CONTENTS

CHAIRMAN'S STATEMENT

Each year when reporting to you I highlight the vital role that Iraq will play in the future of world energy. Let me remind you why. Iraq has the second or third largest proven oil resources in the world, some 115 billion barrels. Production costs, below $2 a barrel, are probably the lowest in the world. There are dozens of proven undeveloped oil discoveries each containing over 1 billion barrels. The West Qurna oil field, with at least 16 billion barrels recoverable, is the best undeveloped oil discovery in the world.

Yet, there has been relatively little oil exploration across the deserts of Iraq or at depth. The total number of oil wells drilled to date in Iraq is less than the number drilled in the Gulf of Mexico. Many experts believe that Iraq will ultimately contain over 300 billion barrels of oil and will rival Saudi Arabia as the world's number one oil producer.

These are the reasons why Petrel focused on Iraq. We have had a continuous presence there since 1999. Since early 2000 we have worked on the large 10,000 sq km Block 6 exploration concession in the western desert. After submitting four tenders to develop oil fields we were successful in 2005 when we were awarded the $197 million Subba and Luhais development contract. In 2005, we negotiated a technical co-operation agreement on the Merjan oil field. We are confident that the passing of the Hydrocarbon Law will open additional and exciting opportunities for Petrel.

Image 1 – Signing of East Safawi Production Sharing Agreement at the World Economic Forum in Jordan

CHAIRMAN'S STATEMENT

To the average investor watching television or reading the newspapers the turmoil in Iraq must suggest the impossibility of normal activities. Yet life goes on. The reality is that in many sectors of society, progress is being made. By far and away the most important development in Iraq is the new Hydrocarbon Law which is expected to pass in 2007. The law, the terms of which have been widely reported, recognises the need to develop Iraq's vast oil resources using international technology and capital. The necessary debate between the various parts of the country as to how oil reserves are controlled and distributed is ongoing and is expected to be resolved in the near term.

Currently Petrel is busy with the large oil field development at Subba and Luhais. This development, the largest awarded in recent years by the Iraqi Oil Ministry, will produce 200,000 barrels of oil a day and 120 million cubic feet of gas when commissioned in 2010 and will cost about $197 million. Most of the work to date has been in engineering design, plant layout and design and project team mobilisation. The Iraqi Ministry of Oil currently produces oil at lower production rates from these fields.

Apart from our work in Subba and Luhais, we are active on the Merjan oil field technical agreement. We were awarded this contract as part of a very good programme whereby the Iraqi authorities ask international oil companies to analyse and evaluate selected undeveloped or complicated oil discoveries. Because of work carried out by Petrel on our Block 6 exploration concession, the authorities commissioned Petrel to study Merjan some 45 km east of Block 6. During 2006, we reprocessed over 500 kms of seismic and conducted structural, stratigraphic, petrophysical and petroleum engineering studies. The final report was presented in May 2007. An additional study is being considered.

We have worked on Block 6 in the western desert of Iraq since 2000. This 10,000 sq km block has had only exploratory seismic surveying and no drilling. Our work suggests that there is significant hydrocarbon potential. Though we signed an agreement on Block 6 with the Oil Ministry in Baghdad we expect the contract to change to reflect the better terms in the new law.

Further, in recent years we have worked with the Oil Ministry to upgrade their technical, financial and commercial skills. This involves Petrel running courses employing world class instructors to work with their technical staff. The courses have been held in Amman and Istanbul.

Partner

We have a significant partnership with ITOCHU of Japan. ITOCHU is one of Japan's leading upstream oil and gas companies. We have had a relationship for some years which was formalised in 2006 with the signing of a strategic partnership to cover future exploration activities in Iraq.

Jordan

For some years now Petrel has been looking at opportunities in Jordan. The work done by Petrel on Block 6 in Iraq showed similar geology and, we hope, for similar opportunities in Jordan close to the Iraq border. In 2005, Petrel signed an initial agreement with the Jordanian authorities on the East Safawi Block, an 8,750 sq km area adjoining the Risha gas field. In May 2006 we negotiated the terms of a Production Sharing Agreement (PSA) which was finally signed in May 2007. The PSA provides for a three year exploration phase leading to drilling. We are currently reprocessing and reinterpreting seismic and well logs. This will be followed by new seismic. Commercial terms are good in Jordan.

CHAIRMAN'S STATEMENT

Future

Having operated in Iraq for the past 8 years we are sanguine about prospects. Much of the future of Iraq lies in oil development. All parties recognise this fact. The Hydrocarbon Law will pass. We expect to benefit from this in a number of ways, ratification of our Block 6 interests, the possibility of obtaining a PSA on Subba and Luhais and interesting opportunities in other projects which are likely to be put on offer.

Our foundations are built on our staff, who over the years have operated in a difficult environment and who have built strong relationships with executives in the Oil Ministry and with people in the country. Over the years we have demonstrated our commitment to Iraq. We are prepared to live, work and invest in the country and we have shown our technical ability to deliver world class projects. The people of Iraq need peace and stability. When they are ready to develop their industry we will be there to participate and grow with them.

John Teeling
Chairman
28th June 2007

MANAGING DIRECTOR'S REPORT

2006 was a crucial year for the development of Iraq's oil. The fully sovereign elected government took charge in May and developed a modern, rational Hydrocarbon Law. This was approved by the government early in 2007 and is expected to be ratified during 2007.

Petrel's long-standing objective since 1999 has been to secure and operate risk-sharing contracts to produce and explore for oil in Iraq. This now will become possible under clear legal title from a fully sovereign elected government in Baghdad.

Commentators focus on disagreements over detail, such as the requirement that ultimate authority rests with the Iraqi Government and its Ministry of Oil, but in contrast to conventional wisdom, it is more striking how much progress has been made recently and how much consensus has been achieved within the industry – given the challenging circumstances.

BACKGROUND

Petrel has been continuously active in Iraq since 1999 and is now considered one of the most established players in the Iraqi oil industry.

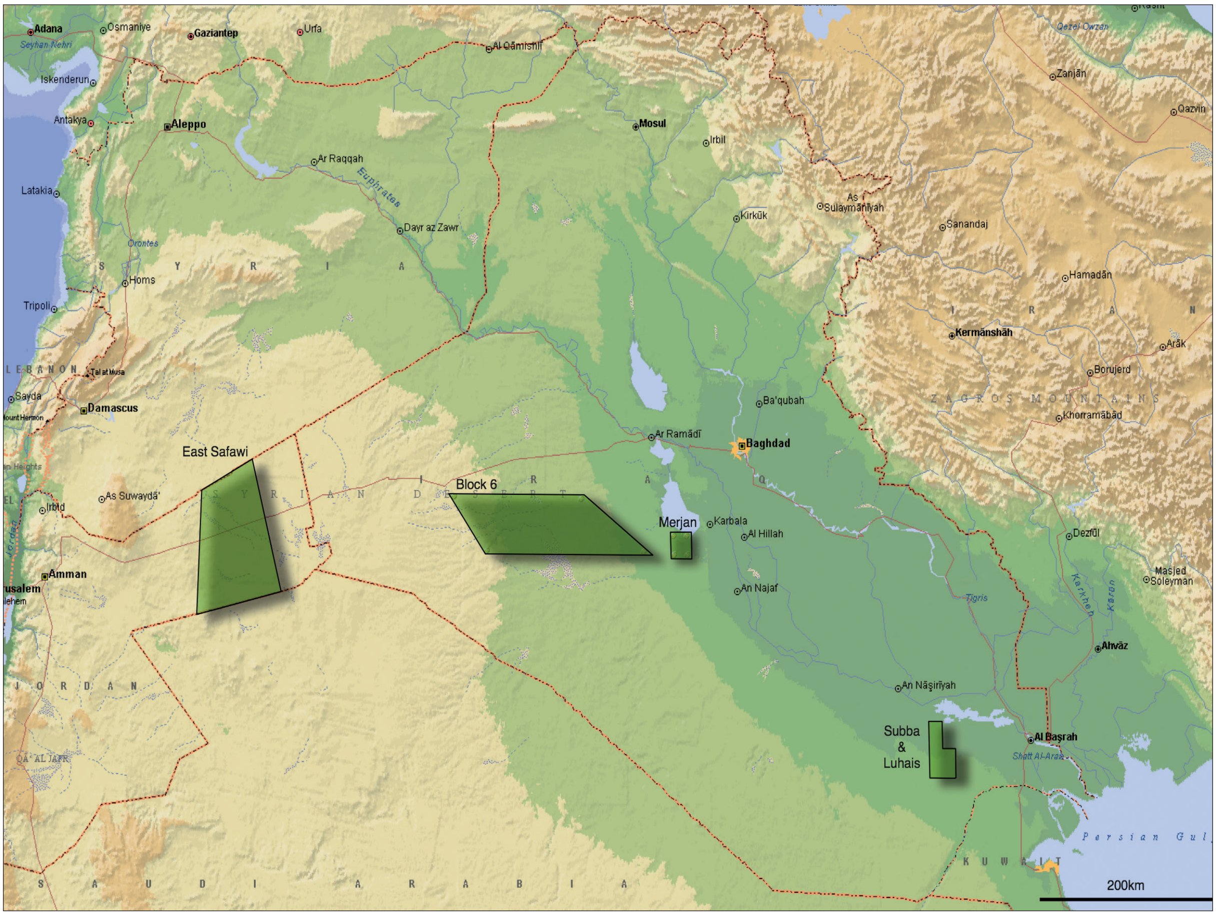

Image 2 – Regional Map of Petrel's Interests

MANAGING DIRECTOR'S REPORT

We operate the largest contract awarded by the Iraqi Ministry of Oil since 2003: the Subba & Luhais Engineering, Procurement and Supervision of Construction project in the south of Iraq, near Basra.

