

second quarter interim report | 2008



GALLEON ENERGY



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**GALLEON ENERGY**

## Letter to Shareholders

The second quarter of 2008 will be notable for record financial results and for continued success in the drilling program focused on light oil and natural gas resource projects.

### SECOND QUARTER 2008 HIGHLIGHTS

- Funds from operations for the three months ending June 30, 2008 were \$61.2 million (\$0.86 per basic share), an increase of 86% from Q2 2007;
- Received an average operating netback of \$49.08/BOE, an increase of \$28.94/BOE recorded in Q2 2007;
- Earnings for the three months ending June 30, 2008 were \$5.7 million (\$0.08 per basic share) and \$16.1 million for the six months ended June 30, 2008 (\$0.23 per basic share);
- Daily production for the quarter averaged 16,191 BOE, an increase of 21% from Q2 2007;
- Drilled nine gross wells resulting in seven (7.0 net) natural gas wells and two (2.0 net) light oil wells; a success rate of 100%;
- At June 30, 2008, net debt was \$229.3 million with available credit facilities of \$310 million.

Commodity prices combined with year over year production growth lifted revenues to record levels in the second quarter of 2008. Galleon has generated funds from operations of \$61.2 million in the second quarter of 2008 and \$116.6 million to June 30, 2008. In comparison, funds from operations of \$131.1 million were recorded for the entire year of 2007. The capital program is expected to be fully funded by funds from operations, another milestone for Galleon.

One of the key achievements in the second quarter of 2008 was the commencement of production from Galleon's first horizontal well in the East Montney project located in Dawson, Alberta. In addition, three successful horizontal wells were drilled in the East Montney project in Q2 2008. The Montney horizontal drilling program is expected to continue over the next eight to ten years due to Galleon's extensive landholdings in the Peace River Arch region of Alberta and British Columbia. Today, Galleon has identified eight Montney resource projects (six projects in Alberta and two in B.C.) spread over a large land base of approximately 0.5 million gross acres.

The success of the Montney horizontal drilling program and new exploration oil and natural gas discoveries have led Galleon to increase the 2008 capital program to approximately \$280 million. The 2008 capital program is expected to be funded by internal cash flow. Approximately 60% of the capital expenditures in the second half of 2008 will be directed to Montney resource projects. Galleon expects to employ seven to eight rigs to drill between 72 and 80 wells in the second half of 2008.

Included in the expansion of the capital program is the construction of two natural gas facilities to be located in Dawson and Kakut, Alberta. At Dawson, a new plant with capacity of 10 Mmcf/d is planned for the southern end of the Eastern Montney pool. Combined with the existing 30 Mmcf/d natural gas plant located 20 km to the north, Galleon will have natural gas processing capacity of approximately 40 Mmcf/d in the area. The new plant is expected to be on-stream in late Q4 2008 or early Q1 2009. Kakut is located in the Central Montney region and is expected to be a significant growth area for Galleon. An owned natural gas plant at Kakut will be expanded from 5 Mmcf/d to 15 Mmcf/d and is scheduled to be on stream in Q4 2008.

Galleon has access to approximately one million gross acres of undeveloped land, of which 90% is located in the Peace River Arch area of Alberta and British Columbia. In combination with this large land base, the success of the drilling program to date, and the drilling opportunities planned during the second half of 2008, Galleon is positioned for production and reserve growth in 2008 and 2009.



Glenn R. Carley  
*Executive Chairman*  
August 13, 2008



Steve Sugianto  
*President and Chief Executive Officer*

## Management's Discussion and Analysis

This Management's Discussion & Analysis ("MD&A") is intended to assist in the understanding of the trends and significant changes in the financial condition and results of operations of Galleon Energy Inc. ("Galleon" or the "Corporation") for the three and six months ended June 30, 2008 with comparisons to the three and six months ended June 30, 2007 and as at December 31, 2007. The MD&A has been prepared by management in accordance with Canadian generally accepted accounting principles ("GAAP") and should be read in conjunction with the unaudited interim financial statements as at and for the three and six month periods ended June 30, 2007 and the audited financial statements and MD&A for the year ended December 31, 2007.

Petroleum and natural gas reserves and volumes are converted to a common unit of measure on a basis of six thousand cubic feet (Mcf) of gas to one barrel (Bbl) of oil. BOEs may be misleading, particularly if used in isolation. The forgoing conversion ratio is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

Amounts are shown in Canadian dollars unless otherwise stated. All production volumes disclosed herein are sales volumes.

This MD&A is based on information available as of, and is dated, August 13, 2008.

### NON-GAAP MEASUREMENTS

The MD&A contains terms commonly used in the oil and gas industry, such as funds from operations, funds from operations per share, and operating netback. These terms are not defined by GAAP and should not be considered an alternative to, or more meaningful than, cash provided by operating activities or net earnings as determined in accordance with Canadian GAAP as an indicator of Galleon's performance. Management believes that in addition to net earnings, funds from operations is a useful financial measurement which assists in demonstrating the Corporation's ability to fund capital expenditures necessary for future growth or to repay debt. Galleon's determination of funds from operations may not be comparable to that reported by other companies. All references to funds from operations throughout this report are based on cash flow from operating activities before changes in non-cash working capital and abandonment expenditures. The Corporation calculates funds from operations per share by dividing funds from operations by the weighted average number of Class A shares outstanding.

Galleon uses the term net debt in the MD&A and presents a table showing how it has been determined. This measure does not have any standardized meaning prescribed by Canadian GAAP and therefore may not be comparable to similar measures presented by other companies.

## FORWARD-LOOKING STATEMENTS

Statements that are not historical facts may be considered forward looking statements including management's assessment of future plans and operations, growth expectations within the Corporation, expected production and production increases, length of drilling program in the Montney resource play, expected general and administration and operating expenses in 2008, expectation that the Corporation will not be taxable in 2008, drilling plans and the timing thereof, facilities to be constructed or expanded and the timing thereof, capital expenditures, the timing thereof and the method of funding thereof. These forward-looking statements sometimes include words to the effect that management believes or expects a stated condition or result. All estimates and statements that describe the Corporation's objectives, goals or future plans are forward-looking statements. Since forward-looking statements address future events and conditions, by their very nature they involve inherent risks and uncertainties including, without limitation, risks associated with oil and gas exploration, development, exploitation, production, marketing and transportation, loss of markets, volatility of commodity prices, currency fluctuations, imprecision of reserve estimates, environmental risks, competition from other producers, inability to retain drilling rigs and other services, incorrect assessment of the value of acquisitions, failure to realize the anticipated benefits of acquisitions, delays resulting from or inability to obtain required regulatory approvals and ability to access sufficient capital from internal and external sources. As a consequence, Galleon's actual results may differ materially from those expressed in, or implied by, the forward-looking statements.

Forward looking statements or information are based on a number of factors and assumptions which have been used to develop such statements and information but which may prove to be incorrect. Although the Corporation believes that the expectations reflected in such forward looking statements or information are reasonable, undue reliance should not be placed on forward looking statements because the Corporation can give no assurance that such expectations will prove to be correct. In addition to other factors and assumptions which may be identified in this document, assumptions have been made regarding, among other things: the impact of increasing competition; the general stability of the economic and political environment in which the Corporation operates; the timely receipt of any required regulatory approvals; the ability of the Corporation to obtain qualified staff, equipment and services in a timely and cost efficient manner; drilling results; the ability of the operator of the projects which the Corporation has an interest in to operate the field in a safe, efficient and effective manor; the ability of the Corporation to obtain financing on acceptable terms; field production rates and decline rates; the ability to replace and expand oil and natural gas reserves through acquisition, development of exploration; the timing and costs of pipeline, storage and facility construction and expansion and the ability of the Corporation to secure adequate product transportation; future oil and natural gas prices; currency, exchange and interest rates; the regulatory framework regarding royalties, taxes and environmental matters in the jurisdictions in which the Corporation operates; and the ability of the Corporation to successfully market its oil and natural gas products.

Readers are cautioned that the foregoing list of all factors and assumptions is not exhaustive. Additional information on these and other factors that could affect Galleon's operations and financial results are included elsewhere herein and in reports on file with Canadian securities regulatory authorities and may be accessed through the SEDAR website ([www.sedar.com](http://www.sedar.com)), or at Galleon's website ([www.galleonenergy.com](http://www.galleonenergy.com)). Furthermore, the forward looking statements contained herein are made as at the date hereof and Galleon does not undertake any obligation to update publicly or to revise any of the included forward looking statements, whether as a result of new information, future events or otherwise, except as may be required by applicable securities laws.

## SECOND QUARTER 2008 HIGHLIGHTS

- Funds from operations for the three months ending June 30, 2008 were \$61.2 million (\$0.86 per basic share), an increase of 86% from Q2 2007;
- Received an average operating netback of \$49.08/BOE, an increase of \$28.94/BOE recorded in Q2 2007;
- Earnings for the three months ending June 30, 2008 were \$5.7 million (\$0.08 per basic share) and \$16.1 million for the six months ended June 30, 2008 (\$0.23 per basic share);
- Daily production for the quarter averaged 16,191 BOE, an increase of 21% from Q2 2007;
- Drilled nine gross wells resulting in seven (7.0 net) natural gas wells and two (2.0 net) light oil wells; a success rate of 100%;
- Spent \$34.9 million on exploration and development activities during the quarter;
- Purchased a natural gas plant for \$8.5 million;
- On May 9, 2008 the Corporation completed the acquisition of Adamant Energy Inc. (“Adamant”);
- At June 30, 2008, net debt was \$229.3 million with available credit facilities of \$310 million.

One of the key achievements in the second quarter of 2008 was the commencement of production from Galleon’s first horizontal well in the East Montney project located in Dawson, Alberta. In addition, three more successful horizontal wells were drilled in the East Montney project in Q2 2008. The Montney horizontal drilling program is expected to continue over the next eight to ten years due to Galleon’s extensive landholdings in the Peace River Arch region of Alberta and British Columbia.

Commodity prices combined with year over year production growth lifted revenues to record levels in the second quarter of 2008. Galleon has generated funds from operations of \$61.2 million in the second quarter of 2008 and \$116.6 million to June 30, 2008. In comparison, funds from operations of \$131.1 million were recorded for the entire year of 2007. The capital program is expected to be fully funded by funds from operations, another milestone for Galleon.

The acquisition of Adamant was completed in Q2 2008. The significance of this acquisition is seen when comparing the close proximity of the Adamant land and production base to Galleon’s existing holdings. Galleon has realized synergies with this acquisition as well as with the acquisition of ExAlta Energy Inc. (“ExAlta”) which was completed in Q1 2008.

