EQUATOR
EXPLORATION LIMITED



Exploring West African Waters

ANNUAL REPORT AND
FINANCIAL STATEMENTS 2006

Equator Exploration is an independent oil and gas exploration and production company founded in December 2000 and was listed on the Alternative Investment Market of the London Stock Exchange in December 2004. Equator's objective is to build a diversified portfolio of exploration, appraisal and production assets in the highly prospective Gulf of Guinea region. The Company also generates revenue from the acquisition, marketing and sale of seismic data.

Contents

CHIEF EXECUTIVE'S STATEMENT

EVENTS DURING 2006

Early in the year, we took steps to increase and diversify our portfolio with the acquisition of interests in three additional offshore blocks. In March 2006, Equator signed two Production Sharing Contracts ('PSC') with the Nigeria National Petroleum Corporation and was awarded 30% interests in both blocks OPL 323 and OPL 321, offshore Nigeria. The Company also signed a PSC with the Nigeria/São Tomé e Príncipe Joint Development Authority and was awarded a 6% interest in Block 2 of the Joint Development Zone, which was subsequently increased to 9%.

In order to enable the Company to fund these investments and to support the exploration, appraisal and development programme for OML 122, in February 2006 we placed 41,050,900 new common shares with institutional investors at a price per share of 350p (US$6.09) for total proceeds of £143.7million (US$250million). In August, the Company raised US$65million of debt from a syndicate of shareholders to provide further funding for the capital development of the Bilabri Field.

The Company continued the development of the Bilabri Field on OML 122, offshore Nigeria, ordering long lead items and contracting a Floating Production, Storage and Offtake Vessel ('FPSO') with BW Offshore. Drilling continued with the Owanare AX-1 exploration well and then three Bilabri appraisal/development wells. However, as a result of these activities, the volumes of oil in the Bilabri Field and of the new gas reserves discovered in the Bilabri and Owanare Fields turned out to be less than originally anticipated.

During 2006, the Company took steps to add expertise to the Board and Management. In May, Dr Kenneth Seymour was appointed General Manager in Nigeria, in August, Jeffrey Auld was appointed as Chief Financial Officer and, in September, Russ Guyatt was appointed Vice President, Technical. However, at the December Annual General Meeting, James Ladner resigned as a director and Jean-Luc Vermeulen also stepped down as an advisor to the Board.

EVENTS DURING 2007

In February 2007, Alexander Dembitz retired unexpectedly from the Board due to personal reasons. In March, Jeffrey Auld resigned as Chief Financial Officer and director and Martin Adams and Tony Renton were appointed non-executive directors. Also in March, Philip Rand was appointed Chief Financial Officer and a director. In July, our Chairman, Sam Jonah, resigned and, at the end of September, Baroness Chalker also resigned from the Board.

The Company's operations on the Bilabri Field development suffered from ongoing security issues including another kidnapping of rig personnel which resulted in protracted inactivity and culminated in the termination of both the drilling rig contract and the FPSO contract. This has put sole funding of the remainder of the project by Equator in some doubt. In September, Equator transferred the responsibility of completing the project to Peak, while retaining a smaller interest in future oil and gas production. Consequently, your Board considers it prudent to make a provision of US$200million, equal to the cumulative expenditure in OML 122 to the end of 2006, to ensure that the likely value is represented conservatively in the financial statements.

On 11 June, the Company announced that it had entered into a conditional Merger Agreement relating to a proposed merger, by reverse takeover, of Equator and Camac Energy Holdings Limited, a wholly owned subsidiary of Camac International Limited. The merger negotiations were terminated in August when it became clear that it was not going to be possible to produce the admission document required under the rules of the Alternative Investment Market.

Finally, we are encouraged with the farm-out of a 20% interest in OPL 323 to BG Exploration and Production Nigeria Limited. The proceeds, together with recently arranged short-term loans of US$22.5million and the further farm-outs contemplated in the near future, are expected to provide the Company with required working capital for the near to mid term.

RESULTS AND DIVIDEND

The Company made a loss of US$235.7million in the year, an increase of US$229.7million over the 2005 loss of US$6.0million. This result reflects both the provision of US$200million against potential recoveries from OML 122 and the write down of pre-license costs incurred during the year of US$23.9million. In addition, a charge of US$4.0million was recorded in the 2006 accounts (2005: US$4.1million) in respect of share based payments. The underlying loss of US$7.7million reflects the significant increase in operating and investing activities during the year. Whilst 2005 costs are for a part year only, the costs in 2006 include a full year of both additional staffing in Nigeria and additional costs relating to offices, systems and infrastructure.

The Company has not paid a dividend during the year and no dividend is proposed for 2006 (2005: US$Nil).

FUTURE PROSPECTS

West Africa is one of the most prolific deep water exploration and production regions in the world. The Company remains very positive about the inherent value of its exploration assets and its access to the prolific hydrocarbon prospectivity in the region. We will continue to accelerate cash flow from our deep water assets, while reducing risk, by farming-out a part of our interests in these blocks. The farm-out to BG confirms wider industry interest in our exploration assets.

The Board acknowledges and wishes to express its gratitude for the commitment and determination of our staff, particularly during some challenging months for the Company. Also, the directors wish to recognize the extensive support of shareholders, business partners and suppliers.

Wade Cherwayko
Chief Executive

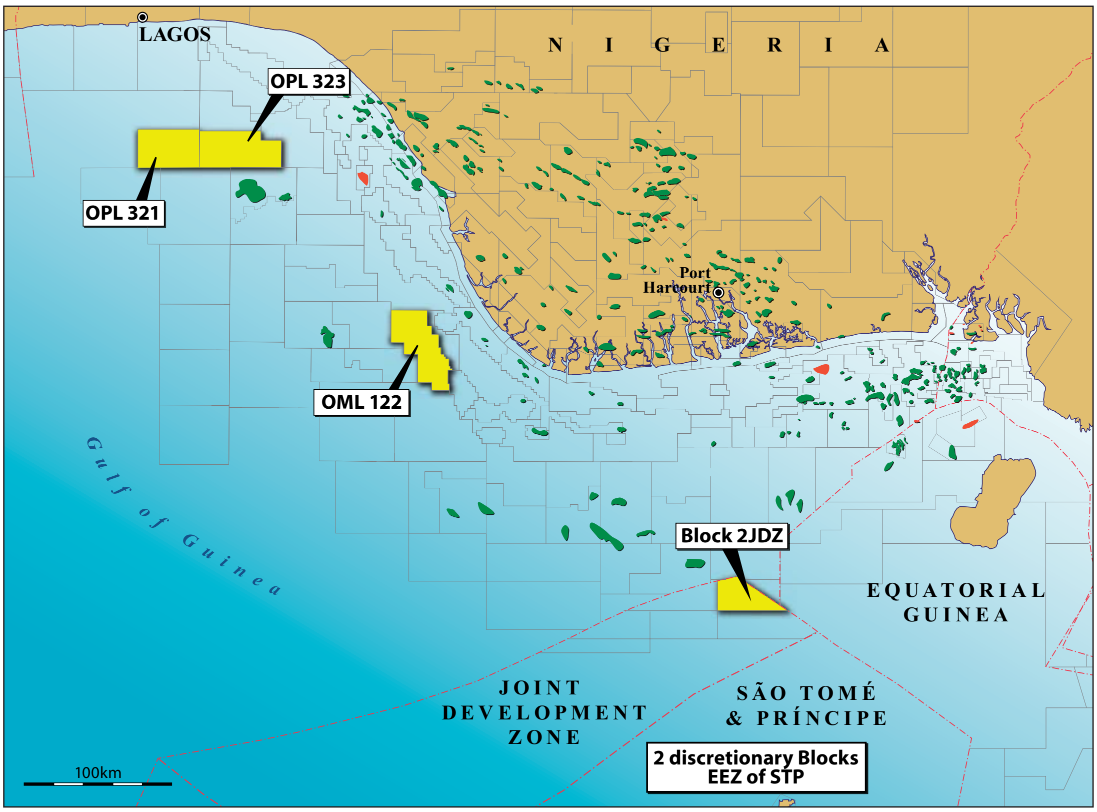
23 October 2007

ASSET REVIEW

OVERVIEW

During 2006, the Company set up offices in Lagos and Port Harcourt and built an operations team of some 20 high quality, motivated staff, both employees and contractors. Many of the staff have been seconded to the joint operations team established to manage the exploration and development activities in OML 122, offshore Nigeria, with the operator and sole lessee of the block, Peak Petroleum Industries Nigeria Limited ('Peak').

Equator intends to continue to operate with the highest ethical standards, partnering with first class companies that have shown themselves to be excellent in their field.



MAP OF EQUATOR'S INTERESTS IN THE GULF OF GUINEA

NIGERIA – OML 122

OML 122 is located 25 to 60km offshore in water depths of 40 to 300 metres. It covers an area of 1,295 square km on the Western Niger Delta, east of the giant Bonga Field on OML 118 and southwest of the EA Field on OML 79, both operated by Shell.

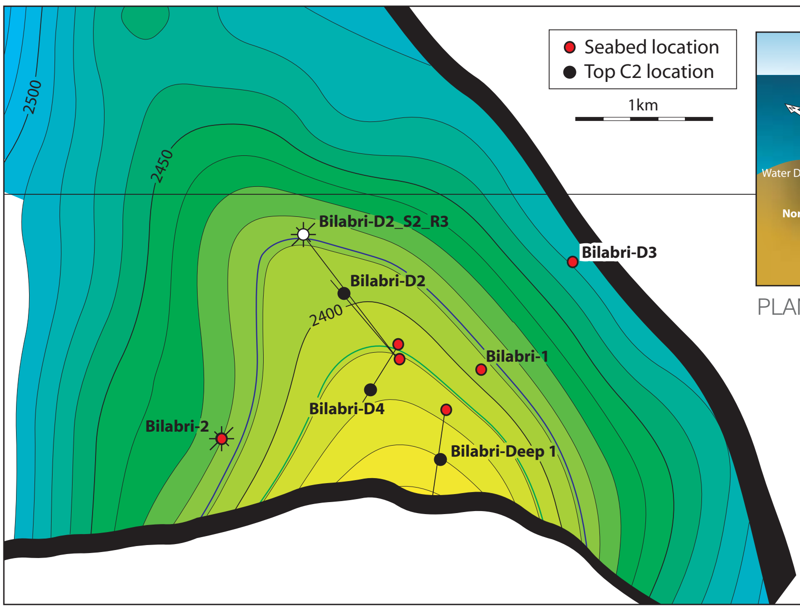
In April 2005, Equator signed a Finance and Service Agreement with Peak. In return for providing funds and supplying technical services for an appraisal well on each of two discoveries and for a selected exploration well, Equator was entitled to a share of the revenues from the oil and gas production of subsequent developments. The Company's objective was to work jointly with Peak to prove significant volumes of gas to supply the gas utilisation projects being developed or planned in close proximity to the lease. In addition, it had a near term objective of developing the oil reservoir discovered in the Bilabri field.

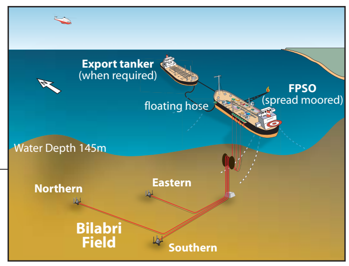
In September 2005, Equator and Peak signed a contract to lease the services of the 'Bulford Dolphin' semi-submersible drilling rig and, in November 2005, commenced drilling their first well, Bilabri DX-1, on a discovery made in the 1970's. The extent of the existing hydrocarbon reservoirs exceeded expectations and, furthermore, the well discovered additional gas reservoirs. On test, the 21 metre oil column in the C2 sand flowed crude oil with a specific gravity of 39 degrees API at a rate of 7,188 barrels per day and the gas reservoir in the overlying C1 sand flowed at a rate of 26 million standard cubic feet per day. The flow testing, combined with the well logs, confirmed that the reservoir properties and crude oil quality of Bilabri were excellent. In addition, pressure data suggested that the C1 and C2 sands were in communication, with the oil leg extending from the C2 sand into the overlying C1 sand. Initial independent analysis of the field indicated that it held Proved plus Probable reserves of 42 million barrels of oil. Based on this interpretation, Equator and Peak initiated a development programme consisting of 6 wells. A contract for the supply of an ('FPSO') was signed with BW Offshore on 17 October 2006.

Following the DX-1 well, the Owanare prospect was selected for the exploration well and the AX-1 well was drilled. Gas was discovered in three reservoirs and the well suspended for a future development.

The Bilabri field was then further appraised with wells D2, D3 and D4. During the drilling programme, operations were disrupted on three occasions when the field was invaded by militants from the Niger Delta. On two occasions, crew members were taken as hostages. Also, Peak defaulted on the cash calls for its share of project expenditure.

The three additional appraisal wells established that the aerial extent of the C2 sand was larger than expected but determined that the C1 sand contained gas only. Netherland, Sewell and





PLANNED OIL DEVELOPMENT

BILABRI FIELD

Associates, Inc ('NSAI'), Independent Competent Person to the Company, assessed the Proved plus Probable reserves as 13.2 million barrels (see table 1 right). In terms of gas, the Best Estimate of Gross Contingent Resources by NSAI was 395 billion standard cubic feet for the Bilabri Field and 106 billion standard cubic feet for the Owanare discovery, giving a total Gross Contingent Gas Resource of 500 billion standard cubic feet discovered by wells funded by Equator in OML 122.