Petrel also operates a Technical Co-operation Agreement on the Merjan Oil Field in the centre of Iraq and provides training and technical support to the Ministry. The initial programme is now complete and we have agreed to extend co-operation.

The status of pre-war contracts, including Petrel's working agreement on Western Desert Block 6 which was signed by Petrel in 2002, awaits confirmation. We expect that appropriate pre-war contracts will be brought into line with the new law, which is more favourable for investors.

Petrel works only with the legitimate Iraqi authorities, especially the professional Ministry of Oil. We have always honoured the exclusive right of the Iraqi people and government to regulate their industry and conduct business with approved players.

The southern Iraqi oil fields continue to produce just over 2 million barrels daily. Iraq continues to export circa 1.5 million barrels daily. Work is conducted by the Iraqi Ministry of Oil and a limited number of contractors, who are acceptable to local communities.

SUBBA & LUHAIS OIL FIELD DEVELOPMENT SERVICES CONTRACT

The Subba & Luhais oil field development services project is currently Petrel's main operation and remains the largest oil-processing project awarded by the Iraqi Oil Ministry this century.

The development of the Subba & Luhais oilfields will provide a minimum capacity of 200,000 barrels of oil per day and 120 million cubic feet of associated gas. This $197 million development services contract continues on schedule with the objective of ensuring that all design work, supplies and services are delivered during the 1st Quarter of 2008.

The Iraqi Ministry of Oil State Company for Oil Projects (SCOP) is preparing the lengthy construction program at the four main processing sites for an anticipated completion during 2009. Petrel will support SCOP during the construction phases of the project. As the principal services contractor Petrel will commission the plants for handover to the Iraqi Ministry of Oil's Southern Oil Company (SOC) for operation.

Our work proceeds well and on schedule. As a result of the efforts by the Iraqi Ministry of Oil engineering (SCOP) and operating (SOC) companies to maintain and increase local production at the Luhais Central field facilities, we have also been asked to design and integrate the new facilities with the existing plant and operations. This will also provide for a fully integrated plant with common safety and operating systems.

Though political events complicate activity, the Subba & Luhais area is relatively calm and we have encountered no insuperable security problems when accessing the site. We maintain our Baghdad office but there are limitations on mobility in the centre of Iraq, especially for non-Arabs.

MANAGING DIRECTOR'S REPORT

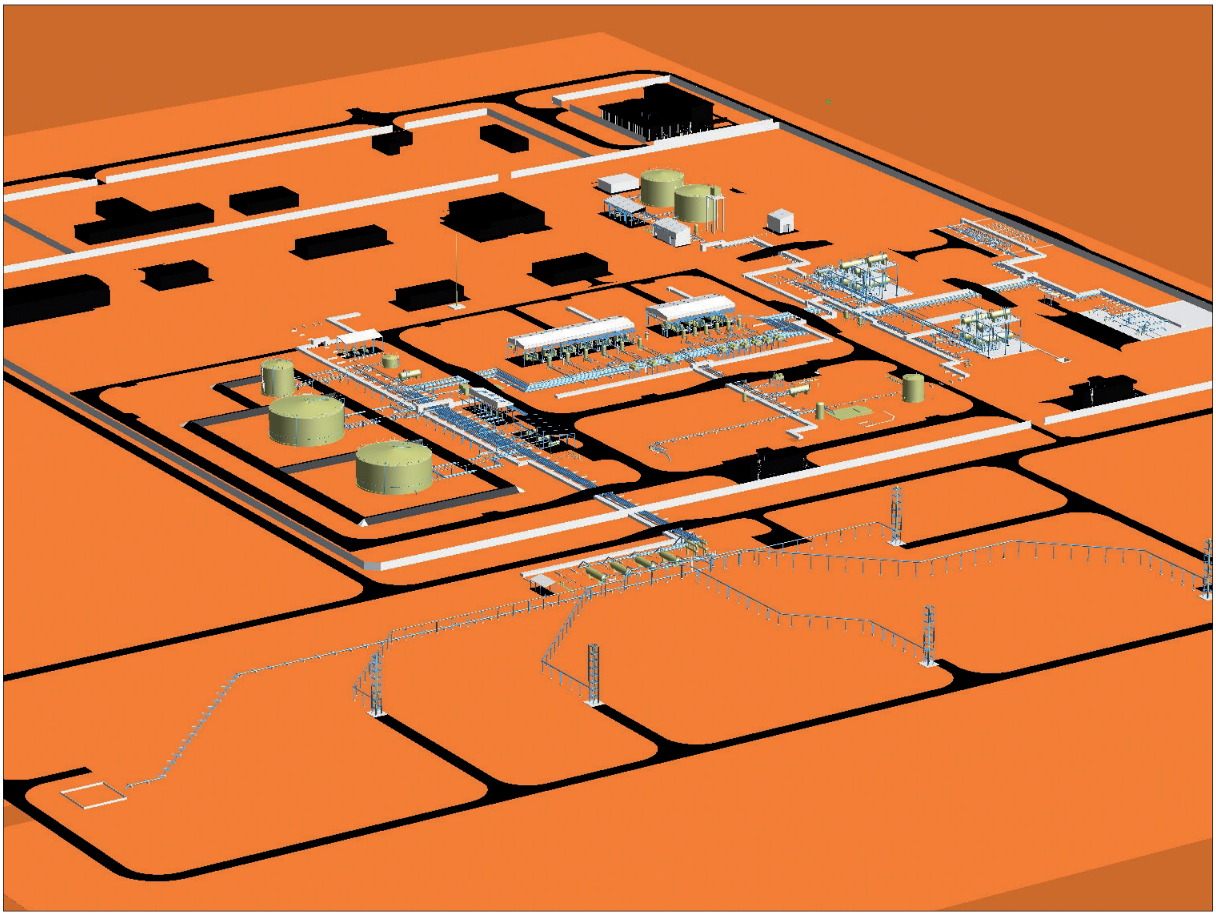

Image 3 – Full Layout of the Subba & Luhais Re-development

We maximise local content where feasible and have developed relationships with local companies and technical personnel. At the request of SCOP, Petrel entered into a Joint Venture arrangement with a major Iraqi company. We have entered the procurement phase of the project, utilising their experience with suppliers for similar developments in Iraq (Khurmala and Himrin).

The project team has grown and now manages the detailed design and manufacturing phases of the project. Forthcoming challenges for logistics and deliveries site are being planned for deliveries of long lead equipment during the 4th Quarter 2007.

The project is mobilised at our various work locations and the main milestones and achievements are summarised:

- Project Management team is mobilised (England, Italy, Turkey and Iraq).
- Joint Venture relationship with local Iraqi partners.
- The $197m Letter of Credit from the Trade Bank of Iraq is opened and is being drawn down.
- We are due and expect to receive an interim milestone payment for the completion of the Basic Design Package for circa $10 million (less contract deduction).

MANAGING DIRECTOR'S REPORT

- Front End Engineering Design (FEED) is complete and Detailed Design is underway in Fano, Italy with ENERECO our Design Contractor. Periodic Technical discussions and meetings with SCOP and SOC continue and have been productive. We hope to work ever more closely with the technical experts of the Ministry of Oil.
- The layouts for the Luhais and Subba processing plants are being updated and finalised and being integrated with the SOC existing operations and requirements.
- Safety reviews have been completed by a joint committee of Petrel, SCOP and SOC and the projects design and operational basis found to be acceptable and meeting the requirements and guidelines of good international oilfield practices.
- No insuperable security problems have yet been encountered. Logistical, offices, services, and resources in Iraq are continuing to be further expanded and developed.
- Work Sites are mobilised and Detailed Design Engineering commenced.

