



PAN ORIENT ENERGY CORP.

**2010 CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009**

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 12, 2011

(signed "William D. Ostlund")
William D. Ostlund
Vice President, Finance & Chief Financial Officer

April 12, 2011

INDEPENDENT AUDITORS' REPORT

To the Shareholders

We have audited the accompanying consolidated financial statements of Pan Orient Energy Corp. ("the Company"), which comprise the consolidated balance sheets as at December 31, 2010 and 2009, the consolidated statements of operations and retained earnings, comprehensive income, and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company as at December 31, 2010 and 2009, and the results of its consolidated operations and its consolidated cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Chartered Accountants
(signed "KPMG LLP")
Calgary, Canada
April 12, 2011

**Pan Orient Energy Corp.
Consolidated Balance Sheets**

(\$000s)	December 31, 2010	December 31, 2009
Assets		
Current		
Cash and cash equivalents	37,061	44,760
Accounts receivable	14,166	13,104
	51,227	57,864
Deposits (note 4)	4,628	4,079
Petroleum and natural gas properties (note 5)	230,296	179,838
	286,151	241,781
Liabilities		
Current		
Accounts payable and accrued liabilities	11,950	14,287
Taxes payable (note 9)	12,509	14,918
	24,459	29,205
Future income tax (note 9)	49,065	34,812
Asset retirement obligations (note 6)	4,274	2,829
	77,798	66,846
Non-controlling interest	18,227	18,705
Shareholders' equity (note 7)		
Share capital	110,576	104,846
Contributed surplus	12,872	8,274
Accumulated other comprehensive income (loss)	(1,155)	(4,149)
Retained earnings	67,833	47,259
	66,678	43,110
	190,126	156,230
Commitments (note 12)		
Subsequent Events (note 14)	286,151	241,781

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	
(\$000s, except per share amounts)	2010	2009
Revenue		
Petroleum revenue	103,019	98,236
Royalties	(6,608)	(6,843)
Interest	118	450
	96,529	91,843
Expenses		
Transportation	3,653	3,866
Operating	9,535	7,555
General and administrative	3,539	4,989
Depletion, depreciation and accretion	19,242	16,680
Stock-based compensation	6,160	1,769
Foreign exchange loss (note 8)	353	6,986
Foreign new venture expenditures (note 5)	474	62
	42,956	41,907
Income before taxes and non-controlling interest	53,573	49,936
Taxes (note 9)		
Special remuneratory benefit	6,413	6,751
Current income tax	14,336	15,423
Future income tax expense	12,350	12,686
	33,099	34,860
Net income for the period	20,474	15,076
Net income for the period attributable to:		
Common Shareholders	20,574	15,145
Non-controlling interest	(100)	(69)
Net income for the period	20,474	15,076
Retained earnings, beginning of year	47,259	32,127
Net income for the period attributed to common shareholders	20,574	15,145
Repurchase of shares (note 7)	-	(13)
Retained earnings, end of year	67,833	47,259
Net income per share attributable to common shareholders (note 7)		
Basic	0.43	0.33
Diluted	0.42	0.31

See accompanying notes to the consolidated financial statements.

Pan Orient Energy Corp.
Consolidated Statements of Comprehensive Income

(\$000s)	Year Ended	
	December 31	
	2010	2009
Net income attributable to common shareholders	20,574	15,145
Foreign exchange gain (loss) on translation of self-sustaining operations	2,994	(3,540)
Foreign exchange gain realized	-	(4,646)
Comprehensive income	23,568	6,959

See accompanying notes to the consolidated financial statements.

