



PAN ORIENT ENERGY CORP.

2008 CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007

MANAGEMENT'S REPORT TO THE SHAREHOLDERS

Management is responsible for the integrity and objectivity of the financial statements and the related management's discussion and analysis. The accompanying financial statements have been prepared by management in accordance with accounting principles generally accepted in Canada using estimates and careful judgment, particularly in those circumstances where transactions affecting a current period are dependent upon future events. The accompanying financial statements have been prepared using policies and procedures established by management and reflect fairly the Company's financial position, results of operations and changes in financial position, within reasonable limits of materiality and within the framework of the accounting policies outlined in the notes to the consolidated financial statements.

Management has established and maintains a system of internal controls which is designed to provide reasonable assurance that assets are safeguarded from loss or unauthorized use and the financial information is reliable and accurate.

The consolidated financial statements have been examined by external auditors. Their examination provides an independent view as to management's discharge of its responsibilities insofar as they relate to the fairness of reported operating results and financial condition of the Company.

The Audit Committee of the Board of Directors has reviewed the consolidated financial statements with management and the external auditors. The consolidated financial statements have been approved by the Board of Directors on the recommendation of the Audit Committee.

(signed "Jeff Chisholm")

Jeff Chisholm

President & Chief Executive Officer

April 17, 2009

(signed "Jason Bednar")

Jason Bednar

Vice President, Finance & Chief Financial Officer

April 17, 2009

AUDITORS' REPORT TO THE SHAREHOLDERS

We have audited the consolidated balance sheets of Pan Orient Energy Corp. as at December 31, 2008 and 2007 and the consolidated statements of operations and retained earnings, comprehensive income and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2008 and 2007 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

(*signed "KPMG LLP"*)

Chartered Accountants

Calgary, Canada

April 17, 2009

PAN ORIENT ENERGY CORP.
CONSOLIDATED BALANCE SHEETS

	December 31 2008	December 31 2007
(\$000s)		
<u>ASSETS</u>		
CURRENT		
Cash and cash equivalents	98,925	36,852
Accounts receivable	13,161	14,501
	<hr/> 112,086	<hr/> 51,353
Deposits (note 4)	4,299	2,177
Petroleum and natural gas properties (note 5)	142,823	88,940
	<hr/> 259,208	<hr/> 142,470
	<hr/> <hr/>	<hr/> <hr/>
<u>LIABILITIES</u>		
CURRENT		
Accounts payable and accrued liabilities	14,739	8,122
Taxes payable	55,260	4,645
	<hr/> 69,999	<hr/> 12,767
Future income tax (note 9)	22,698	7,721
Asset retirement obligation (note 6)	1,964	84
	<hr/> 94,661	<hr/> 20,572
Non-controlling interest (note 5)	18,774	18,018
	<hr/>	<hr/>
<u>SHAREHOLDERS' EQUITY</u> (note 7)		
Share capital	103,078	98,800
Underwriters compensation options	-	119
Contributed surplus	6,531	5,671
Accumulated other comprehensive income (loss)	4,037	(1,722)
Retained earnings	32,127	1,012
	<hr/> 36,164	<hr/> (710)
	<hr/> 145,773	<hr/> 103,880
Commitments and contingencies (note 11)	259,208	142,470
	<hr/> <hr/>	<hr/> <hr/>

See accompanying notes to the consolidated financial statements

Approved on behalf of The Board of Directors:
(signed "Michael Hibberd")
Director

(signed "Paul Wright")
Director

PAN ORIENT ENERGY CORP.

CONSOLIDATED STATEMENTS OF OPERATIONS AND RETAINED EARNINGS

	Year Ended December 31 2008	Year Ended December 31 2007
<i>(\$000s, except per share amounts)</i>		
REVENUES		
Oil	147,554	24,034
Royalties	(10,336)	(1,557)
Interest	991	574
	138,209	23,051
EXPENSES		
Operating	3,809	2,024
Transportation	4,551	864
General and administrative	5,492	3,164
Depletion, depreciation and accretion	18,369	4,705
Stock-based compensation	575	2,601
Foreign exchange (gain) loss	(6,824)	1,326
Foreign new ventures expenditures (note 5)	731	40
	26,703	14,724
INCOME BEFORE TAXES AND NON-CONTROLLING INTEREST	111,506	8,327
TAXES (note 9)		
Special remuneratory benefit	35,489	-
Income tax	30,109	4,646
Future income tax expense (reduction)	14,383	(1,473)
	79,981	3,173
INCOME BEFORE NON-CONTROLLING INTEREST	31,525	5,154
NON-CONTROLLING INTEREST	226	(311)
NET INCOME	31,751	4,843
RETAINED EARNINGS (DEFICIT) BEGINNING OF YEAR	1,012	(3,831)
REPURCHASE OF COMMON SHARES (note 7)	(636)	-
RETAINED EARNINGS END OF YEAR	32,127	1,012
INCOME PER SHARE (note 7)		
Basic	0.70	0.12
Diluted	0.65	0.11

See accompanying notes to the consolidated financial statements

PAN ORIENT ENERGY CORP.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Year Ended December 31 2008	Year Ended December 31 2007
(\$000s)		
Net income	\$ 31,751	\$ 4,843
Foreign exchange gain (loss) on translation of self-sustaining operations	9,561	(430)
Foreign exchange gain realized	(3,802)	-
Comprehensive income	\$ 37,510	\$ 4,413