## RESULTS OF OPERATIONS

Comparative financial results for the quarter are as follows:

Three months ended June 30	2008		2007	
		1,473,414 BOE \$/BOE		1,216,855 BOE \$/BOE
(\$000s)				
Revenues	120,602	81.85	60,735	49.91
Other income	105	0.07	–	–
Royalties	(27,155)	(18.43)	(13,609)	(11.18)
GCA <sup>1</sup>	6,097	4.14	2,603	2.14
Transportation costs	(2,416)	(1.64)	(1,408)	(1.16)
Operating costs	(18,726)	(12.71)	(10,507)	(8.63)
<b>Net</b>	<b>78,507</b>	<b>53.28</b>	<b>37,814</b>	<b>31.08</b>
G&A	(3,698)	(2.51)	(1,797)	(1.48)
Interest costs	(2,977)	(2.02)	(2,682)	(2.20)
Capital and other taxes	(358)	(0.24)	(502)	(0.41)
Realized gain (loss) on financial derivative	(10,317)	(7.00)	–	–
<b>Funds from operations<sup>2</sup></b>	<b>61,157</b>	<b>41.51</b>	<b>32,833</b>	<b>26.99</b>

<sup>1</sup> GCA means Gas Cost Allowance

<sup>2</sup> See "Non-GAAP Measurements"

Six months ended June 30	2008		2007	
		3,020,890 BOE \$/BOE		2,286,770 BOE \$/BOE
(\$000s)				
Revenues	222,118	73.53	113,709	49.72
Other income	228	0.08	–	–
Royalties	(47,823)	(15.83)	(24,625)	(10.77)
GCA <sup>1</sup>	8,520	2.82	5,237	2.29
Transportation costs	(4,031)	(1.33)	(2,995)	(1.31)
Operating costs	(36,186)	(11.98)	(19,985)	(8.74)
<b>Net</b>	<b>142,826</b>	<b>47.29</b>	<b>71,341</b>	<b>31.19</b>
G&A	(6,069)	(2.01)	(3,061)	(1.34)
Interest costs	(5,780)	(1.91)	(4,928)	(2.15)
Capital and other taxes	(697)	(0.23)	(722)	(0.32)
Realized gain (loss) on financial derivative	(13,678)	(4.53)	373	0.16
<b>Funds from operations<sup>2</sup></b>	<b>116,602</b>	<b>38.61</b>	<b>63,003</b>	<b>27.54</b>

<sup>1</sup> GCA means Gas Cost Allowance

<sup>2</sup> See "Non-GAAP Measurements"

## PETROLEUM AND NATURAL GAS REVENUES

Three months ended June 30 (\$000s)	2008		2007	
		%		%
Light oil	51,789	43	21,397	36
Heavy oil	16,830	14	7,491	12
NGLs	3,244	3	1,390	2
Natural gas	48,537	40	30,275	50
Royalty income	202	–	182	–
<b>Total</b>	<b>120,602</b>	<b>100</b>	<b>60,735</b>	<b>100</b>

Six months ended June 30 (\$000s)	2008		2007	
		%		%
Light oil	98,648	44	39,706	35
Heavy oil	30,717	14	14,411	13
NGLs	5,696	3	2,441	2
Natural gas	86,718	39	56,790	50
Royalty income	339	–	361	–
<b>Total</b>	<b>222,118</b>	<b>100</b>	<b>113,709</b>	<b>100</b>

Revenues for the three months ended June 30, 2008 increased by 99% to \$120.6 million from \$60.7 million for the same period of the prior year due to a 21% increase in average production volumes, a 148% increase in heavy oil prices, a 72% increase in light oil prices and a 35% increase in gas prices.

In the second quarter of 2008, on a revenue basis, oil and liquids generated 60% of revenues compared to 50% in the same period of the prior year.

## PRODUCTION

	Three months ended June 30				Six months ended June 30			
	2008		2007		2008		2007	
		%		%		%		%
Light oil (Bbls/d)	4,629	29	3,317	25	5,015	30	3,223	26
Heavy oil (Bbls/d)	2,066	13	2,247	17	2,228	13	2,164	17
NGLs (Bbls/d)	501	3	256	2	471	3	231	1
Natural gas (Mcf/d)	53,971	55	45,314	56	53,307	54	42,097	56
<b>BOE/d (6:1)</b>	<b>16,191</b>	<b>100</b>	<b>13,372</b>	<b>100</b>	<b>16,599</b>	<b>100</b>	<b>12,634</b>	<b>100</b>

Average production volumes of 16,191 BOE/d for second quarter 2008 were 21% greater than the average of 13,372 BOE/d in second quarter 2007. By product, production volumes increased as follows: light oil volumes by 40%, natural gas volumes by 19% and natural gas liquids volumes by 96%. Heavy oil volumes decreased by 8%.

## COMMODITY PRICING AND MARKETING

Petroleum products are sold to major Canadian marketers at spot reference prices based on US WTI for crude oil and AECO for natural gas. As a means of managing the risk of commodity price volatility, Galleon has entered into one term natural gas contract and three crude oil financial contracts. The natural gas contract for 10,000 GJ/day was put in place on January 8, 2008 and has a term from February 1 to December 31, 2008 with pricing subject to a costless collar of \$6.00/GJ and \$8.00/GJ Canadian. For the three and six months ended June 30, 2008, this natural gas contract had realized losses of \$2,456,118 and \$2,869,920 respectively.

An additional natural gas contract was acquired with Adamant. This second contract is for 8,500 GJ/day and was put in place from January 1, 2008 through December 31, 2008 with pricing subject to a costless collar of \$6.00/GJ to \$7.00/GJ Canadian. At the date of acquisition, this contract represented a \$5.3 million liability which will be amortized into income over the remaining life of the contract. At June 30, 2008, the balance of this liability was \$4.6 million.

For crude oil, Galleon entered into one costless collar contract for 2,000 Bbl/day, fixing a floor price of WTI CDN \$70.00/Bbl and a ceiling of WTI CDN \$80.75/Bbl for the period January 1, 2008 to December 31, 2008. A second crude oil costless collar contract was entered into for 1,000 Bbl/day, fixing a floor price of \$75.00 WTI USD and a ceiling price of \$100.00 WTI USD for the period January 1, 2008 to December 31, 2008. A third crude oil costless collar contract was entered into for 1,000 Bbl/day, fixing a floor price of \$110.00 WTI CDN and a ceiling price of \$177.30 WTI CDN for the period July 1, 2008 to December 31, 2008. For the three and six months ended June 30, 2008, the three crude oil contracts resulted in realized losses of \$10.3 million and \$3.4 million, respectively. Unrealized losses of \$32.2 million were recorded as a liability based on the mark to market value at June 30, 2008 of these financial contracts. The contracts will protect base line revenues if the WTI crude oil benchmark falls below floor price. The contracts will be settled monthly based on the average USD and CDN WTI benchmark price. Galleon will receive payments on the contracts if the benchmark USD and CDN WTI price falls below the set floor price and will be required to make payments if the price rises above the set ceiling price. Galleon has recognized these financial instruments on its balance sheet at fair value, and is accounting for the instruments using mark to market accounting.

#### PRICES (NET OF TRANSPORTATION)

	Three months ended June 30		Six months ended June 30	
	2008	2007	2008	2007
Light oil (\$/Bbl)	<b>120.68</b>	70.12	<b>106.77</b>	66.91
Heavy oil (\$/Bbl)	<b>88.93</b>	35.89	<b>75.30</b>	36.21
Total oil including financial derivative contract (\$/Bbl)	<b>93.95</b>	56.42	<b>86.72</b>	54.96
Total oil without financial derivative contract (\$/Bbl)	<b>110.88</b>	56.42	<b>97.09</b>	54.57
NGLs (\$/Bbl)	<b>71.19</b>	59.67	<b>66.42</b>	58.33
Natural gas (\$/Mcf)	<b>9.65</b>	7.14	<b>8.70</b>	7.23

Light oil prices increased by 72% to \$120.68/Bbl, excluding the loss incurred from the crude oil costless collars. Average heavy oil prices of \$88.93/Bbl increased by 148% from the same period of the prior year due to an increase in demand at refineries which resulted in an improvement in heavy oil differentials. Average natural gas prices received in second quarter 2008 of \$9.65/Mcf increased by 35% from the second quarter of 2007. The average gas price calculated includes the impact of the two natural gas contracts.

## PERFORMANCE BY PROPERTY

	Three months ended June 30			2007			2008	
	Production BOE/d	%	Operating netbacks/ BOE <sup>1</sup>	Production BOE/d	%	Operating netbacks/ BOE <sup>1</sup>	Funds from operations <sup>2</sup>	
			\$			\$	%	
Puskwa	2,391	15	65.48	2,128	16	49.78	20	
Eastern Montney gas	3,172	20	42.07	3,826	29	32.74	17	
Eaglesham	2,804	17	58.24	1,713	13	29.83	21	
Dawson conventional	1,824	11	48.44	2,675	20	25.58	11	
Edam and other heavy oil	1,459	9	34.62	2,247	17	10.26	6	
Calais	648	4	44.75	374	3	32.74	4	
McLean Creek	566	3	99.62	–	–	–	7	
Alexis	1,078	7	45.08	–	–	–	6	
Whitelaw	494	3	22.82	–	–	–	1	
Dixonville	346	2	19.43	–	–	–	1	
St. Anne	286	2	37.75	–	–	–	1	
Jack / Pica	88	1	19.02	–	–	–	–	
Other	1,035	6	36.73	409	2	15.65	5	
	<b>16,191</b>	<b>100</b>	<b>49.08</b>	<b>13,372</b>	<b>100</b>	<b>28.94</b>	<b>100</b>	

	Six months ended June 30			2007			2008	
	Production BOE/d	%	Operating netbacks/ BOE <sup>1</sup>	Production BOE/d	%	Operating netbacks/ BOE <sup>1</sup>	Funds from operations <sup>2</sup>	
			\$			\$	%	
Puskwa	2,546	15	60.91	1,828	15	49.83	21	
Eastern Montney gas	3,482	21	38.31	3,328	26	31.52	18	
Eaglesham	2,950	18	51.34	1,634	13	31.12	21	
Dawson conventional	1,963	12	39.63	2,855	23	27.11	11	
Edam and other heavy oil	1,700	10	28.36	2,165	17	10.25	7	
Calais	778	5	36.22	425	3	26.08	4	
McLean Creek	608	4	93.05	–	–	–	8	
Alexis	1,028	6	39.04	–	–	–	5	
Whitelaw	247	1	22.82	–	–	–	1	
Dixonville	173	1	19.43	–	–	–	–	
St. Anne	143	1	37.75	–	–	–	1	
Jack / Pica	44	0	19.02	–	–	–	–	
Other	937	6	32.84	399	3	19.22	3	
	<b>16,599</b>	<b>100</b>	<b>44.39</b>	<b>12,634</b>	<b>100</b>	<b>28.91</b>	<b>100</b>	

<sup>1</sup> Operating netbacks/BOE exclude GCA and are calculated by subtracting royalties and operating costs from revenues and dividing the result by average production for the period.

<sup>2</sup> See "Non-GAAP Measurements".

Volume growth in Q2 2008 compared to Q2 2007 was led by light oil production and by the acquisitions of ExAlta in January 2008 and Adamant in May 2008. Within the last year, Galleon's drilling program has been focused on light oil projects due to rising oil prices and soft natural gas prices. At Puskwa, Eaglesham and Mcleans Creek, Alberta, light oil volumes were 50% higher in Q2 2008 than in Q2 2007.

During second quarter 2008, Galleon experienced operational challenges due to extremely wet conditions caused by a prolonged spring break up period. Drilling operations commenced in June 2008 resulting in the drilling of nine wells for a success rate of 100%. In addition, several service rigs and pipeline crews were mobilized in June 2008. The effects of this activity will be seen in future periods.

At Puskwa, production increased by 12% during second quarter 2008 compared to the same period in 2007. The operating netback was \$65.48/BOE, an improvement of 32% from second quarter 2007. These strong operating netbacks were driven by average light oil prices (net of transportation) in the period of \$125.12/Bbl. During Q2 2008, Puskwa contributed 20% of funds from operations from 15% of the production volumes. Average production volumes at Puskwa during second quarter 2008 were comprised of 83% oil and 17% associated gas.

The Puskwa project has moved into the development stage with the implementation of two enhanced recovery schemes. Currently, wells drilled to date have confirmed that the Beaverhill lake fairway extends over nine miles in length. Down spacing applications to allow up to 16 wells per section are planned within the next year. Galleon plans to drill additional wells for oil targets as well as for injection purposes.