Based on the results from the appraisal drilling, the scope of the Bilabri oil development was reduced from six to three wells, comprising two horizontal completions of the existing D2 and D4 wells plus a vertical completion of the existing DX-1 well.

The FPSO entered the Sembawang shipyard in Singapore on 22 January 2007 for upgrade and delivery in Nigeria in fourth quarter 2007. All of the sub-sea equipment was ordered, scheduled for installation during fourth quarter 2007. To 30 June 2007, Equator funded 100% of the cost of developing Bilabri, with expenditure on OML 122 totalling US$270million. It was estimated that an additional US$100million was required to get to first production.

However, during 2007 the project was beset with considerable operational and security problems, including yet another kidnapping, which caused the shut down of drilling operations. The contract for the Bulford Dolphin drilling rig was terminated for prolonged force majeure on 11 May 2007. Subsequently, BW Offshore terminated the contract for the FPSO.

In September 2007, Equator agreed terms with Peak for it to take over the remaining development of the Bilabri oil project with finance made available by a third party. Under the terms of the settlement agreement, Equator is to receive an upfront payment and Peak will take over the current and future project liabilities. Equator will also retain a carried interest of 5% in the oil project and a paying interest of 12.5% in any gas development. Equator and Peak continue to actively pursue development of the gas reserves and discussions continue with third parties interested in purchasing the gas.

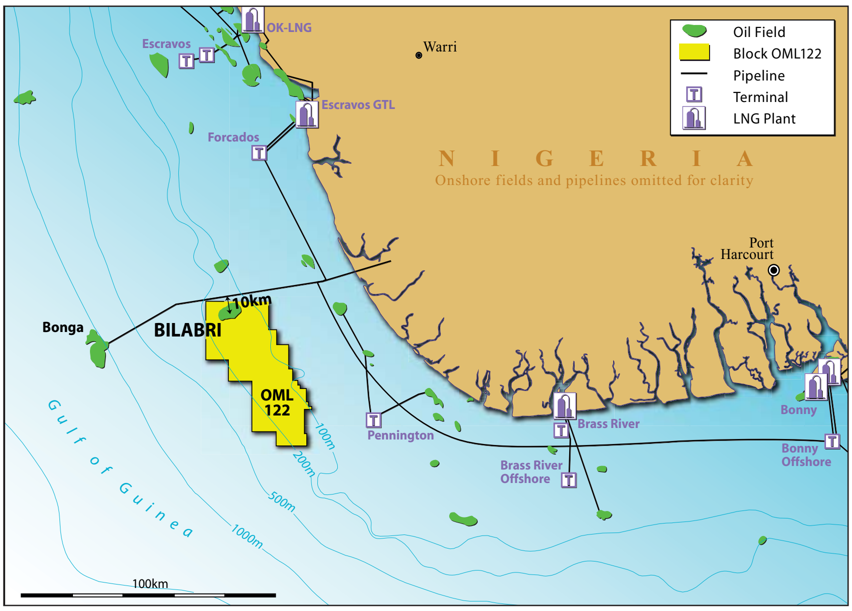
The Equator net values for reserves in the following Table 1 are yet to be calculated by NSAI post the settlement agreement.

TABLE 1 – BILABRI FIELD OIL RESERVES[1]
As at 1 April 2007

	Oil Reserves Thousand Barrels	
Category	Gross	Net[2]
Proved (1P)	10,280.0	tbc
Proved + Probable (2P)	13,160.0	tbc
Proved + Probable + Possible (3P)	16,450.0	tbc

(1) See Statement on Reserves and Resources by Competent Person;

(2) The Equator net values for reserves are yet to be calculated post the settlement agreement.



LOCATION OF OML 122

NIGERIA – OPL 323 AND OPL 321

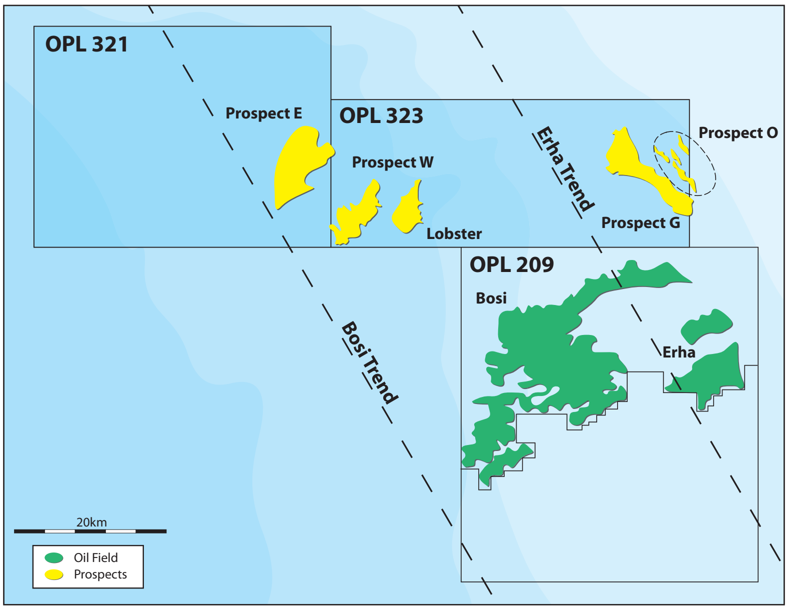
Equator's efforts in the Nigerian 2005 bid round were rewarded on 10 March 2006 when the Company signed two PSC's with the Nigeria National Petroleum Corporation ('NNPC') for a 30% interest in each of the highly prospective deep water blocks, OPL 323 and OPL 321. Having exercised their right of first refusal, the Korean National Oil Corporation ('KNOC') was awarded a 60% interest in the blocks and appointed operator. The remaining 10% was awarded to Local Content Vehicles ('LCV's'), Tulip Energy Resources Nigeria Limited for OPL 321 and NJ Exploration Limited for OPL 323. Equator and KNOC carry the costs of the two LCV's in proportion to their participating interests.

The total signature bonus paid by Equator for the two PSC's was US$161.7million. The Company granted carried interests, amounting to 4.00% in each block, to bidding partners who, because of KNOC's right of first refusal, were prevented from entering the PSC's directly.

Under the terms of the PSC's, Equator was obliged to provide performance bonds of US$42million each to cover its share of the minimum work programmes of two wells on each of the blocks. Equator has negotiated with a Nigerian bank to provide the performance guarantees without the need for cash collateral. Instead, the bank has accepted security over the wholly owned subsidiaries that hold the PSC's.

During 2006, KNOC established an operating office in Lagos, and on 7 June 2007, Equator and its partners signed the Joint Operating Agreements. Equator enhanced its interpretation of the 3D seismic survey, previously licensed from Petroleum Geo-Services ASA ('PGS'), and then transferred the interpretation to KNOC. In turn, KNOC is further refining the prospect evaluation in order to identify the four exploration well locations. It is also negotiating with a drilling contractor for the supply of a fifth generation deep water drilling rig to commence drilling in 2009.

OPL 323 IS LOCATED 80 KILOMETRES OFFSHORE AND LIES IN WATER DEPTHS OF BETWEEN 890 METRES AND 2,080 METRES. FOUR LARGE STRUCTURES HAVE BEEN IDENTIFIED BY INTERPRETATION OF THE 3D SEISMIC SURVEY. WITHIN EACH OF THE GEOLOGICAL STRUCTURES THERE ARE SEVERAL PROSPECTIVE HORIZONS.



PROSPECTS ON OPL 323 AND OPL 321

OPL 323

OPL 323 is located 80 kilometres offshore and lies in water depths of between 890 metres and 2,080 metres. Four large structures have been identified by interpretation of the 3D seismic survey. Within each of the geological structures there are several prospective horizons. Many of the prospect horizons are supported by seismic amplitude anomalies. Furthermore, the proximity of the block to large oil fields in the surrounding blocks supports the presence of source rocks and abundant reservoir sands. OPL 323 is to the west of the Abo Field in OML 125, operated by Agip, and immediately to the north of the Bosi and Erha Fields in OML 133, operated by ExxonMobil. Erha has proved reserves reported by ExxonMobil to be in excess of 500 million barrels and 5 trillion cubic feet of gas and, with its satellite development Erha North, produces in excess of 200,000 barrels of oil per day. Bosi, the second field development on OML 133, is expected to produce 135,000 barrels of oil per day.

NSAI has made a Best Estimate of Unrisked Prospective Resources lying within the block of nearly 2 billion barrels of oil and nearly 9 trillion standard cubic feet of gas (see table 2 below).

During 2006, Agip made a discovery of both oil and gas in the Okodo-1 well on OML 125. This discovery had a direct impact on the prospectivity of the largest prospect on OPL 323, located only 7 kilometres away. This prospect alone has Best Estimate Unrisked Prospective Recoverable Resources of nearly 1 billion barrels of oil and 6 trillion standard cubic feet of gas. It appears to lie in the same channel as the Okodo discovery, which proved that the hanging wall of the common major bounding fault forms a trap for hydrocarbons and that the immediate area has sources of oil and gas and migration paths.

In August 2007, the Company announced the farm-out of two thirds of its 30% interest in OPL 323 to BG Exploration and Production Nigeria Limited ('BG'), for a total consideration of up to US$75million in cash and carry of the future exploration work programme. The Company has applied to NNPC for approval of the assignment of the interest in the PSC.

OPL 321

OPL 321 is located immediately to the west of OPL 323, lying in deeper water in the range 1,900 to 2,600 metres. The block lies on trend with block OPL 322 to the south, where Shell's recent discovery well Bobo-1 encountered a significant column of hydrocarbons. It has access to the same hydrocarbon kitchens as the giant Bosi and Erha Fields located nearby to the southeast. Assessment of the block by NSAI confirms the presence of a very large prospect, which could contain Unrisked Prospective Resources of 1.0 billion barrels of oil and 1.3 trillion standard cubic feet of gas at the Best Estimate level (see table 2 below).

The Company will seek to accelerate cash flow and reduce risk by farming-out a portion of its interest the block in a deal similar to that achieved for OPL 323. Such a structure will limit the exposure by securing a carry on the exploration costs of its remaining interest.

TABLE 2 - OPL 321 & OPL 323 BEST ESTIMATE PROSPECTIVE RESOURCES[1]
As at 1 October 2006

	UNRISKED				RISKED			
	Gross (100 Percent)		Equator Net Interest (30 Percent)[2]		Gross (100 Percent)		Equator Net Interest (30 Percent)[2]	
Prospect Cluster	Oil MMBBL	Gas BCF	Oil MMBBL	Gas BCF	Oil MMBBL	Gas BCF	Oil MMBBL	Gas BCF
323-G	992	6,392	298	1,918	361	1,840	108	552
323-O	265	1,431	80	429	65	362	20	109
323-W	401	524	120	157	138	187	41	56
323-L	261	449	78	135	79	150	24	45
321-E	1,005	1,351	302	405	275	369	83	111
Total	**2,924**	**10,147**	**877**	**3,044**	**918**	**2,908**	**275**	**872**

Totals may not add due to rounding

(1) See Statement on Reserves and Resources by Competent Person;

(2) The Equator net interest for OPL 323 is stated pre the farm-in at 30%. After approval of the assignment of an interest to BG by NNPC, the Equator net interest in the PSC will be reduced to 10%.

JDZ AND EEZ OF SÃO TOMÉ e PRÍNCIPE

JOINT DEVELOPMENT ZONE – BLOCK 2

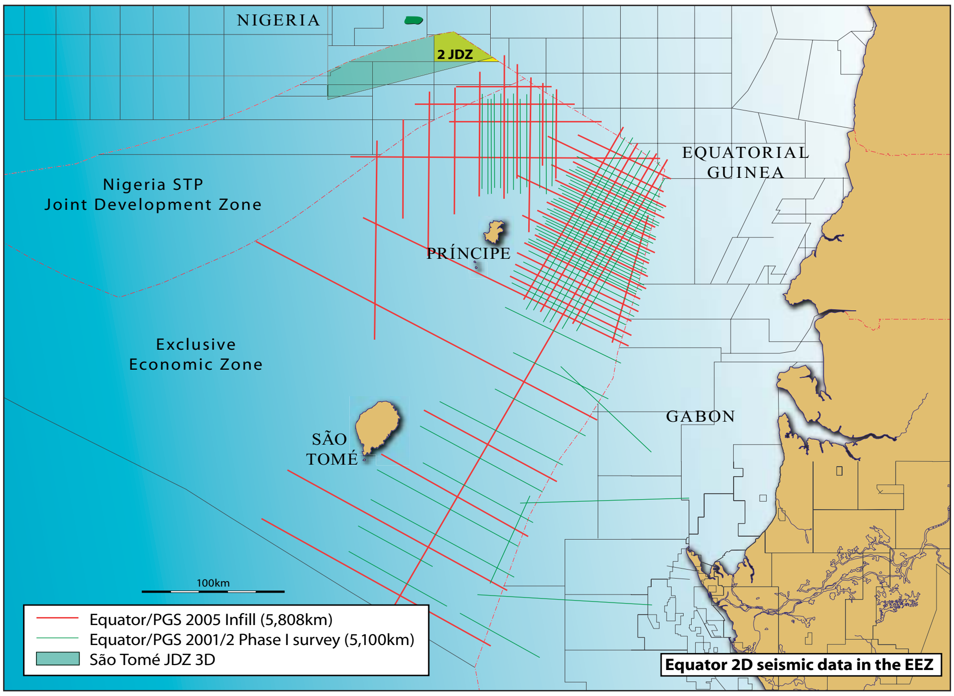
The Joint Development Zone ('JDZ') lies between the Republic of Nigeria and the Republic of São Tomé e Príncipe. Under a treaty signed in 2001, the rights to resources extracted from the JDZ are shared between the two countries in the ratio 60 to 40 respectively. The JDZ is administered by the Joint Development Authority ('JDA') which is staffed by officials from both countries. Following the bidding round in 2005, Equator and one of its bidding partners, ONGC Videsh Limited ('OVL'), were jointly awarded a 15% interest in the highly sought after Block 2, of which Equator received a 6% interest.