See accompanying notes to the consolidated financial statements

PAN ORIENT ENERGY CORP.
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31 2008	Year Ended December 31 2007
(\$000s)		
CASH PROVIDED BY (USED IN)		
OPERATING ACTIVITIES		
Net income	31,751	4,843
Items not affecting cash		
Depletion, depreciation and accretion	18,369	4,705
Stock-based compensation	575	2,601
Future income tax expense (reduction)	14,383	(1,473)
Unrealized foreign exchange (gain) loss	(955)	866
Non-controlling interest	(226)	311
	63,897	11,853
Changes in non-cash working capital	53,337	(10,095)
	117,234	1,758
INVESTING ACTIVITIES		
Petroleum and natural gas properties	(40,491)	(22,226)
Indonesia acquisition (note 3)	(15,157)	-
Acquisition of Signet (note 3)	-	2,644
Changes in non-cash working capital	(1,163)	3,607
Deposits	(2,122)	(1,133)
	(58,933)	(17,108)
FINANCING ACTIVITIES		
Issue of common shares, net of issue costs	430	36,591
Repurchase of common shares	(1,092)	-
	(662)	36,591
INCREASE IN CASH AND CASH EQUIVALENTS	57,639	21,241
EFFECT OF FOREIGN EXCHANGE ON CASH BALANCES	4,434	(511)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	36,852	16,122
CASH AND CASH EQUIVALENTS, END OF YEAR	98,925	36,852
TAXES PAID	19,436	-

See accompanying notes to the consolidated financial statements

PAN ORIENT ENERGY CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1) DESCRIPTION OF BUSINESS

Pan Orient Energy Corp. (“Pan Orient” or the “Company”), is an oil and natural gas company incorporated under the laws of Alberta, which holds properties onshore Thailand and Indonesia as well as interests in subsidiaries with properties in Northern Alberta. The Company pursues other oil and natural gas exploration acreage in Asia.

2) SIGNIFICANT ACCOUNTING POLICIES AND BASIS OF PRESENTATION

The consolidated financial statements for the year ended December 31, 2008 are presented in accordance with Canadian Generally Accepted Accounting Principles (GAAP) and are expressed in Canadian dollars. Tabular amounts, except as otherwise indicated, are presented in thousands of dollars.

a) Principles of Consolidation

The consolidated financial statements include the accounts of Pan Orient and the accounts of its subsidiaries, all of which are wholly owned except for Andora Energy Corporation which is approximately 53.2% (2007 – 55.4%) owned by Pan Orient. The consolidated financial statements include a non-controlling interest representing the 46.8% (2007 – 44.6%) portion of assets and liabilities not owned by Pan Orient.

b) Joint Venture Operations

The Company conducts substantially all its oil and gas exploration and production activities with others. These consolidated financial statements reflect the Company’s proportionate interest in such activities.

c) Cash and Cash Equivalents

Cash and cash equivalents consist of cash on deposit and short-term investments with an original maturity date of less than ninety days.

d) Petroleum and Natural Gas Properties

The Company follows the full cost method of accounting for petroleum and natural gas properties and related expenses whereby all costs associated with the exploration for and development of oil and gas reserves are capitalized and accumulated in cost centres segregated by country. Such costs include royalty acquisition, land acquisition, geological and geophysical, costs of drilling both productive and non-productive wells and tangible equipment and administrative costs directly related to acquisition, exploration and development activities. Gains or losses are not recognized upon disposition of oil and natural gas properties unless crediting the proceeds against accumulated costs would result in a 20% or higher change in the depletion rate.

Exploration costs in the pre-production stage, such as costs associated with the investigating, bidding and acquiring petroleum properties are expensed prior to obtaining a petroleum lease or concession, with the exception of costs deferred on projects for which a bid is outstanding or for seismic and related costs in an area that the Company has existing plans to bid or negotiate a concession. The deferred costs are immediately expensed upon obtaining notice of an unsuccessful bid. Initial expenses and the write down of deferred costs are recorded as “Foreign New Venture Expenditures” in the consolidated statement of operations.

Depletion and Depreciation

The costs in cost centres from which there has been no commercial production are not subject to depletion until commercial production commences. Depletion is provided on costs accumulated using the unit-of-production method based on an independent engineering estimate of the Company's share of proved reserves, before royalties. Included in the depletion base are estimated future costs to be incurred in developing proved reserves and, excluded are estimated salvage values and costs incurred acquiring and evaluating unproved properties.

Impairment

Petroleum and natural gas interests are evaluated quarterly to determine whether the costs capitalized are impaired. The costs are impaired if the carrying value of the assets exceeds the sum of the undiscounted cash flows expected from the production of proved reserves and the lower of cost and market of unproved properties. If the carrying value is assessed as impaired, an impairment loss is recognized to the extent that the carrying value of assets exceeds the sum of the discounted cash flows expected from the production of proved and probable reserves and the lower of cost and market of unproved properties. The cash flows are estimated using expected future product prices and costs, discounted using a risk-free rate. Unproved properties are assessed for impairment when circumstances arise that indicate an unproved property is impaired such as expiration of lease rights or prolonged negative exploration activities. Impairments of unproved properties are transferred to the related full cost pool.