Production averaged 3,172 BOE/d (89% natural gas and 11% oil and liquids) in the Dawson Eastern Montney gas project during second quarter 2008 compared to 3,826 BOE/d in second quarter 2007. This decrease is a result of reduced activity on this project in the form of fewer vertical Montney gas wells being drilled in the second half of 2007 and in Q1 2008. Capital was allocated towards light oil projects given the relative strength of oil prices to gas prices. In addition, Galleon began to consider the benefits of developing this project with horizontal wells rather than vertical wells. Galleon's first horizontal well was drilled in Q1 2008 and commenced production in the latter part of June 2008. Second quarter 2008 production volumes were affected by power plant outages at Galleon's natural gas plant. The operating netback of \$42.07/BOE has improved by 28% from second quarter 2007 as a result of recent strong natural gas prices. The Eastern Montney project contributed 17% to total funds from operating activities based on 20% of production volumes.

Average production at Eaglesham in the second quarter of 2008 averaged 2,804 BOE/d comprised of 66% natural gas and 34% oil and liquids. Average production was 1,713 BOE/d at Eaglesham during second quarter 2007. Eaglesham contributed 21% of the second quarter 2008 funds from operations from 17% of production volumes.

During Q2 2008, production declines in the Dawson conventional area resulted in a decrease of 32% in volumes compared to the prior year. This area represented 11% of funds from operating activities generated from 11% of the production volumes in second quarter 2008.

In Q2 2008, the heavy oil wells located at Edam, Saskatchewan generated 6% of funds from operations from 9% of total production. Operating netbacks of \$34.62/BOE increased by 237% due to the increase in heavy oil prices in the second quarter 2008.

Production volumes of 648 BOE/d were recorded at Calais which generated a netback of \$44.75/BOE and contributed 4% of funds from operations.

McLean Creek has contributed 7% of funds from operations based on 3% of the production volumes. The high netback of \$99.62/BOE in Q2 2008 is attributed to high oil prices received and a royalty holiday period. This deep oil property commenced production in December 2007.

The Alexis property was acquired in the ExAlta acquisition in January 2008. Galleon acquired the properties of Whitelaw, Dixonville, Jack/Pica and St. Anne in the Adamant acquisition in May 2008.

## ROYALTIES

Three months ended June 30	2008	2007
(\$000s, except as indicated)		
Crown	25,007	12,366
Freehold	302	344
GORR and other	1,846	899
<b>Gross royalties</b>	<b>27,155</b>	<b>13,609</b>
GCA	(6,097)	(2,603)
<b>Net royalties</b>	<b>21,058</b>	<b>11,006</b>
% of revenue	22.5	22.4
% of revenue net of GCA	17.5	18.1
Six months ended June 30		
(\$000s, except as indicated)		
Crown	43,570	22,457
Freehold	756	757
GORR and other	3,497	1,411
<b>Gross royalties</b>	<b>47,823</b>	<b>24,625</b>
GCA	(8,520)	(5,237)
<b>Net royalties</b>	<b>39,303</b>	<b>19,388</b>
% of revenue	21.5	21.7
% of revenue net of GCA	17.7	17.1

Gross royalties were 22.5% of revenues for the second quarter of 2008 compared to 22.4% for the same period in 2007. Included in Q2 2008 gross royalties is an amount of \$2.3 million which was paid to the Alberta Government due to a reclassification of some wells at Puskwa from an exploratory class to development. Excluding this adjustment, gross royalties were 20.6% of revenues in second quarter 2008.

By product, for the second quarter of 2008, gross royalties were 18.6% for light oil, 26.1% for natural gas, 22.4% for heavy oil, and 32.6% for liquids. For the second quarter of 2007, gross royalties were 21.9% for light oil, 23.3% for natural gas, 19.8% for heavy oil, and 24.7% for liquids.

During Q2 2008, net royalties were 17.5% of revenues, a decrease from 18.1% in the prior year as a result of greater GCA credits as a percentage of total royalties. After excluding the adjustment related to Puskwa, net royalties as a percentage of revenues in second quarter 2008 were 15.6%.

## OPERATING COSTS

	Three months ended June 30			2007		
	Production %	Operating Costs %	\$/BOE	Production %	Operating Costs %	\$/BOE
Puskwa	15	10	9.35	16	6	3.04
Eastern Montney gas	20	13	8.16	29	15	4.07
Eaglesham	17	15	8.66	13	8	4.43
Dawson conventional	11	18	20.94	20	30	13.03
Edam and other heavy oil	9	19	29.95	17	32	18.23
Calais	4	2	7.67	3	3	8.97
McLean Creek	3	4	15.10	–	–	–
Alexis	7	6	8.55	–	–	–
Dixonville	2	2	15.23	–	–	–
Jack / Pica	1	1	16.64	–	–	–
Whitelaw	3	2	7.53	–	–	–
St. Anne	2	1	10.56	–	–	–
Other	6	7	14.39	2	6	19.04
	100	100	12.71	100	100	8.63

	Six months ended June 30			2007		
	Production %	Operating Costs %	\$/BOE	Production %	Operating Costs %	\$/BOE
Puskwa	15	11	9.15	15	6	3.21
Eastern Montney gas	21	11	5.96	26	14	4.15
Eaglesham	18	15	8.43	13	8	4.97
Dawson conventional	12	21	22.19	23	30	11.58
Edam and other heavy oil	10	20	25.95	17	33	18.53
Calais	5	3	7.56	3	3	8.02
McLean Creek	4	3	12.13	–	–	–
Alexis	6	6	8.81	–	–	–
Dixonville	1	1	15.23	–	–	–
Jack / Pica	–	–	16.64	–	–	–
Whitelaw	1	1	7.53	–	–	–
St. Anne	1	1	10.56	–	–	–
Other	6	7	13.92	3	6	18.04
	100	100	11.98	100	100	8.74

Operating costs were \$18.7 million or \$12.71/BOE for the second quarter of 2008 compared to \$10.5 million or \$8.63/BOE for the same period of the prior year. Galleon's operating costs per barrel of oil equivalent excluding heavy oil costs at Edam, Saskatchewan and Alexis, Alberta was \$9.44/BOE for the second quarter of 2008.

During Q2 2008, Galleon has experienced higher costs associated with operating crude oil wells compared to the costs of operating natural gas wells. Some of the more significant costs of operating crude oil wells include trucking, artificial lift and maintenance costs.

Lower production volumes were recorded in Q2 2008 due to production disruptions caused by extremely wet ground conditions during the spring break up period. As a result of the decreased production volumes, per unit costs are higher.

Operating costs at Puskwa were \$9.35/BOE in the second quarter of 2008 compared to \$3.04/BOE in 2007. At Puskwa, waterflood schemes were implemented in two sections in late Q2 2007 and in additional sections during Q4 2007. The benefits of the waterflood schemes include improved recovery of reserves and greater production. However, there are additional costs associated with enhanced production recovery compared to primary production recovery. During Q2 2008, increased water trucking costs of \$1.00/BOE for injection purposes were incurred due to a water pipeline failure in Q1 2008. Other cost increases at Puskwa included minor work over and well service costs of \$0.79/BOE due to a greater percentage of pumping oil wells in 2008 compared to flowing wells in 2007. Operating costs for the remainder of the year are expected to average below \$8.00/BOE at Puskwa.

In the Eastern Montney natural gas project, operating costs were \$8.16/BOE in Q2 2008 of which \$1.47/BOE were related to annual road and lease maintenance costs, property taxes and EUB fees incurred during June 2008. Operating costs for the remainder of the year are expected to average below \$6.00/BOE in this area.

Eaglesham operating costs for the second quarter 2008 were \$8.66/BOE compared to \$4.43/BOE in 2007. The Eaglesham properties acquired from ExAlta have a high operating cost base which Galleon plans to reduce where possible. For Q2 2008, the Eaglesham operating costs, excluding costs related to the ExAlta Eaglesham wells, were \$6.49/BOE. Operating costs for the remainder of the year are expected to average between \$8.00/BOE and \$9.00/BOE in Eaglesham.

#### GENERAL AND ADMINISTRATION EXPENSES

Three months ended June 30		2008		2007	
(\$000s)		\$/BOE		\$/BOE	
Gross	4,919	3.34	2,556	2.10	
Capitalized overhead	(833)	(0.57)	(541)	(0.44)	
Overhead recoveries	(388)	(0.26)	(218)	(0.18)	
	<b>3,698</b>	<b>2.51</b>	<b>1,797</b>	<b>1.48</b>	
Six months ended June 30		2008		2007	
(\$000s)		\$/BOE		\$/BOE	
Gross	8,803	2.91	5,088	2.22	
Capitalized overhead	(2,042)	(0.68)	(1,677)	(0.73)	
Overhead recoveries	(692)	(0.23)	(350)	(0.15)	
	<b>6,069</b>	<b>2.00</b>	<b>3,061</b>	<b>1.34</b>	

Gross general and administrative expenses (G&A) have increased by \$1.24/BOE to \$3.34/BOE in second quarter 2008 compared to \$2.10/BOE in second quarter 2007. This increase is primarily due to a 38% increase in staffing levels required to manage the growth of the company. Also, in April 2008, Galleon relocated to new and larger office space in order to accommodate the addition of employees and consultants. The office space was 150% greater in area with a rate increase of approximately 30% per square foot. The rate increase reflects current market rates compared to those in 2005. Net G&A expenses of \$2.51/BOE for the second quarter of 2008 increased by \$1.03/BOE compared to the same period of the previous year.

To June 30, 2008, gross G&A has increased by \$0.69/BOE and net G&A has increased by \$0.66/BOE compared to the same periods in 2007. Galleon expects that net G&A will average between \$2.10/BOE and \$2.20/BOE over 2008.

## GENERAL AND ADMINISTRATION EXPENSES BY CATEGORY

	Three months ended June 30		Six months ended June 30	
	2008 %	2007 %	2008 %	2007 %
Salary and employee	44	52	48	51
Office	30	22	25	21
Consulting	10	6	9	7
Computer	7	8	7	8
Investor relations and communications	2	1	3	4
Audit, engineering and legal	4	6	5	5
Other	3	5	3	4
	100	100	100	100

## INTEREST

Interest expense of \$3.0 million for the three months ended June 30, 2008 was higher than \$2.7 million in the same period of the prior year due to increased average debt levels. At June 30, 2008 an amount of \$223.6 million was drawn against the Corporation's credit facility compared to \$168.1 million in the same period of the prior year.

## STOCK BASED COMPENSATION

Stock based compensation was a non-cash expense of \$2.3 million for the three month period ending June 30, 2008 compared to \$2.2 million in the same period of the prior year. The increase was due to a greater number of options outstanding. During the second quarter of 2008, 430,000 stock options were granted to employees at an average exercise price of \$18.18 having fair values of between \$4.76 and \$5.12 per option.

At June 30, 2008, 6,213,485 stock options were outstanding at an average exercise price of \$13.10.

## DEPLETION, DEPRECIATION AND ACCRETION

Depletion and depreciation ("D&D") charges were \$32.4 million or \$22.01/BOE for the three months ended June 30, 2008 compared to \$25.0 million or \$20.53/BOE for the same period of the prior year. The D&D rate increase was due to the ExAlta and Adamant acquisitions and increased finding costs from the drilling program. Reserve additions for the first half of 2008 were estimated internally.

As at June 30, 2008, \$109.9 million (June 30, 2007 – \$84.1 million) of undeveloped land and seismic have been excluded from, and \$112.8 million (June 30, 2007 – \$85.8 million) in future development costs have been added into, the full cost pool for depletion purposes.