Equator subsequently purchased an additional 3% interest from one of the other participants in the block, A & Hatman Limited, increasing its total participating interest to 9%. From this, the Company granted a bidding partner an economic interest equivalent to a 0.25% carried interest in the block. The result is that Equator acquired a net economic interest of 8.75% in Block 2 for a total entry cost of US$9.05million, with an obligation to carry a combined interest of 1.25% during the initial exploration phase. Deferred consideration payments, to a maximum of US$6million depending on the level of oil reserves, may become payable upon approval of a field development.

The PSC was signed with the JDA on 17 March 2006. The participants and their interests are shown in the following table 3:

TABLE 3 – PARTICIPANTS IN BLOCK 2, JDZ

Participants	Participating Share %	Working share %
Sinopec (operator)	28.67	43.34
EHRC	22.00	0.00
Addax	14.33	21.66
OVL	13.50	15.00
Equator	9.00	10.00
Amber Petroleum	5.00	5.00
Foby Engineering	5.00	5.00
A & Hatman	2.50	0.00
	100.00	**100.00**



SEISMIC ACQUIRED BY EQUATOR AND PGS OFFSHORE SÃO TOMÉ e PRÍNCIPE

JDZ Block 2 lies in a prospective area of the deep water Niger basin. It is adjacent to Nigerian Block OML 130, which hosts the 600 million barrel/1 TCF Akpo field (Total 2007) and series of significant discoveries.

During Q2 2006, Chevron and Exxon encountered reservoir sands and discovered oil and gas in the Obo-1 well drilled in the adjoining Block 1. This has improved the Company's chances for success on Block 2 and has also improved the prospectivity of the Exclusive Economic Zone of São Tomé e Príncipe, where Equator has an option on two blocks.

Based on a 3D seismic survey acquired in 2003 by PGS and partially funded by Equator, NSAI has made a Best Estimate of Unrisked Prospective Resources of 1.3 billion barrels of oil and 1.8 trillion standard cubic feet of gas in total in the 10 identified prospects (see table 4 below).

Sinopec, the operator, has established its team and office in Lagos. On behalf of the participants, it has engaged a specialist Shanghai firm, Sino Geophysical Co. Ltd, to reprocess the 3D seismic survey using Pre-Stack Time Migration and state-of-art Common Reflection Surface stack processing. Sinopec has proceeded to interpret the reprocessed data, evaluate the prospects and rank them for drilling.

In March 2007, Sinopec and Addax Petroleum entered into a drilling services agreement with Aban Abraham Pte Ltd. for the provision of the Aban Abraham deep water drillship to drill up to ten wells. The rig sharing agreement between Sinopec and Addax allocates a firm well slot to Sinopec which will be used to drill a well in Block 2 in the second half of 2008. This will fulfil the sole well commitment under the PSC. The rig sharing agreement also allows Sinopec to access more slots for appraisal drilling and for the exploration of more prospects in Block 2. In the conditions of today's tight market for drilling rigs, the maximum day rate of US$410,000 per day is considered attractive.

EXCLUSIVE ECONOMIC ZONE OF SÃO TOMÉ e PRÍNCIPE

The maritime boundaries of São Tomé e Príncipe encompass an area of approximately 160,000 square kilometres. The close proximity of São Tomé e Príncipe's offshore waters to the proven hydrocarbon systems in the adjacent waters of Nigeria, Cameroon, Equatorial Guinea and Gabon suggests the potential for hydrocarbons, which is further supported by regional seismic data.

In a joint venture with PGS, Equator funded the acquisition in 2001 and 2005 of ten thousand kilometres of 2D seismic data and interpreted more than twenty thousand kilometres within the Exclusive Economic Zone of São Tomé e Príncipe ('EEZ'). It was agreed with the government that licences for the seismic data will be sold to oil companies to promote an oil exploration licensing round. In return, Equator gained the right to acquire a 100% interest in two blocks of its choice. In addition, the Company has an option to take up to a 15% share in any eventual back-in participation that the government may secure in other blocks.

During 2006, the Company prepared for its choice of blocks by enhancing its interpretation of the 2D seismic surveys and by ranking the prospectivity of the various areas of the EEZ. During 2007, the government has continued to work with its legal and technical advisers on the delineation of blocks and on drafting new petroleum legislation, including a model PSC. Equator expects to commence formal negotiations for the PSC's for the two option blocks early in 2008.

Equator intends to enhance the value of its opportunity in the EEZ by seeking a farm out to an acknowledged deep water operator.

TABLE 4 - JDZ BLOCK 2 BEST ESTIMATE PROSPECTIVE RESOURCES[1]
As at 1 October 2006

	UNRISKED				RISKED			
	Gross (100 Percent)		Equator Net Interest (9 Percent)		Gross (100 Percent)		Equator Net Interest (9 Percent)	
Prospect Cluster	Oil MMBBL	Gas BCF	Oil MMBBL	Gas BCF	Oil MMBBL	Gas BCF	Oil MMBBL	Gas BCF
Central	369	403	33	36	100	109	9	10
North	410	807	37	73	111	382	10	25
South	440	501	40	45	111	126	10	11
Subthrust	130	158	12	14	30	36	3	3
Total	**1,349**	**1,869**	**121**	**168**	**352**	**553**	**32**	**50**

Totals may not add due to rounding

(1) See Statement on Reserves and Resources by Competent Person

BOARD OF DIRECTORS AND SENIOR EXECUTIVES

Wade Cherwayko
President & Chief Executive Officer

Over the last fourteen years, Mr. Cherwayko has been active in negotiating, developing and financing a number of projects in West and North Africa. Such projects have included the acquisition, financing, exploration and development of several onshore and offshore oil and gas assets for Mart Resources Inc., Abacan Resource Corporation, Centurion Energy International Inc. and Yinka Folawiyo Petroleum Company Ltd. He is also a director of Mart Resources Inc.

Philip Dimmock
Chief Operating Officer

Prior to joining Equator, Mr. Dimmock served as general manager of operations of Houston-based Vanco where he oversaw the company's exploration activities in Africa, including the drilling of deepwater wells in Morocco and Cote d'Ivoire. Prior thereto, he was Vice President International for Ranger Oil, directing business development and operations in the United Kingdom and a number of West African countries. Mr. Dimmock began his career at BP where he spent 26 years and held a number of senior positions. He also serves as a non-executive director of Nautical Petroleum PLC.

Philip Rand
Chief Financial Officer and Company Secretary

Mr. Rand has over thirty years of financial experience of which seventeen have been in the upstream energy sector. Prior to joining Equator, he was chief financial officer of Burren Energy, group treasurer of Monument Oil & Gas and held senior financial roles at Deminex and Louisiana Land & Exploration. Mr. Rand was also finance director of Utilyx and group treasurer of both Sema Group and CMG. Mr. Rand is a Fellow of the Association of Corporate Treasurers.

Tony Renton
Non-executive Director

Mr Renton is currently Chief Executive of Oil Experience Ltd, an oil and gas consultancy based in London. Prior to this he spent 34 years with BP in a number of technical, commercial and management roles across Europe, the US, West Africa, the Far East, Australasia and most recently as Commercial Director responsible for business development across the Middle East. He is also a Director of Berkshire Aviation Services Limited.

Martin Adams
Non-executive Director

An independent specialist in the management and reorganisation of closed end funds and investments in emerging markets, Mr Adams has over 25 years investment and banking experience in Asia and Europe. During the past five years, he has focused particularly on representing and protecting shareholder interests in listed and unlisted funds and companies in a number of different countries. Among his current non-executive positions, Mr Adams is chairman of funds in India and Hungary and a director of investment companies specializing in China, in global emerging markets and in smaller companies the US and UK. He is also chairman of Mekong Capital, the investment manager of three private equity funds in Vietnam.

Dr Kenneth Seymour
Managing Director – Nigeria

Prior to joining Equator in June 2006, Dr. Seymour was an independent consultant and served Roc Oil as their General Manager in Angola. Previously, he developed his career in Ranger Oil in positions ranging from senior drilling engineer to general manager. He was the Director of Business Development when Ranger was sold to Canadian Natural Resources. His started his career with BP as a drilling engineer in the North Sea and China followed by a spell with Danbury Drilling as a consulting engineer.

Russ Guyatt
Vice President – Technical

Russ Guyatt has over 25 years experience working for Operating Oil Companies over a broad range of engineering disciplines. Specifically has been involved in and project managed a number of FPSO and subsea projects in West Africa and the North Sea. Prior to joining Equator he spent 5 years as Vice President, Engineering for PanOcean Energy and 17 years with Ranger Oil, latterly Canadian Natural Resources in a number of senior engineering roles, having started his career with British Gas as a Reservoir Engineer.

Stacey Kivel,
Vice President – Business Development, Legal Affairs

Prior to joining Equator, Ms. Kivel represented major US and European corporations regarding legal and business development in more than thirty African countries; working at presidential or ministerial levels. Her experience included heading the Africa/ Middle East Government Relations and Business Development Division of Institutional Investor Inc. Prior to her involvement in Africa, Ms. Kivel was in-house legal council and head of acquisitions consecutively for Cinequanon International and Image Organisation in Los Angeles, specialising in negotiating international licensing and finance agreements. She is a California qualified attorney at law.

OFFICERS AND PROFESSIONAL ADVISERS

Directors
S E Jonah, KBE, OSG – Executive Chairman
(resigned - 20 July 2007)

Baroness Chalker of Wallasey
(resigned – 28 September 2007)

Mr W Cherwayko

Mr M Adams
(appointed – 16 March 2007)

Mr J Auld
(appointed – 15 August 2006, resigned – 12 March 2007)

Mr A Dembitz
(resigned – 16 February 2007)

Mr P Dimmock

Mr J Ladner
(resigned – 6 December 2006)

Mr P Rand
(appointed – 13 March 2007)

Mr A Renton
(appointed – 16 March 2007)

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STATEMENT ON RESERVES AND RESOURCES BY COMPETENT PERSON

October 19, 2007

The Directors
Equator Exploration Limited
192 Sloane Street, Third Floor
London SW1X 9QX
United Kingdom

Re: Technical Reports of Netherland, Sewell & Associates, Inc.

Dear Sirs:

In accordance with the request of Equator Exploration Limited (Equator), Netherland, Sewell & Associates, Inc. (NSAI) has evaluated the holdings of Equator in Oil Mining Lease 122, as of April 1, 2007, and Oil Prospecting Licenses (OPLs) 321 and 323 and Block 2 of the Joint Development Zone of Nigeria and São Tomé and Príncipe, as of October 1, 2006. These assets include reserves, contingent resources, and prospective resources. We have been asked to provide an updated comment on the reserves and resources estimates prepared on behalf of Equator.

We draw your attention to the following points:

- The recoverable oil volumes in Bilabri Field are classified as reserves based on assurance that the field will be developed within a reasonable time frame, which we take to be a maximum of five years from the date of evaluation. Significant delays to development planning would require these volumes to be reclassified as contingent resources.
- The Equator net interest for OPL 323, as stated in our report dated December 14, 2006, is 30 percent. This interest may be reduced to 10 percent pending approval by Nigerian National Petroleum Corporation for Equator's farmout of 20 percent of its interest to BG Exploration and Production Nigeria Limited.

Our work was undertaken by a team of professional petroleum engineers and geoscientists based on data supplied by Equator. Equator has made available to NSAI a data set of technical information including geological, geophysical, and engineering data and reports together with financial data pertaining to the fiscal terms applicable to the assets. We have relied on this information in carrying out our evaluation. In estimating petroleum in place, reserves, and resources we have used standard petroleum engineering techniques. The estimates in our reports have been prepared in accordance with the 1997 joint definitions of the Society of Petroleum Engineers, the World Petroleum Council, and the American Association of Petroleum Geologists.

Qualifications
NSAI performs consulting petroleum engineering services under Texas Board of Professional Engineers Registration No. F-002699 and has conducted reserves and resources certifications, technical studies, economic evaluations, and advisory work throughout the world. In preparation of its reports, NSAI has maintained, and continues to maintain, a professional consultant-client relationship with Equator. We are independent petroleum engineers, geologists, geophysicists, and petrophysicists; we do not own an interest in these properties and are not employed on a contingent basis.

Correct Extraction
NSAI has reviewed the Annual Report and Financial Statement 2006 (Annual Report) of Equator and confirms that the information contained therein, which relates to information contained in its reports, is accurate, balanced, and complete and not inconsistent with such reports. In particular, NSAI confirms that the information in the Annual Report, where extracted from its reports, is extracted directly and presented in a manner that does not affect its import in this report for the purposes of the AIM Rules for Companies, AIM Rules for Nominated Advisers, and the Guidance Note for Mining, Oil and Gas Companies.