e) Asset Retirement Obligations

The Company recognizes the fair value of statutory, contractual or legal obligations associated with the retirement of assets in the period the asset is put to use, when a reasonable estimate of the fair value can be determined. A corresponding increase to the carrying amount of the related asset is recorded. The liability is accreted over time for changes in the fair value of the liability through charges to asset retirement accretion, which is included in depletion, depreciation and accretion expense. The costs capitalized to the related assets are amortized to earnings in a manner consistent with the depletion and depreciation of the underlying assets. Revisions to the estimated timing of cash flows or to the original estimated undiscounted costs result in an increase or decrease to the obligation. Actual costs incurred upon settlement of the retirement obligation are charged against the obligation to the extent of the liability recorded.

f) Revenue Recognition

Revenue is recognized when title passes to the customer and when collection is reasonably assured.

g) Stock-Based Compensation

The Company accounts for its stock-based compensation plans, as described in Note 7, using the fair value method. Under this method, compensation costs attributable to stock options granted to officers, directors and employees is measured at fair value at the grant date and expensed over the vesting period with a corresponding increase to contributed surplus. Compensation costs attributable to stock options granted to consultants are re-valued each reporting period and expensed over the vesting period with a corresponding increase to contributed surplus. Consideration paid upon the exercise of stock options, together with corresponding amounts previously recognized in contributed surplus, is recorded as an increase to share capital. Previously recognized compensation cost for forfeited options is reversed in the period of forfeiture.

The Company has a share appreciation rights (SARS) plan as described in note 7. Obligations for payments of cash under the SARS plan are accrued as compensation expense over the vesting period based on the positive

difference, if any, between the exercise price and the closing price of Pan Orient common shares on the TSX Venture Exchange. The accrued compensation for a right that is forfeited or cancelled is adjusted by decreasing compensation cost in the period of forfeiture.

h) Income Taxes

The Company follows the asset and liability method of accounting for income taxes. Under this method, income tax liabilities and assets are recognized for the estimated tax consequences attributable to differences between the amounts reported in the financial statements and their respective tax bases, using enacted or substantively enacted tax rates respective to the periods that the temporary differences are expected to reverse. The effect of a change in income tax rates on future income tax liabilities and assets is recognized in income in the period that the change occurs. Tax assets are recognized if they are more likely than not to be realized.

i) Per Share Amounts

Basic per share information is calculated on the basis of the weighted average number of common shares outstanding during the period. Diluted per share information is calculated using the treasury stock method which assumes that any proceeds received by the Company upon the exercise of in-the-money stock options, plus unamortized stock compensation costs, would be used to buy back common shares at the average market price for the period.

j) Foreign Currency Translation

The Company's foreign operations are considered to be self sustaining and are translated to Canadian dollars using average exchange rates for the revenue and expenses. Assets and liabilities are translated at the year end exchange rate and gains and losses resulting from these translations are included in accumulated other comprehensive income. As the parent company realizes its investment, the proportionate amount of translation gains and losses in accumulated other comprehensive income is transferred to the statement of operations and included in the foreign exchange gain (loss).

Transactions denominated in foreign currencies are translated into their Canadian dollar equivalents at exchange rates prevailing at the transaction dates. Carrying values of monetary assets and liabilities reflect the exchange rates at the balance sheet date. Gains and losses on translation or settlement are included in net income.

k) Measurement Uncertainty

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, revenues and expenses, and disclosure of contingent assets and liabilities at the date of the consolidated financial statements. Actual results could differ from those estimates.

The amounts recorded for depletion and depreciation of petroleum and natural gas interests and for asset retirement obligations are based on estimates of petroleum and natural gas reserves and future costs. Proved and probable reserves also provide the basis for determining whether the carrying value of petroleum and natural gas interests is impaired. The determination of stock-based compensation involves estimates of the volatility of the Company's common shares for future rates and expected life. Income tax expense is calculated using tax rates based on the estimated timing of reversal of temporary differences between accounting and tax values of certain assets and liabilities and involves forecasting the amount of the future income tax asset that will be realized. By their nature, these estimates are subject to measurement uncertainty and the impact on the financial statements of future periods could be material.

l) Financial Instruments

All financial assets, liabilities or non-financial derivatives are initially recognized on the balance sheet at fair value and must be classified as one of the following five categories: held-for-trading; held-to-maturity instruments; loans and receivables; available-for-sale financial assets; or other financial liabilities. Loans and receivables, held-to-maturity instruments and other financial liabilities are subsequently measured at amortized cost. Held-for-trading financial assets are measured at fair value with changes in fair value recognized in earnings. Available-for-sale financial assets are measured at fair value with changes in fair value recognized in comprehensive income and reclassified to earnings when derecognized or impaired.

The Company has classified cash and cash equivalents as held-for-trading and accounts receivable, deposits and accounts payable and accrued liabilities are classified as other liabilities and receivables.

m) Accounting Policies Adopted During 2008

Capital Disclosures

Effective January 1, 2008 the Company adopted Section 1535, Capital Disclosures, which requires companies to disclose their objectives, policies and processes for managing capital. See note 8 for disclosure regarding the Company's capital structure.

Financial Instruments Disclosure and Presentation

On January 1, 2008 the Company adopted Section 3862, Financial Instruments – Disclosures and Section 3863 Financial Instruments – Presentation. These disclosure standards were adopted prospectively by the Company and require entities to provide information that enable users to evaluate: 1) the significance of financial instruments for the entity's financial position and performance; and 2) the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the balance sheet date; and 3) how the entity manages its risks. These disclosures are provided in note 10.

International Financial Reporting Standards

Public companies will have to convert from Canadian GAAP to International Financial Reporting Standards (IFRS) beginning on or after January 1, 2011. This transition may materially affect the Company's reported financial position and results of operations although currently the Company cannot reasonably estimate the effect on the financial statements.

