from Tweedsmuir was offset by a compressor problem at Claymore. In 2008, Tweedsmuir was not fully operational and an extended shutdown and reduced compressor availability impacted production from the Fulmar and Ross/Blake fields, respectively.

In Scandinavia, oil and liquids and natural gas production from continuing operations increased due to first production from Rev in January 2009, and new wells on production at Varg, partially offset by natural declines and a planned shutdown.

Natural gas production in Indonesia was 20% higher than last year, averaging 325 mmcf/d due to increased Corridor natural gas production. Malaysia/Vietnam gas production averaged 75 mmcf/d in the quarter, an increase of 16mmcf/d compared to the same period in 2008 due to additional gas production from the Northern Fields, which commenced production in July 2008.

Southeast Asia oil and liquids production from continuing operations increased by 6% relative to the same quarter in 2008 due principally to Song Doc production which began late in the fourth quarter of 2008, and a 37% increase in production in Australia, the result of the Corallina field being brought back on-stream after riser repairs had been completed.

Oil and liquids production from continuing operations in other areas decreased by 10% due principally to OPEC production restrictions and natural declines.

Volumes produced into (sold out of) inventory¹

June 30,	Three months ended		Six months ended	
	2009	2008	2009	2008
UK	(6,346)	1,639	(3,335)	(3,813)
Scandinavia	(560)	(10,190)	(2,971)	(151)
Southeast Asia	2,994	(379)	(4,059)	4,051
Other	(3,542)	(15,348)	(8,903)	1,238
Total produced into (sold out of) inventory – bbls/d	(7,454)	(24,278)	(19,268)	1,325
Total produced into (sold out of) inventory – mmbbls	(0.7)	(2.2)	(3.5)	0.2
Inventory at June 30 - mmbbls	1.6	3.3	1.6	3.3

1. Includes impact of discontinued operations

In the Company's international operations, produced oil is frequently stored in tanks until there is sufficient volume to be lifted. The Company recognizes revenue and the related expenses on crude oil production when liftings have occurred. Volumes presented in the 'Daily Average Production, Before Royalties' table above represent production volumes in the period, which include oil volumes produced into inventory and exclude volumes sold out of inventory.

Company Netbacks ^{1,2}

June 30,	Three months ended		Six months ended	
	2009	2008	2009	2008
Oil and liquids (\$/bbl)				
Sales price	66.48	124.66	59.77	110.16
Hedging loss	-	(0.72)	-	(0.60)
Royalties	8.28	21.04	6.84	18.36
Transportation	1.11	1.09	1.16	1.03
Operating costs	18.72	20.80	17.94	20.22
	38.37	81.01	33.83	69.95
Natural gas (\$/mcf)				
Sales price	4.88	10.55	5.26	9.38
Royalties	0.70	2.22	0.88	1.94
Transportation	0.25	0.33	0.26	0.28
Operating costs	1.20	1.17	1.19	1.09
	2.73	6.83	2.93	6.07
Total (\$/boe) (6 mcf = 1 boe)				
Sales price	47.90	94.46	45.99	83.89
Hedging loss	-	(0.37)	-	(0.31)
Royalties	6.24	17.23	6.08	15.08
Transportation	1.29	1.52	1.35	1.33
Operating costs	12.96	14.01	12.64	13.55
	27.41	61.33	25.92	53.62

1. Netbacks do not include pipeline operations. Additional netback information by major product type and region is included elsewhere in this MD&A.
2. Includes impact of discontinued operations.

During the second quarter, the Company's average netback was \$27.41/boe, 55% lower than in 2008. Talisman's realized price of \$47.90/boe was 49% lower than 2008, due principally to lower global commodity prices.

The Company's realized sales price does not include the impact of financial commodity derivatives discussed in the 'Risk Management' section of this MD&A.