Consent
We hereby give our written consent for the inclusion of our reports and to references to our reports contained in the Annual Report and to our name in the Annual Report in the form and context in which they appear.

Basis of Opinion

The evaluations presented in our reports reflect our informed judgment based on accepted standards of professional investigation but are subject to generally recognized uncertainties associated with the interpretation of geological, geophysical, and engineering data. The evaluations have been conducted within our understanding of petroleum legislation, taxation, and other regulations that currently apply to these interests.

In particular, it should be noted that the technical reports relate to three different categories of assets:

Reserves are those quantities of petroleum which are anticipated to be commercially recovered from known accumulations from a given date forward. Their estimated value can be expressed in terms of Net Present Value (NPV). The relative degree of uncertainty may be conveyed by placing reserves into one of two principal classifications, either proved or unproved. Unproved reserves are less certain to be recovered than proved reserves and may be further sub-classified as probable and possible reserves to denote progressively increasing uncertainty in their recoverability.

> **Proved Reserves** are those quantities of petroleum which, by analysis of geological and engineering data, can be estimated with reasonable certainty to be commercially recoverable, from a given date forward, from known reservoirs and under current economic conditions, operating methods, and government regulations.
>
> **Probable Reserves** are those unproved reserves which analysis of geological and engineering data suggests are more likely than not to be recoverable.
>
> **Possible Reserves** are those unproved reserves which analysis of geological and engineering data suggests are less likely to be recoverable than probable reserves.

Contingent Resources are defined as those quantities of petroleum estimated, as of a given date, to be potentially recoverable from known accumulations but for which the applied project(s) are not yet considered to be mature enough for commercial development because of one or more contingencies. Development of the discovered resources is contingent upon both regulatory and commercial considerations.

Prospective Resources are those quantities of petroleum which are estimated, on a given date, to be potentially recoverable from undiscovered accumulations. Prospective Resources indicate exploration opportunities and development potential in the event a commercial discovery is made and should not be construed as reserves or contingent resources.

It should also be understood that any evaluation, particularly one involving exploration and future petroleum developments, may be subject to significant variations over short periods of time as new information becomes available.

Sincerely,

NETHERLAND, SEWELL & ASSOCIATES, INC.

By:

C.H. (Scott) Rees III, P.E.
President and Chief Operating Officer

DIRECTORS' REPORT
For the year ended 31 December 2006

The directors submit their report and the audited financial statements of the Group for the year ended 31 December 2006.

Principal activity
Equator Exploration Limited ('Equator' or the 'Company') is a company incorporated in the British Virgin Islands. The address of the registered office is given on page 11.

Equator Exploration Limited and its subsidiaries engage in the exploration and development of offshore oil and gas projects in West Africa. The Group's objective is to build a diversified portfolio of exploration, appraisal and production assets in this region.

Review of the business

Development of OML 122 with Peak Petroleum Industries Nigeria Limited ('Peak')
Drilling operations in OML 122, undertaken with the licence holder and operator Peak Petroleum Industries Nigeria Limited, continued with finalisation of the Bilabri DX-1 appraisal well. The well commenced in November 2005 and was finished in February 2006. It confirmed the presence of the previously discovered oil and gas reservoirs, and discovered new gas reservoirs in the Bilabri field.

The drilling of the exploration well, Owanare AX-1 followed immediately. This well discovered gas in shallow zones but drilling was unable to reach the deeper objectives as a result of high pressure and temperature. The well is suspended pending later re-entry for completion as a gas production well once a suitable development plan has been identified and a gas market has been secured.

Following the Owanare AX-1 well, drilling operations continued with the appraisal and development drilling programme for the Bilabri field. The programme during 2006 included 3 wells (D2, D3 and D4) intended both to confirm reserves and for subsequent completion as horizontal production wells in 2007. Whilst the D2 well confirmed increased levels of reserves in the lower C2 sand structure, the D3 well did not prove the reserves forecast to be in the higher C1 sand structure. This resulted in a reduction in the expected recoverable reserves from the Bilabri field to 13 million barrels at the 2P (Proven plus Probable) level. The D4 well had not reached its target at the end of 2006 but successfully appraised the field early in 2007. Additional gas reserves were confirmed by these wells and it is expected that these will be developed as part of a longer term gas project.

Both D3 and D4 encountered operational and technical problems resulting in the loss of downhole tools. D3 was subsequently plugged and abandoned whilst D4 was suspended for re-entry and horizontal completion as a production well.

The development of the Bilabri Field for oil production advanced well in terms of the production and sub-sea facilities. The critical long lead items were procured and a contract was secured for a Floating Production, Storage and Offtake Vessel ('FPSO'), due for delivery in late 2007. However, following major delays with drilling operations in 2007 caused by unrest in the Delta and by operational problems on the rig, the contract for the drilling rig was terminated for prolonged force majeure, as the directors considered that continuation of the project with sole funding from Equator presented an unacceptable risk. BW Offshore subsequently terminated the contract for the FPSO. As explained in note 22 to the accounts, the FPSO contract contains early termination penalties of up to US$52million under certain circumstances.

In September 2007, Equator agreed terms with Peak, to enable Peak to take over the remaining development of the Bilabri oil project with finance made available by a third party. Under the terms of the agreement, Equator is to receive an upfront payment and Peak will assume the current and future project liabilities. Equator will also receive a carried Net Profits Interest ('NPI') of 5% in the oil project and a paying interest of 12.5% in any gas development. The Board believe that the project can be continued and that there will be a significant residual value. However, the Board consider it prudent to make a provision of US$200million to account for the possibility of the Company not recovering all of the historical costs.

Deep Water Nigeria OPL 321 and OPL 323
On 10 March 2006 the Company signed Production Sharing Contracts ('PSC's') for OPL 321 and OPL 323, two of the most highly sought-after deep water blocks in the 2005 Nigerian licensing round. The Korean National Oil Corporation ('KNOC') is the operator of both blocks with a 60% equity interest in each, while Equator has a 30% equity interest (net economic interest 26%). Under the terms of the licensing round, local companies were awarded the remaining 10% equity interest. The two blocks have several very large mapped prospects with gross risked recoverable prospective resources estimated as 918 million barrels of oil and 2.9 billion standard cubic feet of gas by independent reservoir engineers Netherland Sewell & Associates, Inc. ('NSAI'). Since year end, the Company has accepted an offer of a farm-in to 20% of OPL 323 (see Note 23).

Joint Development Zone Block 2

On 17 March 2006, the Company signed a PSC for Block 2 in the Joint Development Zone between Nigeria and São Tomé e Príncipe. Equator's original allocation of a net 6% equity interest was subsequently increased to 9% by a farm-in to the interest of another participant. Equator has a net economic interest of 8.75%. Block 2, which is operated by Sinopec of China, is adjacent to OPL 246 which hosts the large Akpo field operated by Total. The Company posted a guarantee for its share of one obligation well in the first 5 year exploration phase of the PSC. The licence for a 3D seismic survey was purchased. The 3D seismic has been reprocessed using advanced techniques and interpretation, aimed at selecting the location of the well, continues. Recent drilling activity in the region has increased our confidence that Block 2 has the potential to contain significant reserves.

São Tomé e Príncipe Exclusive Economic Zone Rights

Equator awaits the delineation of oil exploration blocks in the Exclusive Economic Zone of São Tomé e Príncipe, anticipated to be completed by the end of 2007. A 2D seismic programme has been acquired and interpreted by the Company. Upon completion of the block delineation, and pursuant to its agreements with the government of São Tomé e Príncipe, Equator will exercise its right to select and acquire a 100% interest in two of the newly delineated blocks. Once these blocks have been selected the Company will seek to negotiate PSC's with the government.

Management and Directors

During 2006, two changes to the Board of Directors were announced. In August, Jeffrey Auld was appointed as an executive director and in December, James Ladner resigned as a non-executive director. In addition, the company made several key senior appointments. Dr Kenneth Seymour was appointed as Managing Director of Equator Exploration Nigeria Limited and Russell Guyatt was appointed as Project Director specifically responsible for the Bilabri development project.

During 2007, Alex Dembitz and Jeffrey Auld resigned as directors in February and March respectively. In March also, Philip Rand was appointed as an executive director and two new non-executive directors, Martin Adams and Tony Renton, were appointed. In July, for personal reasons, Sam Jonah resigned from his position as executive chairman and in September, due to other business commitments, Baroness Chalker of Wallasey resigned from her position as non-executive director.

Shares

As at 31 December 2006, there were 175,165,590 common shares issued. No further shares have been issued since the balance sheet date. As at 31 December 2006, there were 12,852,750 outstanding share options and 15,676,290 outstanding warrants all of which are exchangeable into common shares at prices ranging from US$1.00 per share to £3.05 per share.

Results and dividend

The group made a loss of US$235.65million in the year, an increase of US$229.70million over the 2005 loss of US$5.95million (as restated). This is mainly represented by a provision of US$200million against the value of exploration and evaluation assets. In addition certain pre-licence costs amounting to US$23.9million have been written off under IFRS rules. The operational and investing activities of the group increased significantly during the year as activity increased on the Company's projects resulting in an increase in overheads including office and staff costs of US$3.5million. The comparative costs in 2005 were for a part year only, whereas the costs in 2006 are for a complete year and include additional staffing in Nigeria and additional costs relating to systems and infrastructure. In addition, a charge of US$3.96million was recorded in the 2006 accounts (2005: US$4.13million, restated after prior year adjustment of US$2.24million) in respect of share based payments.

The Company has not paid a dividend during the year (2005: US$Nil).

Risk management

The Equator Group of companies operates in a difficult geographical area and in an industry with a range of risks that have to be managed by the Company. The Group's management assesses and evaluates these risks, both on a company-wide basis and on specific projects. The Group's general philosophy is to pass risk to its partners where they have greater control over the assets and liabilities or where the cost of protection would be substantially lower. In those instances where management deem a risk to be significant, it will consider protecting its own exposure. The main risks to the Group and the mitigating action taken are as follows:

Currency risk is managed by matching costs with income as far as possible. Each of the companies within the Group accounts for its business in its functional currency, US dollars, thereby minimising translation risk.

Interest rate risk on debt is not currently covered by financial instruments because the rates are fixed between 10 and 14 per cent per annum in accordance with loan agreements.

DIRECTORS' REPORT CONTINUED
For the year ended 31 December 2006

Risk management continued

Economic risk to project cash flows is expected to be managed by structuring financing to match debt repayment to project cash flows.

The risks of well blow-out and of oil pollution are covered, in line with industry norms, through insurance policies that limit the Company's exposure to an acceptable deductible amount and provide sufficient coverage for re-drilling.

Security in West Africa is a continuing concern and Equator's management takes all reasonable precautions to ensure the safety of its own and its contractors' staff, whether working onshore or offshore.

Financing
The group's Balance Sheet was strengthened as a result of an additional US$250million of equity being raised through a placement of 41,050,900 shares in February 2006 at £3.50 (US$6.09) per share. Certain options and warrants were exercised during the year as explained in note 18. As a result an additional 2,597,500 common shares were issued at an average price of US$1.29 per share. In addition, Equator completed a US$65million loan from certain of its shareholders in August 2006 as a bridge to obtaining project or other debt to finance the Bilabri development.

Future prospects
The Company has a portfolio of exploration and development projects in the prospective waters in the Gulf of Guinea, offshore West Africa. During 2006 and 2007, exploration drilling in the areas surrounding the Company's blocks has been encouraging. The discovery of hydrocarbons has increased the probability that oil and gas have migrated into the prospects that lie within the blocks.

The prospects identified in the deep water offshore blocks have been evaluated by NSAI with the following results for net Equator share of Prospective Resources:

Table 1 – Best Estimate Prospective Resources (Equator Net Share)

	UNRISKED		RISKED	
	Oil million barrels	Gas billion cubic feet	Oil million barrels	Gas billion cubic feet
OPL 321	302	405	83	111
OPL 323[1]	575	2,639	192	761
JDZ Block 2	121	168	32	50
Total	**998**	**3,212**	**307**	**922**

(1) The Equator net interest for OPL 323 is stated pre the farm-in at 30%. After approval of the assignment of an interest to BG by NNPC, the Equator net interest in the PSC will be reduced to 10%.

Litigation
There was no outstanding litigation at the end of 2006. Legal issues that have arisen since the end of 2006 are explained fully in note 22.

Directors and their interests
The names of the directors who held office during the year and after the year end are disclosed on page 11.

The following directors held the following interest in common shares for the year ended 31 December 2005:

Number of common shares	**At 31 December 2006**	At 31 December 2005
Mr W Cherwayko	**3,350,000**	3,300,000
S E Jonah, KBE, OSG* (resigned – 20 July 2007)	**426,472**	426,472
Mr J Ladner (resigned – 6 December 2006)	**468,000**	468,000

* 176,472 common shares are held in the name of Pictet and Cie.

