



ARAWAK ENERGY CORPORATION

**CONSOLIDATED FINANCIAL STATEMENTS AND NOTES
(UNAUDITED – PREPARED BY MANAGEMENT)**

For the three and nine months ended September 30, 2007

ARAWAK ENERGY CORPORATION
INTERIM CONSOLIDATED BALANCE SHEETS
(Expressed in thousands of U.S. dollars)
Unaudited – prepared by management

As at	Note	September 30, 2007	December 31, 2006
ASSETS			
Cash and cash equivalents		13,488	9,663
Accounts receivable		17,829	9,483
Inventory		10,181	4,992
Other current assets		14,394	9,457
		<u>55,892</u>	<u>33,595</u>
Property and equipment	3	215,450	201,314
Future income tax assets		2,572	2,365
		<u>273,914</u>	<u>237,274</u>
LIABILITIES			
Accounts payable and accrued liabilities		20,994	15,873
Corporate income taxes payable		6,548	2,936
Crude oil sales prepayment facility	4	42,000	30,000
Current portion of long term debt	5	6,900	6,900
Current portion of other long term liabilities		1,104	1,354
		<u>77,546</u>	<u>57,063</u>
Future income tax liabilities		16,157	18,531
Long term debt	5	12,409	15,785
Other long term liabilities		20,905	15,023
Asset retirement obligation		3,197	2,820
		<u>130,214</u>	<u>109,222</u>
SHAREHOLDERS' EQUITY			
Share capital	6	115,051	114,553
Contributed surplus	6	8,380	5,617
Accumulated other comprehensive income	2	1,935	1,541
Retained earnings		18,334	6,341
		<u>143,700</u>	<u>128,052</u>
		<u>273,914</u>	<u>237,274</u>

See accompanying notes to the interim consolidated financial statements.

ARAWAK ENERGY CORPORATION
INTERIM CONSOLIDATED STATEMENTS OF INCOME AND RETAINED EARNINGS (DEFICIT)
(Expressed in thousands of U.S. dollars)
Unaudited – prepared by management

For the period ended September 30	Three months 2007	Three months 2006	Nine months 2007	Nine months 2006
Revenue				
Crude oil and gas sales	56,619	39,638	123,073	101,332
Interest and other income	742	1,739	1,535	2,098
	57,361	41,377	124,608	103,430
Expenses				
Royalties and taxes	10,711	9,490	27,670	21,932
Production costs	5,632	2,896	13,102	7,132
Transportation and selling costs	5,407	4,317	13,099	10,640
General and administrative expenses	4,447	3,420	12,243	9,638
Stock option compensation	1,068	1,397	2,897	3,130
Depletion, depreciation and amortisation	10,469	7,445	24,964	18,495
Accretion expense	82	64	238	181
Interest expense	1,342	1,264	4,932	2,547
Foreign exchange gain	(1,472)	(22)	(1,523)	(632)
	37,686	30,271	97,622	73,063
Income before income taxes	19,675	11,106	26,986	30,367
Current income tax	12,002	6,208	20,129	16,983
Future income tax recovery	(88)	(943)	(2,480)	(2,775)
	11,914	5,265	17,649	14,208
Net income for the period	7,761	5,841	9,337	16,159
Retained earnings (deficit) beginning of the period	7,917	4,220	6,341	(6,098)
Retained earnings end of the period	15,678	10,061	15,678	10,061
Net income per share				
Basic	0.045	0.034	0.054	0.093
Diluted	0.044	0.034	0.053	0.093

See accompanying notes to the interim consolidated financial statements.

ARAWAK ENERGY CORPORATION
INTERIM CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME AND
ACCUMULATED OTHER COMPREHENSIVE INCOME
(Expressed in thousands of U.S. dollars)
Unaudited – prepared by management

For the period ended September 30	Three months 2007	Three months 2006	Nine months 2007	Nine months 2006
<u>Comprehensive income</u>				
Net income for the period	7,761	5,841	9,337	16,159
Other comprehensive income				
Foreign currency translation adjustment	176	156	394	913
Comprehensive income	7,937	5,997	9,731	17,072

<u>Accumulated other comprehensive income</u>				
Accumulated other comprehensive income, beginning of the period	1,759	217	1,541	(540)
Other comprehensive income	176	156	394	913
Accumulated other comprehensive income, end of the period	1,935	373	1,935	373

See accompanying notes to the interim consolidated financial statements.

As at September 30, 2007 the accumulated other comprehensive income consists of foreign currency translation adjustments of \$1,935 million (September 30, 2006 – \$373 million; December 31, 2006 – \$1,541 million).