Pan Orient Energy Corp.
Consolidated Statements of Cash Flows

(\$000s)	Year Ended December 31	
	2010	2009
Cash Provided By (Used in)		
Operating Activities		
Net income	20,474	15,145
Items not affecting cash		
Depletion, depreciation and accretion	19,242	16,680
Stock-based compensation	6,160	1,769
Future income tax expense	12,350	12,686
Unrealized foreign exchange loss (note 8)	314	10,636
Realized gain on Thailand investment transferred to investing activities (note 8)	-	(3,897)
Foreign new venture expenditures	474	(69)
	59,014	52,950
Changes in non-cash working capital	(5,181)	(47,143)
	53,833	5,807
Investing Activities		
Petroleum and natural gas properties	(61,328)	(63,495)
Realized gain on Thailand investment (note 8)	-	3,897
Deposits	(669)	220
Change in non-cash working capital	(3,465)	1,864
	(65,462)	(57,514)
Financing Activities		
Issue of common shares, net of issue costs	3,669	1,135
Repurchase of common shares	-	(24)
	3,669	1,111
Change in cash and cash equivalents	(7,960)	(50,596)
Effect of foreign exchange on cash balances	261	(3,569)
Cash and cash equivalents, beginning of year	44,760	98,925
Cash and cash equivalents, end of year	37,061	44,760
Taxes paid	24,088	57,732

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 based in Calgary, Alberta, which holds properties onshore Thailand and Indonesia as well as an interest in a subsidiary with properties in Northern Alberta. The Company is continually pursuing other oil and natural gas exploration opportunities in Asia.

2) SIGNIFICANT ACCOUNTING POLICIES AND BASIS OF PRESENTATION

The consolidated financial statements for the years ended December 31, 2010 and 2009 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 53.4% owned by Pan Orient. The consolidated financial statements include a non-controlling interest representing the 46.6% portion of assets and liabilities not owned by Pan Orient.

(b) Joint Venture Activities

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.

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 cost, less any impairment, 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 cost, less any impairment, of unproved properties. The cash flows are estimated using expected future product prices and costs,

Pan Orient Energy Corp.
Notes to Consolidated Financial Statements

discounted using a risk-free rate. Unproved properties are assessed for impairment on a regular basis and when circumstances arise that indicate an unproven property is impaired such as expiration of lease rights or prolonged negative exploration activities. Impairments of unproven properties are transferred to the related full cost pool.

(e) Asset Retirement Obligations

The Company recognizes the fair value of statutory, contractual or other legal obligations associated with the retirement of assets in the period the asset is incurred, 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 increased as accretion is recognized over time 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 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.

(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.

(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) Use of Estimates

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.

Pan Orient Energy Corp.
Notes to Consolidated Financial Statements

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 uncertainty and the impact on the financial statements of future periods could be material.

(I) Financial Instruments

All financial assets, liabilities and 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, accounts receivable and deposits as loans and receivables, and accounts payable and accrued liabilities as other liabilities.

3) RECENT ACCOUNTING PRONOUNCEMENTS

On January 1, 2010, Pan Orient adopted the following Canadian Institute of Chartered Accountants ("CICA") Handbook sections:

"Business Combinations", Section 1582, which replaces the previous business combinations standard. The standard requires assets and liabilities acquired in a business combination, contingent consideration and certain acquired contingencies to be measured at their fair values as of the date of acquisition. In addition, acquisition related and restructuring costs are to be recognized separately from the business combination and included in the statement of earnings. The adoption of this standard did not impact the consolidated financial statements.

"Consolidated Financial Statements", Section 1601, which, together with Section 1602 below, replace the former consolidated financial statements standard. Section 1601 establishes the requirements for the preparation of consolidated financial statements. The adoption of this standard had no material impact on Pan Orient's consolidated financial statements.

"Non-controlling Interests", Section 1602, establishes accounting and reporting standards for the non-controlling (minority) interest in a subsidiary as well as the accounting for (i) a parent's loss of control (deconsolidation) of a subsidiary and (ii) changes in a parent's ownership interest in a subsidiary that do not result in deconsolidation. Section 1602 clarifies that a non-controlling interest in a subsidiary is an ownership interest in a consolidated entity that should be reported as equity in the consolidated financial statements. This Section also changes the way the consolidated statements of income (loss) and comprehensive income (loss) are presented by requiring consolidated net income (loss) and comprehensive income (loss) to be reported at amounts that include the amounts attributable to both the parent and the non-controlling interest. Section 1602 required retrospective adoption of the presentation and disclosure requirements for non-controlling interests. All other requirements of Section 1602 have been applied prospectively.