In the 4th Quarter of 2006, Petrel and the JV partner held technical meetings with the Iraqi Ministry of Oil State Company for Oil Projects (SCOP) and the Ministry's South Oil Company (SOC) to present and complete a final review of the Basic Design Package (BDP) documentation and drawings for the Project and the Level 1 plan and schedule.

In December 2006, the BDP was signed off and accepted by SCOP and SOC allowing us to commence FEED and Detailed Design. As a result of the reviews with SCOP and SOC, other design and operational aspects were discussed and formulated to enable the integration of the new Luhais Central oil processing and gas export systems with the existing Luhais plant. SCOP/SOC have implemented and installed additional plant to allow operation and maintainability of the production from Luhais in the last few years (circa 50,000 barrels of oil daily). Hence, an organised integration of the facilities and the control and safety systems is required to ensure continuation of production and commonality of control and safety aspects. This additional work program is now being added into the Project scope.

We anticipate completion of the Detailed Design for the Project in 4th Quarter 2007.

Early involvement of major suppliers (such as for the Gas Compression Systems) for the long lead equipment items has yielded benefits, both commercial and promptness of deliveries. Final assembly of the 18 Gas Compressor packages, supplied by GE Thermodyne, are scheduled for the third quarter of 2007, with deliveries to site soon afterwards. Pipeline material supplies (circa 34,000 tonnes and 600kms of pipe), have been established with deliveries also scheduled for the 4th quarter of 2007. While, due to the very busy manufacturing situation in the markets, deliveries are generally extending we are confident that Petrel will meet the SCOP requirements for deliveries to match their requirements for the Construction and Operation of the new facilities.

Our efforts now are focused on placing orders and maintaining delivery schedules and budgets with support from worksites in Europe and the Middle East.

Hence, our project focus to the year-end 2007 is primarily:

- Completion of Detailed Design in 4th quarter of 2007, with a continuation of follow-on engineering support as required by SCOP.

MANAGING DIRECTOR'S REPORT

- Tendering, negotiating and securing equipment and material delivery conditions for the Equipment and Bulk Material items and ancillaries specification and within budget.
- The subsequent follow on engineering, site supervision during the construction phase, will continue as required by SCOP into 2008 and 2009.

We will be challenged to maintain schedules given the tight market situation. We will adapt and make prompt decisions to secure supplies. A professional working relationship and co-operation with SCOP also enables Petrel to introduce new suppliers in the manufacturing business as well as suppliers from emerging economies beyond the Middle East.

Image 4 (a) & (b) – Subba & Luhais Gas Compressors Ready for Shipment

As with banking and other operations, the valuable experience gained will enhance and support Petrel's future operations in Iraq.

Project Financing: Letters of Credit opened with the Trade Bank of Iraq and withdrawals made.

In March 2006 we agreed with the Iraqi Ministry of Oil (SCOP) and the Trade Bank of Iraq (TBI) the final conditions and procedures for their receipt of the Project Guarantees and Bonds. The Project Letter of Credit (LC) from the TBI was issued in April 2006 and cash withdrawals have been made and are being processed for supplies - as per Petrel's contract with the Ministry of Oil.

We have also established a direct relationship with the TBI for them to issue Letters of Credit on our behalf, through a major European Bank to our suppliers for major equipment and supplies.

Current and working accounts have been established in Iraq, Dubai and the United Arab Emirates to handle project cash flows and financing arrangements.

MANAGING DIRECTOR'S REPORT

Joint Ventures with Local Partners

We are committed to working closely with the local community and Iraqi partners. Petrel was encouraged by the Management of SCOP to involve an experienced Iraqi group, to avail of their local experience and provide logistical and other support. Accordingly, a Joint Venture (JV) with Makman was signed in December 2005.

Structures and responsibilities within the Joint Venture Company have been established with Petrel maintaining overall Project Management and Engineering definition. Our JV partner brought their experience to the project with extended vendor lists and experience based on their involvement in other Iraqi oil field projects.

Work sites are established and personnel mobilised and working in Project offices in Baghdad, London, Italy and Istanbul with further support from our own corporate office and Makman's office in Erbil, northern Iraq.

Security

Security risks are manageable in the south of Iraq.

Subba & Luhais oil fields are located in the relatively calm region of southern Iraq north-west of Basra. We have experienced no difficulties with local people and expect to be able to continue working in the locality. The Iraqi authorities and community forces encourage our activities and are supportive. Professional support services, including security, are available from local people.

Site location is about ninety minutes by good roads from Basra, whose port facilities can also be supplemented by neighbouring Kuwait. This local infrastructure provides excellent staging points for transportation, deliveries and services to support our work program.

Support for the elected government in this area of Iraq is high. It does not share the security challenges of central Iraq or the legal complications of the Kurdish-speaking area of Iraq. The area is flat desert with good road and pipeline infrastructure.

Technical and Financial Co-operation

Petrel has been successfully involved in training and transfer of technology with the Ministry of Oil for several years. Technical courses have been run in Europe and the Middle East. At the Ministry's request, from 2005 to 2007 Petrel provided training on possible legal and financial structures for future development of the Iraqi oil industry, sequence stratigraphy and state-of-the-art geological concepts and tools.

The Ministry takes technology transfer seriously. Iraqi officials participating were of a high level of skill and participated enthusiastically. Material was covered in greater detail and intensity than in leading universities – albeit with a more practical focus on Iraq's particular circumstances. They saw the potential to learn from past experiences of managing oil fields in neighbouring countries, as well as experience from more difficult operations in less attractive producing areas worldwide. They expect the same boost in production performance from applying best international practice as Russian fields experienced from applying the 'Texan toolkit' post 1991. The political events,

MANAGING DIRECTOR'S REPORT

which delayed development of Iraq's oil industry, may ironically lead to much higher recoveries than would otherwise have occurred.

As part of the Framework of Case Study agreement Petrel Resources undertook two technology transfer Training Courses for Ministry staff. Ten staff members attended each intensive course, which took place in Istanbul during January and March 2007. The courses were:

1: Understanding Seismic: Seismic for Non-Geophysicists.
2: Modern geological concepts in petroleum exploration.

In April 2007, Petrel was asked to continue this technical co-operation support and training to the Iraqi Ministry of Oil. We expect that the next phase of this co-operation will involve the study of a southern Iraqi oil field and begin in July 2007. ITOCHU will continue to participate, under our general co-operation agreement.

ITOCHU

Petrel has received considerable support from the leading Japanese conglomerate, ITOCHU. We have gotten to know ITOCHU well over several years and developed valuable technical relations with many senior staff. There is a near perfect fit with Petrel's activities in Iraq. ITOCHU, one of Japan's leading companies, with its strong balance sheet and long-term perspective, is a strong player in upstream oil and gas business. There is no better partner for us in our quest to expand and deepen our Iraqi activities.

During 2006, Petrel Resources signed a strategic partnership and co-operation agreement with ITOCHU Corporation. The strategic partnership will cover future exploration and development activities in the Iraqi oil and gas industry.

ITOCHU is one of the largest and most respected Japanese conglomerates. ITOCHU launched its upstream activities in Indonesia and Sakhalin Island in the 1970s and has been a successful player in the upstream energy sector ever since through its active participation in the challenging environments of Algeria and Azerbaijan, as well as other oil producing regions such as the North Sea and Western Australia. In addition to its upstream activities, the ITOCHU group is also one of the largest traders of crude oil in the Far East and is a major force in numerous business sectors, including areas such as steel pipe supply, finance, logistic and plant businesses.

The co-operation agreement between Petrel and ITOCHU initially covered work on the Merjan oil field under a Technical Co-operation Agreement with the Iraqi Ministry of Oil, subject to applicable laws. ITOCHU will also have a first look at future Petrel projects in the Iraqi oil & gas upstream sector.

As part of the co-operation agreement, ITOCHU will contribute towards Petrel's historic costs in the Iraqi oil & gas sector and will cover a fixed share of the costs of the current study.