Accretion expense on the Corporation's asset retirement obligation was \$464,000 for the second quarter of 2008 compared to \$356,000 in the same quarter of the prior year. Accretion expense increased due to a greater asset retirement obligation which is driven by the number of wells and facilities in which Galleon has an interest. During the quarter, \$4.4 million of asset retirement liabilities were added due to the acquisition of Adamant.

## CAPITAL AND FUTURE TAXES

The current tax provision of \$358,000 for the second quarter was comprised of Saskatchewan capital and resource taxes, as was the \$502,000 provision for the second quarter of 2007. The provision is calculated based on revenues earned in Saskatchewan. It is not expected that Galleon will pay any income taxes in 2008.

The provision for future income taxes was \$2.9 million for the second quarter of 2008 compared to \$2.0 million for the same period in the prior year. The increase in future taxes was a result of higher net earnings before taxes during the period.

## CAPITAL EXPENDITURES

	(\$000s)
Property & equipment balance at December 31, 2007	739,643
Additions to property and equipment	106,182
Acquisition of property and equipment	9,402
Acquisition of ExAlta	92,345
Acquisition of Adamant	71,909
Well abandonments	897
Asset retirement obligation acquired	7,834
Asset retirement obligation additions	1,247
Depletion and depreciation	(66,052)
<b>Property &amp; equipment balance at June 30, 2008</b>	<b>963,407</b>

During the second quarter of 2008, \$76.3 million was recorded in property and equipment additions, including asset retirement obligations of \$4.4 million due to the acquisition of Adamant.

Three months ended June 30		2008		2007	
(\$000s)		%		%	
Land	3,732	11	1,812	8	
Geological and geophysical	2,723	8	3,200	13	
Drilling and completion	19,008	54	15,240	64	
Plant and facilities	8,512	24	3,275	15	
Other assets	881	3	141	–	
<b>Exploration and Development Expenditures</b>	<b>34,856</b>	<b>100</b>	<b>23,668</b>	<b>100</b>	
Six months ended June 30		2008		2007	
(\$000s)		%		%	
Land	5,771	5	5,445	6	
Geological and geophysical	8,076	8	6,130	7	
Drilling and completion	63,401	60	55,793	66	
Plant and facilities	27,920	26	18,048	21	
Other assets	1,014	1	186	–	
<b>Exploration and Development Expenditures</b>	<b>106,182</b>	<b>100</b>	<b>85,602</b>	<b>100</b>	

Exploration and development expenditures during the second quarter of 2008 were \$34.9 million which included the drilling and completion of nine gross (9.0 net) wells in June 2008. Seven (7.0 net) natural gas wells and two (2.0 net) light oil wells were cased for production representing a success rate of 100%. Facilities expenditures of \$8.5 million were incurred with land and seismic expenditures of \$3.7 million and \$2.7 million, respectively, in second quarter 2008. Management has established an exploration and development capital budget of up to \$280 million for 2008 which is expected to be funded from funds from operations.

## LIQUIDITY AND CAPITAL RESOURCES

June 30	2008	2007
(\$000s)		
Bank debt	223,562	168,091
Capital leases – non current	2,467	–
Working capital deficiency	3,311	9,787
Total net debt	229,340	177,878

## FUNDING OF CAPITAL PROGRAM

Three months ended June 30	2008	2007
(\$000s)		
Issuance of shares, net of costs	7,966	29,746
Funds from operations	61,157	32,833
Change in bank debt	(6,304)	(21,323)
Change in debt and working capital from acquisitions	9,336	–
Change in capital leases	(624)	–
Change in working capital and other	(24,382)	(11,416)
	47,149	29,840

Six months ended June 30	2008	2007
(\$000s)		
Issuance of shares, net of costs	9,712	30,542
Funds from operations	116,602	63,003
Change in bank debt	60,184	45,095
Change in debt and working capital from acquisitions	(36,947)	–
Change in capital leases	(1,108)	–
Change in working capital and other	(28,062)	(18,885)
	120,381	119,755

During the quarter option exercises of \$8.0 million and funds from operations of \$61.2 million, and an additional \$9.3 million in working capital from acquisitions, were used to pay down \$6.3 million in bank debt and fund \$47.1 million of acquisition and exploration and development expenditures.

At June 30, 2008, the Corporation has extendible revolving term credit facilities of \$310 million in place with a bank syndicate. The facilities bear interest at rates ranging from the bank's prime rate to prime plus 0.75% per annum on \$290 million and at rates ranging from the bank's prime rate plus 0.95% to prime plus 1.75% on \$20 million based on the Corporation's debt to cash flow ratio. The Corporation may also borrow at the prevailing Banker's Acceptance rate. Collateral for the facilities consists of a demand debenture for \$500 million collateralized by a first floating charge over all of the property and equipment of the Corporation. At June 30, 2008, an amount of \$223.6 million was drawn against the credit facilities (June 30, 2007 – \$168.1 million).

## COMMITMENTS

## Drilling Rig

The Corporation has entered into a Master Daywork Contract whereby it is entitled to the use of a drilling rig for a two year period which commenced November 15, 2007. Future minimum payments under this contract are as follows:

Year	(\$000)
2008	1,970
2009	4,170

#### Minimum Lease Payments

At June 30, 2008 the Corporation has committed to future minimum payments under operating leases that cover office space as follows:

Year	(\$000)
2008	1,334
2009	2,514
2010	1,800

The above commitment includes an estimate of the Corporation's share of operating expenses, utilities and taxes for the duration of the office lease.

#### Vehicle and equipment

At June 30, 2008 the Corporation committed to future minimum payments under leases for vehicles and compressors, under operating leases, as follows:

Year	(\$000)
2008	41

The Corporation has entered into a series of equipment lease financing arrangements. Under these arrangements, the Corporation is committed to annual minimum lease payments as follows:

	(\$000)
2008	1,222
2009	2,274
2010	1,605
Total minimum lease payments	5,101
Less interest included in payments	(350)
Principal portion of minimum lease payments	4,751
Less current portion	(2,284)
<b>Capital lease obligation at June 30, 2008</b>	<b>2,467</b>

#### Flow-through Shares

In connection with the Corporation's flow-through share offering in 2007, Galleon is obligated to spend \$60.0 million on qualifying exploration expenses prior to December 31, 2008. As at June 30, 2008, approximately \$2.5 million of the required qualifying expenditures remain to be incurred.

## FINANCIAL INSTRUMENTS

Refer to the "Commodity Pricing and Marketing" section.

## BUSINESS RISKS

Galleon is engaged in the exploration, development and production of crude oil and natural gas. The oil and gas business is inherently risky and there is no assurance that hydrocarbon reserves will be discovered and economically produced. Operational risks include competition, reservoir performance uncertainties, environmental factors, and regulatory, environment and safety concerns. Financial risks associated with the petroleum industry include fluctuations in commodity prices, interest rates, currency exchange rates and the cost of goods and services.

Galleon employs highly qualified people, uses sound operating and business practices, and evaluates all potential and existing wells using the latest applicable technology. Galleon complies with government regulations and has in place an up-to-date emergency response program. Environment and safety policies and standards are adhered to. Asset retirement obligations are recognized upon acquisition, construction, development and/or normal use of the assets. Galleon maintains property and liability insurance coverage. The coverage provides a reasonable amount of protection from risk of loss; however, not all risks are foreseeable or insurable.

Financial risks include fluctuations in commodity prices, interest rates and the Canadian/US dollar exchange rate, and the cost of goods and services. The Corporation currently has three financial contracts with a Canadian chartered bank and two term natural gas contracts (see "Commodity Pricing and Marketing" for details). The Corporation also manages these risks by maintaining a healthy balance sheet with prudent levels of debt measured by debt to funds from operations and debt coverage ratios. This allows for strong financial capacity to maintain exploration and development activities in any downturn in commodity prices. An additional risk is credit risk for failure of performance by counter-parties. This risk is controlled by an evaluation of the credit risk before contract initiation and ensuring product sales and delivery contracts are made with well-known and financially strong crude oil and natural gas marketers.

All phases of the oil and natural gas business present environmental risks and hazards and are subject to environmental regulation pursuant to a variety of federal, provincial and local laws and regulations. Compliance with such legislation can require significant expenditures and a breach may result in the imposition of fines and penalties, some of which may be material. Environmental legislation is evolving in a manner expected to result in stricter standards and enforcement, larger fines and liability and potentially increased capital expenditures and operating costs. In 2002, the Government of Canada ratified the Kyoto Protocol (the "Protocol"), which calls for Canada to reduce its greenhouse gas emissions to specified levels. There has been much public debate with respect to Canada's ability to meet these targets and the Government's strategy or alternative strategies with respect to climate change and the control of greenhouse gases. Implementation of strategies for reducing greenhouse gases whether to meet the limits required by the Protocol or as otherwise determined could have a material impact on the nature of oil and natural gas operations, including those of the Corporation. Given the evolving nature of the debate related to climate change and the control of greenhouse gases and resulting requirements, it is not possible to predict either the nature of those requirements or the impact on the Corporation and its operations and financial condition.

## CHANGES IN ACCOUNTING POLICIES

As of January 1, 2008, Galleon adopted several new CICA standards, section 1400 "General Standards of Financial Statement Presentation", section 1535 "Capital Disclosures", section 3031 "Inventories", section 3862 "Financial Instruments – Disclosures" and Section 3863 "Financial Instruments – Presentation,".

CICA 1400, General Standards of Financial Statement Presentation, was amended to include requirements to assess and disclose an entity's ability to continue as a going concern. The new requirements are effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2008. The adoption of this standard did not have an impact on the Corporation's financial statements.

Section 1535 establishes standards for disclosing information regarding the capital of the entity and how it is managed. The section specifies the disclosure of i) objectives, policies, and processes for managing capital by the entity; ii) quantitative data about what the entity regards as capital; iii) whether the entity has complied with any capital requirements; and iv) if it has not complied, the consequences of such non-compliance.

CICA 3031, Inventories replaces CICA 3030, Inventories and establishes standards for measurement and disclosure of inventories. This standard provides guidance on the determination of cost and subsequent recognition as an expense, including any write-down to net realizable value and the reversal of previous write-downs when there is a subsequent increase in the value of inventories. It also provides guidance on the cost formulas that are used to assign costs. The adoption of this standard did not have an impact on the Corporation's financial statements.

Sections 3862 and 3863 replace section 3861 "Financial Instruments – Disclosure and Presentation" which revises and enhances financial instruments disclosure requirements and leaves unchanged its presentation requirements. The objective of section 3862 is to provide financial statement disclosure to enable users to evaluate the significance of financial instruments to the Corporation's financial position and performance. The section also requires increased disclosure on the nature and extent of risks arising from financial instruments that the Corporation is exposed to during the reporting period and the balance sheet date and how the corporation is managing those risks. The purpose of section 3863 is to enhance the financial statement users' understanding of the significance of financial instruments to the Corporation's financial position, performance and cash flows.

The Canadian Accounting Standards Board (AcSB) has confirmed that the use of the International Financial Reporting Standards ("IFRS") will be required in 2011 for publicly accountable profit-oriented enterprises. IFRS will replace Canada's current GAAP for those enterprises that are responsible to large or diverse groups of stakeholders. The official changeover date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. Companies will be required to provide comparative IFRS information for the previous fiscal year. Galleon is currently evaluating the impact of adopting IFRS.