ARAWAK ENERGY CORPORATION
INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS
(Expressed in thousands of U.S. dollars)
Unaudited – prepared by management

For the period ended September 30	Three months 2007	Three months 2006	Nine months 2007	Nine months 2006
<u>Operating Activities</u>				
Net income for the period	7,761	5,841	9,337	16,159
Items not affecting cash:				
Stock option compensation	1,069	1,397	2,898	3,130
Depletion, depreciation and amortisation	10,469	7,445	24,964	18,495
Accretion expense	82	64	238	181
Future income tax recovery	(88)	(943)	(2,480)	(2,775)
Funds from operations	19,293	13,804	34,957	35,190
Changes in non-cash working capital	(4,196)	(5,230)	(7,082)	(5,481)
	15,097	8,574	27,875	29,709
<u>Financing Activities</u>				
Changes in prepayment facility	1,000	-	12,000	12,500
Long term debt repayments	-	(1,500)	(3,550)	(4,500)
Proceeds from long term debt	-	4,500	-	4,500
Change in other long term liabilities	4,538	(149)	5,632	535
Proceeds from issue of common shares	-	124	498	305
Foreign exchange loss (gain)	176	156	393	912
	5,714	3,131	14,973	14,252
<u>Investing Activities</u>				
Acquisitions in Russia	-	-	-	(8,473)
Acquisitions in Kazakhstan	(5,781)	-	(5,781)	-
Purchase of property and equipment	(15,692)	(13,878)	(33,242)	(36,585)
	(21,473)	(13,878)	(39,023)	(45,058)
Net change in cash during the period	(662)	(2,173)	3,825	(1,097)
Cash, beginning of the period	14,150	15,361	9,663	14,285
Cash, end of the period	13,488	13,188	13,488	13,188

See accompanying notes to the interim consolidated financial statements.

**ARAWAK ENERGY CORPORATION
NOTES TO THE INTERIM FINANCIAL STATEMENTS
FOR THE THREE AND SIX MONTHS ENDED SEPTEMBER 30, 2007
UNAUDITED – prepared by management**

All amounts are in thousands of U.S. dollars unless otherwise stated except per share amounts and number of shares.

1. SIGNIFICANT ACCOUNTING POLICIES

Principles of consolidation

The interim consolidated financial statements of Arawak Energy Corporation (“Arawak” or the “Company”) have been prepared in accordance with Canadian generally accepted accounting principles (“GAAP”) following the same accounting principles and methods of application as the audited consolidated financial statements for the year ended December 31, 2006. The disclosures provided herein are incremental to those included in the annual consolidated financial statements. These interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the notes thereto in the Company’s annual report for the year ended December 31, 2006.

Presentation of comparative figures

Certain comparative figures have been reclassified to conform to the presentation adopted for the current period.

2. CHANGES IN ACCOUNTING POLICIES

Effective April 1, 2007 the operations in Azerbaijan reached commercial production and accordingly the Company’s proportionate share of revenues and expenses have been recognized in the statement of operations for the quarter ended June 30, 2007. In prior periods, all revenues and expenses were reflected in the carrying value of the Azerbaijani assets.

Effective January 1, 2007 the Company adopted the Canadian Institute of Chartered Accountants Handbook Section 1530 “Comprehensive income”, Section 3251 “Equity”, Section 3865 “Hedges” and Section 3855 “Financial instruments – recognition and measurement”. As required by the new standards, prior periods have not been restated, except to reclassify the foreign currency translation balance as described under “Comprehensive income”. The adoption of these Handbook sections had no impact on opening retained earnings or accumulated other comprehensive income.

Comprehensive income

This standard introduces a new “Statement of comprehensive income” and establishes accumulated other comprehensive income as a separate component of shareholders’ equity. Comprehensive income is defined as the change in equity from transactions and other events from non-owner sources and includes all changes in equity during a period except those resulting from investments by owners and distributions to owners. Other comprehensive income comprises revenues, expenses, gains and losses that, in accordance with GAAP, are recognised in comprehensive income but excluded from net income. Amounts included in accumulated other comprehensive income are reclassified to net income when realised. Upon adoption of Section 1530, cumulative translation adjustments relating to self-sustaining foreign operations were reclassified to accumulated other comprehensive income and comparative amounts have been restated.

Equity

The equity section establishes standards for the presentation of equity and changes in equity during the reporting period.

