



**PAN ORIENT ENERGY CORP.**

**2007 CONSOLIDATED FINANCIAL STATEMENTS**

FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006

## **MANAGEMENT'S REPORT TO THE SHAREHOLDERS**

Management is responsible for the integrity and objectivity of the financial statements. 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

( *signed "Jason Bednar"* )

**Jason Bednar**

Vice President, Finance & Chief Financial Officer

April 30, 2008

## AUDITORS' REPORT TO THE SHAREHOLDERS

We have audited the consolidated balance sheets of Pan Orient Energy Corp. as at December 31, 2007 and 2006 and the consolidated statements of operations and retained earnings (deficit), 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, 2007 and 2006 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 30, 2008

**PAN ORIENT ENERGY CORP.**  
**CONSOLIDATED BALANCE SHEETS**

	December 31 2007	December 31 2006
<b><u>ASSETS</u></b>		
<b>CURRENT</b>		
Cash and cash equivalents	\$ 36,852,216	\$ 16,121,554
Accounts receivable	14,500,981	2,925,414
	<hr/> 51,353,197	19,046,968
Deposits (Note 3)	2,176,798	1,144,188
Petroleum and natural gas properties (Note 6)	88,940,081	58,652,742
	<hr/> \$ 142,470,076	\$ 78,843,898
<b><u>LIABILITIES</u></b>		
<b>CURRENT</b>		
Accounts payable and accrued liabilities	\$ 12,767,447	\$ 1,952,070
Future income tax	7,721,130	8,192,052
Asset retirement obligation (Note 7)	83,601	20,001
	<hr/> 20,572,178	10,164,123
Non-controlling interest (Notes 4 and 5)	18,018,350	7,726,888
<b><u>SHAREHOLDERS' EQUITY</u></b>		
SHARE CAPITAL (Note 8)	98,799,973	61,962,901
UNDERWRITERS COMPENSATION OPTIONS (Note 8)	118,820	365,000
CONTRIBUTED SURPLUS	5,670,825	2,456,194
ACCUMULATED OTHER COMPREHENSIVE LOSS (Note 8)	(1,722,221)	-
RETAINED EARNINGS (DEFICIT)	1,012,151	(3,831,208)
	<hr/> (710,070)	(3,831,208)
	<hr/> 103,879,548	60,952,887
Commitments and Contingencies (Note 11)	\$ 142,470,076	\$ 78,843,898

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 (DEFICIT)**

	Year Ended December 31 2007	Year Ended December 31 2006
<b>REVENUES</b>		
Oil	\$ 24,033,578	\$ 1,256,447
Royalties	(1,556,697)	(179,280)
Interest	574,563	704,827
	23,051,444	1,781,994
<b>EXPENSES</b>		
Depletion, depreciation and accretion	4,704,925	843,863
General and administrative	3,164,316	1,743,260
Stock based compensation (Note 8)	2,601,325	1,773,121
Production and operating	2,024,265	779,121
Foreign exchange loss (gain)	1,325,627	(141,125)
Transportation costs	864,024	45,085
Foreign new ventures expenditures	40,000	126,297
	14,724,482	5,169,622
<b>INCOME (LOSS) BEFORE TAXES AND NON-CONTROLLING INTEREST</b>	<b>8,326,962</b>	<b>(3,387,628)</b>
Income taxes (Note 9)		
Future tax reduction	1,472,967	1,072,000
Current	(4,645,510)	-
<b>INCOME (LOSS) BEFORE NON-CONTROLLING INTEREST</b>	<b>5,154,419</b>	<b>(2,315,628)</b>
<b>NON-CONTROLLING INTEREST</b>	<b>(311,060)</b>	<b>29,139</b>
<b>NET INCOME (LOSS) FOR THE YEAR</b>	<b>4,843,359</b>	<b>(2,286,489)</b>
<b>DEFICIT, BEGINNING OF YEAR</b>	<b>(3,831,208)</b>	<b>(1,544,719)</b>
<b>RETAINED EARNINGS (DEFICIT) END OF YEAR</b>	<b>\$ 1,012,151</b>	<b>\$ (3,831,208)</b>
<b>INCOME (LOSS) PER SHARE – Basic</b>	<b>\$ 0.12</b>	<b>\$ (0.07)</b>
– Diluted	<b>0.11</b>	<b>(0.07)</b>