Directors and their interests continued

Directors held the following options to subscribe for common shares at 31 December 2006:

	Note	Exercise price	Number of shares	Date of grant	Date of expiry	Exercised during year	Date exercisable from
Mr J Auld	a	£1.220	500,000	06/10/2006	05/10/2011	–	06/10/2008
Baroness Chalker of Wallasey		£1.560	150,000	22/07/2005	21/07/2010	–	22/07/2007
Mr W Cherwayko		£1.000	1,600,000	23/11/2004	23/11/2014	–	23/11/2006
Mr W Cherwayko		£2.068	400,000	09/11/2005	08/11/2010	–	09/11/2006
Mr A Dembitz		£1.000	80,000	23/11/2004	23/11/2014	–	23/11/2006
Mr A Dembitz		£1.560	20,000	22/07/2005	21/07/2010	–	22/07/2007
Mr P Dimmock		£1.560	325,000	22/07/2005	21/07/2010	–	22/07/2007
Mr P Dimmock		£2.068	200,000	09/11/2005	08/11/2010	–	09/11/2007
Mr P Dimmock		£1.220	393,750	06/10/2006	05/10/2011	–	06/10/2008
S E Jonah, KBE, OSG		£1.000	400,000	23/11/2004	23/11/2014	–	23/11/2006
S E Jonah, KBE, OSG		£1.560	1,800,000	22/07/2005	21/07/2010	–	22/07/2007
Mr J Ladner	b	US$1.250	200,000	22/08/2003	21/08/2008	–	22/08/2003
Mr J Ladner		£1.000	80,000	23/11/2004	23/11/2014	–	23/11/2006
Mr J Ladner		£1.560	20,000	22/07/2005	21/07/2010	–	22/07/2007

Note a – J Auld's options were forfeit on his resignation
Note b – options vested at date of grant
All other options vest evenly over 2 years from the date of grant

Market price (pence/share)		
At 31 December 2006		71.0
Range during year	High	405.0
	Low	52.0

Going concern
On 7 June 2007 the Company entered into an agreement with Camac Energy EP Limited, a subsidiary of Camac International Limited, for the merger of its wholly owned subsidiary, Camac Energy Holdings Limited ('CEHL'), and Equator. The agreement included various refinancing provisions. On 31 August 2007, the merger agreement was terminated by mutual consent. The directors have examined the financial status of the Company and are of the opinion that there are sufficient alternative funding sources available to the Group. These sources include the farm out of 20 per cent of OPL 323 announced in August 2007 and the new short term working capital facilities announced in September 2007. Therefore the Board considers it appropriate to prepare the financial statements on a going concern basis.

Statement of disclosure of information to auditors
So far as each of the directors is aware, there is no relevant audit information of which the company's auditors are unaware.

Each of the directors has taken all the steps that he/she ought to have taken as director in order to make himself/herself aware of any relevant audit information and to establish that the company's auditors are aware of that information.

Suspension of shares
On 4 May 2007, as a result of unusual activity in Equator's shares, the Company announced that a corporate transaction was being discussed that could lead to Equator acquiring a larger entity in the form of a reverse takeover. As a result, trading in the shares was suspended. Details of the conditional proposed merger with CEHL were announced on 11 June 2007. Following termination of the merger agreement on 31 August 2007 and publication of these financial statements and the interim statement as at 30 June 2007, trading in the shares is expected to recommence.

DIRECTORS' REPORT CONTINUED
For the year ended 31 December 2006

Substantial shareholders
The following shareholders had interest in 3% or more of the voting capital of the Company as at 31 December 2006:

Holder	No. of shares	%
Morstan Nominees Ltd	24,642,961	14.64
Bear Stearns Securities Corp	15,350,006	7.02
N.Y. Nominees Ltd	11,671,165	6.93
HSBC Global Custody Nominee (UK) Ltd	8,854,863	5.26
Merrill Lynch International	8,222,118	4.88
Goldman Sachs Securities (Nominees) Ltd	7,756,696	5.87
Vidacos Nominees Ltd	7,478,939	4.44
Credit Suisse Securities (Europe) Ltd	7,221,061	4.29
Citigroup Global Markets UK Equity Ltd	7,000,000	4.16
Barclays Capital Nominees (no 3) Ltd	8,784,321	5.22
Euroclear Nominees Ltd	5,523,194	3.28
Credit Industriel & Commercial	5,199,191	3.09
The Bank of New York (Nominees) Ltd	4,766,303	3.60

Charitable donations
The Company made no charitable donations during the year but provided a supply of medicines during a cholera epidemic to São Tomé e Príncipe (2005: NIL).

Supplier payment policy
The Company's policy is to pay suppliers within the credit period granted by each supplier.

Auditors
Chantrey Vellacott, the previous auditors resigned on 29 November 2006. The directors appointed PricewaterhouseCoopers LLP to fill the casual vacancy and a resolution for the re-appointment of PricewaterhouseCoopers LLP as auditors of the Company is to be proposed at the forthcoming annual general meeting.

Wade Cherwayko
Director – Chief Executive

Philip Rand
Director – Chief Financial Officer

23 October 2007

CORPORATE GOVERNANCE

Corporate Governance Statement
The directors are committed to applying the Combined Code applicable to listed Companies. As an AIM quoted company, the Company is complying with all the recommendations applicable to a company of its current size. The Company has a Governance Handbook, which covers Board and General Corporate Governance.

Board Structure
The Board is accountable to shareholders for the effective management of the Company.
During 2006, the Board consisted of four executive directors and three non-executive directors. The Board met quarterly for full meetings and, on several other occasions, to give attention to individual issues immediately they arose. The Board has a schedule of matters specifically referred to it for decision. These include strategy and policy, risk management, structure and capital, financial reporting and controls and major capital projects, investments, acquisitions, divestments and contracts.

Board Committees
The Board has established the following Committees:

Audit Committee
This Committee provides the link between the auditors and the Board, independently of the Company's executives. It assists the Board in fulfilling its responsibilities in relation to financial reporting and control. The Committee met four times during the year. The members were Alexander Dembitz (Chairman), James Ladner and Baroness Chalker, all non-executive directors. All have since retired from the Committee when they left the Board, James Ladner in December 2006, Alexander Dembitz in February 2007 and Baroness Chalker in September 2007.

Currently, Martin Adams is Chairman of the Committee and Tony Renton is a member, both non-executive directors.

Nomination and Governance Committee
This Committee makes recommendations on corporate governance to the Board. It is then accountable for evaluating the performance of the Company against these recommendations and for determining the independence of non-executive directors. It also leads the process for succession planning and appointments to the Board. The Committee met four times during the year. The members were Baroness Chalker (Chairman), Sam Jonah and Alexander Dembitz. All have since retired from the Committee, Alexander Dembitz in February 2007, Sam Jonah in July 2007 and Baroness Chalker in September 2007.

Martin Adams and Tony Renton serve as members.

Compensation Committee
This Committee makes recommendations on executive remuneration, benefits and bonuses to the Board. The Committee met four times during the year. The members were James Ladner (Chairman), Alexander Dembitz, Sam Jonah and Baroness Chalker. All have subsequently resigned, as above.

Currently, the Committee is chaired by Tony Renton and Martin Adams is a member.

Internal Controls
The Board has responsibility for establishing and maintaining the Company's system of internal controls and reviewing its effectiveness. The procedures which include inter alia financial, operational and compliance matters and risk management are reviewed on an on-going basis by the relevant Board Committee and as part of the Schedule of Matters Reserved for the meetings of the full Board.

The internal control system can only provide reasonable and not absolute assurance against material misstatement or loss. The Board has considered the need for an internal audit function but does not consider it necessary at the current time.

Relations with shareholders
The Board is fully committed to maintaining regular and effective communications with shareholders. In addition to the Annual General Meeting there is regular dialogue and meetings with the larger shareholders and enquiries are received and are welcomed from all shareholders. The Company's website www.equatorexploration.com is also regularly updated with Press Releases and statements and shareholders are invited to visit and comment on this website.

Directors Service Agreements
No directors have service or consultancy agreements with a notice period in excess of one year.

CORPORATE AND SOCIAL RESPONSIBILITY STATEMENT

The Group is an ethical company, working in compliance with laws and regulations wherever we operate. This statement summarises the policies and standards that are in place to guide the appropriate ethical and professional behaviour for all employees, directors and contractors to the Group.

Ethics
The Company requires that all employees and directors should always act with the highest standards of honesty, integrity and fairness in all their business dealings with others, wherever they may be operating. We are committed to transparency in all our dealings.

Conflicts of Interest
The Nomination and Governance Committee of the Board monitors to ensure that all employees and directors avoid conflicts of interest between their private financial and personal activities and their role in the conduct of Company business.

Health, Safety and the Environment
The Company places a high degree of importance on health, safety and the environment and the well being of all those connected to it and its activities. Specific policies are supported by the HSE Management System Framework that documents the responsibilities and activities of every employee in the Company with respect to HSE.

Communities
The Company places a high value on the support of and the endorsement of its activities by the communities in which it operates. We assist those communities where we can, for example by providing training and medical supplies to communities in Nigeria and São Tomé e Príncipe.

Employees
The Company is committed to creating a work environment of mutual trust where every employee is treated with dignity and respect. Our policy is to recruit, select, develop and promote employees on merit, irrespective of race, colour, gender, religion, age, national origin, sexual orientation, marital status or disability.

Public and Political Activities
The Group neither supports political parties nor contributes to the funds of groups whose activities are calculated to promote partisan party interests. Therefore no political donations for the financial year 2006 were paid.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

Under the Company's Articles of Association, the directors are responsible for preparing financial statements for each financial year which give a true and fair view of the state of affairs of the Company and the group and of the profit or loss of the Company and group for that period. In preparing those financial statements, the directors are required to:

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

The directors confirm that they have complied with the above requirements in preparing the financial statements.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF EQUATOR EXPLORATION LIMITED

We have audited the group and parent company financial statements (the "financial statements") of Equator Exploration Limited for the year ended 31 December 2006 which comprise the Consolidated and Company Income Statements, Consolidated and Company Balance Sheets, Consolidate and Company Cash Flow Statements, Consolidated and Company Statements of Change in Shareholders' Equity and the related notes. These financial statements have been prepared under the accounting policies set out therein.

Respective responsibilities of directors and auditors
The directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the company's members as a body in accordance with the terms of our engagement letter and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the financial statements give a true and fair view. We report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements. We also report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. The other information comprises only the Directors' Report and the Chief Executive's Statement. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion
We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the group's and company's circumstances, consistently applied and adequately disclosed.

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

Opinion
In our opinion:

- the group financial statements give a true and fair view, in accordance with IFRS, of the state of the group's affairs as at 31 December 2006 and of its losses and cash flows for the year then ended;
- the parent company financial statements give a true and fair view, in accordance with IFRS, of the state of the parent company's affairs as at 31 December 2006 and of its losses and cash flows for the year then ended;
- the information given in the Directors' Report is consistent with the financial statements.

Emphasis of matter: Material uncertainty – Going concern
In forming our opinion, we have considered the adequacy of the disclosures made in the financial statements concerning the basis of preparation. The financial statements have been prepared on a going concern basis and, as described in the accounting policies note on pages 31 to 36, this depends on the Company raising adequate funding to enable it to meet its working capital requirements over the next 12 months. Details of the circumstances relating to this material uncertainty relating to going concern are described in the note on pages 31 to 36. Should sufficient financing not be available to the Company, the valuation of certain assets, principally the exploration and evaluation assets, which are valued at US$191million, may be impaired. The financial statements do not include any adjustments that would result from a failure to obtain additional funds. In view of the significance of this uncertainty, we consider that it should be drawn to your attention but our opinion is not qualified in this respect.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London

23 October 2007

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2006

	Note	2006 US$'000	2005 US$'000 (Restated)
Continuing operations			
Revenue	2	**277**	102
Cost of sales		**(807)**	(606)
Gross loss		**(530)**	(504)
Administrative expenses (2005 restated – see note 2)		**(36,272)**	(8,682)
Exceptional item: impairment charge	2	**(200,000)**	–
Loss from operations	3	**(236,802)**	(9,186)
Finance income	6	**6,282**	3,233
Finance costs	6	**(5,132)**	–
Finance income – net		**1,150**	3,233
Loss before income tax		**(235,652)**	(5,953)
Income tax expense		**–**	–
Loss for the year		**(235,652)**	(5,953)
Loss per share	7		
Basic		**(US$1.35)**	(US$0.05)
Diluted		**(US$1.35)**	(US$0.05)

The notes on pages 31 to 52 form part of these financial statements.

COMPANY INCOME STATEMENT

For the year ended 31 December 2006

	Note	2006 US$'000	2005 US$'000 (Restated)
Continuing operations			
Revenue	2	**277**	102
Cost of sales		**(807)**	(606)
Gross loss		**(530)**	(504)
Administrative expenses (2005 restated – see note 2)		**(33,396)**	(8,403)
Exceptional item: impairment charge	2	**(200,000)**	–
Loss from operations	3	**(233,906)**	(8,907)
Finance income	6	**25,182**	3,233
Finance costs	6	**(5,132)**	–
Finance income – net		**20,050**	3,233
Loss before income tax		**(213,856)**	(5,674)
Income tax expense		**–**	–
Loss for the year		**(213,856)**	(5,674)
Loss per share	7		
Basic		**(US$1.22)**	(US$0.05)
Diluted		**(US$1.22)**	(US$0.05)

The notes on pages 31 to 52 form part of these financial statements.