## CONTROLS AND PROCEDURES OVER FINANCIAL REPORTING

Galleon has established disclosure controls and procedures to provide reasonable assurance that material information relating to Galleon, including its consolidated subsidiaries, is made known to the Chief Executive Officer (CEO) and the Chief Financial Officer (CFO) by others within those entities, particularly during the period in which the annual and interim filings have been prepared. The CEO and the CFO have designed or caused to be designed under their supervision, internal controls over financial reporting to provide reasonable assurance regarding the reliability of the Corporation's financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP.

The Corporation's CEO and CFO are required to cause the Corporation to disclose any change in the Corporation's internal controls over financial reporting that occurred during the Corporation's most recent interim period that has materially affected, or is reasonably likely to materially affect, the Corporation's internal controls over financial reporting. No material changes in the Corporation's internal controls over financial reporting were identified during the Corporation's most recent interim period that has materially affected, or are reasonably likely to materially affect, the Corporation's internal controls over financial reporting.

It should be noted that a control system, including the Corporation's disclosure and internal controls and procedures, no matter how well conceived, can provide only reasonable, but not absolute, assurance that the objectives of the control system will be met and it should not be expected that the disclosure and internal controls and procedures will prevent all errors or fraud.

## SHARE INFORMATION

The following table summarizes the outstanding shares of Galleon as of June 30:

	2008	2007
Class A shares outstanding		
Basic	72,817,827	59,734,952
Diluted <sup>1</sup>	79,031,312	65,133,902
Class B shares outstanding	922,500	922,500
Class A shares issuable on conversion of Class B shares <sup>2</sup>	447,816	525,941

<sup>1</sup> Includes total outstanding options of 6,213,485 (June 30, 2007 – 5,398,950).

<sup>2</sup> Assumes a conversion at the June 30, 2008 closing price of \$20.60 per Class A share (June 30, 2007 - \$17.54). The actual conversion rate varies based on a formula related to the trading price of the Class A shares.

At June 30, 2008, the market value of Galleon's class A and class B shares was \$1.5 billion based on the June 30, 2008 closing price of \$20.60 per class A share and \$9.65 per class B share. As of August 13, 2008, the number of class A shares, class B shares, and options outstanding are 72,918,493, 922,500 and 6,466,152 respectively.

## ADDITIONAL INFORMATION

Additional information relating to Galleon, including Galleon's Annual Information Form, can be accessed on-line on SEDAR at [www.sedar.com](http://www.sedar.com), or from the Corporation's website at [www.galleonenergy.com](http://www.galleonenergy.com).

## OUTLOOK

The successes of the Montney horizontal drilling program and new exploration oil and natural gas discoveries have led Galleon to increase the 2008 capital program to approximately \$280 million. The 2008 capital program is expected to be funded by internal cash flow. Approximately 60% of the capital expenditures in the second half of 2008 will be directed to Montney resource projects. Today, Galleon has identified eight Montney resource projects (six projects in Alberta and two in B.C.) spread over a large land base of approximately 0.5 million gross acres. Galleon expects to employ seven to eight rigs to drill between 72 and 80 wells in the second half of 2008.

Included in the expansion of the capital program is the construction of two natural gas facilities to be located in Dawson and Kakut, Alberta. At Dawson, a new plant with capacity of 10 Mmcf/d is planned for the southern end of the Eastern Montney pool. Combined with the existing 30 Mmcf/d natural gas plant located 20 km to the north, Galleon will have natural gas processing capacity of approximately 40 Mmcf/d in the area. The new plant is expected to be on-stream in late Q4 2008 or early Q1 2009. Kakut is located in the Central Montney region and is expected to be a significant growth area for Galleon. An owned natural gas plant at Kakut will be expanded from 5 Mmcf/d to 15 Mmcf/d and is scheduled to be on stream in Q4 2008.

Galleon has access to approximately one million gross acres of undeveloped land, of which 90% is located in the Peace River Arch area of Alberta and British Columbia. In combination with this large land base, the success of the drilling program to date, and the drilling opportunities planned during the second half of 2008, Galleon is positioned for production and reserve growth in 2008 and 2009.

## Quarterly Highlights

	2008			2007			2006	
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
<b>Production</b>								
Light oil (Bbl/d)	4,629	4,871	4,419	3,375	3,317	3,127	2,419	1,823
Heavy oil (Bbl/d)	2,066	2,919	1,746	1,949	2,247	2,081	2,100	1,984
Natural Gas (Mcf/d)	53,971	52,644	49,486	48,989	45,314	38,845	36,733	33,068
Liquids (Bbl/d)	501	441	283	237	256	206	230	102
<b>BOE/d</b>	<b>16,191</b>	17,005	14,695	13,726	13,372	11,888	10,869	9,420
Total BOE produced	1,473,414	1,547,476	1,351,986	1,262,762	1,216,855	1,069,915	999,982	866,646
<b>Daily BOE of production per million Class A shares – basic<sup>1</sup></b>								
	<b>229</b>	254	232	229	226	206	191	172
<b>Prices (net of transportation)</b>								
Light oil (\$/Bbl)	120.68	94.79	83.38	78.43	70.12	63.24	63.03	75.65
Heavy oil (\$/Bbl)	88.93	63.52	37.32	40.04	35.89	36.55	31.16	47.01
Crude oil (\$/Bbl)	110.88	85.20	64.40	63.25	56.30	52.57	47.19	53.35
Natural Gas (\$/Mcf)	9.65	7.73	6.16	5.73	7.14	7.36	6.84	5.58
NGLs (\$/Bbl)	71.19	59.59	72.90	64.05	59.67	56.64	56.02	69.83
<b>Per BOE (\$)</b>								
Revenues	81.85	65.60	52.77	47.64	49.91	49.51	45.26	46.06
Royalties, net of ARTC and GCA	(14.29)	(11.79)	(8.55)	(8.41)	(9.04)	(7.84)	(6.02)	(7.20)
Transportation costs	(1.64)	(1.04)	(1.18)	(1.13)	(1.16)	(1.47)	(1.37)	(1.25)
Operating costs	(12.71)	(11.28)	(10.52)	(8.35)	(8.63)	(8.86)	(9.65)	(10.66)
<b>Net</b>	<b>53.21</b>	41.49	32.52	29.75	31.08	31.34	28.22	26.95
Other revenue	0.07	0.08	–	–	–	–	–	–
G&A	(2.51)	(1.53)	(2.00)	(1.19)	(1.48)	(1.18)	(2.67)	(0.80)
Interest	(2.02)	(1.81)	(1.83)	(2.14)	(2.20)	(2.10)	(1.49)	(1.39)
Capital and other taxes	(0.24)	(0.22)	0.05	(0.18)	(0.41)	(0.21)	(0.21)	(0.33)
Realized gain (loss) on financial derivative	(7.00)	(2.18)	(2.49)	(0.44)	–	0.35	–	–
<b>Funds from operations<sup>2</sup></b>	<b>41.51</b>	35.83	26.25	25.80	26.99	28.20	23.85	24.43

<sup>1</sup>Restated to reflect a three-for-two Class A share split in June 2006.

<sup>2</sup>See “Non-GAAP Measurements”

## Quarterly Highlights

(unaudited)	2008		2007	
	Q2	Q1	Q4	Q3
<b>Financial (\$000s)</b>				
Revenues	120,602	101,516	71,339	60,156
Operating costs	(18,726)	(17,460)	(14,227)	(10,547)
General & administrative expenses	(3,698)	(2,371)	(2,712)	(1,507)
Interest expense	(2,977)	(2,803)	(2,476)	(2,707)
<b>Funds from operations<sup>2</sup></b>	<b>61,157</b>	<b>55,445</b>	35,483	32,566
Per share, basic <sup>1, 2</sup>	0.86	0.83	0.56	0.54
Per share, diluted <sup>1, 2</sup>	0.84	0.81	0.55	0.53
<b>Earnings</b>	<b>5,673</b>	<b>10,417</b>	(495)	1,590
Per share, basic <sup>1</sup>	0.08	0.16	(0.01)	0.03
Per share, diluted <sup>1</sup>	0.08	0.15	(0.01)	0.03
<b>Total assets</b>	<b>1,070,765</b>	<b>975,911</b>	799,359	743,932
Weighted average outstanding Class A shares-basic <sup>1</sup>	70,741,901	67,034,895	63,206,585	59,880,135
Weighted average outstanding Class A shares-diluted <sup>1</sup>	72,575,607	68,630,474	64,716,872	61,724,550

	2007		2006	
	Q2	Q1	Q4	Q3
<b>Financial (\$000s)</b>				
Revenues	60,734	52,974	45,264	39,921
Operating costs	(10,507)	(9,478)	(9,651)	(9,243)
General & administration expenses	(1,797)	(1,264)	(2,670)	(692)
Interest expense	(2,681)	(2,246)	(1,487)	(1,202)
<b>Funds from operations<sup>2</sup></b>	<b>32,834</b>	<b>30,170</b>	23,857	21,178
Per share, basic <sup>1, 2</sup>	0.55	0.52	0.42	0.39
Per share, diluted <sup>1, 2</sup>	0.54	0.50	0.40	0.37
<b>Earnings</b>	<b>3,270</b>	<b>3,921</b>	1,906	2,196
Per share, basic <sup>1</sup>	0.06	0.07	0.03	0.04
Per share, diluted <sup>1</sup>	0.05	0.07	0.03	0.04
<b>Total assets</b>	<b>699,112</b>	<b>692,749</b>	614,565	540,980
Weighted average outstanding Class A shares-basic <sup>1</sup>	59,204,393	57,800,899	56,761,415	54,854,334
Weighted average outstanding Class A shares-diluted <sup>1</sup>	61,175,217	59,947,494	59,234,229	57,447,555

<sup>1</sup> Restated to reflect a three-for-two Class A share split in June 2006.

<sup>2</sup> See "Non-GAAP Measurements".

## Consolidated Balance Sheets

As at	June 30, 2008	December 31, 2007
(\$000s) (unaudited)		
<b>ASSETS</b>		
Current		
Accounts receivable	56,336	35,406
Deposits and prepaid expenses	9,437	5,459
	<b>65,773</b>	<b>40,865</b>
Goodwill (notes 3 and 4)	34,628	16,022
Equipment inventory	6,957	2,829
Property and equipment (notes 3, 4, 5, 6 and 7)	963,407	739,643
	<b>1,070,765</b>	<b>799,359</b>
<b>LIABILITIES</b>		
Current		
Accounts payable and accrued liabilities	66,800	71,044
Gas contract (note 5)	4,577	–
Capital leases (notes 4 and 9)	2,284	–
Bank loan (note 8)	223,562	163,378
Fair value of financial derivatives (note 13)	32,180	9,075
	<b>329,403</b>	<b>243,497</b>
Asset retirement obligation (note 7)	35,351	25,535
Capital leases (notes 4 and 9)	2,467	–
Future income taxes (note 11)	83,108	52,299
	<b>450,329</b>	<b>321,331</b>
<b>SHAREHOLDERS' EQUITY</b>		
Share capital (note 10)	543,413	419,011
Contributed surplus (note 10)	20,980	19,064
Retained earnings	56,043	39,953
	<b>620,436</b>	<b>478,028</b>
	<b>1,070,765</b>	<b>799,359</b>