The above CICA Handbook sections are converged with International Financial Reporting Standards ("IFRS"). Pan Orient will be required to report its results in accordance with IFRS beginning January 1, 2011.

4) NON-CURRENT DEPOSITS

The Company has cash deposits relating to: 1) guarantees to the Thailand and Indonesia governments for the Company's work commitments; 2) customs importation permits in Thailand; and 3) deposits for service providers in Indonesia.

Pan Orient Energy Corp.
Notes to Consolidated Financial Statements

5) **PETROLEUM AND NATURAL GAS PROPERTIES**

As at December 31, 2010 (\$000s)	Cost	Accumulated Depreciation and Amortization	Net Book Value
Oil & Natural Gas			
Canada	58,663	-	58,663
Thailand	176,933	(57,969)	118,964
Indonesia	52,158	-	52,158
Office equipment	1,940	(1,429)	511
	289,694	(59,398)	230,296

As at December 31, 2009 (\$000s)	Cost	Accumulated Depreciation and Amortization	Net Book Value
Oil & Natural Gas			
Canada	56,624	-	56,624
Thailand	123,936	(39,429)	84,507
Indonesia	37,958	-	37,958
Office equipment	1,754	(1,005)	749
	220,272	(40,434)	179,838

General and administrative and stock-based compensation costs totaling \$4.2 million (2009 - \$2.8 million) that were directly related to exploration and development activities have been capitalized for the year ended December 31, 2010.

Costs subject to depletion included \$33.0 million (2009 - \$20.5 million) of estimated future development costs for proved reserves, less costs already incurred for Thailand inventory of \$6.8 million (2009 - \$7.0 million). Costs associated with unproven properties of \$5.2 million (2009 - \$14.0 million) with respect to the Thailand 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.

Recoverability of the Canadian and Indonesian capitalized costs is dependent on successfully completing development of the properties. With respect to the Canadian properties, recoverability is also dependent on determining the technical feasibility of the project. Capitalized costs incurred to date do not necessarily represent present or future values.

In 2010 costs of \$0.5 million (2009 - \$0.1 million) related to unsuccessful bids for production sharing contracts in Indonesia were reclassified from petroleum and natural gas properties to foreign new venture expenditures.

The Company performed a ceiling test calculation at December 31, 2010 and 2009 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, 2010 and 2009.

The benchmark prices used in the 2010 ceiling test calculation were as follows:

Year	WTI Oil (\$US/bbl)	\$US/\$CAD Exchange Rate	WTI Oil (\$CAD/bbl)
2011:	88.40	1.02	89.81
2012:	89.14	1.02	90.57
2013:	88.77	1.02	90.19
2014:	88.88	1.02	90.30
2015:	90.22	1.02	91.66
2016:	91.57	1.02	93.04
Escalate Thereafter:	1.5% per annum		1.5% per annum

Pan Orient Energy Corp.
Notes to Consolidated Financial Statements

6) ASSET RETIREMENT OBLIGATIONS

(\$000s)	Year Ended December 31	
	2010	2009
Asset retirement obligations, beginning of year	2,829	1,964
Obligations incurred	1,263	607
Revisions to obligations	(96)	-
Accretion	278	258
Asset retirement obligations, end of year	4,274	2,829

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.

Total undiscounted cash flows, escalated at 2.0%, required to settle the Company's asset retirement obligations are estimated to be \$13.0 million (2009 - \$8.5 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 and 2025. Estimated costs incurred in 2010 have been discounted at Pan Orient's credit-adjusted, risk-free interest rate of 8% (2009 and prior - 10%).

7) SHARE CAPITAL

a) Authorized

Unlimited Common Voting Shares
Unlimited Preferred Shares

b) Issued and Outstanding Class A Common Shares

Common Shares	Number of shares	Amount (000s)
Balance as at January 1, 2009	45,568,366	\$ 103,078
Exercise of stock options ⁽ⁱ⁾	750,000	1,135
Repurchase of shares ⁽ⁱⁱ⁾	(5,000)	(11)
Transfer from contributed surplus on exercise of stock options	-	644
Balance as at December 31, 2009	46,313,366	104,846
Exercise of stock options ⁽ⁱ⁾	2,427,500	3,669
Transfer from contributed surplus on exercise of stock options	-	2,061
Balance as at December 31, 2010	48,740,866	\$ 110,576

i. Issued pursuant to stock option agreements with exercise prices between \$0.75 and \$5.03.

ii. On September 28, 2009 Pan Orient announced that it acquired 5,000 of its common shares at a price of \$4.91 per share. These shares, purchased outside of the Company's expired normal course issuer bid, were cancelled and returned to treasury. As the consideration paid exceeded the stated value of the shares, the excess amount of \$13,000 was recorded as a reduction to retained earnings.