CONSOLIDATED BALANCE SHEET

As at 31 December 2006

	Notes	2006 US$'000	2005 US$'000 (Restated)
Assets			
Non–current assets			
Intangibles: Goodwill	8	**175**	1,373
Exploration and evaluation assets	9	**190,283**	50,334
Multi–client library	10	**1,791**	2,598
		192,249	54,305
Tangibles: Property, plant and equipment	11	**908**	739
		193,157	55,044
Current assets			
Inventories	15	**1,508**	–
Trade and other receivables	14	**4,818**	3,945
Cash and cash equivalents	16, 22	**86,708**	135,972
		93,034	139,917
Total assets		**286,191**	194,961
Equity			
Capital and reserves attributable to equity holders of the Company			
Share capital	17	**–**	–
Capital reserves (2005 restated – note 2)		**458,643**	204,409
Accumulated losses (2005 restated – note 2)		**(245,516)**	(9,864)
		213,127	194,545
Liabilities			
Non-current liabilities	19		
Borrowings		**54,818**	–
Long term payables		**3,064**	–
Deferred income		**10,902**	–
Current liabilities			
Trade and other payables	20	**4,280**	416
Total equity and liabilities		**286,191**	194,961

Approved by the Board of Directors on 17 October 2007

Signed on behalf of the Board of Directors:

Martin Adams
Director

Philip Rand
Director – Chief Financial Officer

The notes on pages 31 to 52 form part of these financial statements.

COMPANY BALANCE SHEET

As at 31 December 2006

	Notes	2006 US$'000	2005 US$'000 (Restated)
Assets			
Non–current assets			
Intangibles: Exploration and evaluation assets	9	**–**	13,898
Multi–client library	10	**1,791**	2,598
Receivables from subsidiary undertakings	12	**200,423**	37,711
Investments in subsidiaries	13	**2,317**	3,198
		204,531	57,405
Tangibles: Property, plant and equipment	11	**306**	109
		204,837	57,514
Current assets			
Inventories	15	**1,358**	–
Trade and other receivables	14	**1,969**	1,824
Cash and cash equivalents	16, 22	**86,655**	135,613
		89,982	137,437
Total assets		**294,819**	194,951
Equity			
Capital and Reserves attributable to equity holders of the Company			
Share capital	17	**–**	–
Capital reserves (2005 restated – note 2)		**458,643**	204,409
Accumulated losses (2005 restated – note 2)		**(223,616)**	(9,760)
		235,027	194,649
Liabilities			
Non-current liabilities	19		
Borrowings		**54,818**	–
Long term payables		**902**	–
Current liabilities			
Trade and other payables	20	**4,072**	302
Total equity and liabilities		**294,819**	194,951

Approved by the Board of Directors on 17 October 2007

Signed on behalf of the Board of Directors:

Martin Adams
Director

Philip Rand
Director – Chief Financial Officer

The notes on pages 31 to 52 form part of these financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2006

	Share capital US$'000	Capital reserves US$'000	Retained earnings US$'000	Total US$'000
Balance at 31 December 2004	–	142,159	(5,084)	137,075
Restatement of prior period share based payments (see note 2)	–	(1,173)	1,173	–
Restated balance at 31 December 2004	–	140,986	(3,911)	137,075
Changes in equity for 2005				
Loss for the year as previously reported	–	–	(3,713)	(3,713)
Prior year adjustment (see note 2)	–	–	(2,240)	(2,240)
Loss for the year (as restated)	–	–	(5,953)	(5,953)
Total recognised expense for the year	–	–	(5,953)	(5,953)
Issue of share capital	–	61,070	–	61,070
Cost of shares issued	–	(1,777)	–	(1,777)
Share based transactions	–	4,130	–	4,130
	–	63,423	(953)	57,470
Restated balance at 31 December 2005	**–**	**204,409**	**(9,864)**	**194,545**
Changes in equity for 2006				
Loss for the year	–	–	(235,652)	(235,652)
Total recognised expense for the year	–	–	(235,652)	(235,652)
Total loss for the year	–	–	(235,652)	(235,652)
Shares issued	–	253,484	–	253,484
Cost of shares issued	–	(11,010)	–	(11,010)
Share based transactions	–	3,960	–	3,960
Capital contribution	–	7,800	–	7,800
	–	254,234	(235,652)	18,582
Balance at 31 December 2006	**–**	**458,643**	**(245,516)**	**213,127**

Included in capital reserves as at 31 December 2006 are amounts attributable to share based transactions of US$8,674,449 (2005: US$4,649,164 – restated). There were no liabilities for which the right of a counterparty to cash or other assets had vested by 31 December 2006.

The notes on pages 31 to 52 form part of these financial statements.

COMPANY STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2006

	Share capital US$'000	Capital reserves US$'000	Retained earnings US$'000	Total US$'000
Balance at 31 December 2004 – as restated	–	142,159	(5,259)	136,900
Restatement of prior period share based payments (see note 2)	–	(1,173)	1,173	–
Restated balance at 31 December 2004	–	140,986	(4,086)	136,900
Changes in equity for 2005				
Loss for the year as previously reported	–	–	(3,434)	(3,434)
Prior year adjustment (see note 2)	–	–	(2,240)	(2,240)
Loss for the year (as restated)	–	–	(5,674)	(5,674)
Total recognised expense for the year	–	–	(5,674)	(5,674)
Issue of share capital	–	61,070	–	61,070
Cost of shares issued	–	(1,777)	–	(1,777)
Share based transactions	–	4,130	–	4,130
	–	63,423	(5,674)	57,749
Restated balance at 31 December 2005	**–**	**204,409**	**(9,760)**	**194,649**
Changes in equity for 2006				
Loss for the year	–	–	(213,856)	(213,856)
Total recognised expense for the year	–	–	(213,856)	(213,856)
Total profit for the year	–	–	(213,856)	(213,856)
Shares issued	–	253,484	–	253,484
Cost of shares issued	–	(11,010)	–	(11,010)
Share based transactions	–	3,960	–	3,960
Capital contribution	–	7,800	–	7,800
	–	254,234	(213,856)	40,378
Balance at 31 December 2006	**–**	**458,643**	**(223,616)**	**235,027**

Included in capital reserves as at 31 December 2006 are amounts attributable to share based transactions of US$8,674,449 (2005: US$4,649,164 – restated). There were no liabilities for which the right of a counterparty to cash or other assets had vested by 31 December 2006.

The notes on pages 31 to 52 form part of these financial statements.

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2006

	Notes	2006 US$'000	2006 US$'000	2005 US$'000	2005 US$'000 (Restated)
Cash flows from operating activities					
Loss from operations		**(236,802)**		(9,186)	
Adjustments for:					
Impairment provision		**200,000**		–	
Pre-licence costs written off		**23,885**		–	
Amortisation of multi–client library		**807**		606	
Share based transactions		**3,960**		4,130	
Warrant adjustment		**(4,000)**		–	
Goodwill written down		**1,198**		–	
Depreciation on fixtures and equipment		**372**		135	
Operating cash flows before movement in working capital		**(10,580)**		(4,315)	
(Increase) in inventory		**(1,508)**		–	
(Increase) in trade and other receivables		**(873)**		(3,677)	
Increase in trade payables		**519**		371	
Increase in other payables		**2,895**		–	
Net cash used in operating activities			**(9,547)**		(7,621)
Cash flows from investing activities					
Interest received		**6,282**		3,233	
Interest paid		**–**		–	
Acquisition of multi–client library		**–**		(1,052)	
Acquisition of exploration and evaluation assets		**(352,932)**		(48,085)	
Acquisition of fixtures and equipment		**(541)**		(833)	
Net cash used in investment activities			**(347,191)**		(46,737)
Cash flows from financing activities					
Loan proceeds		**65,000**		–	
Share capital issued (net of costs)		**242,474**		59,293	
Net cash from financing activities			**307,474**		59,293
Net increase/(decrease) in cash and cash equivalents			**(49,264)**		4,935
Cash and cash equivalents at beginning of period			**135,972**		131,037
Cash and cash equivalents at end of period	16		**86,708**		135,972

Cash and cash equivalents includes restricted cash balances of US$12.8million (2005: US$NIL) as detailed in note 22.

The notes on pages 31 to 52 form part of these financial statements.

COMPANY CASH FLOW STATEMENT

For the year ended 31 December 2006

	Notes	2006 US$'000	2006 US$'000	2005 US$'000	2005 US$'000
Cash flows from operating activities					
Loss from operations		**(233,906)**		(8,907)	
Adjustments for:					
Impairment provision		**200,000**		–	
Pre-licence costs written off		**23,296**		–	
Amortisation of multi–client library		**807**		605	
Share based transactions		**3,960**		4,130	
Warrant adjustment		**(4,000)**		–	
Goodwill written down		**1,198**		–	
Depreciation on fixtures and equipment		**111**		41	
Operating cash flows before movement in working capital		**(8,534)**		(4,131)	
(Increase) in inventory		**(1,358)**		–	
(Increase) in trade and other receivables		**(145)**		(1,555)	
Increase in trade payables		**515**		257	
Increase in other payables		**645**		–	
Cash used in operating activities			**(8,877)**		(5,429)
Intercompany interest received			**–**		–
Net cash used in operating activities			**(8,877)**		(5,429)
Cash flows from investing activities					
Interest received		**6,282**		3,232	
Interest paid		**–**		–	
Acquisition of subsidiaries		**(316)**		–	
Acquisition of multi–client library		**–**		(1,052)	
Acquisition of exploration and evaluation assets		**(2,898)**		(13,649)	
Acquisition of fixtures and equipment		**(308)**		(109)	
Loans to subsidiary undertakings		**(350,315)**		(37,710)	
Net cash used in investment activities			**(347,555)**		(49,288)
Cash flows from financing activities					
Loan proceeds		**65,000**		–	
Share capital issued (net of costs)		**242,474**		59,293	
Net cash from financing activities			**307,474**		59,293
Net increase/(decrease) in cash and cash equivalents			**(48,958)**		4,576
Cash and cash equivalents at beginning of period			**135,613**		131,037
Cash and cash equivalents at end of period	16		**86,655**		135,613

Cash and cash equivalents includes restricted cash balances of US$12.8million (2005: US$NIL) as detailed in note 22.

The notes on pages 31 to 52 form part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS
For the year ended 31 December 2006

1. BASIS OF PREPARATION

The Group and Company financial statements have been prepared in accordance with International Financial Reporting Standards.

Certain new accounting standards and interpretations are in issue which are not required to be adopted until after 2006 and which have not been adopted early by the Group. The key standards that will affect the group are:

IFRS 7 'Financial Instruments: Disclosures' requires changes in certain disclosures related to the Group's financial instruments for the year ending 31 December 31, 2007. Adoption will not affect the Group's accounting policies. The Group already provides certain of the disclosures required and does not expect that adoption of this standard will have a significant impact on the presentation of its Consolidated Financial Statements.

IFRS 8 'Operating Segments' is effective from 1 January, 2009, although early adoption by the Group is under consideration. The standard replaces IAS 14 Segment Reporting. The adoption of that standard will not have a significant impact on the presentation of its consolidated financial statements.

The financial statements are presented in US dollars since this is the currency in which the majority of the Group's transactions are denominated.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements have been prepared on the historical cost basis. The principal accounting policies adopted are set out below.

Going Concern
At the time of approving the accounts the Company did not have in place sufficient committed facilities to enable it to meet its working capital requirements for a period of at least 12 months. However, the Company has both short-term working capital facilities for a total of US$5million and has agreed terms for the farm-out of part of OPL 323 subject to the approval of NNPC. The Board considers that these will provide sufficient working capital for the foreseeable future and therefore the Board considers it appropriate to prepare the financial statements on a going concern basis.

Basis of consolidation
The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries) made up to 31 December each year. Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the period are included in the consolidated income statement from the effective date of acquisition and up to the effective date of disposal, as appropriate.

All intra-group transactions, balances, income and expenses are eliminated on consolidation.

Business combinations
The acquisition of subsidiaries is accounted for using the purchase method. The cost of the acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 are recognised at their fair value at the acquisition date, except for non-current assets (or disposal groups) that are classified as held for resale in accordance with IFRS 5 'Non Current Assets Held for Sale and Discontinued Operations', which are recognised and measured at fair value less costs to sell.

Goodwill arising on acquisition is recognised as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognised. If, after reassessment, the Group's interest in the fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in profit or loss.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2006

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

Interest in joint ventures

A joint venture is a contractual arrangement whereby the Company and other parties undertake an economic activity, which is subject to joint control.

Joint venture arrangements which involve the establishment of a separate entity in which each venturer has an interest are referred to as jointly-controlled entities. The Company reports its interest in jointly-controlled entities using the equity method. In the exploration and development phase of joint ventures, the costs are capitalised as intangible or tangible assets being subject to a regular impairment review.

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods and services provided in the normal course of business, net of discounts and sales related taxes.

Revenue from sales of multi-client library data is recognised when the majority owner of the seismic surveys has received the revenue from the customer as agreed under the joint agreement.

Interest income is accrued on a time basis, by reference to the principal outstanding and the interest rate applicable.

Employee services settled in equity instruments

The Group issues equity-settled share-based payments to certain employees. These are measured at fair value (excluding the effect of non market-based vesting conditions) at the date of grant. The fair value determined at the grant date is expensed on a cliff vesting basis over the vesting period, based on the Group's estimate of shares that will eventually vest and adjusted for the effect of non market-based vesting conditions.

Fair value is measured by use of the Black-Scholes model. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations.