A fuller Corporate Profile is available on the ITOCHU website at:
http://www.itochu.co.jp/main/index_e.html

MANAGING DIRECTOR'S REPORT

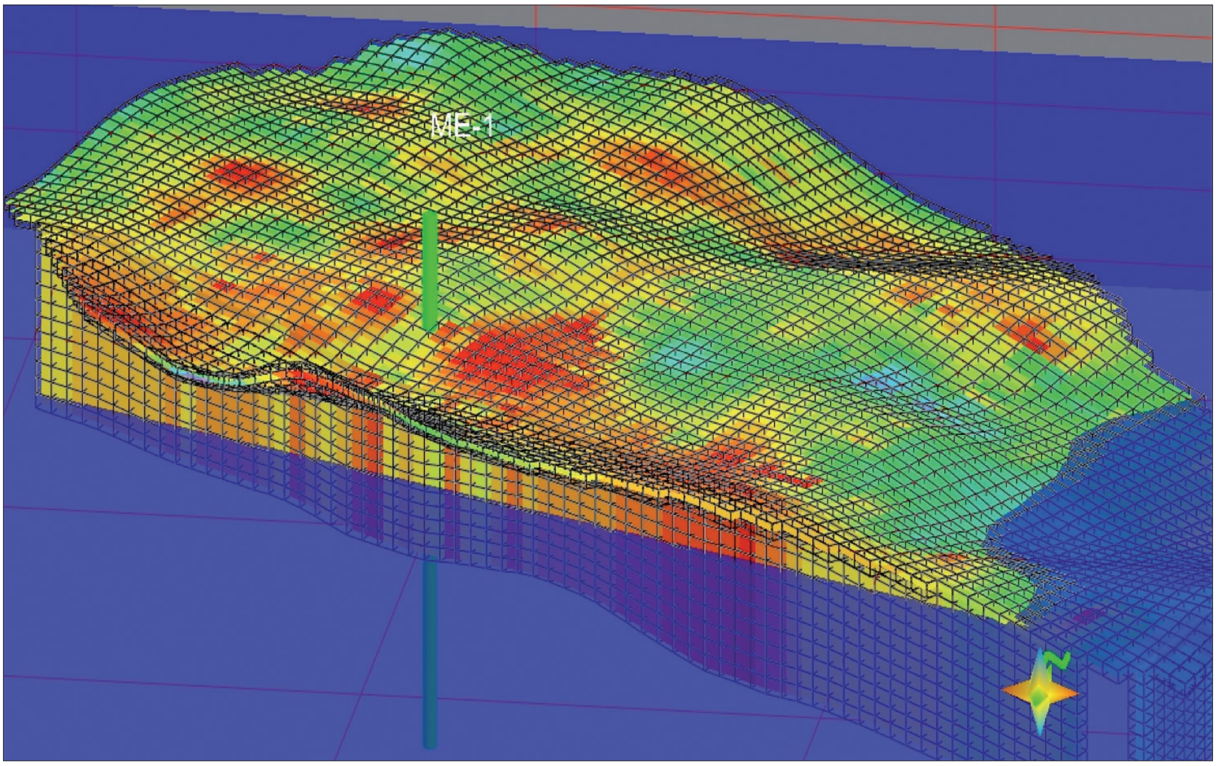

Image 5 – Fugro-Jason (UK) Ltd. Modelling of Seismic Data on the Merjan Block

IRAQI EXPLORATION

Merjan Oil Field Technical Co-operation Agreement

In 2005, Petrel signed a Framework of Case Study (Technical Co-operation Agreement) with the Iraqi Ministry of Oil's to study the Merjan Field Block between Kerbala and Western Desert Block 6. This undeveloped field was discovered in 1983 at shallow stratigraphic levels while drilling.

Technical Co-operation Agreements give no formal rights, but provide confidential access to much-coveted data on some of the world's highest potential oil prospects.

The Merjan Oil Field Block in central Iraq is 45km east of Block 6 and falls within the regional work Petrel has already conducted.

The Iraqi Ministry of Oil has successfully used co-operation Framework of Case studies to extend their understanding of existing undeveloped discoveries and problematic oilfields within Iraq.

The Merjan Block lies in a geologically interesting zone astride the boundary between the productive Mesopotamian Basin and the largely unexplored Western Shelf. In 1983, a discovery well within the block (Me-1) was drilled seeking Jurassic reef reservoirs, but discovered oil in the shallow Upper Cretaceous Hartha Formation. The principal aims of the Merjan co-operation study were to determine the oil entrapment mechanism in the Me-1 well and to estimate possible reserves in the oilfield.

MANAGING DIRECTOR'S REPORT

In May 2006, the Ministry of Oil/Petrel Steering Group finally formally started the work programme.

Seismic and well data relating to the Merjan project were downloaded onto Petrel's contractors' workstations in Amman, Jordan, during summer 2006. Arising out of the original work programme, Petrel and its partner ITOCHU suggested enhancing the seismic data with state-of-the-art inversion work, which extended the work programme until February 2007.

The final report on the project was presented to the Ministry of Oil Steering Group in May 2007. Approximately 500 km of seismic data were reprocessed by the Geophysical Service Center (GSC), Amman, and interpreted by Petrel staff with the assistance from GSC personnel. Petrel conducted Landsat structural interpretation and detailed stratigraphic studies, together with petrophysical and petroleum engineering analysis of the well data.

In order to determine the limits of porosity in the Hartha oil reservoir Petrel commissioned Fugro-Jason in London to carry out acoustic impedance inversion of the seismic data and subsequently to undertake modeling of the data to determine the reservoir volumetrics. The final report to the Ministry of Oil included all the detailed technical studies, together with conclusions and recommendations for future work.

NEXT STEPS

All players in the Iraqi oil industry are keen to boost Iraqi oil production.

This can only be done in a reasonable time with international investment, technology and skills. Iraq's oil infrastructure has been depleted by 20 years of wars and sanctions, and most of it requires significant upgrading. Technical experts are over-stretched and under pressure because of security and travel restrictions. Without external help, it will take decades to regenerate the oil industry to the high level of, say, Saudi Arabia today.

Iraqi practices arise out of these difficult circumstances. Gas is being flared including oil-condensate. Anywhere else the valuable liquids would be stripped-out and the gas sold, used to generate power for the grid or re-injected to boost oil production and for future use.

The Iraq government is expected to offer risk-sharing arrangements under a new Hydrocarbon Law (approved by the Iraqi Government in January 2007 and is expected to pass through Parliament shortly).

It is not feasible to develop the Iraqi oil industry in a reasonable time using 'multiple service contracts'. Even under the most optimum circumstances, the bid process can be lengthy: taking Petrel's Subba & Luhais EPC project, for example, this was first discussed during the 1990s, while tender documents were issued in 2004. Following updates, meetings and clarifications, the contract was formally awarded in September 2005, and signed in December 2005. The Project Letter of Credit was not opened until March 2006. Getting Ministry sign-off on detailed design, etc. is also a lengthy process. Friction in the system lengthens development time. This implies no criticism of brave and diligent Iraqi technicians, who do an impressive job in challenging circumstances. Without solidarity of the international oil industry they are being asked to do the impossible.

MANAGING DIRECTOR'S REPORT

Better to give contractors a mission and incentives and let the private sector worry about how to deliver the project.

Likewise picking the lowest bid rarely delivers the highest value in complex oil & gas projects and provides little incentive for contractors to accelerate the work. The lowest bid involves basic equipment of minimum acceptable standard delivered piecemeal. Project returns are maximized by reducing the overall system cost: skid-mounted equipment, high reliability standards for key packages, built-in redundancy for cheap items and spares.

Iranian-style Buy-Back arrangements pander to nationalistic sentiment but leave oil in the ground by encouraging contractors to minimize time and risk by not fine-tuning new techniques to unique circumstances. Much of the oil left behind will never be recovered. Project returns and policy objectives (environmental, supply maximisation, safety) are maximized by aligning the contractors' interests with those of Iraq.

Those prepared and able to work immediately in Iraq should be awarded risk-sharing incentives (Production Sharing Agreements or equivalent). Terms should offer adequate risk-adjusted returns to raise equity and debt.

Passing the Hydrocarbon Law & Negotiating Contracts
Iraq's hydrocarbons belong to the Iraqi people. There is no prospect of appropriating state property or infringing Iraqi sovereignty over the medium-term.

The passionate debate over Iraqi oil and the Hydrocarbon Law is really a re-run of the debate over the 2003 war. Nationalists, NGOs and the anti-war lobby are convinced that Anglo-US companies will be unfairly favoured. Ironically, the bitterness generated by the conflict has made it impossible for such companies to work in Iraq for the near term.

Missing from the debate is a realisation of the enhanced value from new technology. In some cases, modern techniques can double overall oil recoveries. Most of this would otherwise never be recovered – and dramatically boosts economic returns from oil projects. The corporate profit share should be set at the level required to attract investment. The size of the cake should be the focus – not the required rate of return for contractors.

Iraqi Hydrocarbon Law
The Hydrocarbon Law is revolutionary in that it envisages and prepares for full participation by international players in exploring for and developing Iraqi oil & gas. Possible model contracts drafted include:

- Exploration & Production Contracts
- Field Development Contracts
- Exploration & Development Contracts
- Development & Production Contracts

These detailed and well-written laws and contracts clarify future investment parameters. They reflect best practice internationally recognising the reality of resource nationalism but also the

MANAGING DIRECTOR'S REPORT

need to attract investors and technology by offering adequate risk-adjusted returns. Exact terms are to be negotiated on a field-by-field basis. The authorities naturally want early work conducted, so logically should focus on those players ready to deliver.