3) ACQUISITION ACTIVITIES

a) Indonesia

During 2008 the Company acquired all of the issued and outstanding shares of three privately-held companies with interests in Indonesia. These entities hold a 90% operated working interest in the Batu Gajah Production Sharing Contract (PSC) located onshore south Sumatra, a 69% operated working interest in the Citarum PSC located onshore West Java and a 90% operated interest in a joint study located onshore Sumatra, which subsequently became the South CPP PSC. The allocation of the purchase price is as follows:

PAN ORIENT ENERGY CORP.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(\$000s)

Consideration:

Cash	14,741
Common shares	4,124
Transaction costs	1,115
	<u>19,980</u>

Allocated as follows:

Petroleum and natural gas properties	20,180
Working capital, including cash of \$0.7 million	264
Asset retirement obligations	(464)
	<u>19,980</u>

The purchase is reported in the consolidated statement of cash flows as \$15.1 million which represents the cash acquisition cost of \$14.7 million plus transaction costs of \$1.1 million less cash acquired of \$0.7 million.

b) Andora Acquisition of Signet

On September 19, 2007, the Company's subsidiary, Andora, acquired Signet Energy Inc. ("Signet"). Signet was a private oil and gas company holding heavy oil interests in Sawn Lake, Alberta. The combination was effected by way of a plan of arrangement under the Business Corporations Act (Alberta) whereby the security holders of Signet received, in aggregate, 10,741,128 common shares of Andora with an estimated value of \$17.2 million. Certain shareholders of Signet exercised their right to dissent to the combination, and as such Andora recorded a liability of \$3.7 million. In addition to Signet's heavy oil interests, Andora received Signet's working capital, comprised mainly of cash, of \$3.1 million.

In connection with the transaction, Andora also issued 310,000 share purchase warrants, to an existing third party Signet warrant holder, with an exercise price of \$2.86 per Andora share, expiring November 17, 2008. The estimated fair value of these warrants was not significant on the combination date.

Following the combination described above, Pan Orient owned approximately 53.5% of the issued and outstanding common shares of Andora.

The acquisition was accounted for as follows:

(\$000s)

Consideration:

Shares issued by Andora	\$	17,186
Consideration payable for Signet shares		3,717
Acquisition costs		433
	\$	<u>21,336</u>

Allocated as follows:

Petroleum and natural gas properties	\$	22,009
Working capital, including cash of \$3.1 million		3,054
Future income tax		(3,663)
Asset retirement obligation		(64)
	\$	<u>21,336</u>

PAN ORIENT ENERGY CORP.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

In addition to the \$22.0 million increase in petroleum and natural gas properties above, the dilution of Pan Orient's holdings in Andora, from 67% to 53.5%, resulted in a decrease in petroleum and natural gas properties of \$8.8 million (net \$13.2 million increase), and a decrease in the future income tax liability of \$2.6 million. Non-controlling interest also increased by \$10.9 million.

On December 30, 2007 Pan Orient exercised its 2.25 million warrants to acquire common shares of Andora for \$3.6 million. As a result, Pan Orient owned 55.4% of the issued and outstanding common shares of Andora. The exercise of the warrants, which increased Pan Orient's ownership of Andora by approximately 1.9%, resulted in a decrease in non-controlling interest of \$0.9 million, a decrease in future taxes of \$0.3 million and a decrease in petroleum and natural gas properties of \$1.3 million.

4) DEPOSITS

The Company has cash deposits relating to: 1) guarantees to the Thailand and Indonesia governments for the Company's work commitments; and 2) customs importation permits in Thailand.

5) PETROLEUM AND NATURAL GAS PROPERTIES

(\$000s)	Cost	Accumulated Depreciation and Amortization	Net Book Value
As at December 31, 2008			
Oil and natural gas			
Canada	55,075	-	55,075
Thailand	81,765	(23,303)	58,462
Indonesia	28,504	-	28,504
Office	1,491	(709)	782
	166,835	(24,012)	142,823
As at December 31, 2007			
Oil and natural gas			
Canada	56,182	-	56,182
Thailand	37,336	(5,284)	32,052
India	395	-	395
Office	679	(368)	311
	94,592	(5,652)	88,940

General and administrative and stock-based compensation expenses totaling \$0.5 million (2007 - \$0.8 million) that were directly related to exploration and development activities have been capitalized for the year ended December 31, 2008.

Costs associated with unproved properties of \$13.8 million (2007 - \$11.2 million) with respect to the Thai full cost pool have been excluded from the depletion calculation. The capitalized costs associated with Canada and Indonesia are not subject to depletion as production has not commenced.

PAN ORIENT ENERGY CORP.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

The Company was not successful in its bid for various oil and gas concessions in India. As a result, capitalized costs of \$0.7 million pertaining to India were expensed in the year and included in foreign new venture expenditures.

The Company performed a ceiling test calculation at December 31, 2008 to assess any impairment of petroleum and natural gas interests in Thailand. Based on the assumptions in the calculation there was no impairment at December 31, 2008. The benchmark prices used in the ceiling test calculation were as follows:

	WTI Oil (\$US/bbl)	\$US/\$CAD Exchange Rate	WTI Oil (\$CAD/bbl)
2009:	60.00	1.18	70.59
2010:	71.40	1.18	84.00
2011:	83.20	1.11	92.44
2012:	90.20	1.05	94.95
2013:	97.40	1.00	97.40
2014:	99.40	1.00	99.40
Thereafter:	Escalated at 2% per annum	1.00	Escalated at 2% per annum

The carrying value of the Company's unproved Canadian and Indonesian properties are expected to be recoverable and as such no writedown has been recorded.