Hedges

This section prescribes new hedge accounting standards. Hedge accounting continues to be optional. At the inception of the hedge, the Company must formally document the designation of the hedge, the risk management objectives, the hedging relationships between the hedged items and the hedging instruments and the methods for testing the hedge’s effectiveness. The Company assesses at

inception and throughout its term whether the hedging instruments are highly effective in offsetting changes in fair values or cash flows of hedged items.

Financial instruments

The accounting standard on financial instruments establishes the recognition and measurement criteria for financial assets, liabilities and derivatives. All financial instruments are required to be measured at fair value on initial recognition while measurement in subsequent periods depends on its classification as “held-for-trading”, “available-for-sale”, “held-to-maturity”, “loans and receivables” or “other financial liabilities” as defined by the standard.

Financial instruments “held-for-trading” are measured at fair value with changes to fair value recognised in net income, “available-for-sale” are measured at fair value with changes to fair value recognised in other comprehensive income and “held-to-maturity”, “loans and receivables” and “other financial liabilities” are measured at amortised cost using the effective interest rate method of amortisation.

Cash and cash equivalents are classified as “held-for-trading” and are measured at carrying value, which approximates fair value due to their short term nature. Accounts receivable and other current assets are classified as “loans and receivables”. Accounts payable and accrued liabilities, corporate income taxes payable, crude oil sales prepayment facility, long term debt and other long term liabilities are classified as “other liabilities”.

Upon adoption of this standard and its transition provisions, with respect to the amortised cost using the effective interest rate method of long term debt, deferred financing costs of \$0.9 million previously included in deferred charges have been reclassified as unamortised debt issue costs which reduce the carrying value of the long term debt.

3. PROPERTY AND EQUIPMENT

	Cost	Accumulated depletion and depreciation	Net book value
September 30, 2007			
Oil and gas properties	275,343	63,814	211,529
Office equipment	4,331	410	3,921
	279,674	64,224	215,450
December 31, 2006			
Oil and gas properties	237,207	38,893	198,314
Office equipment	3,342	342	3,000
	240,549	39,235	201,314

For the three months ended September 30, 2007, the Company capitalised \$0.8 million of general and administrative costs (three months ended September 30, 2006 – \$0.7 million).

Capitalised costs of \$29.5 million relating to unproved properties in Kazakhstan (2006 – \$25.6 million) have been excluded from the depletion calculation.

4. CRUDE OIL SALES PREPAYMENT FACILITY

Subject to certain conditions, Vitol S.A., an affiliated company of a significant shareholder, has the right to be the exclusive buyer of crude oil exported from the Company’s subsidiary in Kazakhstan until May, 2011 and provides a crude oil prepayment facility allowing the Company to draw prepayments on future oil sales. The amount available for prepayment is up to 90 percent of the expected value of the next nine months crude oil export sales from Kazakhstan, subject to a maximum of \$50.0 million (December 31, 2006 maximum – \$35.0 million). A financing charge of LIBOR plus 3.5% is charged on the outstanding balance held in the Netherlands while LIBOR plus 4.4%, which includes local withholding taxes, is charged on the outstanding balance held in Kazakhstan. Interest is due monthly.

The balance outstanding at September 30, 2007 is \$42.0 million (December 31, 2006 – \$30.0 million).

5. LONG TERM DEBT

The Company's 50% owned operating companies in Russia have a bank borrowing base facility agreement carrying interest at LIBOR plus 4.4%. The facility is repayable in equal \$1.725 million quarterly payments and interest is paid quarterly. The borrowing is secured against Russian export crude oil sales and proportionate shareholder guarantees.

	September 30, 2007	December 31, 2006
Bank loan	20,000	23,550
Short term portion	(6,900)	(6,900)
Unamortised debt issue costs	(691)	(865)
Long term debt	12,409	15,785

6. SHARE CAPITAL

Authorised:

Unlimited common shares, without par value

Unlimited preference shares, without par value

Common shares outstanding as at:	30 September 2007		December 31, 2006	
	Number of shares	\$000	Number of shares	\$000
<u>Issued:</u>				
Balance, beginning of period	171,181,702	112,626	170,184,729	111,565
Issued for cash	-	-	-	-
Exercise of stock options	200,000	498	366,667	511
Exchanged during period	2,210,163	1,927	630,306	550
Share issue costs	-	-	-	-
Issued and outstanding	173,591,865	115,051	171,181,702	112,626
<u>Exchangeable shares:</u>				
Balance, beginning of period	2,210,163	1,927	2,840,469.00	2,477
Exchanged	(2,210,163)	(1,927)	(630,306)	(550)
Exchangeable shares outstanding	-	-	2,210,163	1,927
Balance, end of period	173,591,865	115,051	173,391,865	114,553

In 2005, the Company funded an acquisition by issuing 13.9 million exchangeable shares of Arawak Acquisition Inc., a wholly-owned subsidiary of Arawak. The exchangeable shares were exchangeable for Arawak common shares on a one for one basis. There were no exchangeable shares outstanding as of September 30, 2007 (2,210,958 as of December 31, 2006).