Pan Orient Energy Corp.
Notes to Consolidated Financial Statements

c) Options to Purchase Common Shares

	Number of options	Weighted average exercise price (\$)
Balance as at January 1, 2009	4,441,500	3.54
Granted	800,000	4.46
Exercised	(750,000)	1.51
Forfeited	(50,000)	11.75
Balance as at December 31, 2009	4,441,500	3.66
Granted ⁽¹⁾	2,501,500	7.14
Exercised	(2,427,500)	1.51
Forfeited	(62,500)	7.72
Balance as at December 31, 2010	4,453,000	6.73

1. On April 16, 2010 Pan Orient granted options to purchase 2,411,500 common shares under Pan Orient's stock option plan, of which 2,275,000 were granted to directors and officers. Each option has an exercise price of \$7.15 (being the April 15, 2010 closing price of the shares on the TSX Venture Exchange); vest as to 1/3 on the grant date and 1/3 on each of the first and second anniversaries of the grant date and expire on April 16, 2014.

Exercise Price (\$)	Options Outstanding December 31, 2010			Options Exercisable December 31, 2010		
	Number of Options	Weighted Average Exercise Price (\$)	Weighted Average Remaining Contractual Life (years)	Number of Options	Weighted Average Exercise Price (\$)	Weighted Average Remaining Contractual Life (years)
2.75 – 4.00	1,101,500	3.57	1.65	961,500	3.56	1.41
4.01 – 6.00	300,000	5.67	3.44	116,667	5.60	3.43
6.01 – 8.00	2,501,500	7.14	3.35	826,335	7.14	3.34
11.75	550,000	11.75	1.95	550,000	11.75	1.95
2.75 – 11.75	4,453,000	6.73	2.76	2,454,502	6.71	2.28

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 years ended December 31, 2010 and 2009, including modified stock options, were as follows:

	Year Ended December 31	
	2010	2009
Risk free interest rate (%)	1.8	1.0
Expected lives (years)	3.3	5.0
Expected volatility (%)	60	83
Dividend per share (%)	-	-
Forfeiture rate (%)	10	10
Weighted average fair value (\$)	3.38	2.99

Pan Orient Energy Corp.
Notes to Consolidated Financial Statements

e) Andora Energy Corporation

i) Issued and Outstanding Common Shares

As at December 31, 2010 Andora had 57.3 million (December 31, 2009 – 57.6 million) common shares issued and outstanding of which Pan Orient held 53.4% (December 31, 2009 – 53.2%).

During 2010, Andora settled a \$0.6 million receivable related to a lawsuit that was outstanding at December 31, 2009. In lieu of a cash settlement, 375,000 shares of Andora that were held in escrow were released to Andora and cancelled, increasing Pan Orient's interest from 53.2% to 53.5%. In May 2010, Andora issued 100,000 shares in lieu of cash severance payment to a director who resigned and this decreased Pan Orient's interest from 53.5% to 53.4%.