Commodity Prices ¹ and Exchange Rates

June 30,	Three months ended			Six months ended		
	2009	2009 vs 2008 (%)	2008	2009	2009 vs 2008 (%)	2008
Oil and liquids (\$/bbl)						
North America	56.55	(46)	105.27	49.29	(47)	93.07
UK	67.73	(45)	123.25	61.70	(44)	110.78
Scandinavia	67.89	(47)	129.08	61.91	(46)	113.98
Southeast Asia	70.61	(48)	136.86	61.79	(48)	117.91
Other	69.75	(51)	141.12	63.95	(47)	120.90
	66.48	(47)	124.66	59.77	(46)	110.16
Natural gas (\$/mcf)						
North America	4.37	(57)	10.25	4.94	(46)	9.08
UK	4.24	(57)	9.76	5.22	(43)	9.16
Scandinavia	4.22	(38)	6.77	7.24	15	6.28
Southeast Asia	6.01	(49)	11.67	5.69	(45)	10.41
	4.88	(54)	10.55	5.26	(44)	9.38
Total \$/boe (6 mcf = 1 boe)	47.90	(49)	94.46	45.99	(45)	83.89
Benchmark prices and foreign exchange rates						
WTI (US\$/bbl)	59.62	(52)	123.98	51.33	(54)	110.94
Dated Brent (US\$/bbl)	58.79	(52)	121.38	51.60	(53)	109.14
Tapis (US\$/bbl)	57.17	(55)	125.73	53.17	(53)	113.02
NYMEX (US\$/mmbtu)	3.60	(67)	10.80	4.23	(55)	9.45
AECO (\$/gj)	3.27	(66)	9.68	3.97	(54)	8.59
US dollar/Canadian dollar exchange rate	1.17	18	0.99	1.21	22	0.99
Pound sterling/Canadian dollar exchange rate	1.81	(9)	1.99	1.80	(10)	1.99

1. Includes impact of discontinued operations.

Realized oil and liquids prices decreased by 47%, and natural gas prices decreased by 54% relative to the second quarter of 2008, in line with the decline in global oil and gas prices. Scandinavian gas prices during the six months ended June 30, 2009 were positively impacted by the commissioning of Rev, which is priced off the European gas market. North America natural gas prices include the impact of physical commodity contracts.

Royalties¹

June 30,	Three months ended			
	2009		2008	
	%	\$ millions	%	\$ millions
North America	11	55	18	208
UK	-	2	-	1
Southeast Asia	31	132	41	320
Other	41	32	54	179
Corporate Average	12	221	19	708

June 30,	Six months ended			
	2009		2008	
	%	\$ millions	%	\$ millions
North America	14	140	18	362
UK	-	2	-	5
Southeast Asia	34	277	41	523
Other	47	102	54	179
Corporate Average	14	521	18	1,069

1. Includes impact of royalties related to sales volumes.

The corporate royalty expense from continuing operations for the second quarter was \$221 million (12%), down \$487 million from \$708 million (19%) in 2008 due to reduced commodity prices.

Unit Operating Expenses¹

June 30,	Three months ended			Six months ended		
	2009	2009 vs 2008	2008	2009	2009 vs 2008	2008
	\$/boe	(%)	\$/boe	\$/boe	(%)	\$/boe
North America	10.19	6	9.65	10.06	13	8.87
UK	23.91	(18)	29.19	22.44	(23)	29.10
Scandinavia	17.80	(10)	19.81	17.39	(17)	21.04
Southeast Asia	6.81	6	6.43	6.61	14	5.80
Other	7.42	33	5.57	7.03	19	5.92
	12.96	(7)	14.01	12.64	(7)	13.55

1. Includes impact of production volumes and expenses from discontinued operations.

Total Operating Expenses¹

June 30, (\$ millions)	Three months ended		Six months ended	
	2009	2008	2009	2008
North America	154	158	305	282
UK	216	227	427	443
Scandinavia	62	80	137	137
Southeast Asia	64	56	131	90
Other	8	15	25	16
	504	536	1,025	968

1. Includes operating expenses related to sales volumes.

Talisman has implemented a global review to identify and implement cost savings and operational efficiencies. Some of the initiatives include reducing the number of vessels needed to support operations, improved logistics coordination and material handling and renegotiations with suppliers. Operating costs are starting to be reduced by these initiatives, but the effect is impacted by the timing of maintenance activities and timing of crude oil liftings.

In North America, operating expenses were lower than the prior year due principally to lower power and maintenance costs.

In the UK, operating expenses decreased due principally to less maintenance work occurring in the second quarter of 2009 than the corresponding period in 2008, which included maintenance work at Tartan, Clyde, Piper, Flotta and Ross/Blake, the strengthening of the Canadian Dollar in relation to the British pound and savings from the cost reduction initiative offset by the timing of liftings. Unit operating expenses decreased following the disposition of higher cost properties.

In Scandinavia, operating expenses decreased due principally to the timing of liftings and cost reduction initiatives, partially offset by Rev production commencing in the first quarter of 2009.