During the year Andora settled a \$3.7 million account payable related to certain dissenting shareholders from the Signet acquisition, that was outstanding at December 31, 2007 (see note 3). In lieu of a cash settlement Andora issued 2.2 million common shares which diluted Pan Orient's interest from 55.4% to 53.2%. The transaction resulted in a decrease in accounts payable of \$3.7 million, a decrease in petroleum and natural gas properties of \$3.6 million, a decrease in the future income tax liability of \$0.9 million and an increase in non-controlling interest of \$1.0 million.

6) ASSET RETIREMENT OBLIGATIONS

<i>(\$000s)</i>	Year Ended December 31	
	2008	2007
Asset retirement obligations, beginning of year	84	20
Obligations acquired	464	64
Obligations incurred	616	-
Revisions to obligations	791	-
Accretion	9	-
Asset retirement obligations, end of year	1,964	84

Asset retirement obligations are based on the Company's net ownership of wells and facilities in Thailand, Indonesia and Canada, management's estimates of costs to abandon and reclaim those wells and facilities and the potential future timing of the costs to be incurred.

PAN ORIENT ENERGY CORP.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Total undiscounted cash flows, escalated at 2.0%, required to settle the Company's asset retirement obligations are estimated to be \$6.2 million (2007 - \$0.1 million). Payments to settle these obligations will occur over the operating lives of the underlying assets estimated, for the majority of wells, to be between 2020 to 2025. Estimated costs have been discounted at Pan Orient's credit-adjusted, risk-free interest rate of 10%.

7) SHARE CAPITAL

a) Authorized

Unlimited Class A and B Common Voting Shares
 Unlimited Class C Common Non Voting Shares
 Unlimited Preferred Shares

b) Issued and outstanding Class A common shares

	Number of Shares	Amount (000s)
Balance as at January 1, 2007	40,056,842	\$ 61,963
Issued for cash	5,000,000	38,400
Less: Share issue costs	-	(2,464)
Underwriters compensation options exercised	162,000	655
Reclassification upon exercise of underwriters compensation options	-	246
Balance as at December 31, 2007	45,218,842	98,800
Indonesia acquisition	378,324	4,124
Exercise of stock options	94,600	115
Underwriters compensation options exercised	78,000	433
Repurchase of shares	(201,400)	(455)
Transfer from contributed surplus	-	61
Balance as at December 31, 2008	45,568,366	\$ 103,078

On June 18, 2008 the Company issued 378,324 shares to partially satisfy the purchase price of its Indonesian acquisition (see note 3).

On August 6, 2008 the Company announced that the TSX Venture Exchange approved a share repurchase program through a normal course issuer bid (NCIB) the terms of which permit Pan Orient to purchase up to 2,288,488 (5%) of its issued and outstanding common shares prior to August 10, 2009.

A total of 201,400 common shares were acquired to December 31, 2008 at prices ranging from \$3.80 to \$8.00 per share. Shares purchased pursuant to the NCIB were cancelled and returned to treasury. As the consideration paid exceeded the stated value of the shares, the amount of excess totaling \$0.6 million was recorded as a reduction to retained earnings.

PAN ORIENT ENERGY CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In connection with an offering completed in 2006, the Company issued 240,000 underwriters compensation options that were exercisable into common shares at \$4.04 per share at any time prior to April 28, 2008. During the year ended December 31, 2008, 78,000 (2007 - 162,000) underwriters compensation options were exercised for common shares of the Company.

On July 13, 2007, the Company issued, by way of a non-brokered private placement, 1.5 million common shares at \$4.25 per share, for gross proceeds of \$6.4 million (\$6.0 million net of finders fee and other costs paid).

On November 14, 2007, the Company issued by way of a brokered private placement, 3.5 million common shares at \$9.15 per share for gross proceeds of \$32.1 million (\$29.9 million net of commission and other costs paid).

c) Options to purchase common shares

	2008		2007	
	Number of Options	Weighted Average Exercise Price (\$)	Number of Options	Weighted Average Exercise Price (\$)
Balance, beginning of year	4,512,150	3.36	3,793,150	1.77
Granted	110,000	8.45	759,000	11.29
Exercised	(94,600)	1.22	-	-
Forfeited	(86,050)	2.88	(40,000)	3.00
Balance, end of year	4,441,500	3.54	4,512,150	3.36

Exercise Price(\$)	Options Outstanding			Options Exercisable		
	Number of Options	Weighted Average Remaining Contractual Life (years)	Weighted Average Exercise Price(\$)	Number of Options	Weighted Average Remaining Contractual Life (years)	Weighted Average Exercise Price(\$)
0.75	2,217,334	1.29	0.75	2,217,334	1.29	0.75
1.80 - 2.08	66,666	1.91	1.80	66,666	1.91	1.80
2.75 - 3.90	1,368,500	2.46	3.44	1,266,835	2.38	3.45
11.00 - 11.75	789,000	4.00	11.68	377,000	3.98	11.72
0.75 - 11.75	4,441,500	2.14	3.54	3,927,835	1.91	2.69