In accordance with the new accounting policy on non-controlling interests (note 3), increases or decreases in a parent's ownership interest while retaining control is a capital transaction. The transactions resulted in a decrease in non-controlling interest of \$0.4 million and a decrease in contributed surplus of \$0.2 million.

ii) Options to Purchase Common Shares of Andora

	2010		2009	
	Number	Weighted Average Exercise Price	Number	Weighted Average Exercise Price
Balance, beginning of year	1,325,000	\$ 1.60	5,175,000	\$ 1.42
Granted ⁽¹⁾	5,775,000	0.72	-	-
Expired	(50,000)	1.60	(3,750,000)	1.35
Cancelled ⁽¹⁾	(1,275,000)	1.60	-	-
Forfeited	-	-	(100,000)	1.60
Balance, end of year	5,775,000	\$ 0.72	1,325,000	\$ 1.60

(1) On April 19, 2010 Andora cancelled 1,275,000 of the options outstanding and granted options to purchase 5,775,000 common shares under Andora's stock option plan. Of the 5,775,000 options, 2,700,000 were issued to officers or directors of Andora who are also officers or directors of the Company. Each option has an exercise price of \$0.72; vest as to 1/3 on the grant date and 1/3 each year after the grant date and expire on April 19, 2014.

The following stock options of Andora are outstanding and exercisable at December 31, 2010:

Options Outstanding December 31, 2010				Options Exercisable December 31, 2010		
Exercise Price (\$)	Number of Options	Weighted Average Exercise Price (\$)	Weighted Average Remaining Contractual Life (years)	Number of Options	Weighted Average Exercise Price (\$)	Weighted Average Remaining Contractual Life (years)
0.72	5,775,000	0.72	3.30	1,925,000	0.72	3.30

Weighted average assumptions and resultant fair values used in the Black Scholes calculations for Andora stock options granted or revalued during the years ended December 31, 2010 and 2009 were as follows:

	Year Ended December 31	
	2010	2009
Risk free interest rate (%)	2.7	1.7
Expected lives (years)	3.0	2.0
Expected volatility (%)	40	20
Dividend per share (%)	-	-
Forfeiture rate (%)	10	10
Weighted average fair value (\$)	0.25	0.20

Pan Orient Energy Corp.
Notes to Consolidated Financial Statements

f) Contributed Surplus

(\$000s)	Year Ended December 31	
	2010	2009
Balance, beginning of year	8,274	6,531
Pan Orient stock-based compensation expense	5,365	1,742
Pan Orient stock-based compensation capitalized	552	499
Andora stock-based compensation expense	795	27
Andora stock-based compensation capitalized	96	119
Change in Andora interest	(149)	-
Transferred to share capital on exercise of options	(2,061)	(644)
Balance, end of year	12,872	8,274

Capitalized stock-based compensation relates to options granted to individuals engaged in exploration and development activities. The future income tax liability increased by \$0.2 million (2009 - \$0.2 million) as a result of capitalization of these costs.

g) Net Income per Share Attributable to Common Shareholders

The basic weighted average and diluted common shares outstanding were as follows:

	Year Ended December 31	
	2010	2009
Weighted average basic shares outstanding	48,186,507	46,007,897
Dilutive effect of stock options	636,368	2,116,856
Weighted average diluted	48,822,875	48,124,753

Options to purchase 3,051,500 common shares for the year ended December 31, 2010 (December 31, 2009 – 925,000) were not included in the computation of weighted average diluted common shares because they were anti-dilutive.

8) FOREIGN EXCHANGE

The Company's reporting currency is the Canadian dollar and its functional currencies are the Canadian dollar, the Thai baht and the US dollar. Each reporting period, the changes in the values of the baht and U.S. dollar relative to the Company's reporting currency must be recognized.

The Company's treasury function has been established with the goal of minimizing foreign currency exchange fluctuations to the extent possible. In addition to expatriating surplus funds from Thailand to Canada to hold in Canadian dollars, an integral part of this process is maintaining an appropriate cushion of baht in Thailand to satisfy payments in that currency as they come due, the most significant of which are the Company's Special Remuneratory Benefit and taxes.

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The Company's Thailand operations have a functional currency of Thai baht. Prior to April 1, 2009, the Company's net investment in the Thailand operations included intercompany loans that were denominated in baht, U.S. dollars and Canadian dollars and there was no planned or anticipated settlements of these loans contemplated. Accordingly, foreign currency translation gains and losses on these intercompany loans and the Company's investment in the shares of its Thailand subsidiaries were recognized in other comprehensive income. As a result, translation gains and losses on the Thailand operations were included in accumulated other comprehensive income (AOCI) on the balance sheet. Commencing April 1, 2009 the Company made a decision to repatriate funds from the Thailand operations through settlement of the intercompany loans and payment of dividends. Once this decision was reached, the intercompany loans were not considered as part of the Company's net investment in the Thailand operations. Therefore, effective April 1, 2009:

- translation gains and losses included in accumulated other comprehensive income on the investment in the Thailand operations that was planned to be repatriated was reclassified to net; and
- translation gains and losses on the permanent investment in the Thailand operations continue to be included in other comprehensive income.