See accompanying notes to the consolidated financial statements

**PAN ORIENT ENERGY CORP.**

**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

	Year Ended December 31 2007	Year Ended December 31 2006
Net Income (loss)	\$ 4,843,359	\$ (2,286,489)
Unrealized loss recorded on translation of assets and liabilities of self-sustaining operations denominated in foreign currency	(430,530)	-
Comprehensive income	<u>\$ 4,412,829</u>	<u>\$ (2,286,489)</u>

**PAN ORIENT ENERGY CORP.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

	Year Ended December 31 2007	Year Ended December 31 2006
<b>CASH PROVIDED BY (USED IN)</b>		
<b>OPERATING ACTIVITIES</b>		
Net income (loss) for the year	\$ 4,843,359	\$ (2,286,489)
Items not affecting cash		
Stock based compensation	2,601,325	1,773,121
Future income tax reduction	(1,472,967)	(1,072,000)
Depletion, depreciation and accretion	4,704,925	843,863
Unrealized foreign exchange loss (gain)	865,627	(141,125)
Non-controlling interest	311,060	(29,139)
	<u>11,853,329</u>	<u>(911,769)</u>
Change in non-cash working capital	(10,095,136)	(212,781)
	<u>1,758,193</u>	<u>(1,124,550)</u>
<b>INVESTING ACTIVITIES</b>		
Acquisition of Andora	2,644,123	(8,846,947)
Deposits	(1,132,610)	(1,144,188)
Petroleum and natural gas properties	(22,226,211)	(11,344,224)
Change in non-cash working capital	3,607,275	1,915,378
	<u>(17,107,423)</u>	<u>(19,419,981)</u>
<b>FINANCING ACTIVITIES</b>		
Issue of common shares net of share issue cost	36,590,892	28,050,058
Convertible debentures	-	(86,162)
	<u>36,590,892</u>	<u>27,963,896</u>
<b>INCREASE (DECREASE) IN CASH</b>	<b>21,241,662</b>	<b>7,419,365</b>
<b>EFFECT OF FOREIGN EXCHANGE ON CASH BALANCES</b>	<b>(511,000)</b>	<b>-</b>
<b>CASH, BEGINNING OF YEAR</b>	<b>16,121,554</b>	<b>8,702,189</b>
<b>CASH, END OF YEAR</b>	<b>\$ 36,852,216</b>	<b>\$ 16,121,554</b>

See accompanying notes to the consolidated financial statements

**PAN ORIENT ENERGY CORP.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**1) BASIS OF PRESENTATION**

Pan Orient Energy Corp. ("Pan Orient" or the "Company"), is an oil and natural gas company based in Calgary, Alberta, which holds properties onshore Thailand and interests in subsidiaries with properties in Northern Alberta. In addition, the Company is pursuing other oil and natural gas exploration acreage in Asia.

**2) SIGNIFICANT ACCOUNTING POLICIES**

**(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 55.4% (2006 - 67%) owned by Pan Orient.

Pan Orient's financial statements record a non-controlling interest representing the 44.6% ( 2006 - 33%) portion of assets and liabilities not owned by Pan Orient.

**(B) Cash And Cash Equivalents**

Cash and cash equivalents consist of balances with banks and investments in highly liquid short-term deposits with an original maturity date of less than ninety days.

**(C) 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 country-by-country cost centres. Such costs include royalty acquisition, land acquisition, geological and geophysical, carrying charges of non producing wells and general administrative costs.

Costs associated with the investigating, bidding and acquiring petroleum properties are expensed prior to obtaining a petroleum lease or concession. Costs may be 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.

Gains or losses are not recognized upon disposition of oil and gas properties unless crediting the proceeds against accumulated costs would result in a change in the rate of depletion of 20% or more.

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. For purposes of the depletion calculation, gross proved oil and gas reserves, as determined by engineering consultants, are used and converted to a common unit of measure based on their approximate energy content of six thousand cubic feet of natural gas to one barrel of crude oil.