PAN ORIENT ENERGY CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

d) Stock-based compensation

A Black-Scholes option pricing model is used to estimate the fair value of options on the date of the grant and revalue stock options granted to consultants on a quarterly basis. The fair value of the stock based compensation is amortized over the vesting period of the options, generally being two to three years. Weighted average assumptions and resultant fair values for stock options granted or revalued during the year ended December 31, 2008 were as follows:

	Year Ended December 31	
	2008	2007
Risk free interest rate (%)	3.3	4.5
Expected lives (years)	3	5
Expected volatility (%)	75	65
Dividend per share (%)	-	-
Weighted average fair value (\$)	3.10	6.56

e) Options to purchase common shares of Andora

In the current year 1,150,000 Andora stock options were granted, 775,000 of which vested upon grant, with the remainder vesting over 3 years. Each of these options has an exercise price of \$1.60 and an expiry of five years from the date of grant. Of the 4,900,000 options outstanding 3,750,000 were granted in 2006. The following table provides Andora's stock options outstanding and exercisable at December 31, 2008:

Exercise Price (\$)	Number of Options	Options Outstanding		Number of Options	Options Exercisable	
		Weighted Average of Remaining Contractual Life (years)	Weighted Average Exercise Price (\$)		Weighted Average Remaining Contractual Life (years)	Weighted Average Exercise Price (\$)
1.35	3,750,000	0.90	1.35	3,750,000	0.90	1.35
1.60	1,150,000	2.40	1.60	775,000	2.24	1.60
1.35-1.60	4,900,000	1.41	1.25	4,525,000	1.13	1.39

Weighted average assumptions and resultant fair values used in the Black Scholes calculations for Andora stock options granted during the year ended December 31 were as follows:

	Year Ended December 31	
	2008	2007
Risk free interest rate (%)	3.10	-
Expected lives (years)	3	-
Expected volatility (%)	20	-
Dividend per share (%)	-	-
Weighted average fair value (\$)	0.29	-

PAN ORIENT ENERGY CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

f) Contributed surplus

(\$000s)	Year Ended December 31	
	2008	2007
Balance, beginning of year	5,671	2,456
Pan Orient stock-based compensation expense	463	2,301
Andora stock-based compensation expense	112	300
Pan Orient stock-based compensation capitalized	250	474
Andora stock-based compensation capitalized	96	140
Transferred to share capital on exercise of options	(61)	-
Balance at end of year	6,531	5,671

Capitalized stock-based compensation relates to options granted to individuals engaged in exploration and development activities. The future income tax liability increased by \$0.1 million (2007 - \$0.2 million) as a result of capitalization of these costs.

g) Share appreciation rights plan

During 2008 a share appreciation rights (SARs) plan was approved by the Board of Directors. Each right entitles the participant to receive cash from the Company an amount equal to the positive difference, if any, between the exercise price and the closing price of Pan Orient common shares on the TSX Venture Exchange on the date of exercise.

At December 31, 2008, 55,000 SARs, with an exercise price of \$4.00, were outstanding and exercisable with an expiry of October 20, 2013. For the year ended December 31, 2008, no compensation cost has been recorded for these SARs as the exercise price exceeds the closing price at the end of the reporting period.

h) Accumulated other comprehensive income (loss)

(\$000s)	Year Ended December 31	
	2008	2007
Balance at beginning of year	(1,722)	-
Unrealized gain (loss) on foreign currency translation	9,561	(1,292)
Foreign exchange gain realized	(3,802)	(430)
Balance at end of year	4,037	(1,722)

PAN ORIENT ENERGY CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

i) Income per share

The number of shares used in basic and diluted net income per share calculations are as follows:

	Year Ended December 31	
	<u>2008</u>	<u>2007</u>
Weighted average basic shares outstanding	45,495,486	41,268,767
Dilutive effect of stock options	3,431,674	1,216,122
Weighted average diluted	<u>48,927,160</u>	<u>42,484,889</u>

With respect to the dilutive effect of stock options, in the current year 789,000 (2007 - 719,000) stock options were excluded from the calculation as they were out-of-the-money.

8) CAPITAL MANAGEMENT

Pan Orient's primary objective for managing its capital structure is to maintain financial capacity for the purpose of sustaining the future development of the business and maintaining investor, creditor and market confidence.

The Company considers its capital structure to include shareholders' equity and working capital. Management is continually monitoring changes in economic conditions and the risk characteristics of the underlying petroleum and natural gas industry. The Company currently has sufficient cash on hand to carry out its planned activities however, in the event that adjustments to the capital structure are necessary, the Company may consider issuing additional equity, raising debt or revising its capital investment programs.

Pan Orient's share capital is not subject to any external restrictions. The Company has not paid or declared any dividends since the date of incorporation, nor are any currently contemplated. There were no changes to the Company's approach to capital management during the year.

9) INCOME TAXES AND SPECIAL REMUNERATORY BENEFIT

The Company is required to pay both Special Remuneratory Benefit (SRB) and income tax in Thailand. Thai income tax is calculated at 50% of taxable income which is basically comprised of cash flow from operations before changes in working capital less capital expenditures and other permitted deductions.

SRB is calculated separately for each of the Company's four concessions and is not charged until all capital has been recovered. The sliding scale SRB rate ranges from 0 - 75% and is principally driven by production and pricing but is also subject to other adjustments such as changes in Thailand's consumer price index, wholesale price index and cumulative meters drilled on the concession. The calculated rate is applied to petroleum profits as defined in Thai tax legislation which includes a deduction for capital spent.