Other goods or services settled in equity instruments

Goods or services (other than employee services) received in exchange for equity-settled share-based payments are measured directly at their current fair value at each balance sheet date. The proceeds received on exercise of the options, net of any directly attributable transaction costs, are credited to share capital (nominal value) and share premium when the options are exercised.

Foreign currencies

Transactions in currencies other than US dollars are recorded at the rates of exchange prevailing on the dates of the transactions. Monetary assets and liabilities denominated in such currencies are retranslated at the rates prevailing on the balance sheet date. Profits and losses arising on exchange are included in the income statement for the period.

Prior year adjustment

The cost of issuing options and warrants was calculated in prior years based on six-monthly breaks as the options vested. This calculation methodology has been amended in 2006 to provide for the cost of issuing options and warrants on a monthly basis on a projected vesting schedule. This has resulted in an increase in the amount that should have been charged in the year ended 31 December 2005 of US$2.24million and this amount is shown as a prior year adjustment within administrative expenses in the Income Statements and to Capital Reserves in the Balance Sheets for both the Company and the Group. This has had the effect of reducing Capital Reserves and reducing Retained losses by US$2.24million in the year ended 31 December 2005 (increase of US$1.17million at 1 January 2005). The impact on both 2005 basic and 2005 diluted losses per share is an increase of 1.8 pence per share.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

Goodwill

Goodwill arising on consolidation represents the excess of the cost of acquisition over the Company's interest in the fair value of the identifiable assets, liabilities and contingent liabilities of a subsidiary or jointly controlled entity at the date of acquisition. Goodwill is recognised as an asset and is tested for impairment annually, or on such occasions that events or changes in circumstances indicate that its value might be impaired in accordance with IAS 36.

Goodwill arising on the acquisition of subsidiaries is presented separately in the balance sheet.

On disposal of a subsidiary, associate or jointly controlled entity, the attributable amount of unamortized goodwill, which has not been subject to impairment, is included in the determination of the profit or loss on disposal.

Exploration and evaluation assets

The Group has capitalised at cost expenditure which is directly associated with the acquisition, exploration and appraisal of their oil and gas interests using the successful efforts method.

The exploration and evaluation assets are reviewed for impairment at least at each balance sheet date and when fact and circumstances suggest that the carrying amount exceeds the recoverable amount.Any impairment loss is calculated and recognized as an expense in accordance with IAS 36.

Fixtures and equipment

Fixtures and equipment are stated at cost less accumulated depreciation and any impairment losses. Depreciation is charged so as to write off the costs over their estimated useful lives, using the straight-line method commencing in the month following the purchase, on the following basis:

Fixtures and equipment	3 years
Motor Vehicles	3 years

The gain or loss arising on the disposal of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in income.

Investment in multi–client library

This investment represents the Group's participating interest in seismic surveys that are licensed to customers on a non-exclusive basis. All costs directly or indirectly incurred in acquiring, processing and otherwise completing seismic surveys are capitalised in the multi-client library. Group policy is to amortise the survey costs over five years from the point that the survey has been completed.

Segmental reporting

The Company has only one business segment, being classified as offshore, West Africa, exploration and production, and therefore does not report any geographical or business segmental splits.

Impairment

At each balance sheet date, the group reviews the carrying amount of its tangible and intangible assets with finite lives to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). For the purposes of impairment the Group estimates the recoverable amount of the cash-generating unit to which assets belong.

Goodwill arising on acquisitions is allocated to cash-generating units. The recoverable amount of the cash-generating unit to which goodwill is allocated is tested for impairment annually, or on such other occasions that events or changes in circumstances indicate that it might be impaired.

If the recoverable amount of a cash-generating unit is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. Impairment losses are recognised as an expense immediately, unless the relevant asset is land or buildings at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2006

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

Impairment continued

Where an impairment loss subsequently reverses, the carrying amount of the asset (or cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (or cash-generating unit) in prior periods. A reversal of an impairment loss is recognised as income immediately, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase. However, impairment losses relating to goodwill may not be reversed.

Derivatives and financial instruments

Financial assets and financial liabilities are recognised in the group's and Company's balance sheets when the group or Company has become a party to the contractual provisions of the instrument and are revalued to fair value at the end of the period. Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value.

Inventories

Inventories comprise stocks of drilling and related equipment and are valued at the lower of cost and net realisable value.

Trade receivables

Trade receivables are stated at their nominal value as reduced by appropriate provisions for estimated irrecoverable amounts to the fair value. Appropriate provisions for estimated irrecoverable amounts are recognised on profit or loss when there is objective evidence that the assets are impaired.

Cash and cash equivalents

Cash and cash equivalents comprise cash on hand and demand deposits, and other short-term highly liquid investments that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value.

Financial liabilities and equity

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidence a residual interest in the asset of the Group after deducting all of its liabilities.

Trade payables

Trade payables are stated at their nominal value less any discount or rebate received to arrive at fair value.

Equity instruments

Equity issued by the Company is recorded at the proceeds received, net of direct issue costs.

Taxation

The Company is not subject to tax in the British Virgin Islands. Operations within Nigeria and other jurisdictions are subject to local taxation and when applicable will be included in the financial statements.

Deferred tax

Deferred income taxes are calculated applying the liability method on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax assets are measured at the tax rates that are expected to apply in the time period when the asset is realized or the liability is expected to be settled. Deferred tax assets are recognized to the extent it is probable that future taxable income will be available to utilize those recognized deferred tax assets against such income.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

Key accounting estimates and judgements

In order to prepare the Consolidated Financial Statements in conformity with IFRS, management of the Group has to make estimates and judgements. The matters described below are considered to be the most important in understanding the judgements that are involved in preparing these statements and the uncertainties that could impact the amounts reported in the results of operations, financial condition and cash flows. Group accounting policies are described in Note 2.

Recoverable amount of intangible fixed assets

As at 31 December 2006 the Company had incurred £211million of costs, which is capitalized within intangible fixed assets, relating to a development project off the coast of Nigeria. At the time of approving these financial statements the Company did not have sufficient working capital facilities to enable it fund the remaining development activity required to bring the field to ‘first oil’. In the event that the Company is unable to complete its obligations under the agreement there exists an uncertainty as to whether the carrying value of the assets could be realized. In addition, the Company may incur additional costs associated with terminating certain other contractual commitments associated with the project. Management continues to pursue a number of alternatives for the funding of the project and currently the directors consider that there is sufficient uncertainty over the attainment of oil production in the near future. The directors therefore consider it prudent to record an impairment provision against the recorded value of the assets.

Estimation of oil and gas reserves

Oil and gas reserves are key elements in the Group’s investment decision-making process. They are also an important element in testing for impairment. Changes in proved and probable oil and gas reserves will also affect the evaluation of discounted cash flows.

Proved and probable oil and gas reserves are the estimated quantities of crude oil, natural gas and natural gas liquids which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions, i.e., prices and costs as of the date the estimate is made. Estimates of oil and gas reserves are inherently imprecise, require the application of judgement and are subject to future revision. Accordingly, financial and accounting measures (such as the evaluation of discounted cash flows, depreciation, depletion and amortisation charges, and decommissioning provisions) that are based on proved reserves are also subject to change.

Proved and probable reserves are estimated by reference to available reservoir and well information, including production and pressure trends for producing reservoirs and, in some cases, subject to definitional limits, to similar data from other producing reservoirs. Proved reserves estimates are attributed to future development projects only where there is a significant commitment to project funding and execution and for which applicable governmental and regulatory approvals have been secured or are reasonably certain to be secured. Furthermore, estimates of proved and probable reserves only include volumes for which access to market is assured with reasonable certainty. All proved reserves estimates are subject to revision, either upward or downward, based on new information, such as from development drilling and production activities or from changes in economic factors, including product prices, contract terms or development plans. In general, changes in the technical maturity of hydrocarbon reserves resulting from new information becoming available from development and production activities have tended to be the most significant cause of annual revisions.

In general, estimates of reserves for undeveloped or partially developed fields are subject to greater uncertainty over their future life than estimates of reserves for fields that are substantially developed and depleted. As a field goes into production, the amount of proved reserves will be subject to future revision once additional information becomes available through, for example, the drilling of additional wells or the observation of long-term reservoir performance under producing conditions. As those fields are further developed, new information may lead to revisions.

Un-drilled exploration prospects are based on third party independent evaluation of seismic data and adjacent geological and geophysical information including the results of drilling in nearby blocks.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2006

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

Exploration costs

Exploration drilling costs are capitalised unless it is judged that those costs are not representative of the intrinsic valuation of the costs incurred and the prospective resources. If there is a change in one of these judgements in a subsequent period, then the related capitalised exploration drilling costs would be expensed in that period, resulting in a charge to income.

Impairment of assets

For properties with proved and probable reserves, the carrying amounts of major property, plant and equipment are reviewed for possible impairment annually, while all assets are reviewed whenever events or changes in circumstances indicate that the carrying amounts for those assets may not be recoverable. If assets are determined to be impaired the carrying amounts of those assets are written down to their recoverable amount, which is the higher of fair value less costs to sell and value in use determined as the amount of estimated discounted future cash flows. For this purpose, assets are grouped based on separately identifiable and largely independent cash flows. Impairments can also occur when decisions are taken to dispose of assets. Impairments, except those relating to goodwill, are reversed as applicable to the extent that the events or circumstances that triggered the original impairment have changed.

Estimates of future cash flows are based on management estimates of future commodity prices, market supply and demand, product margins and, in the case of oil and gas properties, the expected future production volumes. Other factors that can lead to changes in estimates include restructuring plans and variations in regulatory environments. Expected future production volumes, which include both proved reserves as well as volumes that are expected to constitute proved reserves in the future, are used for impairment testing because the Group believes this to be the most appropriate indicator of expected future cash flows, used as a measure of value in use. Estimates of future cash flows are risk-weighted to reflect expected cash flows and are consistent with those used in Group companies' business plans. A discount rate based on the Group's marginal cost of debt is used in impairment testing. Expected cash flows are then risk-adjusted to reflect specific local circumstances or risks surrounding the cash flows. The Group reviews the discount rate to be applied on an annual basis although it has been stable in recent years.

Asset impairments or their reversal will impact income. The assumption on future oil prices tends to be stable because the Group does not consider short-term increases or decreases in prices as being indicative of long-term levels. At the end of 2006 the estimated oil and gas prices used for impairment testing were lower than prices prevailing in the market at that time.

Provisions

Provisions are recognised in the period when it becomes probable that there will be a future outflow of funds resulting from past operations or events which can be reasonably estimated. The timing of recognition requires the application of judgement to existing facts and circumstances, which can be subject to change.

Estimates of the amounts of provisions recognised are based on current legal and constructive requirements, technology and price levels. Because actual outflows can differ from estimates due to changes in laws, regulations, public expectations, technology, prices and conditions, and can take place many years in the future, the carrying amounts of provisions are regularly reviewed and adjusted to take account of such changes.

The Group is subject to claims and actions. The facts and circumstances relating to particular cases are evaluated in determining whether it is 'probable' that there will be a future outflow of funds and, once established, whether a provision relating to a specific litigation is sufficient. Accordingly, significant management judgement relating to contingent liabilities is required since the outcome of litigation is difficult to predict. Despite this uncertainty, actual payments related to litigation during the two years ended 31 December, 2006 have not been material to the Group's financial condition or results of operations.

A change in estimate of a recognised provision would result in a charge or credit to income in the period in which the change occurs. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

3. LOSS FROM OPERATIONS

	2006 US$'000	2005 US$'000
Loss from operations has been arrived at after charging/(crediting):		
Net foreign exchange loss/(gain)	**(2)**	67
Impairment provision	**200,000**	–
Pre-licence costs written off	**23,885**	–
Share based transactions	**3,960**	4,130
Revaluation of warrants	**(4,000)**	–
Amortisation of multi-client library	**807**	606
Depreciation on fixtures and equipment	**372**	135
Goodwill impairment on Aqua Exploration	**1,198**	–
Inventory written off	**377**	–
Auditors' fees	**190**	30
Directors' remuneration	**2,097**	722
Staff costs	**1,859**	324

The audit fee for the parent company was US$160,000 (2005: US$25,000).

4. STAFF COSTS

	2006 No.	2005 No.
The average monthly number of employees (including executive directors) was:	**15**	6

Their aggregate remuneration comprised (excluding executive directors):

	2006 US$'000	2005 US$'000
Wages and salaries	**1,589**	290
Social security costs	**120**	22
Other pension costs	**150**	12
	1,859	324

The Group contributes to individual personal pension plans.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2006

5. KEY MANAGEMENT COMPENSATION

Remuneration paid to key management including directors and key executives during the period was as follows:

	2006 US$'000	2005 US$'000
Salaries	**1,691**	210
Fees	**190**	422
Pensions	**216**	90
	2,097	722

The highest paid director was paid the following amounts

	2006 US$'000	2005 US$'000
Salary	**425**	198
Pension	**64**	30
	489	228

The remuneration of directors and key executives is decided by the Compensation Committee having regard to comparable market statistics.