The costs in cost centres from which there has been no commercial production are periodically assessed to determine whether it is likely such costs will be recovered in the future. To the extent there are costs which are not likely to be recovered in the future, they are written off. Petroleum and natural gas properties, for which there has been commercial production, are subject to a ceiling test in each reporting period to determine that the costs are recoverable and do not exceed the fair value of the properties. The costs are assessed to be recoverable if the sum of the undiscounted cash flows expected from the production of proved reserves and the lower of cost and market of unproved properties exceed the carrying values of the petroleum and natural gas properties. If the carrying value of the petroleum and natural gas properties is not assessed to be recoverable, an impairment loss is recognized to the extent that the carrying value exceeds an estimated fair value. The fair value estimate is normally based on 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 forecast product prices and costs and are discounted using a risk-free interest rate.



**PAN ORIENT ENERGY CORP.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(D) Asset Retirement Obligations**

The Company recognizes the fair value of obligations associated with the retirement of long-lived assets in the period the asset is put to use, with the corresponding increase to the carrying amount of the related asset. The obligations recognized are statutory, contractual or legal obligations. 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, amortization and accretion expense. The costs capitalized to the related assets are amortized to earnings in a manner consistent with the depreciation and amortization of the underlying assets. Revisions to the estimated timing of cash flows or to the original estimated undiscounted costs could also 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.

**(E) Joint Operations**

The Company conducts substantially all its oil and gas exploration and production activities with others. The financial statements reflect only the Company's interest in such activities.

**(F) Income Taxes**

The Company follows the asset and liability method of accounting for income taxes. Under this method, temporary differences arising from the tax basis of an asset or liability and its carrying amount on the balance sheet are used to calculate future income tax liabilities or assets. Future income tax liabilities or assets are calculated using substantively enacted tax rates anticipated to apply in the periods that the temporary differences are expected to reverse. Tax assets are recognized if they are more likely than not to be realized.

**(G) Estimates**

The balance sheet is prepared in accordance with Canadian generally accepted accounting principles. Management makes estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the balance sheet. By their nature, these estimates are subject to measurement uncertainty and the effect on the balance sheet of changes in such estimates in future periods could be significant. These estimates are primarily related to cost recovery tests and ceiling tests which are based upon estimates of market values of unproven properties, proven and probable reserves, petroleum prices, future costs and other assumptions.

**(H) Foreign Currency Translation**

Prior to October 1, 2007, the Company's foreign operations were considered to be integrated and were translated to Canadian dollars using average exchange rates for the year for revenue and expenses. Monetary assets and liabilities were translated at the year-end current exchange rate and non-monetary assets and liabilities were translated using historical rates of exchange. Gains or losses resulting from these translation adjustments were included in net income. Effective October 1, 2007, 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. Gains and losses resulting from these translations are included in other comprehensive income.

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.

**(I) Stock Base Compensation**

The Company accounts for all stock options and warrants granted using the fair value method. Under this method, compensation expense is measured at fair value at the grant date using the Black-Scholes option pricing model and recognized over the vesting period with corresponding credit to contributed surplus.

**PAN ORIENT ENERGY CORP.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Consideration received upon the exercise of stock options together with the amount of non-cash compensation expense recognized in contributed surplus is recorded as share capital.

**(J) Per Share Amounts**

Basic per share amounts are computed by dividing the earnings or loss by the weighted average shares outstanding during the reporting period. Diluted amounts are computed using the treasury stock method. The treasury stock method assumes that proceeds received from the exercise of options and warrants where the market price exceeds the exercise price are used to repurchase shares at the average market price for the period. The difference between the number of shares that could have been purchased at market prices in the period and the number of in-the-money options warrants is added to the weighted average shares outstanding.

**(K) Revenue Recognition**

Revenue from the sale of oil is recognized when the product is delivered.

**(L) Financial Instruments**

On January 1, 2007, the Company adopted new Canadian accounting standards pertaining to financial instruments recognition and measurement, financial instruments - presentation and disclosures, hedging, comprehensive income and equity. As prescribed by the new standards, prior periods have not been restated.