Objections that the Iraqi authorities were intimidated or misled by foreigners are untrue. Ministry staff are highly sophisticated and include natural negotiators. In 2005, Petrel provided detailed training on financial analysis and negotiating techniques. The key module was provided by AUPEC, a consulting group linked to the University of Aberdeen, which normally advises governments. The course ended with a detailed computer game, during which negotiators assessed how different approaches impacted Iraq. The impact was quantified and issues debated.

It is likely that early players will receive more favourable terms than will be available when the security situation has calmed. It is possible that early contracts will subsequently be re-negotiated if a future Iraqi Government considers them too generous.

In the meantime, outstanding issues like the role of the Iraqi National Oil Company or influence of regional authorities will have little impact on Petrel's projects. Petrel has always worked closely with the Ministry of Oil in Baghdad. We did not take oil-for-food contracts under sanctions and do not deal with regional authorities. This greatly simplifies operations and minimises risk.

Criticism of the law has rarely concentrated on its provisions. The debate has been a proxy-fight among those disagreeing about federalism vs. central control, withdrawal date for Coalition military, and especially how Iraq will be run. Nevertheless, any government will have similar objectives: to increase oil production and exports as soon as possible.

Critics refer to the role of foreign consultants in shaping the oil law in Iraq. But the Iraqi Ministry took soundings industry-wide and studied other situations and available options carefully. Iraqi technocrats are well-informed patriots, conscious of the need to develop while maintaining sovereignty. They will not be rolled over by super-majors, as nationalists and critics fear.

EAST SAFAWI BLOCK, JORDAN

Petrel's work in the Iraqi part of the Arabian Desert opened opportunities in neighbouring countries. In particular, the Jordanian Natural Resources Authority works hard to attract explorers for gas and particularly oil. Construction of the Arab Gas Pipeline integrates Jordan into the regional gas network and eventually to Turkey and the European market. The Risha gas pipeline and inoperative Haifa oil pipeline (last operated in 1948) already runs through East Safawi, as will future export pipelines from Iraq.

Petrel signed a Memorandum of Understanding (MOU) with the Jordanian Natural Resources Authority (NRA) in 2005. This covered an 8,750 sq. km. area, known as the East Safawi Block, in the Jordanian panhandle adjoining the Jordanian National Petroleum Company Risha Block, which contains the producing Risha gas field.

MANAGING DIRECTOR'S REPORT

Technical work convinced Petrel that the East Safawi Block has hydrocarbon potential at several stratigraphic levels. Oil targets are in shallow formations while there are well-established gas plays at deeper levels. Accordingly, Petrel formally applied for conversion of the MOU to a Production Sharing Agreement (PSA) under terms negotiated with the NRA.

This is a time of resource nationalism worldwide, with sensitivities over foreign activities. Petrel's PSA provoked neither Parliamentary questions nor adverse comment in the local press. This smooth passage displays the advantages of engaging with local people and transparency in operations – as well as the diligent work of the NRA. The PSA was signed in the presence of King Abdullah in May 2007 at the World Economic Forum.

Jordanian production sharing terms are world class. The contractor receives 60% of oil production – or gas equivalent – up to 10,000 barrels daily, with a sliding scale to a 35% share of production over 100,000 barrels daily.

The Production Sharing Agreement allows for a 3 year first exploration phase. Initial work includes seismic reprocessing and reinterpretation as well as new seismic. Targets identified will be followed up by drilling. Work already completed by Petrel on the block suggests a number of exploration targets. Drilling could possibly occur in 2008 or more likely early 2009, depending on operational developments.

Image 6 – Topography of the East Safawi Block

MANAGING DIRECTOR'S REPORT

The main elements of the first year's work programme on East Safawi are to complete the re-processing and interpretation of the available seismic data, initiated during the MOU, and to make detailed studies of the logs and rock samples from the four existing widely spaced wells on the block. These will include Apatite Fission Track Analysis (AFTA), maturation and petrophysical studies.

The work programme for years 2 and 3 of the PSA calls for acquisition and interpretation of new seismic data, prior to drilling a well. Petrel technical staff has recently collected the data and samples necessary to initiate this work. The company intends to use cutting-edge oil industry technologies and concepts to identify drillable targets on the East Safawi Block.

Jordan is a good business location with generally normal security issues. The excellent support provided by the NRA and the general stable and encouraging work environment make Jordan an attractive country in which to operate.

FINANCE

The small loss, circa €416,000, is within projections and mainly due to investment in training and technical co-operation with the Iraqi Ministry of Oil. It does not include any revenue in connection with the Subba & Luhais contract, on which the Project Letter of Credit was opened and the initial $20 million received in April 2006.

We have prepared since the 1990s for the opportunity of risk-sharing contracts now opened up by the Iraqi Hydrocarbon Law.

Petrel will aggressively expand and deepen its exploration and development activities in Iraq as quickly as possible.

David Horgan
Managing Director
28th June 2007

REPORT OF THE DIRECTORS

The directors present their annual report and the audited financial statements for the year ended 31 December 2006.

REVIEW OF ACTIVITIES AND FUTURE DEVELOPMENTS

The company is engaged in oil and gas exploration. The company commenced development of an oil field in Iraq in the current year.

Further details of the group's activities and future developments are given in the chairman's statement.

RESULTS FOR THE YEAR

The consolidated loss for the year after taxation was €415,570 (2005 : loss after taxation €481,535).

The directors do not recommend that a dividend be declared for the year ended 31 December 2006 (2005: €Nil).

PERFORMANCE REVIEW

The performance review is set out in the Chairman's Statement and Managing Director's Report.

RISKS AND UNCERTAINTIES

The risks and uncertainties facing the group including political and security uncertainties are outlined in the Managing Director's Report. The realisation of these intangible assets is dependant on the successful development of economic reserves.

BOOKS OF ACCOUNT

To ensure that proper books and accounting records are kept in accordance with Section 202 of the Companies Act, 1990, the directors have employed appropriately qualified accounting personnel and have maintained appropriate computerised accounting systems. The books of account are located at the company's office at 162 Clontarf Road, Dublin 3.

DIRECTORS

The current directors are set out on the inside back cover.

There were no changes in directors or secretary during the year.

REPORT OF THE DIRECTORS

DIRECTORS' AND SECRETARY'S INTERESTS IN SHARES

The directors and secretary at 31 December 2006 held the following beneficial interest in the shares of the company:

	01/04/2007 Ordinary Shares of €0.0125	01/04/2007 Options- Ordinary Shares of €0.0125	31/12/2006 Ordinary Shares of €0.0125	31/12/2006 Options - Ordinary Shares of €0.0125	1/01/2006 Ordinary Shares of €0.0125	1/01/2006 Options - Ordinary Shares of €0.0125
	'000	'000	'000	'000	'000	'000
J. Teeling	3,615	1,900	3,615	1,900	3,615	1,900
D. Horgan	2,715	1,650	2,715	1,650	2,715	1,650
G. Delbes	240	-	240	-	140	100
J. Finn (Secretary)	1,015	870	1,015	870	1,015	870
S. Borghi	155	250	155	250	55	310

During the year, no share options were issued to the directors and secretary, and no share options lapsed.

On 9 February 2006, Mr Guy Delbes exercised options over 100,000 shares at Stg£0.025 each. On 6 March 2006 Stefano Borghi exercised options over 60,000 shares at Stg£0.05 each.

SUBSTANTIAL SHAREHOLDINGS

The share register records that, in addition to the directors, the following shareholders held 3% or more of the issued share capital as at 31 May 2007:

	Number of Ordinary Shares	%
HSBC Global Custody Nominee 813259	4,185,051	6.06%
Goodbody Stockbrokers Nominees Limited	3,798,364	5.50%
HSBC Global Custody Nominee 915810	3,340,000	4.83%
L. R. Nominees Limited	3,215,870	4.65%
Citibank Nominees (Ireland) Limited (CLRLUX)	3,007,980	4.35%
TD Waterhouse Nominee (Europe) Limited	2,991,791	4.33%
W. B. Nominees Limited	2,551,007	3.69%
Littledown Nominees Limited	2,425,401	3.51%

POST BALANCE SHEET EVENTS

On 6 March 2007,the company issued 1,633,713 shares at Stg£0.50 each.The proceeds were for working capital.

REPORT OF THE DIRECTORS

GOING CONCERN

The directors, having made the necessary enquiries, have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. The directors therefore propose the continued preparation of the financial statements on a going concern basis.