Earnings per share

Per share amounts are calculated using the weighted average number of common shares outstanding during the period as follows:

For the period ended September 30	Three months		Nine months	
	2007	2006	2007	2006
Basic	173,591,865	173,283,198	173,517,872	173,201,352
Diluted	174,710,926	174,123,075	174,787,875	174,041,229

For the purposes of calculating the weighted average number of shares, the exchangeable shares have been treated as common shares issued.

The stock options granted are the reconciling items between the weighted average basic and diluted number of common shares, though not all of the outstanding stock options are dilutive.

Stock options

On June 5, 2007 the Company adopted an amended stock option plan under which the Board of Directors may grant options for the purchase of common shares to directors, officers, consultants and employees for up to 12% of the outstanding common shares. The exercise price of each option shall not be lower than the closing price of common shares on the Toronto Stock Exchange on the last trading day immediately prior to the date the stock option is granted. The options are granted for a maximum term of five years and are fully vested after 36 months from the date of grant. Options granted prior to June 2007 were granted under the 1998 and 2003 stock option plans.

	Number of options	Weighted average exercise price
Outstanding December 31, 2005	5,700,000	CAD 2.01
Granted February 3, 2006	300,000	CAD 2.50
Granted May 10, 2006	5,235,000	CAD 2.94
Exercised	(366,667)	CAD 1.20
Cancelled	(83,333)	CAD 2.34
Outstanding December 31, 2006	10,785,000	CAD 2.50
Granted June 15, 2007	3,042,500	CAD 2.69
Exercised	(200,000)	CAD 2.10
Cancelled	(150,000)	CAD 2.10
Outstanding September 30, 2007	13,477,500	CAD 2.58

The number of stock options outstanding and exercisable at September 30, 2007, is as follows:

Options outstanding		Options exercisable	
Number outstanding	Average remaining life in years	Number outstanding	Average remaining life in years
13,477,500	3.5	8,756,655	2.9

Contributed surplus

As at:	September 30, 2007	December 31, 2006
Balance, beginning of period	5,617	1,818
Stock based compensation expense	2,898	3,928
Exercised options	(134)	(129)
Balance, end of period	8,381	5,617

7. FINANCIAL INSTRUMENTS

Market risk

The Company is exposed to changes in oil and gas prices in world and domestic markets. From time to time the Company enters into derivative contracts to manage its crude oil price exposure. The instruments are not used for trading purposes. The Company manages its exposure to petroleum commodity prices by entering into crude oil options when deemed appropriate. These derivative contracts are not accounted for as hedges.

Foreign currency exchange risk

Due to our operations in Russia, Kazakhstan and Azerbaijan, the Company is exposed to foreign currency fluctuations as domestic oil sales in Russia and Kazakhstan and a large portion of local expenses are denominated in local currencies.

Credit risk

A substantial portion of accounts receivable is related to export oil sales from Russia and Kazakhstan with one major customer. As described in Note 4, this customer also provides a crude oil prepayment facility allowing the Company to draw prepayments on future oil sales and diminishing the risk of collection. The Company's credit risk is mitigated on domestic sales by receiving full or majority payment in advance of each sale.

Interest rate risk

The Company is exposed to interest rate cash flow risk related to the variable interest rates on the crude oil sales prepayment facility, long term debt and interest-bearing other long term liabilities.

8. RELATED PARTY BALANCES AND TRANSACTIONS

Crude oil sales

Export crude oil sales from Russia and Kazakhstan to Vitol S.A. during the three months ended September 30, 2007 is \$45.6 million (three months ended September 30, 2006 – \$31.2 million). Related accounts receivable at September 30, 2007 include \$15.3 million and at December 31, 2006 include \$6.7 million.

Crude oil sales prepayment facility

The balance of the crude oil sales prepayment facility provided by Vitol S.A. at September 30, 2007 is \$42.0 million (December 31, 2006 – \$30.0 million) with related interest expense for the three months ended September 30, 2007 of \$1.0 million (three months ended September 30, 2006 – \$0.2 million).

These transactions were, to the knowledge of management, at terms and rates no more and no less favourable than those with unrelated parties.