See accompanying notes

# Consolidated Statements of Earnings

## COMPREHENSIVE INCOME AND RETAINED EARNINGS

	Three months ended June 30		Six months ended June 30	
(\$'000s, except per share amounts) (unaudited)	2008	2007	2008	2007
<b>REVENUE</b>				
Petroleum and natural gas revenue	120,602	60,735	222,118	113,709
Royalties, net of GCA	(21,058)	(11,006)	(39,303)	(19,388)
Realized gain on gas contract (note 5)	763	–	763	–
Other income	105	–	228	–
	<b>100,412</b>	<b>49,729</b>	<b>183,806</b>	<b>94,321</b>
<b>EXPENSES</b>				
Operating	18,726	10,507	36,186	19,985
Transportation	2,416	1,408	4,031	2,995
General and administration	3,698	1,797	6,069	3,061
Interest	2,977	2,682	5,780	4,928
Stock-based compensation (note 10)	2,271	2,193	5,042	4,054
Accretion	464	356	1,032	673
Depletion and depreciation	32,433	24,979	66,052	47,001
Realized loss (gain) on financial derivative (note 13)	10,317	–	13,678	(373)
Unrealized loss (gain) on financial derivative (note 13)	18,178	26	23,105	(453)
	<b>91,480</b>	<b>43,948</b>	<b>160,975</b>	<b>81,871</b>
<b>EARNINGS BEFORE TAXES</b>	<b>8,932</b>	<b>5,781</b>	<b>22,831</b>	<b>12,450</b>
<b>Income taxes (note 11)</b>				
Capital and other taxes	358	502	697	722
Future income taxes	2,901	2,008	6,044	4,536
	<b>3,259</b>	<b>2,510</b>	<b>6,741</b>	<b>5,258</b>
<b>NET EARNINGS AND COMPREHENSIVE INCOME</b>	<b>5,673</b>	<b>3,271</b>	<b>16,090</b>	<b>7,192</b>
<b>RETAINED EARNINGS, BEGINNING OF PERIOD</b>	<b>50,370</b>	<b>35,588</b>	<b>39,953</b>	<b>31,667</b>
<b>RETAINED EARNINGS, END OF PERIOD</b>	<b>56,043</b>	<b>38,859</b>	<b>56,043</b>	<b>38,859</b>
<b>NET EARNINGS AND COMPREHENSIVE INCOME PER SHARE (note 10)</b>				
Basic	0.08	0.06	0.23	0.12
Diluted	0.08	0.05	0.23	0.12
Weighted average Class A shares – basic	70,741,901	59,204,393	68,862,794	58,506,523
– diluted	72,575,607	61,175,217	70,419,898	60,427,881

See accompanying notes

## Consolidated Statements of Cash Flows

	Three months ended June 30		Six months ended June 30	
(\$'000s) (unaudited)	2008	2007	2008	2007
Cash provided by (used in):				
<b>OPERATING ACTIVITIES</b>				
Net earnings	5,673	3,271	16,090	7,192
Items not requiring cash:				
Future income taxes	2,901	2,008	6,044	4,536
Depletion and depreciation	32,433	24,979	66,052	47,001
Accretion	464	356	1,032	673
Stock-based compensation	2,271	2,193	5,042	4,054
Unrealized loss (gain) on financial derivative	18,178	26	23,105	(453)
Realized gain on gas contract	(763)	–	(763)	–
Abandonment costs	(91)	(109)	(1,194)	(456)
Change in non-cash working capital	(4,613)	(1,619)	(17,570)	(3,682)
	<b>56,453</b>	<b>31,105</b>	<b>97,838</b>	<b>58,865</b>
<b>FINANCING ACTIVITIES</b>				
Issue of common shares	8,055	31,378	9,893	32,178
Share issue costs	(89)	(1,632)	(181)	(1,636)
Capital lease payment	(624)	–	(1,108)	–
Working capital assumed on acquisition of ExAlta <i>(note 4)</i>	1,317	–	(44,966)	–
Working capital assumed on acquisition of Adamant <i>(note 5)</i>	8,019	–	8,019	–
Bank loan	(6,304)	(21,323)	60,184	45,095
	<b>10,374</b>	<b>8,423</b>	<b>31,841</b>	<b>75,637</b>
<b>INVESTING ACTIVITIES</b>				
(Additions to) disposal of equipment inventory	(2,444)	(272)	(2,567)	453
Additions to oil and gas properties	(34,856)	(23,668)	(106,182)	(85,602)
Acquisition of oil and gas properties <i>(note 3, 4, 5 and 6)</i>	(9,849)	(5,900)	(11,632)	(34,606)
Change in non-cash working capital	(19,678)	(9,688)	(9,298)	(14,747)
	<b>(66,827)</b>	<b>(39,528)</b>	<b>(129,679)</b>	<b>(134,502)</b>
<b>CHANGE IN CASH</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>
<b>CASH, BEGINNING AND END OF PERIOD</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>
<b>SUPPLEMENTARY INFORMATION</b>				
Cash interest paid	2,972	2,933	5,775	5,168
Cash taxes paid	56	168	446	333

See accompanying notes

# Notes to the Consolidated Financial Statements

FOR THE THREE AND SIX MONTH PERIODS ENDED JUNE 30, 2008 AND 2007 (unaudited)

Unless otherwise stated, amounts presented in these notes are in Canadian dollars and tabular amounts are in thousands of Canadian dollars, except number of shares and per share amounts.

## 1. ACCOUNTING POLICIES

### Nature of Business and Basis of Presentation

Galleon Energy Inc. ("Galleon" or the "Corporation") was incorporated under the Business Corporations Act of Alberta on March 27, 2003. The business of the Corporation is the acquisition of, exploration for and development of petroleum and natural gas properties in western Canada. Galleon is listed on the TSX under the symbols "GO.A" and "GO.B".

These unaudited interim consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"), and follow the same accounting policies as the financial statements for the year ended December 31, 2007, except as noted below.

These notes do not include all disclosures required in annual financial statements and are incremental to, and should be read in conjunction with the audited financial statements for the year ended December 31, 2007.

## 2. CHANGES IN SIGNIFICANT ACCOUNTING POLICIES

As of January 1, 2008, Galleon adopted several new CICA standards, section 1400 "General Standards of Financial Statement Presentation", section 1535 "Capital Disclosures", section 3031 "Inventories", section 3862 "Financial Instruments – Disclosures" and Section 3863 "Financial Instruments – Presentation,".

CICA 1400, General Standards of Financial Statement Presentation, was amended to include requirements to assess and disclose an entity's ability to continue as a going concern. The new requirements are effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2008. The adoption of this standard did not have an impact on the Corporation's financial statements.

Section 1535 establishes standards for disclosing information regarding the capital of the entity and how it is managed. The section specifies the disclosure of i) objectives, policies, and processes for managing capital by the entity; ii) quantitative data about what the entity regards as capital; iii) whether the entity has complied with any capital requirements; and iv) if it has not complied, the consequences of such non-compliance.

CICA 3031, Inventories replaces CICA 3030, Inventories and establishes standards for measurement and disclosure of inventories. This standard provides guidance on the determination of cost and subsequent recognition as an expense, including any write-down to net realizable value and the reversal of previous write-downs when there is a subsequent increase in the value of inventories. It also provides guidance on the cost formulas that are used to assign costs. The adoption of this standard did not have an impact on the Corporation's financial statements.

Sections 3862 and 3863 replace section 3861 "Financial Instruments – Disclosure and Presentation" which revises and enhances financial instruments disclosure requirements and leaves unchanged its presentation requirements. The objective of section 3862 is to provide financial statement disclosure to enable users to evaluate the significance of financial instruments to the Corporation's financial position and performance. The section also requires increased disclosure on the nature and extent of risks arising from financial instruments that the Corporation is exposed to during the reporting period and the balance sheet date and how the Corporation is managing those risks. The purpose of section 3863 is to enhance the financial statement users' understanding of the significance of financial instruments to the Corporation's financial position, performance and cash flows.

The Canadian Accounting Standards Board (AcSB) has confirmed that the use of the International Financial Reporting Standards ("IFRS") will be required in 2011 for publicly accountable profit-oriented enterprises. IFRS will replace Canada's current GAAP for those enterprises that are responsible to large or diverse groups of stakeholders. The official changeover date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. Companies will be required to provide comparative IFRS information for the previous fiscal year. Galleon is currently evaluating the impact of adopting IFRS.

#### Accounting for Leases

The Corporation's leases are classified as either capital or operating. Assets under capital lease are initially recorded at the present value of the minimum lease payments at inception of the lease. Payments under operating leases are expensed as incurred.

### 3. ACQUISITION OF PARTNERSHIP

On February 1, 2007, the Corporation closed a transaction resulting in an acquisition of an interest in a partnership and the minority partnership's holdings resulting in a 100% consolidated interest. The partnership held oil and gas assets within Galleon's core area of Dawson, Alberta. The total consideration of \$28.7 million was paid in cash. The business combination has been accounted for as a purchase as at the closing date of the transaction, with the purchase price allocated to assets and liabilities as follows:

Allocation of Purchase Price	\$
Property and equipment	30,874
Goodwill	5,883
Asset retirement obligation	(980)
Future income taxes	(7,045)
	<u>28,732</u>
Calculation of Purchase Price	
Cash for purchase of interest	28,664
Transaction costs	68
	<u>28,732</u>

#### 4. ACQUISITION OF EXALTA ENERGY INC.

On January 16, 2008, the Corporation acquired all of the outstanding common shares of ExAlta Energy Inc. ("ExAlta"). The ExAlta acquisition was accounted for by the purchase method and shares were acquired for an aggregate of \$62.5 million by the issuance of 4,334,856 Class A shares of Galleon at a value of \$14.42 per share plus the assumption of \$48.5 million of net debt including capital leases. The acquisition has been accounted for as a purchase as at the closing date of the transaction, with the purchase price allocated on a preliminary basis to assets and liabilities as follows:

Allocation of Purchase Price	\$
Property and equipment	95,748
Equipment inventory	1,290
Goodwill	18,606
Future income taxes	582
Bank debt and working capital assumed (including bank debt of \$43.1 million)	(44,966)
Asset retirement obligation	(3,403)
Capital lease	(3,575)
	64,282
Calculation of Purchase Price	
Fair value of shares issued	62,509
Transaction costs	1,773
	64,282

#### 5. ACQUISITION OF ADAMANT ENERGY INC

On May 9, 2008, the Corporation acquired all of the outstanding common shares of Adamant Energy Inc. ("Adamant"). The Adamant acquisition was accounted for by the purchase method and shares were acquired for an aggregate of \$65.2 million by the issuance of 4,193,288 Class A shares of Galleon at a value of \$15.55. The acquisition has been accounted for as a purchase as at the closing date of the transaction, with the purchase price allocated on a preliminary basis to assets and liabilities as follows:

Allocation of Purchase Price	\$
Property and equipment	76,340
Equipment inventory	271
Working capital assumed (including cash of \$2.4 million)	8,019
Future income taxes	(9,196)
Asset retirement obligation	(4,431)
Gas contract	(5,340)
	65,663
Calculation of Purchase Price	
Fair value of shares issued	65,206
Transaction costs	457
	65,663

The gas contract will be amortized over the term of the contract which is to December 31, 2008.

## 6. PROPERTY AND EQUIPMENT

On July 3, 2007 the Corporation purchased oil and gas properties in the Eaglesham/Kakut area of Alberta for cash of \$15.7 million. An asset retirement obligation of \$436,367 has been recorded for this property purchase.

On June 29, 2007 the Corporation purchased oil and gas properties in the Shadow area of Alberta for cash of \$5.1 million. An asset retirement obligation of \$65,750 has been recorded for this property purchase.

As at June 30, 2008, \$109.9 million (June 30, 2007 - \$84.1 million) of undeveloped land and seismic have been excluded from and \$112.8 million (June 30, 2007 - \$85.8 million) in future development costs have been added into the full cost pool for depletion purposes. For the three and six months ended June 30, 2008, \$332,066 and \$569,722, respectively (June 30, 2007 - \$217,874 and 350,374 respectively) of exploration salaries have been capitalized.