SUBSIDIARIES

Details of the company's subsidiaries are set out in Note 6 to the financial statements.

AUDITORS

Deloitte & Touche, Chartered Accountants, will continue in office as auditors in accordance with Section 160(2) of the Companies Act 1963.

Signed on behalf of the Board :

John Teeling
David Horgan } DIRECTORS

28th June 2007

STATEMENT OF DIRECTORS' RESPONSIBILITIES

Irish company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and the group and of the profit or loss of the group for that period. In preparing those financial statements, the directors are required to

- select suitable accounting policies for the group and the parent company financial statements and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper books of account which disclose with reasonable accuracy at any time the financial position of the company and to enable them to ensure that the financial statements are prepared in accordance with accounting standards generally accepted in Ireland and comply with Irish statute comprising the Companies Acts, 1963 to 2006 and the European Communities (Companies : Group Accounts) Regulations 1992. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF PETREL RESOURCES PLC

We have audited the financial statements of Petrel Resources Plc for the year ended 31 December 2006 which comprise the Consolidated Profit and Loss Account, the Consolidated Balance Sheet, the Company Balance Sheet, the Consolidated Cash Flow Statement, the Statement of Accounting Policies and the related notes 1 to 20. These financial statements have been prepared under the accounting policies set out in the Statement of Accounting Policies.

This report is made solely to the groups members, as a body, in accordance with Section 193 of the Companies Act, 1990. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The directors are responsible for preparing the financial statements, as set out in the Statement of Directors' Responsibilities, in accordance with applicable law and accounting standards issued by the Accounting Standards Board and published by the Institute of Chartered Accountants in Ireland (Generally Accepted Accounting Practice in Ireland).

Our responsibility, as independent auditors, is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view, in accordance with Generally Accepted Accounting Practice in Ireland, and are properly prepared in accordance with Irish statute comprising the Companies Acts, 1963 to 2006, and the European Communities (Companies: Group Accounts) Regulations, 1992. We also report to you whether in our opinion: proper books of account have been kept by the company; whether, at the balance sheet date, there exists a financial situation requiring the convening of an extraordinary general meeting of the company; and whether the information given in the Directors' Report is consistent with the financial statements. In addition, we state whether we have obtained all the information and explanations necessary for the purposes of our audit and whether the groups balance sheet is in agreement with the books of account.

We also report to you if, in our opinion, any information specified by law regarding directors' remuneration and directors' transactions is not disclosed and, where practicable, include such information in our report.

We read the other information contained in the annual report and consider the implications for our report if we become aware of any apparent misstatement or material inconsistencies with the financial statements. The other information comprises only the Chairman's Statement, the Managing Director's Report and the Directors' Report. Our responsibilities do not extend to other information.

BASIS OF AUDIT OPINION

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF PETREL RESOURCES PLC

an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements and of whether the accounting policies are appropriate to the group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we evaluated the overall adequacy of the presentation of information in the financial statements.

FUNDAMENTAL UNCERTAINTY
In forming our opinion we have considered the adequacy of the disclosures made in notes 5 and 6 to the financial statements concerning the valuation of intangible fixed assets. The realisation of the intangible fixed assets of €3,410,242 (2005: €4,919,367) included in the consolidated balance sheet and of the intangible and financial assets of €3,410,242 (2005: €4,333,799) included in the company balance sheet is dependent on the successful development of economic reserves including the ability to raise sufficient finance to develop the projects. In view of the significance of this uncertainty we consider that it should be drawn to your attention. Our opinion is not qualified in this respect.

OPINION
In our opinion the financial statements:

- give a true and fair view, in accordance with Generally Accepted Accounting Practice in Ireland, of the state of the affairs of the company and the group as at 31 December 2006 and of the loss of the group for the year then ended; and
- have been properly prepared in accordance with the Companies Acts, 1963 to 2006 and the European Communities (Companies: Group Accounts) Regulations, 1992.

We have obtained all the information and explanations we considered necessary for the purpose of our audit. In our opinion proper books of account have been kept by the company. The company's balance sheet is in agreement with the books of account.

In our opinion the information given in the Directors' Report is consistent with the financial statements.

The net assets of the company, as stated in the company balance sheet are more than half the amount of its called-up share capital and, in our opinion, on that basis there did not exist at 31 December 2006 a financial situation which, under Section 40(1) of the Companies (Amendment) Act, 1983, would require the convening of an extraordinary general meeting of the company.

Deloitte & Touche
Chartered Accountants and Registered Auditors
Deloitte & Touche House
Earlsfort Terrace
Dublin 2
28th June 2007

STATEMENT OF ACCOUNTING POLICIES

The significant accounting policies adopted by the company are as follows:

BASIS OF PREPARATION
The financial statements are prepared in accordance with the historical cost convention, the relevant Statements of Recommended Practice for the oil and gas industry, other applicable accounting standards generally accepted in Ireland and Irish statute comprising the Companies Acts, 1963 to 2006 and the European Communities (Companies: Group Accounts) Regulations, 1992.

BASIS OF CONSOLIDATION
The consolidated financial statements consolidate the financial statements of the parent company and all its subsidiary undertakings made up to the end of the financial year. Undertakings in which the parent company can exercise a dominant influence over the undertaking are included in the consolidated financial statements.

The group has certain contractual arrangements with other participants to engage in joint activities that do not create an entity carrying on a trade or business of its own. The group includes its share of assets, liabilities and cash flows in such joint arrangements, measured in accordance with the terms of each arrangement, which is usually pro-rata to the group's risk interests in the joint arrangement.

DEFERRED DEVELOPMENT EXPENDITURE
Exploration costs are capitalised until the results of the projects, which are based in geographic areas, are known. Exploration costs include an allocation of administration and salary costs as determined by management. If the project is successful, then the related exploration costs are written off over the life of the estimated oil reserve on a unit of production basis. Where a project is terminated, the related exploration costs are written off immediately.

STOCK
Work in progress relates to costs incurred to date on the Subba 8 Luhais oil pipeline and is stated at the lower of cost and net realisable value. Amounts previously capitalised in deferred development relating to this project were transferred to work in progress.

Where the outcome of the construction contract can be estimated reliably, revenue and costs are recognised by reference to the stage of completion of the contract at the balance sheet date. Costs are measured by the proportion that contract costs incurred for work performed to date bear to the estimated total contract costs, except where this would not be representative of the stage of completion. The balance of payments received on account in excess of amounts matched with turnover and off set against long term work in progress balances is classified as payments on accounts and included within creditors.

Where the outcome of the construction contract can not be estimated reliably, contract revenue is recognised only to the extent of contract costs incurred. Furthermore it must be probable that such costs will be recoverable. Contract costs are recognised as expenses in the period in which they are incurred.

STATEMENT OF ACCOUNTING POLICIES

When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately.

FOREIGN CURRENCY
Monetary assets and liabilities denominated in foreign currencies are translated into Euro at the rate of exchange prevailing at the balance sheet date. Transactions in foreign currencies are recorded at the rate of exchange prevailing at the date of the transactions.

DEFERRED TAXATION
Deferred taxation is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date.

Deferred tax assets are only recognised to the extent that they are regarded as recoverable. They are regarded as recoverable to the extent that, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

SHARE ISSUE EXPENSES
Expenses arising on the issue of share capital are charged to the share premium account.

SHARE-BASED PAYMENTS
The group issues equity-settled share based payments to certain employees. The group has applied the requirements of FRS 20 “Share-based Payments”. In accordance with the transitional provisions, there is no charge to the profit and loss account relating to share-based payments as the company does not have any equity instruments granted after 7 November 2002 that had not vested by 1 July 2006.

CONSOLIDATED PROFIT AND LOSS ACCOUNT

FOR THE YEAR ENDED 31 DECEMBER 2006

	Notes	2006 €	2005 €
Administrative expenses		(483,108)	(521,255)
LOSS ON ORDINARY ACTIVITIES BEFORE INTEREST		(483,108)	(521,255)
Interest receivable and similar income	1	67,538	39,720
LOSS FOR THE YEAR BEFORE TAXATION	2	(415,570)	(481,535)
Taxation	3	-	-
LOSS FOR THE YEAR AFTER TAXATION	13	(415,570)	(481,535)
Loss per share - basic	4	(0.62c)	(0.77c)
Loss per share – fully diluted	4	(0.62c)	(0.77c)

All gains and losses are dealt with through the profit and loss account. Results derive from continuing operations.