PAN ORIENT ENERGY CORP.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

The future income tax provision reflects an effective rate which differs from the expected statutory tax rate of a Canadian entity of 29.5% (2007 - 32.1%). Differences were accounted for as follows:

(\$000s)	Year Ended December 31	
	2008	2007
Income before income taxes and non-controlling interest	111,506	8,327
Expected income taxes at the statutory rate	32,894	2,673
Increase (decrease) resulting from:		
Non-deductible stock-based compensation	170	650
Special remuneratory benefit tax	35,489	-
Income taxes in jurisdictions with different rates	11,457	2,417
Effect of tax rate reduction	-	(1,295)
Change in valuation allowance and other	(29)	(1,272)
Income taxes	79,981	3,173

The components of the net future income tax liability as at December 31 are as follows:

	2008	2007
Operating losses (expire up to 2028)	(4,744)	(4,029)
Petroleum and natural gas properties	23,969	11,510
Share issue costs	(1,161)	(1,161)
Valuation allowance	4,634	1,401
	22,698	7,721

10) FINANCIAL INSTRUMENTS**Overview**

The nature of Pan Orient's operations expose the Company to credit risk, liquidity risk and market risk, and changes in commodity prices, foreign exchange rates and interest rates may have a material effect on cash flows, net income and comprehensive income.

This note provides information about the Company's exposure to each of the above risks as well as the Company's objectives, policies and processes for measuring and managing these risks.

Pan Orient's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and to monitor market conditions and the Company's activities. The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework and policies.

Credit Risk

Credit risk is the risk of financial loss to the Company if counterparties do not fulfill their contractual obligations. The most significant exposure to this risk is relative to the sale of oil production; all of the Company's production is sold to a refinery owned by the Thai National Oil Company. Pan Orient is paid for its production on a monthly basis, typically within a week of the end of the month. The Company has assessed the risk of non-collection from the Thai government as minimal. As at December 31, 2008 the Company's accounts receivable from the Thai government was \$9.5 million which was collected subsequent to December 31, 2008.

Cash and cash equivalents consist of cash bank balances and short-term deposits maturing in less than 90 days. The Company's short-term investments are held with a chartered bank or the Thai government and are monitored to ensure a stable return. The Company's short-term investments currently consist of term deposits, bankers acceptances and government bonds and it is not the Company's policy to utilize complex, higher-risk investment vehicles.

The carrying amount of accounts receivable and cash and cash equivalents represents the maximum credit exposure. The Company did not have an allowance for doubtful accounts at December 31, 2008 and did not write-off any receivables during the years ended December 31, 2008 or 2007.

As at December 31, 2008 there were no significant amounts past due or impaired.

Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its work commitments and other financial obligations as they are due. Pan Orient's approach to managing liquidity is to ensure, to the extent possible, that it will have sufficient liquidity to meet its liabilities when due without incurring unacceptable losses or risking harm to the Company's reputation.

The Company's liquidity is dependent upon its operating cash flows. To forecast and monitor liquidity the Company prepares annual operating and capital expenditure budgets in each country which are monitored and updated as considered necessary. Expected future cash flow from the Thailand properties currently exceeds operating and future capital expenditures. Considering these circumstances and the cash balance at December 31, 2008 of \$98.9 million, the Company's liquidity risk is assessed as low.

The Company's only reported financial liabilities are accounts payable and accrued liabilities of \$14.7 million which will mature within one year. Taxes payable of \$55.3 million are not considered a financial instrument however, this amount is significant and Pan Orient is obligated to remit the reported amount by May 31, 2009.

The Company has work commitments in Thailand and Indonesia (see note 11) which are expected to be funded through cash balances and deposits currently held and expected future cash flow from Thailand properties.

PAN ORIENT ENERGY CORP.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****Market Risk**

Market risk is the risk that changes in foreign exchange rates, commodity prices and interest rates will affect the Company's cash flows, net income and comprehensive income. The objective of market risk management is to manage and control market risk exposures within acceptable limits, while maximizing returns.

Foreign Currency Exchange Rate Risk

Foreign currency exchange rate risk is the risk that future cash flows, net income and comprehensive income will fluctuate as a result of changes in foreign exchange rates. All of the Company's petroleum sales are denominated in Thai baht based on a \$USD oil price, and all operational and capital activities related to the Thailand properties are transacted in either Thai baht or the U.S. dollar. As well, the underlying market prices in Thailand for petroleum are impacted by changes in the exchange rate between the Thai baht and U.S. dollar.

The work commitments in Indonesia are expected to be carried out in U.S. dollars.

Changes in foreign exchange rates between the Canadian dollar and the U.S. dollar and Thai baht can affect net income and other comprehensive income as a portion of the Company's operations is considered a self-sustaining foreign operation. As at December 31, 2008 the following financial instruments were denominated in currencies other than the Canadian dollar:

	Thai Baht (000s of Thai Baht)	U.S. Dollar (\$000s USD)
Cash and cash equivalents	2,239,756	7,675
Accounts receivable	305,993	1,753
Deposits	44,000	2,250
Accounts payable	(1,777,251)	(5,886)
Taxes payable	(1,570,818)	-
Net exposure	(758,320)	5,792
Net exposure in CDN dollars⁽¹⁾ (\$000s)	(26,677)	7,082
Effect of a \$0.02 change in CDN \$ to USD (000s CDN \$):		
Pre-tax net income		83
Other comprehensive income		33
Effect of a 1.0 baht change in baht to CDN \$ (000s CDN \$):		
Other comprehensive income	971	

(1) Translated at December 31, 2008 exchange rate of US \$1 = CAD \$1.223.