The new standards require all financial instruments within its scope, including all derivatives, to be recognized on the balance sheet initially at fair value. Subsequent measurement of all financial assets and liabilities except those held-for-trading and available for sale are measured at amortized cost determined using the effective interest rate method. 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. There was no impact on the financial statements as result of adopting the new standards.

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

**(M) New Accounting Pronouncements**

New Canadian accounting recommendations for capital disclosures have been issued which will require additional disclosure of both qualitative and quantitative information about objectives, policies and processes for managing capital. These recommendations are effective for years beginning January 1, 2008.

New Canadian accounting recommendations for additional disclosures about financial instruments have been issued which will require additional disclosure about the nature and extent of risks arising from financial instruments to which Pan Orient is exposed. These recommendations are effective for years beginning January 1, 2008.

In February 2008, the Canadian Institute of Chartered Accountants confirmed that Canadian GAAP for publicly accountable enterprises will be converted to International Financial Reporting Standards (IFRS) on January 1, 2011.

**3) DEPOSITS**

Included in deposits is approximately \$0.85 million (\$0.87 million USD) of cash deposits securing a Standby Letter of Credit posted in favor of the Government of Thailand guaranteeing the Company's work program on its 100% owned L53/48 onshore concession. The remainder of deposits are comprised mainly of cash deposits issued to the Thai government relating to importation permits.

**PAN ORIENT ENERGY CORP.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****4) ANDORA ENERGY CORPORATION (“ANDORA”)**

In the third quarter of 2006 the Company acquired 67 percent of the issued and outstanding shares of Andora. Andora is a private oil and gas company with oilsands leases in the Sawn Lake area of Northern Alberta. The acquisition was completed through a series of transactions resulting in: (i) the disposition of the Company’s Canadian oil and natural gas properties (Sawn Lake assets) in exchange for 10,000,000 shares of Andora; (ii) the Company acquiring 4,981,481 Andora common shares from treasury for \$6,275,000 cash; and (iii) the Company acquiring 13,414,634 Andora common shares from existing Andora common shareholders for \$2,145,621 in cash and the issuance of 4,257,222 Pan Orient shares. As part of the transaction, the Company’s wholly owned subsidiary (Pan Orient Energy Ltd.) and Andora amalgamated, immediately prior to which time all of Pan Orient Energy Ltd’s remaining assets were transferred to the Company. In conjunction with (ii) above, the Company received warrants to purchase an additional 2,250,000 common shares of Andora for \$3,600,000 (\$1.60 per share).

Pan Orient was deemed the acquirer of Andora and consequently Pan Orient has accounted for Andora as an acquisition using the purchase method of accounting as follows:

**Consideration**

Shares issued to Andora shareholders	\$ 15,751,721
Shares acquired from treasury, cash	6,275,000
Share acquisition from Andora shareholders, cash	2,145,621
Pan Orient’s 10 percent Sawn Lake interest, at cost	1,564,965
Acquisition costs	426,326

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\$ 26,163,633

**Purchase Price at Fair Value**

Property and equipment	\$ 39,514,288
Working capital (deficiency)	(2,585,577)
Future income taxes	(9,264,052)
Asset retirement obligation	(20,001)
Non-controlling interest	(1,481,025)

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\$ 26,163,633

**PAN ORIENT ENERGY CORP.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**5) ANDORA ACQUISITION OF SIGNET ENERGY INC.**

On September 19, 2007, the Company's subsidiary, Andora, acquired with 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 \$17,185,820. Certain shareholders of Signet exercised their right to dissent to the combination, and as such Andora has recorded a liability of \$3,716,675. 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.

Andora was deemed the acquirer of Signet and consequently Andora has accounted for Signet as an acquisition using the purchase method of accounting as follows:

Consideration

Shares issued by Andora	\$ 17,185,820
Consideration payable for signet shares	3,716,675
Acquisition costs	433,778
	<hr/>
	\$ 21,336,273
	<hr/>

Purchase Price at Fair Value

Petroleum and natural gas properties	\$ 22,009,165
Working capital, including cash of \$3.1 million	3,053,753
Future income tax	(3,663,045)
Asset retirement obligation	(63,600)
	<hr/>
	\$ 21,336,273
	<hr/>

The purchase price equation is preliminary and subject to change.