As at June 30, 2008

	Cost \$	Accumulated depletion \$	Net book value \$
Petroleum and natural gas properties & equipment	1,359,328	(404,068)	955,260
Equipment under capital lease	10,601	(4,359)	6,242
Office furniture and equipment	2,873	(968)	1,905
	<b>1,372,802</b>	<b>(409,395)</b>	<b>963,407</b>

As at December 31, 2007

	Cost \$	Accumulated depletion \$	Net book value \$
Petroleum and natural gas properties & equipment	952,752	(213,401)	739,351
Equipment under capital lease	—	—	—
Office furniture and equipment	1,025	(733)	292
	<b>953,777</b>	<b>(214,134)</b>	<b>739,643</b>

## 7. ASSET RETIREMENT OBLIGATION

The Corporation's asset retirement obligations result from net ownership interests in petroleum and natural gas assets including well sites, gathering systems and processing facilities. The Corporation estimates the total undiscounted amount of cash flows required to settle its asset retirement obligation is approximately \$75.8 million, which will be incurred over the next 18 years. Credit adjusted risk free rates of 5% and 8% and an inflation rate of 2% were used to calculate the fair value of the asset retirement obligation.

	Six months ended June 30, 2008 \$	Year ended December 31, 2007 \$
Balance, beginning of period	25,535	21,432
Accretion expense	1,032	1,949
Liabilities incurred	1,247	3,346
Liabilities acquired	7,834	980
Revision of liabilities	—	—
Settlement of liabilities	(297)	(2,172)
<b>Balance, end of period</b>	<b>35,351</b>	<b>25,535</b>

## 8. AVAILABLE CREDIT FACILITY

The Corporation has extendible revolving term credit facilities of \$310 million in place with a bank syndicate. The facilities bear interest at rates ranging from the bank's prime rate to prime plus 0.75% per annum on \$290 million and at rates ranging from the bank's prime rate plus 0.95% to prime plus 1.75% on \$20 million based on the Corporation's debt to cash flow ratio. The Corporation may also borrow at the prevailing Banker's Acceptance rate. Collateral for the facilities consists of a demand debenture for \$500 million collateralized by a first floating charge over all of the property and equipment of the Corporation. At June 30, 2008, an amount of \$223.6 million was drawn against the credit facilities (December 31, 2007 - \$163.4 million).

## 9. CAPITAL LEASE OBLIGATIONS

The Corporation has entered into a series of equipment lease financing arrangements. Under these arrangements, the Corporation is committed to annual minimum lease payments as follows:

	\$
2008	1,222
2009	2,274
2010	1,605
Total minimum lease payments	5,101
Less interest included in payments	(350)
Principal portion of minimum lease payments	4,751
Less current portion	(2,284)
<b>Capital lease obligation at June 30, 2008</b>	<b>2,467</b>

Interest expense of \$0.1 million and \$0.2 million, respectively, was incurred on the capital leases during the three and six month periods ending June 30, 2008 (June 30, 2007 – \$nil and \$nil, respectively).

The applicable terms and commitments are summarized in the following table:

End of lease term	Outstanding principal	Purchase price at end of lease	Interest rate
June 2009	\$196	\$142	2.2 percent above the 30-day bankers' acceptance rate
October 2009	\$326	–	2.1 percent above the 30-day banker's acceptance rate
December 2009	\$1,526	–	6.0 percent
September 2010	\$2,703	\$1,000	6.3 percent

A general security agreement and a first charge against the equipment have been provided as collateral.

## 10. SHARE CAPITAL

## Authorized

Unlimited number of preferred shares with no par value

Unlimited number of voting Class A shares with no par value

Unlimited number of voting Class B shares with no par value, convertible (at the option of the Corporation) at any time after December 31, 2007 and before December 31, 2008, into Class A shares. The conversion factor is calculated by dividing \$10 by the greater of \$1 and the then current market price of Class A shares. If conversion has not occurred by the close of business on December 31, 2008, the Class B shares become convertible (at the option of the shareholder) into Class A shares on the same basis. Effective February 1, 2009, all remaining Class B shares will be deemed to be converted to Class A shares.

## Issued and outstanding

Class A shares	Number of Shares	Amount \$
<b>Balance at December 31, 2006 (a)</b>	57,712,077	334,662
Issued for cash (b)	1,869,200	30,001
Issue of flow-through shares for cash (b)	2,944,900	60,000
Issued for cash on exercise of stock options	689,375	3,256
Tax effect of flow through shares	–	(11,692)
Share issue costs, net of tax of \$1,431	–	(3,494)
Transfer from contributed surplus	–	1,071
<b>Balance at December 31, 2007</b>	<b>63,215,552</b>	<b>413,804</b>
Issued as consideration for shares in ExAlta Energy Inc. (b)	4,334,856	62,509
Issued for cash on exercise of stock options	247,866	1,838
Tax effect of flow through shares	–	(16,200)
Share issue costs, net of tax of \$25	–	(67)
Transfer from contributed surplus	–	599
<b>Balance at March 31, 2008</b>	<b>67,798,274</b>	<b>462,483</b>
Issued as consideration for shares in Adamant Energy Inc. (b)	4,193,288	62,206
Issued for cash on exercise of stock options	826,265	8,055
Share issue costs, net of tax of \$24	–	(65)
Transfer from contributed surplus	–	2,527
<b>Balance at June 30, 2008</b>	<b>72,817,827</b>	<b>538,206</b>
<b>Class B shares</b>		
Balance at June 30, 2008 and December 31, 2007	922,500	5,207
<b>Total share capital at June 30, 2008</b>	<b>73,740,327</b>	<b>543,413</b>

- a) On June 7, 2006, the shareholders of the Corporation approved a three-for-two Class A share split. The number of Class A shares above has been restated to reflect the share split.
- b) On May 9, 2008, the Corporation issued 4,193,288 Class A shares at \$15.55 per share as consideration for shares in Adamant Energy Inc. as described in Note 5.

On January 16, 2008, the Corporation issued 4,334,856 Class A shares at \$14.42 per share as consideration for shares in ExAlta Energy Inc. as described in Note 4.

On September 28, 2007, the Corporation issued 1,869,200 Class A shares at \$16.05 per share and 1,463,400 flow-through Class A shares at \$20.50 per share pursuant to a public offering for aggregate gross proceeds of \$60.0 million.

Galleon is obligated to incur qualifying exploration expenses of \$30.0 million prior to December 31, 2008. As at June 30, 2008 approximately \$2.5 million of the required qualifying expenditures remain to be incurred.

On April 19, 2007, the Corporation issued 1,481,500 flow-through Class A shares at \$20.25 per share by way of private placement for gross proceeds of \$30.0 million. Galleon is obligated to incur qualifying exploration expenses of \$30.0 million prior to December 31, 2008. As at June 30, 2008, all of the required qualifying expenditures have been incurred.

The tax effect of \$16.2 million related to the renouncement in January 2008 of the flow-through shares was recorded in Q1 2008.

The Corporation has a share option plan which was approved on May 19, 2005 and amended on August 25, 2005 and June 19, 2007. In 2008, the exercise price of each option equals the market price of the Corporation's Class A shares on the date of the grant. Compensation expense is recognized as the options vest (one third immediately and one third on each of the first and second anniversaries of the date of the grant). The options expire five years from the date of grant. The Corporation may grant up to 10% of the aggregate number of Class A shares and Class B shares outstanding and no one optionee is permitted to hold options entitling such optionee to purchase more than 5% of the aggregate number of issued and outstanding Class A and Class B shares. Class A shares have been reserved for all options granted.

	Six months ended June 30, 2008	Year ended December 31, 2007
	\$	\$
Contributed surplus, beginning of period	19,064	11,619
Stock based compensation expense	5,042	8,516
Transfer to share capital	(3,126)	(1,071)
<b>Contributed surplus, end of period</b>	<b>20,980</b>	<b>19,064</b>

The fair value of options granted was estimated at the date of grant using a Black-Scholes Option Pricing Model with the following assumptions: risk-free interest rates of 2.00-4.51%; dividend yield of 0%; volatility factors of the market price of the Corporation's common shares of 34-46%; and, an average expected life of the options of 3 years.

	Number of Shares <sup>1</sup>	Weighted Average Exercise Price <sup>1</sup> \$
Outstanding, December 31, 2006	5,310,325	10.28
Granted	1,720,000	15.51
Cancelled	(130,000)	(9.60)
Exercised	(689,375)	(4.72)
Outstanding, December 31, 2007	6,210,950	12.36
Granted	965,000	13.80
Cancelled	(131,667)	(19.58)
Exercised	(247,866)	(7.42)
Outstanding, March 31, 2008	6,796,417	12.64
Granted	430,000	18.18
Cancelled	(186,667)	21.59
Exercised	(826,265)	9.75
<b>Outstanding, June 30, 2008</b>	<b>6,213,485</b>	<b>13.10</b>

<sup>1</sup> Restated to reflect the three-for-two Class A share split in June 2006.

### Earnings per share

The Corporation utilizes the treasury stock method in the determination of diluted per share amounts. Under this method, the diluted weighted average number of shares is calculated assuming the proceeds that arise from the exercise of outstanding and in the money options are used to purchase common shares of the Corporation at their average market price for the period. For the three and six months ended June 30, 2008, 1,152,500 and 1,995,000 options, respectively have been excluded from the diluted earnings per share calculation as they are anti-dilutive (June 30, 2007 – 1,172,500 and 1,715,000, respectively). For the three and six months ended June 30, 2008, the dilutive weighted average number of Class A shares outstanding after deemed conversion of the Class B shares is 73,083,871 and 70,973,955, respectively (June 30, 2007 – 61,714,779 and 60,981,538, respectively). The prior year amounts have been restated to reflect the three-for-two Class A share split in June 2006.

## 11. INCOME TAXES

The future income tax liability is comprised of the following temporary differences as at:

	June 30, 2008	December 31, 2007
	\$	\$
Property and equipment	65,377	47,108
ACRI benefit	(870)	(870)
Share issue costs	(3,323)	(3,716)
Asset retirement obligation	(553)	(209)
Non-capital losses	–	(27,020)
Gas contract	(1,236)	–
Partnership income tax deferral	33,684	39,517
Capital leases	(1,283)	–
Financial derivative	(8,688)	(2,511)
<b>Future income tax liability</b>	<b>83,108</b>	<b>52,299</b>

## 12. COMMITMENTS

### Drilling Rig

The Corporation has entered into a Master Daywork Contract whereby it is entitled to the use of a drilling rig for a two year period which commenced in November, 2007. Future minimum payments under this contract are as follows:

Year	Amount \$
2008	1,970
2009	4,170

### Minimum Lease Payments

At June 30, 2008 the Corporation has committed to future minimum payments under operating leases that cover office space as follows:

Year	Amount \$
2008	1,334
2009	2,514
2010	1,800

The above commitment includes an estimate of the Corporation's share of operating expenses, utilities and taxes for the duration of the office lease.

#### Vehicle and equipment

At June 30, 2008 the Corporation committed to future minimum payments under leases for vehicles and compressors, under operating leases, as follows:

Year	Amount \$
2008	41

#### Flow-through Shares

In connection with the Corporation's flow-through share offerings in 2007, Galleon is obligated to spend \$60.0 million on qualifying exploration expenses prior to December 31, 2008. As at June 30, 2008, approximately \$2.5 million of eligible capital expenditures remained to be incurred.