The financial statements were approved by the Board of Directors on 28th June 2007 and signed on its behalf by:

John Teeling } DIRECTORS
David Horgan

CONSOLIDATED BALANCE SHEET
AS AT 31 DECEMBER 2006

	Notes	2006 €	2005 €
FIXED ASSETS			
Intangible assets	5	3,410,242	4,919,367
CURRENT ASSETS			
Stock – work in progress	7	10,396,141	-
Debtors	8	43,895	37,716
Cash at bank and in hand		9,450,875	3,729,121
		19,890,911	3,766,837
CREDITORS : (Amounts falling due within one year)	9	(15,957,136)	(1,718,353)
NET CURRENT ASSETS		3,933,775	2,048,484
NET ASSETS		7,344,017	6,967,851
CAPITAL AND RESERVES			
Called-up share capital	10	843,351	828,851
Capital conversion reserve fund	11	7,694	7,694
Share premium	12	9,840,861	9,063,625
Profit and loss account (deficit)	13	(3,347,889)	(2,932,319)
EQUITY SHAREHOLDERS' FUNDS	14	7,344,017	6,967,851

The financial statements were approved by the Board of Directors on 28th June 2007 and signed on its behalf by:

John Teeling
David Horgan } DIRECTORS

COMPANY BALANCE SHEET

AS AT 31 DECEMBER 2006

	Notes	2006 €	2005 €
FIXED ASSETS			
Intangible assets	5	3,399,005	4,322,562
Financial assets	6	11,237	11,237
		3,410,242	4,333,799
CURRENT ASSETS			
Debtors	8	2,977,540	37,716
Cash at bank and in hand		2,218,683	3,729,121
		5,196,223	3,766,837
CREDITORS : (Amounts falling due within one year)	9	(1,262,448)	(1,132,785)
NET CURRENT ASSETS		3,933,775	2,634,052
NET ASSETS		7,344,017	6,967,851
CAPITAL AND RESERVES			
Called-up share capital	10	843,351	828,851
Capital conversion reserve fund	11	7,694	7,694
Share premium	12	9,840,861	9,063,625
Profit and loss account - (deficit)		(3,347,889)	(2,932,319)
EQUITY SHAREHOLDERS' FUNDS	14	7,344,017	6,967,851

The financial statements were approved by the Board of Directors on 28th June 2007 and signed on its behalf by:

John Teeling

David Horgan

DIRECTORS

CONSOLIDATED CASH FLOW STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2006

	Notes	2006 €	2005 €
NET CASH INFLOW FROM OPERATING ACTIVITIES	16(a)	14,533,274	1,051,421
RETURNS ON INVESTMENT AND SERVICING OF FINANCE			
Interest received		67,538	39,720
NET CASH INFLOW FROM RETURNS ON INVESTMENTS AND SERVICING OF FINANCE		67,538	39,720
TAXATION			
Corporation tax paid		-	-
CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT			
Payments to acquire intangible assets		(10,023,638)	(2,700,958)
Receipts in respect of disposal of intangible assets		1,136,622	-
NET CASH INFLOW/OUTFLOW BEFORE FINANCING		5,713,796	(1,609,817)
FINANCING			
Issue of ordinary share capital		7,958	5,477,382
Share issue expenses		-	(136,131)
NET CASH INFLOW FROM FINANCING		7,958	5,341,251
INCREASE IN CASH	16(b)	5,721,754	3,731,434

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

1. INTEREST RECEIVABLE AND SIMILAR INCOME

	2006	2005
	€	€
Bank interest	67,538	39,720

2. LOSS ON ORDINARY ACTIVITIES BEFORE TAXATION

The loss on ordinary activities before taxation is stated after charging the following items:

	2006	2005
	€	€
Depreciation	-	596
Directors' remuneration		
- fees	100,000	78,000
- salary	144,000	148,000
Auditors' remuneration	15,000	9,500
Staff costs - salaries	11,162	13,434
- payroll taxes	-	3,222
Foreign exchange loss	10,427	57,798

The company had an average of one employee during the year.

All the groups expenditure relates to development projects in Iraq but arises in the Republic of Ireland.

Segmental Analysis

By geographical market	2006	2005
	Net assets	Net assets
	€	€
Iraq	6,963,930	6,633,068
Jordan	380,087	334,783
	7,344,017	6,697,851

3. TAXATION

	2006	2005
	€	€
Corporation tax	-	-
Loss for the year before taxation	(415,570)	(481,535)

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2006

3. TAXATION (continued)

	2006	2005
Loss on ordinary activities multiplied by the standard rate of tax in the Republic of Ireland of 12.5% (2005: 12.5%)	€ (51,946)	€ (60,192)
Effects of:		
Loss relief	51,946	60,192
Corporation tax payable	-	-

No charge to taxation arises in the current year as the company has not incurred a taxable profit.

No deferred tax asset has been recognised on accumulated tax losses as the recoverability of any assets is not considered likely in the foreseeable future. At the year end deferred tax assets totalling €262,461 (2005: €210,515) were not recognised.

4. LOSS PER SHARE

Basic earnings per share is computed by dividing the loss after taxation for the year available to ordinary shareholders by the sum of the weighted average number of ordinary shares in issue and ranking for dividend during the period. Diluted earnings per share is computed by dividing the loss after taxation for the year by the weighted average number of ordinary shares in issue, adjusted for the effect of all dilutive potential ordinary shares that were outstanding during the year.

The following table sets forth the computation for basic and diluted earnings per share (EPS):

	2006	2005
	€	€
Numerator		
Numerator for basic and diluted EPS retained loss	(415,570)	(481,535)
Denominator		
Denominator for basic EPS	67,314,450	62,463,194
Effect of diluted securities – options	-	-
Denominator for diluted EPS	67,314,450	62,463,194
Basic EPS	(0.62c)	(0.77c)
Diluted EPS	(0.62c)	(0.77c)

Basic and diluted EPS are the same in respect of 2006 as the effect of outstanding options is anti-dilutive and therefore excluded.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

5. INTANGIBLE ASSETS

	Group		Company	
	2006	**2005**	**2006**	**2005**
	€	**€**	**€**	**€**
Deferred development expenditure:				
Cost:				
Opening balance	4,919,367	2,218,409	4,322,562	2,218,409
Additions	3,421,929	2,700,958	3,302,716	2,104,153
Disposals	(1,997,409)	-	(1,292,628)	-
Transfer to work in progress	(2,933,645)	-	-	-
Transfer to subsidiary undertakings	-	-	(2,933,645)	-
Closing balance	3,410,242	4,919,367	3,399,005	4,322,562
Net book value:				
Opening balance	4,919,367	2,218,409	4,322,562	2,218,409
Closing balance	3,410,242	4,919,367	3,399,005	4,322,562

Deferred development expenditure at 31 December 2006 represents exploration and related expenditure in respect of projects in Iraq.

The realisation of these intangible assets is dependent on the successful development of economic reserves, including the ability to raise finance to develop the projects. Should this prove unsuccessful the value included in the balance sheet would be written off.

The directors are aware that by its nature there is an inherent uncertainty in such development expenditure as to the value of the asset. In addition, the current economic and political situation in Iraq is uncertain. Having reviewed the deferred development expenditure at 31 December 2006, the directors are satisfied that the value of the intangible asset is not less than net book value.

Regional Analysis – Group	**Iraq**	**Jordan**	**Total**
	€	**€**	**€**
At 1 January 2006	4,584,584	334,783	4,919,367
Additions	3,376,625	45,304	3,421,929
Disposals	(1,997,409)	-	(1,997,409)
Transfer to work in progress	(2,933,645)	-	(2,933,645)
	3,030,155	380,087	3,410,242

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

6. FINANCIAL ASSETS

	2006	2005
	€	€
Investment in subsidiary companies parent company		
Shares at cost - unlisted:		
Opening balance	11,237	11,237
Closing balance	11,237	11,237

The group consisted of the parent company and the following wholly owned subsidiaries as at 31 December 2006:

Name	Registered Office	Group Share	Nature of Business
Petrel Industries Limited	162 Clontarf Road, Dublin 3, Ireland	100%	Dormant
Petrel Resources of the Middle East Offshore S.A.L.	Damascus Street Beirut, Lebanon	100%	Dormant

The company has entered into a joint venture with Makman to develop the Subba and Luhais Development Project in Iraq. The company has ultimate control of this project and in accordance with FRS 2 it has been consolidated as a subsidiary.