9. SEGMENTED INFORMATION

The commercial activities of the Company are concentrated in Kazakhstan, Russia and Azerbaijan and are considered separate business segments for operational and presentation purposes. The table below sets out key financial data for the Company by geographical segment.

	Kazakhstan	Russia	Azerbaijan	Other	Total
<u>For the three months ended September 30, 2007</u>					
Revenue:					
Crude oil and gas sales	37,511	18,869	239	-	56,619
Interest and other income	470	245	-	27	742
Expenses:					
Royalties and taxes	1,422	9,289	-	-	10,711
Production costs	3,867	1,764	1	-	5,632
Transportation and selling costs	4,816	591	-	-	5,407
General and administrative	1,290	673	281	2,203	4,447
Stock option compensation	-	-	-	1,068	1,068
Depletion, depreciation and amortisation	6,824	3,392	156	97	10,469
Accretion expense	37	45	-	-	82
Interest expense	993	673	-	(324)	1,342
Foreign exchange loss/(gain)	(197)	(1,617)	-	342	(1,472)
Current income tax	10,293	1,709	-	-	12,002
Future income tax recovery	490	(578)	-	-	(88)
Net income	8,146	3,173	(199)	(3,359)	7,761
<u>For the nine months ended September 30, 2007</u>					
Revenue:					
Crude oil and gas sales	72,892	49,612	569	-	123,073
Interest and other income	732	341	-	462	1,535
Expenses:					
Royalties and taxes	2,317	25,353	-	-	27,670
Production costs	8,291	4,651	160	-	13,102
Transportation and selling costs	11,375	1,724	-	-	13,099
General and administrative	3,539	1,977	572	6,155	12,243
Stock option compensation	-	-	-	2,897	2,897
Depletion, depreciation and amortisation	14,649	9,729	381	205	24,964
Accretion expense	110	128	-	-	238
Interest expense	2,895	2,338	-	(301)	4,932
Foreign exchange loss/(gain)	(91)	(1,874)	-	442	(1,523)
Current income tax	16,842	3,287	-	-	20,129
Future income tax recovery	(636)	(1,844)	-	-	(2,480)
Net income	14,333	4,484	(544)	(8,936)	9,337
<u>As at September 30, 2007</u>					
Property and equipment	122,762	58,125	33,244	1,319	215,450
Total assets	160,180	75,373	34,116	4,245	273,914
Total liabilities	82,488	34,674	10,253	2,799	130,214

	Kazakhstan	Russia	Azerbaijan	Other	Total
<u>For the three months ended September 30, 2006</u>					
Revenue:					
Crude oil sales	23,839	15,799	-	-	39,638
Interest and other income	0	930	-	809	1,739
Expenses:					
Royalties and taxes	543	8,947	-	-	9,490
Production costs	1,895	1,001	-	-	2,896
Transportation and selling costs	3,740	577	-	-	4,317
General and administrative expenses	820	903	-	1,697	3,420
Stock option compensation	0	0	-	1,397	1,397
Depletion, depreciation and amortization	4,946	2,463	-	36	7,445
Accretion expense	32	32	-	0	64
Interest expense	315	915	-	33	1,263
Foreign exchange loss/(gain)	140	(177)	-	15	(22)
Current income tax	5,188	1,021	-	0	6,209
Future income tax recovery	(62)	(180)	-	(701)	(943)
Net income	6,282	1,227	-	(1,669)	5,841
<u>For the nine months ended September 30, 2006</u>					
Revenue:					
Crude oil sales	61,409	39,923	-	-	101,332
Interest and other income	19	1,063	-	1,016	2,098
Expenses:					
Royalties and taxes	1,347	20,585	-	-	21,932
Production costs	4,179	2,953	-	-	7,132
Transportation and selling costs	9,512	1,128	-	-	10,640
General and administrative	2,507	1,786	-	5,345	9,638
Stock option compensation	0	0	-	3,130	3,130
Depletion, depreciation and amortization	12,519	5,875	-	101	18,495
Accretion expense	93	88	-	0	181
Interest expense	433	2,024	-	90	2,547
Foreign exchange loss/(gain)	(56)	(601)	-	25	(632)
Current income tax	14,010	2,973	-	0	16,983
Future income tax recovery	(685)	(202)	-	(1,888)	(2,775)
Net income	17,569	4,377	-	(5,787)	16,159
<u>As at September 30, 2006</u>					
Property and equipment	82,619	59,056	26,877	711	169,263
	113,21				
Total assets	6	70,388	28,658	4,745	217,007
Total liabilities	37,184	40,917	7,510	1,667	87,278