Exchange gains or losses on assets and liabilities held in Canada are included in earnings and translation gains or losses from the Company's self-sustaining Indonesia entities are recorded in AOCI.

Accumulated Other Comprehensive Income

Activity related to the AOCI balance for the years ended December 31, 2010 and 2009 was as follows:

(\$000s)	Year Ended December 31	
	2010	2009
Balance at beginning of year	(4,149)	4,037
Unrealized foreign currency translation gain (loss)	2,994	(3,540)
Foreign exchange loss realized	-	(4,646)
Balance at end of year	(1,155)	(4,149)

Accumulated other comprehensive income (loss) at the following balance sheet dates was comprised of the following:

(\$000s)	As at	
	December 31, 2010	December 31, 2009
Foreign exchange gain (loss) related to Thailand	3,064	(2,633)
Foreign exchange loss related to Indonesia	(4,219)	(1,516)
Total Accumulated Other Comprehensive Income (Loss)	(1,155)	(4,149)

The amount included in AOCI for Thailand relates to translation gains and losses on the non-temporary portion of the investment and will continue to fluctuate based on the exchange rates between the Thai baht and Canadian dollar. The balance of the Indonesia AOCI will continue to fluctuate in future periods depending on the amount of capital invested in Indonesia and the exchange rates between the Canadian and U.S. dollar.

9) THAILAND SPECIAL REMUNERATORY BENEFIT TAX AND INCOME TAXES

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 and any operating losses have 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 SRB tax rate is applied to petroleum profits as defined in Thai tax legislation which includes a deduction for capital spent. SRB is paid annually after the end of the calendar year.

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The future income tax provision reflects an effective rate which differs from the expected statutory tax rate of a Canadian entity of 28.0% (2009 – 29.0%). Differences were accounted for as follows:

(\$000s)	Year Ended December 31	
	2010	2009
Income before income taxes and non-controlling interest	53,573	49,936
	28%	29.0%
Expected income taxes at the statutory rate	15,000	14,481
Increase (decrease) resulting from:		
Non-deductible stock-based compensation	1,725	513
Special remuneratory benefit tax	3,199	6,751
Income taxes in jurisdictions with different rates	12,895	10,885
Foreign exchange translation differences	-	2,729
Change in valuation allowance and other	280	(499)
Income taxes	33,099	34,860

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

	2010	2009
Operating losses (expire up to 2030)	(8,841)	(4,078)
Petroleum and natural gas properties	52,383	33,906
Share issue costs	-	(519)
Valuation allowance	5,523	5,503
	49,065	34,812

A summary of tax payable for the years ended December 31, 2010 and 2009 are as follows:

(\$000s)	Year Ended December 31	
	2010	2009
Balance, beginning of year	14,918	55,260
SRB expense – current year	6,413	6,751
Income tax – current year	14,336	15,423
Prior period SRB paid	(6,585)	(36,048)
Prior period income tax paid	(17,503)	(21,684)
Foreign exchange	930	(4,784)
Balance, end of year	12,509	14,918

10) CAPITAL MANAGEMENT

The Company's capital consists of the following:

(\$000s)	Year Ended December 31	
	2010	2009
Working capital and long term deposits	31,396	32,738
Share Capital	110,576	104,846

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

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The Company considers its capital structure to include shareholders' equity and working capital plus long term deposits. 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.

11) FINANCIAL INSTRUMENTS

Overview

The nature of Pan Orient's operations exposes the Company to credit risk, liquidity risk and market risk. 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.

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.

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 write-off any receivables during the years ended December 31, 2010 or 2009.

As at December 31, 2010 and 2009 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, the cash balance at December 31, 2010 of \$37.1 million, and the funds raised subsequent to year end (note 14) exceeds operating and future capital expenditures. The Company's liquidity risk is assessed as low.