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.

**ANDORA WARRANTS**

On December 30, 2007, Pan Orient exercised its 2,250,000 warrants to acquire common shares of Andora for \$3,600,000. As a result, Pan Orient owns 55.4 percent 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 percent, resulted in a decrease in non-controlling 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.

**PAN ORIENT ENERGY CORP.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**6) PETROLEUM AND NATURAL GAS PROPERTIES**

		Cost	Accumulated Amortization	Net Book Value
2007	Canada	\$ 56,181,558	-	56,181,558
	Thailand	37,336,185	(5,284,000)	32,052,185
	India	395,410	-	395,410
	Office equipment - Canada	679,415	(368,487)	310,928
		<u>\$ 94,592,568</u>	<u>(5,652,487)</u>	<u>88,940,081</u>
2006	Canada	\$ 42,563,139	-	42,563,139
	Thailand	16,171,760	(749,000)	15,422,760
	India	329,521	-	329,521
	Office equipment - Canada	535,524	(198,202)	337,322
		<u>\$ 59,599,944</u>	<u>(947,202)</u>	<u>58,652,742</u>

General and administrative expenses totaling \$294,167 (2006 - \$182,916) that were directly related to exploration and development activities have been capitalized for the year ended December 31, 2007. In addition \$613,305 (2006 - \$0) of stock based compensation was capitalized (\$824,305 including related future taxes).

Costs associated with unproven properties of \$11.2 million (2006 - \$3.5 million) associated with the Thai full cost pool have been excluded from the depletion calculation. The capitalized costs associated with Canada, India and Indonesia are not subject to depletion as production has not commenced.

For the year ended December 31, 2007, no ceiling test writedown was required for the Company's Thailand properties. The benchmark prices for which the ceiling test was based, are as follows:

2008:	US\$ 93.52 / barrel WTI
2009:	US\$ 88.42 / barrel WTI
2010:	US\$ 85.83 / barrel WTI
2011:	US\$ 82.50 / barrel WTI
2012:	US\$ 81.18 / barrel WTI
After that:	+2% per annum

The carrying value of the Company's unproven Canadian, Indian and Indonesian properties are expected to be recoverable and as such no writedown was required.

**PAN ORIENT ENERGY CORP.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****7) ASSET RETIREMENT OBLIGATION**

The Company estimates the total undiscounted amount of cash flows required to settle its Canadian asset retirement obligation is approximately \$200,000 which will be incurred in approximately 20 years. A discount rate of 8.5% and an inflation rate of 2% was used to estimate the asset retirement obligation.

**8) 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 common shares

Common Shares	Number	Amount
Balance as at January 1, 2006	27,362,810	\$ 17,229,589
Shares issued on Tiger acquisition	319,163	855,357
Issued for Tiger litigation settlements	117,647	441,176
Issued for cash	8,000,000	30,000,000
Issued for Andora acquisition	4,257,222	15,751,721
Less: Share issue costs		
- cash	-	(1,949,942)
- compensation options (Note 8e)	-	(365,000)
Balance as at December 31, 2006	40,056,842	\$ 61,962,901
Issued for cash	5,000,000	38,400,000
Less: Share issue costs	-	(2,463,588)
Underwriters compensation options exercised	162,000	654,480
Reclassification upon exercise of underwriters compensation options	-	246,180
Balance as at December 31, 2007	45,218,842	\$ 98,799,973

**2007 Financing**

During the year ended December 31, 2007, 162,000 underwriters compensation options were exercised for common shares of the Company at a price of \$4.04 per share. Subsequent to December 31, 2007, the remaining 78,000 underwriters compensation options were exercised.

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 \$6,375,000 (\$6,036,984 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 \$32,025,000 (\$29,899,428 net of commission and other costs paid).

**PAN ORIENT ENERGY CORP.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

2006 Financings

On April 28, 2006, the Company issued 8,000,000 common shares at price of \$3.75 per common share, for gross proceeds of \$30,000,000 (\$28,050,058 net of commissions and associated costs).