#### Litigation

The Corporation is involved in various other claims and legal actions arising from the normal course of business. The Corporation does not expect that the outcome of these proceedings will have a material adverse effect on the Corporation as a whole.

### 13. FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS

#### Fair Value of Financial Assets

The Corporation's financial instruments recognized in the balance sheet consist of accounts receivable, accounts payable, bank loan and financial derivative ("financial instruments"). The carrying value of accounts receivable and accounts payable approximated their fair values at June 30, 2008 due to their short-term nature. The carrying value of the bank loan approximates their fair value due to the floating interest rate on the facility. The fair value of the financial derivative is recognized on the balance sheet as described below.

#### Credit risk

Credit risk is the risk that a customer or counterparty will fail to perform an obligation or fail to pay amounts due causing a financial loss. The Corporation's accounts receivable are with customers and joint venture partners in the oil and gas industry and are subject to normal credit risks. A portion of the Corporation's production is currently sold through joint venture partners under normal industry sale and payment terms. As at June 30, 2008, approximately 60% of the accounts receivable balance is due from two customers, compared to 70% at June 30, 2007. These customers are considered to have high credit worthiness. The Corporation generally grants unsecured credit but routinely assesses the financial strength of its customers and joint venture partners. No provision has been made for past due receivables as of June 30, 2008 as the Corporation has assessed there are no impaired receivables.

As at June 30, the aging analysis of trade receivables is as follows:

	2008 \$
Current	51,898
30 – 60 days	4
60 – 90 days	1,043
greater than 90 days	3,391
<b>Total</b>	<b>56,336</b>

#### Liquidity risk

Liquidity risk arises through excess financial obligations over available financial assets due at any point in time. The Corporation's objective in managing liquidity risk is to maintain sufficient available reserves in order to meet its liquidity requirements at any point in time. The Corporation believes that it has access to sufficient capital through internally generated cash flows and external equity sources, and to undrawn committed credit facilities to meet current spending forecasts. All of the Corporation's liabilities mature in 2008.

#### Interest rate risk

The Corporation is exposed to interest rate risk as changes in interest rates may affect future cash flows and the fair value of its financial instruments. The Corporation's primary debt facility has a floating interest rate that will fluctuate based on prevailing market conditions. Cash flows are sensitive to changes in interest rates on this instrument. Given the amount of debt employed, the Corporation's strategy is to manage interest rate risk within the current framework. If interest rates on the floating instrument were to change by 1% it is estimated that annual cash flow would change by approximately \$2.0 million.

#### Market risk

Market risk is the risk of uncertainty arising from possible market price movements and their impact on the future performance of the business. The market price movements that could adversely affect the value of the Corporation's financial assets, liabilities and expected future cash flows include commodity price risk and interest rate risk. It is estimated that annual cash flow would change approximately by \$2.3 million and by \$4.5 million, respectively, due to a \$1 USD WTI and a \$0.25/Mcf CDN change in oil and natural gas prices.

The Corporation has the following costless collar financial derivatives in place for crude oil as at June 30, 2008:

#### Crude Oil

January 1, 2008 – December 31, 2008	2,000 Bbl/d	WTI CDN \$70.00-\$80.75/Bbl
January 1, 2008 – December 31, 2008	1,000 Bbl/d	WTI USD \$75.00-\$100.00/Bbl
July 1, 2008 – December 31, 2008	1,000 Bbl/d	WTI CDN \$110.00-\$177.30/Bbl

Galleon has entered into the above financial derivative contracts for the purpose of protecting funds generated from operations from the volatility of crude oil prices. For the three and six months ended June 30, 2008, the contracts had realized losses of \$10.3 million and \$13.7 million, respectively (June 30, 2007, \$nil and a gain of \$0.4 million, respectively).

The Corporation recognizes the fair value of its financial derivatives on the balance sheet each reporting period with the change in fair value recognized as an unrealized gain or loss on the statement of earnings. The fair value is based on quoted market prices. At June 30, 2008 the fair value was estimated to be a liability of \$32.2 million.

The fair value of a financial instrument is the amount of consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act. Fair values can be determined by reference to prices for that instrument in active markets to which the Corporation has access. Fair value is determined using inputs that are quoted prices in active markets for identical assets or liabilities that the Corporation has the ability to access. In determining fair values, the Corporation uses quoted prices for identically traded commodities obtained from active exchanges such as the New York Mercantile Exchange and the Natural Gas Exchange, or obtained directly from brokers, or other publicly available market data providers.

The Corporation has the following costless collar physical derivative contract in place for natural gas at June 30, 2008: :

#### Natural Gas

February 1, 2008 – December 31, 2008	10,000 GJ/day	CDN \$6.00-\$8.00 GJ
January 1, 2008 – December 31, 2008	8,500 GJ/day	CDN \$6.00-\$7.00 GJ

Galleon has entered into the above physical derivative contracts for the purpose of protecting funds generated from operations from the volatility of natural gas prices.

#### 14. CAPITAL STRUCTURE FINANCIAL POLICIES

The Corporation defines capital as total debt and shareholders' equity comprised of retained earnings and share capital. The Corporation's primary capital management objective is to maintain a strong balance sheet affording the Corporation financial flexibility to achieve goals of continued growth and access to capital. The basis for the Corporation's capital structure is dependent on the Corporation's expected business growth and changes in the business environment. The Corporation manages its capital structure and makes adjustments according to market conditions to maintain flexibility while achieving the objectives stated above. To manage the capital structure, the Corporation may adjust capital spending, issue new shares, issue new debt or repay existing debt.

The Corporation monitors its progress through the following two measures utilizing book values: net debt to funds from operations and total debt to total debt and shareholders' equity. Net debt to funds from operations is calculated as current liabilities and long term debt less current assets divided by the most recent quarters annualized funds from operations. Total debt to total debt plus shareholders' equity is calculated as short term debt plus long term debt divided by short term debt plus long term debt plus shareholders' equity.

The Corporation's strategy is to maintain net debt to funds from operations at or below a level of 1.5 to 1. While the Corporation may exceed this rate from time to time, variations are viewed as short term, and efforts are made after a period of variation to bring the measure back in line.

The Corporation's strategy concerning capitalization is to utilize more equity than debt. This is measured by targeting total debt to total debt plus shareholders' equity at a ratio of less than 0.4 to 1. The Corporation has no externally imposed capital requirements.

At June (\$'000s)	Target Measure	2008 \$	2007 \$
Components of ratios			
Current assets (excluding fair value of financial derivative)		65,773	28,674
Current liabilities (including short term debt and excluding fair value of financial derivative and gas contract)		292,646	206,552
Short term debt (bank loan and current portion of capital lease)		225,846	168,091
Net debt (working capital and capital leases)		229,340	177,878
Total debt (bank loan and capital leases)		228,313	168,091
Shareholders' equity (share capital plus retained earnings)		599,456	398,775
Total capitalization (total debt plus shareholders' equity)		827,769	566,866
Funds from operations <sup>1</sup> (six months ended June 30 annualized)		233,204	126,006
Net debt/funds from operations	< 1.5 times	1.0	1.4
Total debt/total debt plus shareholders' equity	< 0.4 times	0.3	0.3

<sup>1</sup> Funds from operations is a non-GAAP measure and is based on cash flow from operating activities before changes in non-cash working capital and abandonment expenditures.

The decrease in the net debt to funds from operations ratio from 2007 to 2008 resulted primarily from a large increase of 85% in funds from operations compared to an increase of 29% in net debt.

## 15. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform to the current period's consolidated financial statement presentation.

## ABBREVIATIONS

Oil and Natural Gas Liquids		Natural Gas	
<b>Bbl</b>	barrel	<b>Mcf</b>	thousand cubic feet
<b>Bbls</b>	barrels	<b>MMcf</b>	million cubic feet
<b>Mbbls</b>	thousand barrels	<b>Mcf/d</b>	thousand cubic feet per day
<b>MMbbls</b>	million barrels	<b>MMcf/d</b>	million cubic feet per day
<b>Mstb</b>	1,000 stock tank barrels	<b>MMbtu</b>	million British Thermal Units
<b>Bbls/d</b>	barrels per day	<b>Bcf</b>	billion cubic feet
<b>NGLs</b>	natural gas liquids	<b>GJ</b>	gigajoule
<b>STB</b>	standard tank barrels	<b>MM</b>	Million

## Other

<b>AECO</b>	A natural gas storage facility located at Suffield, Alberta
<b>API</b>	American Petroleum Institute
<b>°API</b>	An indication of the specific gravity of crude oil measured on the API gravity scale.
<b>ARTC</b>	Alberta Royalty Tax Credit
<b>BOE</b>	Barrel of oil equivalent of natural gas and crude oil on the basis of 1 BOE for 6 Mcf of natural gas (this conversion factor is an industry accepted norm and is not based on either energy content or current prices)
<b>BOE/d</b>	barrel of oil equivalent per day
<b>GCA</b>	gas cost allowance
<b>m<sup>3</sup></b>	cubic metres
<b>MBOE</b>	thousand barrels of oil equivalent
<b>MMBOE</b>	million barrels of oil equivalent
<b>\$000s</b>	thousands of dollars
<b>WTI</b>	West Texas Intermediate, the reference price paid in U.S. dollars at Cushing, Oklahoma for crude oil of standard grade

## COMPANY DEFINITION

Throughout the Quarterly Report, Galleon Energy Inc. is referred to as “Galleon”, or the “Corporation”.

## VOLUME REPORTING

Barrel of oil equivalent (BOE) (6:1) figures for the periods presented throughout this document are expressed at a conversion rate of six thousand cubic feet of natural gas to one barrel of crude oil. BOEs may be misleading, particularly if used in isolation. The forgoing conversion ratio is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

## Corporate Information

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### BOARD OF DIRECTORS

John A. Brussa<sup>3</sup>  
Glenn R. Carley, *Executive Chairman*<sup>2</sup>  
William L. Cooke<sup>1 2 3</sup>  
Daryl H. Gilbert  
Brad R. Munro<sup>1</sup>  
Steve Sugianto  
<sup>1</sup> Member of the Audit and Reserves Committee  
<sup>2</sup> Member of the Compensation Committee  
<sup>3</sup> Member of the Corporate Governance Committee

### OFFICERS

Steve Sugianto, *President and Chief Executive Officer*  
Glenn R. Carley, *Executive Chairman*  
Shivon M. Crabtree, *Vice President, Finance & Chief Financial Officer*  
Jim Iverson, *Vice President, Exploration East*  
Dale Orton, *Vice President, Engineering*  
Devin Sundstrom, *Vice President, Production*  
Chris Tibbles, *Vice President, Land*  
Bill Wee, *Vice President, Corporate Development*  
C. Steven Cohen, *Secretary*

### AUDITOR

Ernst & Young LLP  
Calgary, Alberta

### BANK

The Bank of Nova Scotia  
Calgary, Alberta  
ATB Financial  
Calgary, Alberta  
HSBC Bank Canada  
Calgary, Alberta  
The Toronto-Dominion Bank  
Calgary, Alberta  
Fortis Capital Canada Ltd.  
Calgary, Alberta  
Union Bank of California  
Canada Branch  
Calgary, Alberta

### LEGAL COUNSEL

Burnet, Duckworth & Palmer LLP  
Calgary, Alberta

### EVALUATION ENGINEERS

DeGolyer and MacNaughton  
Canada Limited  
Calgary, Alberta

### REGISTRAR AND TRANSFER AGENT

Valiant Trust Company  
Calgary, Alberta

### STOCK EXCHANGE LISTING

Toronto Stock Exchange  
Trading Symbols GO.A and GO.B