The Company's only reported financial liabilities are accounts payable and accrued liabilities of \$12.0 million which will mature within one year. Taxes payable of \$12.5 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, 2011.

The Company has work commitments in Thailand and Indonesia (see note 12) which are expected to be funded through cash balances and deposits and expected future cash flow from Thailand properties.

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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.

The Company's reporting currency is the Canadian dollar and its functional currencies are the Canadian dollar, the Thai baht and the U.S. dollar (USD). 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 the following financial instruments were denominated in currencies other than the Canadian dollar:

(\$000s)	As at December 31, 2010		As at December 31, 2009	
	Thai baht (000s of Thai baht)	USD (\$000s)	Thai baht (000s of Thai baht)	USD (\$000s)
Cash and cash equivalents	588,958	8,744	796,260	2,759
Accounts receivable	334,929	1,097	323,721	780
Non-current deposits	44,000	3,144	44,000	2,613
Accounts payable	(256,943)	(2,260)	(314,203)	(3,483)
Taxes payable	(372,792)	-	(460,704)	-
Net exposure in functional currency	338,152	10,725	389,074	2,669
Net exposure in Canadian dollars (\$000s)	11,346	10,667	12,340	2,808

Based on financial instruments held at December 31, 2010 and 2009, fluctuations in the exchange rates as indicated below would have the following estimated effect on net income and other comprehensive income:

(\$000s)	As at December 31	
	2010	2009
Effect of 1% change in CAD\$ to USD exchange rate:		
Pre-tax net income	(16)	13
Other comprehensive income	(4)	17
Effect of 1% change in CAD\$ to baht exchange rate:		
Pre-tax net income	-	-
Other comprehensive income	115	130

The Company did not have any forward exchange contracts in place as at or during the years ended December 31, 2010 or 2009.

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.

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The Company did not have any commodity price contracts in place as at or during the years ended December 31, 2010 and 2009.

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 years ended December 31, 2010 and 2009.

Fair Value of Financial Instruments

The Company's financial instruments as at December 31, 2010 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.

12) COMMITMENTS

As at December 31, 2010 the Company's estimated outstanding capital commitments were as follows:

Country and Concession Name	Remaining Work Program Commitment	Obligation Period Ending	Estimated Net Financial Commitment	
			USD (\$000s)	CAD (\$000S) ⁽¹⁾
Thailand				
L 44/43	▪ study and training fund	July 2012	18	18
L33/43	▪ geological studies	July 2012	30	30
	▪ study and training fund		18	18
L 53/48	▪ drill 3 exploration wells	January 2013	975	961
	▪ geological studies		55	55
	▪ study and training fund		47	47
Indonesia ⁽²⁾⁽³⁾				
Citarum	▪ drill 3 exploration wells	October 2011	12,846	12,853
Batu Gajah	▪ 400 km ² 3D seismic	January 2012	22,379	22,392
	▪ drill 3 exploration wells			
South CPP	▪ 200 km 2D seismic	November 2011	5,511	5,514
	▪ drill one exploration well			
Total			41,879	41,888

(1) Translated at December 31, 2010 exchange rates.

(2) At December 31, 2010, the Company owned a 90% 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 working interest in the South CPP PSC (formerly the Pamai Taluk joint study agreement) located onshore south central Sumatra. Amounts recorded in the financial statements and work commitments related to these PSCs include amounts paid by Pan Orient on behalf of a partner's carried interest (10% for Batu Gajah, 11% for Citarum and 10% for South CPP).

(3) Subsequent to December 31, 2010 the Company owned a 97% working interest in the Batu Gajah and South CPP PSCs and a 77% working interest in the Citarum PSC as the carried interest were reduced to 3% for all three PSCs.

Indonesia financial commitments as provided above represent the work program required under the initial 3-year exploration period of the PSC. With respect to Citarum and Batu Gajah, extension of this initial exploration period has been successfully negotiated with the Government of Indonesia (GOI) to the dates indicated above. If Pan Orient exercises its options to continue beyond the exploration period, additional commitments will be determined on a year-by-

Pan Orient Energy Corp.
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year basis through submission of a work program and approval from the GOI. Estimated costs to satisfy these commitments are determined based on the Company's capital budgets as approved by the GOI.