Shares issued in Tiger acquisition

On October 21, 2005, Pan Orient acquired 92 percent of the issued and outstanding shares of Tiger Petroleum Inc. ("Tiger"). During the first quarter of 2006, the remaining 8 percent of Tiger was acquired for 319,163 shares of Pan Orient. In addition, 117,647 shares of Pan Orient were issued to settle certain claims that were outstanding at the date of acquisition.

c) Options to purchase common shares	Number of Shares	Weighted Average Exercise Price
Balance, January 1, 2006	2,350,000	\$ 0.78
Granted	1,443,150	3.53
Balance, January 1, 2007	3,793,150	\$ 1.77
Granted	759,000	11.29
Forfeited	(40,000)	(3.00)
	4,512,150	\$ 3.36

Options Outstanding			Options Exercisable		
Exercise Price	Number of Options	Weighted Average Remaining Contractual (years)	Weighted Average Exercise Price	Number of Options	Weighted Average Exercise Price
\$ 0.75	2,283,334	2.4	\$ 0.75	2,272,223	\$ 0.75
1.80 - 2.08	99,816	3.1	1.89	66,544	1.89
2.75 - 3.90	1,410,000	3.5	3.40	856,667	3.44
11.75	719,000	5.0	11.75	179,750	11.75
\$ 0.75 - 11.75	4,512,150	3.2	\$ 3.36	3,375,184	\$ 2.04

A Black-Scholes option pricing model, with the following weighted average assumptions was used to estimate the fair value of options on the date of the grant, for inclusion as stock-based compensation expense. The fair value of the stock based compensation is amortized over the vesting period of the options, generally being two years.

	<u>2007</u>	<u>2006</u>
Risk free interest rate	4.50%	4.50%
Expected lives	5 years	5 years
Expected volatility	65%	61%
Dividend per share	0.00%	0.00%

**PAN ORIENT ENERGY CORP.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

The weighted average grant date fair value of options issued during 2007 was \$6.56 per option (2006 - \$1.90). Stock based compensation totalled \$2.8 million in 2007 (2006 - \$1.8 million) of which, \$0.5 million (2006 - \$nil) was capitalized as it related to options granted to employees and consultants engaged in exploration activities.

**d) Options to purchase common shares of Andora**

The 2007 stock-based compensation expense includes the cost associated with 3,750,000 options that were granted in Andora, a 55.4 percent owned subsidiary of the Company, which entitle the holders to acquire common shares of Andora. A Black-Scholes option pricing model, with assumptions of a 4.5% risk free interest rate, 3 year expected lives, volatility of 20%, and no expected dividends was used to estimate the grant date fair value of the options as \$0.12 per option. The fair value of the Andora options was estimated to be \$400,000, net of expected forfeitures, of which \$300,000 was included as stock-based compensation expense and \$100,000 was capitalized as it related to employees directly involved in exploration and development activities.

**e) Underwriters compensation options**

In conjunction with the Company's \$30,000,000 April 2006 financing (8,000,000 shares at \$3.75 per share) the underwriting syndicate was granted 240,000 compensation options. The compensation options expire on April 28, 2008 and are exercisable at a price of \$4.04 per option. A Black-Scholes option pricing model with a 2 year expected life, a 4.5% risk free interest rate and expected volatility of 64% was used to value the compensation options at \$1.52 per option, for a total amount of \$365,000.

**f) Escrowed securities**

Included in the shares outstanding at December 31, 2007 are a total of 671,250 shares owned by directors, officers and certain non-management shareholders of Pan Orient which are subject to escrow restrictions, either voluntary or those imposed by the TSXV. These shares will be releasable from escrow in April 2008. The depository for the escrowed shares is Valiant Trust Company.

**g) Accumulated other comprehensive loss**

	2007	2006
Balance at beginning of year	\$ -	\$ -
Unrealized foreign exchange loss on October 1, 2007		
from change in translation method (Note 2h)	(1,291,691)	-
Unrealized foreign currency translation loss	(430,530)	-
Balance at end of year	\$ (1,722,221)	\$ -

**h) Income per share**

The income per share is based on the weighted average of shares outstanding for the year of 41,268,767 shares (2006-34,376,370 shares). For the year ended December 31, 2007, the diluted number of shares outstanding was 42,484,889 shares.