7. STOCK

	Group		Company	
	2006	2005	2006	2005
	€	€	€	€
Work in progress:				
Opening balance	-	-	-	-
Transferred from deferred development expenditure	2,933,645	-	-	-
Expenditure incurred in period	7,462,496	-	-	-
	10,396,141	-	-	-

The replacement value of stocks does not differ materially from the amounts stated above.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

8. DEBTORS

	Group		Company	
	2006	2005	2006	2005
	€	€	€	€
Group and Company				
Amounts falling due within one year:				
VAT refund due	28,646	21,104	28,646	21,104
Other debtors	15,249	16,612	15,249	16,612
Amounts due from related subsidiary undertakings	-	-	2,933,645	-
	43,895	37,716	2,977,540	37,716

9. CREDITORS : (Amounts falling due within one year)

	Group		Company	
	2006	2005	2006	2005
	€	€	€	€
Project payments received on account	14,694,687	-	-	-
Accruals	1,229,169	1,718,353	1,229,165	1,132,782
Amount due to group undertaking	-	-	3	3
Other Creditors	33,280	-	33,280	-
	15,957,136	1,718,353	1,262,448	1,132,785

10. SHARE CAPITAL

	Group and Company	
	2006	2005
	€	€
Authorised:		
200,000,000 ordinary shares of € 0.0125	2,500,000	2,500,000
Allotted, Called-Up and Fully Paid:		
Opening 66,308,039 (2005: 59,725,150) ordinary shares of € 0.0125 each	828,851	746,565
Issued:		
1,160,000 (2005:6,582,889) ordinary shares of €0.0125 each	14,500	82,286
Closing 67,468,039 (2005:66,308,039) ordinary shares of € 0.0125 each	843,351	828,851

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2006

10. SHARE CAPITAL (continued)

During the year, 1,160,000 ordinary shares were issued at prices ranging from Stg£0.025 (€0.037) to Stg£0.54 (€0.78). 1,000,000 of these shares were issued at Stg £0.54 each to engineering consultants engaged by the company in lieu of fees for work done during the year. The remainder were issued for cash.

The total number of options outstanding at 31 December 2006, including to directors was 4,670,000 (2005: 4,830,000) shares. The options are exercisable at prices ranging between €0.0127 and €0.61 in accordance with the option agreement.

11. CAPITAL CONVERSION RESERVE FUND

	Group and Company	
	2006	2005
	€	€
Opening and closing balance	7,694	7,694

12. SHARE PREMIUM

	Group and Company	
	2006	2005
	€	€
Opening balance	9,063,625	3,804,660
Arising on shares issued during the year	777,236	5,395,096
Less share issue expenses	-	(136,131)
Closing balance	9,840,861	9,063,625

13. PROFIT AND LOSS ACCOUNT (DEFICIT) - GROUP

	2006	2005
	€	€
Opening balance	(2,932,319)	(2,450,784)
Loss retained for the year	(415,570)	(481,535)
Closing balance	(3,347,889)	(2,932,319)

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

14. RECONCILIATION OF MOVEMENT IN EQUITY SHAREHOLDERS' FUNDS - GROUP

	2006	2005
	€	€
Opening shareholders' funds	6,967,851	2,108,135
Loss for the year	(415,570)	(481,535)
Issue of shares:		
- at par	14,500	82,286
- share premium (net of costs)	777,236	5,258,965
Closing shareholders' funds	7,344,017	6,967,851

15. PROFIT ATTRIBUTABLE TO PETREL RESOURCES PLC

A separate profit and loss account for Petrel Resources plc (the company) has not been prepared because the company has complied with the conditions laid down in Section 43(2) of the European Communities (Companies : Group Accounts) Regulations 1992. The loss for the year was €415,570 (2005: Loss €492,769).

16. CASH FLOW STATEMENT

(a) Reconciliation of operating loss to net cash outflow from operating activities

	2006	2005
	€	€
Operating loss	(483,108)	(521,255)
Increase in creditors	15,022,561	1,466,889
(Increase)/decrease in debtors	(6,179)	105,191
Depreciation	-	596
Net cash inflow from operating activities	14,533,274	1,051,421

(b) Analysis of net funds

Analysis of net funds	At 1 January 2006	Cash flow	At 31 December 2006
	€	€	€
Cash at bank and in hand	3,729,121	5,721,754	9,450,875

(c) Reconciliation of net cash flow to movement in net funds

	2006	2005
	€	€
Increase in cash in the year	5,721,754	3,731,434
Change in net funds resulting from cash flows	5,721,754	3,731,434
Movement in net funds in the year	5,721,754	3,731,434
Net funds/(debt) at start of year	3,729,121	(2,313)
Net funds at end of year	9,450,875	3,729,121

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2006

17. RISK MANAGEMENT

The group's financial instruments comprise cash balances and various items such as trade debtors and trade creditors which arise directly from trading operations. The main purpose of these financial instruments is to provide working capital to finance group operations.

The group does not enter into any derivative transactions, and it is the group's policy that no trading in financial instruments shall be undertaken.

The main financial risk arising from the group's financial instruments is liquidity risk.

Interest Rate Risk

The group finances its operations through the issue of equity shares, and has no fixed interest rate agreements. The group has no significant exposures to interest rate risk.

Liquidity Risk

As regards liquidity, the group's exposure is confined to meeting obligations under short term trade creditor agreements. This exposure is not considered to be significant, and is fully financed from operating cashflow, or where this is insufficient funds during the development stage, through additional issues of ordinary equity shares.

Foreign Currency Risk

Although the group is based in the Republic of Ireland, amounts held as deferred development expenditure were originally expended in currencies other than Euro aligned currencies. However, this expenditure is not considered to be a monetary asset, and has been translated to the reporting currency at the rates of exchange ruling at the dates of the original transactions. At 31 December 2006, the group held €9,354,589 in sterling and U.S. dollar denominated bank accounts (2005: €3,716,976) and held no significant other currency monetary assets or liabilities.

The group also has transactional currency exposures. Such exposures arise from expenses incurred by the group in currencies other than the functional currency. It is expected that almost all future revenue will arise in US dollars. The group seeks to minimise its exposure to currency risk by closely monitoring exchange rates, and restricting the buying and selling of currencies to predetermined exchange rates within specified bands.

The group does not presently utilise swaps or forward contracts to manage its currency exposures, although such facilities are considered and may be used where appropriate in the future.

18. RELATED PARTY TRANSACTIONS

During the year the company paid consultancy fees to Guy Delbes amounting to €31,919 (2005 : €36,700). Guy Delbes is a director of the company.

19. NON-CASH TRANSACTIONS

On 10 February 2006, the company issued 1,000,000 shares at Stg£0.54 each to engineering consultants engaged by the company in lieu of fees for work done during the year.

20. POST BALANCE SHEET EVENTS

On 6 March 2007, the company issued 1,633,713 shares at Stg£0.50 each.The proceeds were for working capital.

NOTICE OF MEETING

Notice is hereby given that the annual general meeting of the members of Petrel Resources plc will be held on 22nd August 2007 in the Westbury Hotel, Grafton Street, Dublin 2 at 12 noon for the following purposes:

1. To receive the Report of the Directors and audited financial statement for the year ended December 31, 2006.

2. To re- appoint director: J. Teeling retires in accordance with article 95 and seeks re-election.

3. To authorise the directors to fix the remuneration of the auditors.

4. To transact any other ordinary business of an annual general meeting.

By order of the Board
James Finn
Secretary

28th June 2007

FORM OF PROXY

I/We ....
(BLOCK LETTERS)

of ....
being (an) ordinary shareholder(s) of Petrel Resources plc, hereby appoint the Chairman of the Meeting#

....

of ....
as my / our proxy to vote for me / us and on my / our behalf at the Annual General Meeting of the Company to be held on 22nd August 2007 in the Westbury Hotel, Grafton Street, Dublin 2 at 12 noon and at any adjournment thereof.

I/We direct my / our proxy to vote on the resolutions set out in the Notice convening the Meeting as follows:

	FOR *	**AGAINST ***
Reports and Accounts	☐	☐
Re-election of Director : J. Teeling	☐	☐
Remuneration of Auditors	☐	☐

Signature ....

Dated this ....day of 2007

If it is desire to appoint another person as proxy other than the Chairman of the Meeting the name and address of the proxy, who need not be a member of the Company, should be inserted, the words “the Chairman of the meeting” deleted and the alterations initialled.

* The manner in which the proxy is to vote should be indicated by inserting an “X” in the boxes provided. Proxies not marked as for or against will be regarded as giving the proxy authority to vote, or to abstain at his/her discretion.

NOTES:
1. In the case of a corporation this proxy must be under its common seal or under the hand of an officer or attorney duly authorised in writing.
2. To be effective this proxy must reach the address on the reverse hereof not less than 48 hours before the time of the meeting.
3. In the case of joint holders, the vote of the senior who tenders a vote whether in person or by proxy, shall be accepted to the exclusion of the votes of the other joint holders and for this purpose seniority shall be determined by the order in which the names stand in the Register of member in respect of such holding.

FOLD 2

The Company Registrar,
Computershare Services (Ireland) Ltd,
Heron House,
Corrig Road,
Sandyford Industrial Estate,
Dublin 18.

FOLD 3
(then turn in)

FOLD 1