The Company did not have any forward exchange contracts in place as at or during the year ended December 31, 2008.

PAN ORIENT ENERGY CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Commodity Price Risk

Commodity price risk is the risk that future cash flows will fluctuate as a result of changes in commodity prices, affecting results of operations and cash generated from operating activities. Such prices may also affect the value of exploration and development properties and level of spending for future activities. Prices received by the Company for its production are largely beyond Pan Orient's control as petroleum prices are impacted by world economic events that dictate the levels of supply and demand. All of Pan Orient's oil production is sold at spot rates exposing the Company to the risk of price movements.

The Company did not have any commodity price contracts in place as at or during the year ended December 31, 2008.

Interest Rate Risk

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The Company is exposed to interest rate fluctuations on its cash and cash equivalents which bear a floating rate of interest.

The Company did not have any interest rate swaps or financial contracts in place as at or during the year ended December 31, 2008. For the year ended December 31, 2008, a difference in the interest rate of 1.0% would change net income before tax by an estimated \$0.7 million, assuming all other variables are constant.

Fair Value of Financial Instruments

The Company's financial instruments as at December 31, 2008 included cash and cash equivalents, accounts receivable, deposits and accounts payable and accrued liabilities. The fair value of these financial instruments, except for the deposits, approximate their carrying amounts due to their short terms to maturity. The fair value of the deposits approximate their carrying value as they bear interest at market rates.

The Company will assess at each reporting period whether financial assets, other than those classified as held-for-trading, are impaired. Any impairment loss will be included in net income for the period.

PAN ORIENT ENERGY CORP.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****11) COMMITMENTS AND CONTINGENCIES**

As at December 31, 2008 the Company's outstanding capital commitments were as follows:

Country and Concession Name	Work Program Commitment	Obligation Period Ending	Net Financial Commitment	
			(USD \$000s)	(CAD \$000s) ⁽¹⁾
Thailand				
L 53/48	Geological studies, drill 2 wells	January 2013	780	954
L 44/43	Study and training fund	July 2009	24	29
Indonesia				
Batu Gajah	500 kilometres of 2D seismic, 400 km ² of 3D seismic and drill 3 exploration wells	January 2010	32,952	40,294
Citarum	1,250 kilometres of 2D seismic, drill 1 exploration well	October 2009	20,456	25,014
South CPP	200 kilometres 2D seismic reprocessing, 1 exploration well	November 2011	5,050	6,175
Total			59,262	72,466

(1) Translated at December 31, 2008 exchange rate of US \$1 = CAD \$1.223.

Indonesia financial commitments only include the current exploration phase that the Company is conducting. If Pan Orient exercises its options to continue beyond the obligation periods noted above, additional commitments will be determined on a year by year basis through submission of a work program and approval from the Indonesian government.

A 750 km 2D Seismic program is currently underway on Citarum and all seismic operations are anticipated to be completed by the end of 2009 with drilling anticipated in the second quarter of 2010.

Batu Gajah 2D seismic operations are planned to commence by the end of the second quarter of 2009. It is anticipated this program will be completed late in the third quarter of 2009 with the drilling of up to 3 wells to commence in the first quarter of 2010.

The intended timing of these capital activities does not always fall within the "obligation period ending" in the table above. Each year the Company submits a work program for each PSC to the Government of Indonesia (GOI) and along with it, a request to roll forward any incomplete commitments from the previous year. The above obligation periods for the Citarum and Batu Gajah operations represent the most recently-approved work programs for 2009 pursuant to this practice. Although in the past, such requests on behalf of Pan Orient have been approved by the GOI, and management has no reason to believe that they will not be in the future, there is no guarantee that the GOI will approve future requests.

PAN ORIENT ENERGY CORP.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

The Company is committed to future minimum payments for office space in Thailand, Indonesia and Canada. Payments required under these commitments for each of the next five years are as follows:

(\$000s)				
Year	Thailand	Indonesia	Canada	Total
2009	59	51	198	308
2010	-	58	201	259
2011	-	5	201	206
2012	-	-	205	205
2013	-	-	171	171
Thereafter	-	-	-	-
Total	59	114	976	1,149

As a result of an acquisition completed by Andora, a lawsuit was assumed, the likely outcome and potential costs of which are both indeterminable. Management believes the lawsuit has a low probability of success.

12) SEGMENTED INFORMATION

The Company has oil and gas properties in three geographical locations being conventional oil and gas properties in Thailand and Indonesia and a heavy oil property in Canada.

As at and for the year ended December 31 (\$000s)

2008	Thailand	Indonesia	Canada	Total
Revenue	148,060	-	485	148,545
Net Income (loss)	33,062	(490)	(821)	31,751
Depletion, depreciation and accretion	18,142	32	195	18,369
Total assets	147,388	36,967	74,853	259,208
Capital expenditures for the year	31,319	7,345	1,827	40,491
2007	Thailand	Indonesia	Canada	Total
Revenue	24,067	-	541	24,608
Net Income (loss)	8,780	-	(3,937)	4,843
Depletion, depreciation and accretion	4,535	-	170	4,705
Total assets	45,503	-	96,967	142,470
Capital expenditures for the year	21,164	-	1,062	22,226



PAN ORIENT ENERGY CORP.

1505, 505 - 3rd Street SW, Calgary Alberta Canada T2P 3E6