**PAN ORIENT ENERGY CORP.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****9) INCOME TAXES**

Income tax expense (reduction) differs from the amount that would be computed by applying the Canadian federal and provincial statutory income tax rates to the loss for the year as follows:

	2007	2006
Income (loss) before taxes and non-controlling interest	\$ 8,326,962	\$ (3,387,628)
Statutory tax rate in Canada	32.1%	34.5%
Expected income tax expense (reduction) at statutory rate	2,673,000	(1,169,000)
Decrease (increase) resulting from:		
Non-deductible stock-based compensation expense	650,000	612,000
Income taxed in jurisdiction with higher tax rate	2,417,000	-
Effect of tax rate reduction	(1,295,000)	-
Change in valuation allowance and other	(1,272,457)	(515,000)
	<u>\$ 3,172,543</u>	<u>\$ (1,072,000)</u>

The components of the net future income tax asset (liability) at December 31 are summarized below:

	2007	2006
Operating losses (expire up to 2028)	\$ 4,029,000	\$ 2,655,000
Petroleum and natural gas properties	(11,510,000)	(11,415,052)
Share issue costs	1,161,000	630,000
	<u>(6,320,000)</u>	<u>(8,130,052)</u>
Less: valuation allowance	(1,401,130)	(62,000)
	<u>\$ (7,721,130)</u>	<u>\$ (8,192,052)</u>

**10) FINANCIAL INSTRUMENTS**

The Company is exposed to foreign currency fluctuations as it holds US dollar and Thai baht cash and cash equivalents and accounts receivable and has obligations denominated in baht and US dollars. In addition, a portion of the Company's costs are incurred in each of the above currencies. There are no exchange rate contracts in place.

The fair value of the Company's financial instruments, including cash and cash equivalents, accounts receivable and accounts payable and accrued liabilities approximate their carrying values due to their short terms to maturity.

The majority of the Company's accounts receivable are due from an entity controlled by the government of Thailand. In addition, all of the Company's oil revenues are received from this entity.

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

The Company has entered into agreements to lease premises in both Canada and Thailand, requiring future minimum payments totaling \$1.0 million. Minimum annual payments during the next five fiscal years are as follows:

2008	\$ 238,465
2009	\$ 188,789
2010	\$ 142,680
2011	\$ 142,680
2012	\$ 146,247

On January 9, 2007, the Company signed a new concession agreement with the government of Thailand for block L53/48, located onshore Thailand. The concession agreement includes a minimum three year first exploration phase commitment of \$1,870,000 USD, for which the Company posted a standby letter of credit, secured by cash. At December 31, 2007, \$848,000 has yet to be expended.

As a result of the Signet acquisition, the Company inherited a lawsuit, the likely outcome and potential costs of which are both indeterminable. The Company believes the lawsuit is without merit.

**12) SEGMENTED INFORMATION**

The Company operates in two industry segments; the exploration for and production of conventional oil and gas in Asia (predominantly Thailand) and the development of heavy oil in Canada through its 55.4% owned subsidiary Andora.

2007	Canada	Thailand	Total
Revenue	\$ 540,773	\$ 24,067,368	\$ 24,608,141
Net income (loss)	(3,936,872)	8,780,231	4,843,359
Depletion, depreciation and accretion	169,925	4,535,000	4,704,925
Total assets	96,967,062	45,503,014	142,470,076
Capital expenditures for the year	1,062,111	21,164,100	22,226,211

  

2006	Canada	Thailand	Total
Revenue	\$ 704,827	\$ 1,256,447	\$ 1,961,274
Net income (loss)	(1,299,792)	(986,697)	(2,286,489)
Depletion, depreciation and accretion	165,863	678,000	843,863
Total assets	60,098,454	18,745,444	78,843,898
Capital expenditures for the year	41,581,827	9,276,084	50,857,911



**PAN ORIENT ENERGY CORP.**

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