In Southeast Asia, operating expenses increased due the timing of liftings, various shutdowns in the regions, and first oil production from Northern Fields in March 2009 and Song Doc coming on-stream in November 2008, offset by cost reductions and operational efficiencies.

Unit Depreciation, Depletion and Amortization (DD&A) Expense¹

June 30,	Three months ended			Six months ended		
	2009 \$/boe	2009 vs 2008 (%)	2008 \$/boe	2009 \$/boe	2009 vs 2008 (%)	2008 \$/boe
North America	18.84	11	16.96	18.32	9	16.76
UK	23.99	19	20.11	24.11	30	18.49
Scandinavia	24.65	(11)	27.82	23.98	(15)	28.16
Southeast Asia	8.74	17	7.48	9.75	40	6.95
Other	5.62	19	4.74	5.61	2	5.52
	17.63	11	15.86	17.51	12	15.62

1. Includes impact of DD&A expense related to sales volumes.

Total DD&A Expense¹

June 30, (\$ millions)	Three months ended		Six months ended	
	2009	2008	2009	2008
North America	283	269	554	523
UK	218	167	453	310
Scandinavia	87	110	190	174
Southeast Asia	82	63	192	111
Other	9	14	23	14
	679	623	1,412	1,132

1. Includes DD&A expense related to sales volumes.

Total DD&A expense from continuing operations was \$679 million, up 9% from the same period in 2008. The increase in DD&A expense is principally related to a decline in oil reserves due to low oil prices.

The downward revision of reserves volumes at year-end resulting from low oil prices increased UK DD&A expense. In Scandinavia, the impact of the reserves reduction and commencement of Rev production in the first quarter of 2009 was more than offset by lower production at Brage and Gyda.

As noted in the 2008 year-end MD&A, the requirement to use year-end prices to calculate reserves resulted in one property in the UK and one property in Scandinavia having no proved reserves. As a result the net book value of these properties was charged to DD&A. Therefore, these producing properties will have no DD&A expense unless development capital is incurred, in which case it will be depleted immediately until the properties have proved reserves.

The DD&A expense in North America increased due principally to an increase in the land base being amortized.

Southeast Asia DD&A expense increased due principally to the timing of liftings and the commissioning of Northern Fields and Song Doc in 2008.

Corporate and Other

June 30, (\$ millions)	Three months ended		Six months ended	
	2009	2008 ¹	2009	2008 ¹
General and administrative (G&A) expense	86	75	167	139
Dry hole expense	51	70	295	134
Exploration expense	58	115	126	170
Interest on long-term debt	45	37	90	81
Capitalized interest	8	16	17	30
Stock-based compensation	117	270	150	260
Loss on held-for-trading financial instruments	438	530	365	598
Other revenue	(26)	(37)	(60)	(59)
Other expense, net	88	(6)	103	(22)

¹ Restated for operations classified as discontinued subsequent to June 30, 2008.

G&A expense increased by \$11 million relative to 2008, largely as a result of costs associated with executing the new corporate strategy, reorganization costs and other seasonal costs.

Dry hole expense decreased by \$19 million compared to the same period in 2008. The reduction is due principally to the receipt of \$36 million from the sale of tax credits relating to exploration activity in Alaska previously expensed as dry hole.

Interest on long-term debt increased by \$8 million relative to the same period in 2008 due principally to a decrease in capitalized interest. Capitalized interest costs are associated with the Yme development project in Scandinavia and the Auk North and South developments in the UK. When the assets are substantially complete interest is no longer capitalized. Capitalized interest decreased from the prior year as Northern Fields commenced production in July 2008 and Rev commenced production in January 2009.

Stock-based compensation relates principally to the change in value of the Company's outstanding stock options and cash units for the period. The Company's stock-based compensation expense is principally based on the difference between the Company's share price and the exercise price of its stock options or cash units. During the second quarter of 2009, the Company recorded stock-based compensation expense of \$117 million relating principally to its stock option and cash unit plans. Since the introduction of the cash feature, approximately 97% of options exercised have been exercised for cash, resulting in reduced dilution of shares.

Talisman recorded a loss on held-for-trading financial instruments of \$438 million. A mark to market loss of \$661 million that was due principally to the increase in oil prices was partially offset by the receipt of \$193 million of cash settlements in relation to commodity derivatives gains that were accrued at March 31, 2009.

Other revenue of \$26 million includes \$24 million of pipeline and processing revenue.

Other expense consists principally of foreign exchange losses.