Although extension of the exploration period is a departure from the original contract, it is considered standard practice in Indonesia. In the past, such applications on behalf of Pan Orient have been approved by the GOI and management has no reason to believe that future requests will not be granted approval however there is no guarantee. Upon default of a commitment related to any of the first three years of a PSC the operator is required to relinquish 15% of the original PSC area, the actual acreage at the discretion of the operator. To date, both Citarum and Batu Gajah have complied with these penalty relinquishments. Depending on the stage of the PSC, failure to fulfill the required commitments may also result in penalty payment equal to the unspent commitments and/or forfeiture of the PSC.

The expenditures as provided in the table above represent management's estimates of the costs to fulfill the work program requirements in Thailand and Indonesia. Actual expenditures required to carry out these commitments may be significantly different than the estimates. The Company intends to fund commitments through existing cash surplus, expected cash flows from Thailand operations and funds from the 2011 financing.

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
2011	102	117	202	421
2012	51	-	205	256
2013	-	-	171	171
2014	-	-	-	-
2015	-	-	-	-
Total	153	117	578	848

13) SEGMENTED INFORMATION

The Company has properties in three countries, each of which is considered a separate operating segment. The three segments consist of: 1) partially developed conventional petroleum and natural gas properties in Thailand; 2) undeveloped petroleum and natural gas properties in Indonesia; and 3) an undeveloped heavy oil property in Canada. The following table provides information for each geographical segment as at and for the year ended December 31:

(\$000s)	Year Ended December 31	
	2010	2009
Petroleum revenue		
Thailand	103,019	98,236
Indonesia	-	-
Canada	-	-
Total	103,019	98,236
Interest revenue		
Thailand	68	407
Indonesia	-	-
Canada	50	43
Total	118	450
Current income tax expense ⁽¹⁾		
Thailand	20,749	22,174
Indonesia	-	-
Canada	-	-
Total	20,749	22,174

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(\$000s)	Year Ended December 31	
	2010	2009
Depletion, depreciation and accretion		
Thailand	19,017	16,447
Indonesia	47	47
Canada	178	186
Total	19,242	16,680
Net income (loss) attributable to common shareholders ⁽²⁾		
Thailand	26,361	14,544
Indonesia	179	(632)
Canada	(5,966)	1,233
Total	20,574	15,145
Capital expenditures ⁽³⁾		
Thailand	43,441	51,996
Indonesia	17,024	10,582
Canada	863	917
Total	61,328	63,495
Total assets		
Thailand	150,100	119,155
Indonesia	57,362	43,559
Canada	78,689	79,067
Total	286,151	241,781

(1) Includes SRB and income tax.

(2) In 2009, the net income for Canada is a result of the general and administrative expenses, stock based compensation expense, depreciation, and foreign new venture expenses being more than offset by realized foreign exchange gains and a future income tax recovery of \$1.5 million relating to Andora.

(3) Does not include acquisition activities, asset retirement costs, or foreign exchange.

14) SUBSEQUENT EVENTS

In February 2011, through its subsidiaries, the Company increased its interests in the Batu Gajah and South CPP Production Sharing Contracts ("PSC's") in Indonesia from 90% to 97%. The Company purchased a 7% carried interest on each of these PSCs previously owned by a third party for consideration of USD \$1.3 million, including the issuance of 28,958 shares in the Company at a deemed market value of USD \$0.2 million.

On March 8, 2011, the Company completed a bought deal financing of 7,557,264 common shares at a price of \$6.55 per common share for gross proceeds of \$49.5 million on a private placement basis.

In March 2011, through its subsidiaries, the Company increased its interest in the Citarum PSC in Indonesia from 69% to 77%. The Company repurchased an 8% carried interest on the PSC previously owned by a third party for consideration of USD \$0.5 million, including the issuance of 21,719 shares in Pan Orient at a deemed market value of USD \$0.15 million.



PAN ORIENT ENERGY CORP.

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