6. FINANCE INCOME AND COSTS

	2006 US$'000	2005 US$'000
Group		
Interest received on bank deposits	**6,282**	3,233
Interest payable on borrowings	**(2,612)**	–
Unwind of discount on borrowings	**(2,520)**	–
	(5,132)	–

	2006 US$'000	2005 US$'000
Company		
Interest receivable on group funding	**18,900**	–
Interest received on bank deposits	**6,282**	3,233
	25,182	3,233
Interest payable on borrowings	**(2,612)**	–
Unwind of discount on borrowings	**(2,520)**	–
	(5,132)	–

7. LOSS PER SHARE

The calculations of the basic and diluted loss per share is based on the following data:

	2006 US$'000	2005 US$'000
Group		
Loss for the purpose of basic loss per share (net loss for the year)	**(235,652)**	(5,953)
Effect of dilutive options and warrants	**–**	–
Loss for the purposes of diluted loss per share	**(235,652)**	(5,953)

	2006 US$'000	2005 US$'000
Company		
Profit/(Loss) for the purpose of basic loss per share (net loss for the year)	**(213,856)**	(5,674)
Effect of dilutive options and warrants	**–**	–
Loss for the purposes of diluted loss per share	**(213,856)**	(5,674)
Number of shares		
Weighted average number of common shares in issue during the year	**171,432,878**	113,710,957
Effect of dilutive options and warrants	**9,385,000**	9,111,563
Weighted average number of common shares in issue during the year for the purpose of diluted loss per share	**180,817,878**	122,822,520

8. INTANGIBLE ASSETS – GOODWILL – GROUP ONLY

	US$'000
Cost	
At 1 January 2006 and 31 December 2006	1,762
Impairment provision	
At 31 December 2006	**1,587**
At 31 December 2005	389
Carrying amount	
At 31 December 2006	**175**
At 31 December 2005	1,373

An impairment provision has been recognized to reflect the recoverable value of Aqua Exploration Limited at its value in Use using a discount rate of 15% per annum for the current estimate. The amount of impairment has been reflected in administrative expenses.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED
For the year ended 31 December 2006

9. EXPLORATION AND EVALUATION ASSETS

	West Africa US$'000
Group	
Cost	
At 1 January 2005	2,249
Additions	48,085
At 1 January 2006	50,334
Additions	363,834
Impairment provision – note 1	(200,000)
Pre-licence costs taken to Income Statement	(23,885)
At 31 December 2006	**190,283**

Cost by licence	2006 US$'000	2005 US$'000
OML122	**210,838**	34,147
OPL 321	**60,869**	–
OPL 323	**105,983**	–
JDZ Block 2	**10,593**	–
EEZ	**2,000**	2,000
Impairment provision – note 1	**(200,000)**	–
Geological and geophysical studies	**–**	14,187
At 31 December 2006	**190,283**	50,334

	West Africa US$'000
Company	
Cost	
At 1 January 2005	249
Additions	13,649
At 1 January 2006	13,898
Additions	2,898
Pre-licence costs taken to Income Statement	(16,796)
At 31 December 2006	**–**

Cost by licence	2006 US$'000	2005 US$'000
Geological and geophysical studies	**–**	13,898

Note 1: The carrying amount of the OML 122 development has been reduced to its recoverable amount, based on its value in use using a discount rate of 15% per annum, through the recognition of an impairment provision against evaluation and exploration assets. This has been included as an exceptional item in the Income Statements of both the Group and the Company.

10. INVESTMENT IN MULTI-CLIENT LIBRARY

	US$'000
Group and Company	
Cost	
At 1 January 2005	2,983
Additions	1,052
At 1 January 2006	4,035
Additions	–
At 31 December 2006	**4,035**
Accumulated amortisation	
At 1 January 2005	830
Charge for year	607
At 1 January 2006	1,437
Charge for year	807
At 31 December 2006	**2,244**
Carrying amount	
At 31 December 2006	**1,791**
At 31 December 2005	2,598

The amortisation of the multi-client library is reflected within cost of sales.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2006

11. FIXTURES AND EQUIPMENT

	Fixtures and fittings US$'000	Equipment and Software US$'000	Motor vehicles US$'000	Total US$'000
Group				
Cost				
At 1 January 2005	–	43	–	43
Additions	251	219	363	833
At 1 January 2006	251	262	363	876
Additions	142	333	66	541
At 31 December 2006	**393**	**595**	**429**	**1,417**
Accumulated depreciation				
At 1 January 2005	–	2	–	2
Charge for year	36	57	42	135
At 1 January 2006	36	59	42	137
Charge for the year	93	144	135	372
At 31 December 2006	**129**	**203**	**177**	**509**
Carrying amount				
At 31 December 2006	**264**	**392**	**252**	**908**
At 31 December 2005	215	203	321	739

	Fixtures and fittings US$'000	Equipment US$'000	Total US$'000
Company			
Cost			
At 1 January 2005	–	43	43
Additions	–	109	109
At 1 January 2006	–	152	152
Additions	47	261	308
At 31 December 2006	**47**	**413**	**460**
Accumulated depreciation			
At 1 January 2005	–	2	2
Charge for year	–	41	41
At 1 January 2006	–	43	43
Charge for the year	5	106	111
At 31 December 2006	**5**	**149**	**154**
Carrying amount			
At 31 December 2006	**42**	**264**	**306**
At 31 December 2005	–	109	109

12. AMOUNT OWED BY SUBSIDIARY UNDERTAKINGS (COMPANY ONLY)

Loans have been provided to subsidiaries to provide funds for investment in the group's principal activity. There are no set repayment dates on the loans and interest is charged at market rates monthly on the outstanding amounts.

13. INVESTMENTS (COMPANY ONLY)

	Investment in subsidiary undertakings US$'000
At 1 January 2005	3,198
At 1 January 2006	3,198
Additions:	
Equator Exploration Nigeria Limited	79
Equator Exploration 321 Nigeria Limited	79
Equator Exploration 323 Nigeria Limited	79
Equator JDZ Nigeria Block 2 Limited	79
Investment in Aqua written down	(1,197)
At 31 December 2006	**2,317**

The write down of the investment in Aqua result from a review of the expected revenues to be generated from the sale of seismic data and represents the realisable value of such sales.

The subsidiary undertakings of the company are as follows:

Name	**Percentage owned**	**Country of registration**
Aqua Exploration Limited	100%	Bahamas
Equator Exploration Nigeria Limited	100%	Nigeria
Equator Exploration (OML 122) Limited	100%	BVI
Equator Exploration (Congo) Limited	100%	BVI
Equator JDZ Nigeria Block 2 Limited	100%	Nigeria
Equator Exploration 321 Nigeria Limited (note a)	100%	Nigeria
Equator Exploration 323 Nigeria Limited (note b)	100%	Nigeria
Equator Exploration Nigeria OML 122 Limited (note c)	100%	Nigeria

Note a: The company was formed on 1 February 2006
Note b: The company was formed on 31 January 2006
Note c: The company was formed on 17 May 2006 and is owned directly by Equator Exploration (OML 122) Limited

The principal activity of the above companies is the exploration and development of oil and gas projects.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED
For the year ended 31 December 2006

14. TRADE AND OTHER RECEIVABLES

	2006 US$'000	2005 US$'000
Group		
Trade receivables	**971**	157
Other receivables	**1,881**	1,594
Short term loans	**–**	900
Prepayments and accrued income	**1,966**	1,294
	4,818	3,945

	2006 US$'000	2005 US$'000
Company		
Trade receivables	**865**	157
Other receivables	**32**	765
Short term loans	**–**	900
Prepayments and accrued income	**1,072**	2
	1,969	1,824

The short term loan was converted into an advance success fee on completion of the Owanare exploration well on 2 April 2006. Interest is charged at 5% per annum payable on repayment of the capital amount. The principal plus interest is recoverable from revenues from the Bilabri field.

Trade receivables at both the Company and Group level include the sum of US$426,000 receivable from a partner company under a joint bidding agreement under which the parties agreed to share costs on an agreed basis. The receivable amount represents the agreed recoverable share of such costs paid by the Company.

The directors consider that the carrying amount of trade and other receivables approximates to their fair value.

Credit risk

The group's principal financial assets are bank balances and cash, trade receivables, other receivable and short term loans.

The group's credit risk is primarily attributable to its trade receivables, other receivable and short term loans. An impairment allowance is recognized where there is an identified loss event.

The credit risk on liquid funds is limited because the counterparties are banks with high credit ratings assigned by international credit-rating agencies.

15. INVENTORIES

	2006 US$'000	2005 US$'000
Group		
Stocks of drilling equipment	**1,508**	–
	1,508	–

	2006 US$'000	2005 US$'000
Company		
Stocks of drilling equipment	**1,358**	–
	1,358	–

Inventory is held at both the Company and subsidiary level and is charged to joint operations at cost on a first in first out basis. During the year US$377,000 (2005: US$NIL) was expensed.

16. CASH AND CASH EQUIVALENTS

Cash and cash equivalents comprise cash held by the group and Company and short-term deposits with an original maturity of three months or less. These amounts are denominated in US Dollars and the carrying amount of these assets approximate their fair value.

	2006 US$'000	2005 US$'000
Group		
Cash	**8,950**	3,002
Short-term deposits	**77,758**	132,970
	86,708	135,972

	2006 US$'000	2005 US$'000
Company		
Cash	**8,897**	2,643
Short-term deposits	**77,758**	132,970
	86,655	135,613

17. SHARE CAPITAL

	2006 No.	2005 No.
Issued and fully paid		
Common shares with no par value	**175,165,590**	131,417,190

On 19 January 2006, the Company issued 380,000 common shares for US$1.31 per share on exercise of warrants.

On 8 February 2006, the Company issued 2,030,000 common shares for US$1.31 per share on exercise of warrants.

On 6 March 2006, the Company issued 41,050,900 common shares for US$6.09 per share.

On 23 March 2006, the Company issued 73,836 common shares for £1.00 per share on exercise of share options.

On 30 March 2006, the Company issued 100,000 common shares for US$1.31 per share on exercise of warrants.

On 24 May 2006, the Company issued 113,664 common shares for £1.00 per share on exercise of options.

18. SHARE BASED PAYMENTS

During the year ended 31 December 2006, the Company had the following share options and warrants in issue. Awards of options are equity settled and there are no performance related conditions attached. Volatility is measured by comparison to a peer group of companies:

A	**Number of options**
Outstanding at 1 January 2006	400,000
Exercised during year	–
Outstanding at 31 December 2006	**400,000**

The 400,000 options outstanding as at 31 December 2006 were granted on 21 August 2003 with an exercise price of US$5.00 per share. Due to the split of shares on a four to one basis on 26 October 2004, the exercise price was reduced to US$1.25 per share. The options are exercisable until 21 August 2008 with each option convertible into one common share.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED
For the year ended 31 December 2006

18. SHARE BASED PAYMENTS CONTINUED

B	Number of warrants
Outstanding at 1 January 2006	11,395,000
Exercised during year	(2,410,000)
Outstanding at 31 December 2006	**8,985,000**

The 8,985,000 warrants outstanding as at 31 December 2006 were granted on 8 October 2004 with an exercise price of US$1.31 per share. The options are exercisable until 7 October 2007 with each warrant convertible into one common share.

Of the warrants exercised during the year, 280,000 were exercised when the average share price was £2.725, 2,030,000 were exercised when the average share price was £3.5225, and 100,000 were exercised when the average share price was £3.6065.

C	Number of options
Outstanding at 1 January 2006	3,360,000
Exercised during year	–
Outstanding at 31 December 2006	**3,360,000**

The Company granted 3,360,000 options to officers, directors, employees and consultants on 23 November 2004. The options had an exercise price of £1 and expire on 23 November 2014. The options vest on a pro-rata basis over 24 months. Management has estimated the fair value of these options, once vested, to be US$0.89 per option. The value of these options was determined using the Black Scholes option-pricing model with assumptions of a risk free rate of 4.5%, an average term of 9 years, a share value at time of granting of £1 and a volatility of 30%. The amount of US$477,633 was recorded in the consolidated income statement for the year ended 31 December 2006.

D	Number of options
Outstanding at 1 January 2006	2,400,000
Exercised during year	–
Outstanding at 31 December 2006	**2,400,000**

On 3 December 2004, the Company granted 2,400,000 assignable options to ODL Securities Limited as partial consideration for their advisory services in connection with the admission of the Company to AIM. These options have an exercise price of £1 and expire on 9 December 2007. Management has estimated the fair value of these options to be US$0.48 per option, totalling US$1,163,000. The value of these options was determined using the Black-Scholes option-pricing model with assumptions of a risk free rate of 3.75%, a term of 3 years, a share value at time of granting of £1 and a volatility of 30%. The total value of US$1,163,000 was recorded in other reserves in 2004. This did not affect the consolidated income statement as the cost was taken to the capital reserve as an expense of the issue of common shares on AIM.

E	Number of options
Outstanding at 1 January 2006	1,134,000
Exercised during year	187,500
Outstanding at 31 December 2006	**946,500**

On 3 December 2004, the Company granted 1,134,000 assignable options to NWCF LLP as partial consideration for their advisory services in connection with the admission of the Company to AIM. These options have an exercise price of £1 and expire on 9 December 2009. Management has estimated the fair value of these options to be US$0.65 per option, totalling US$752,000. The value of these options was determined using the Black-Scholes option-pricing model with assumptions of a risk free rate of 4.25%, a term of 5 years, a share value at time of granting of £1 and a volatility of 30%. The total value of US$752,000 was recorded in other reserves in 2004. This did not affect the consolidated income statement as the cost was taken to the capital reserve as an expense of the issue of common shares on AIM.

Of the options exercised during the year, 73,836 were exercised when the average share price was £3.41875 and 113,664 when the average share price was £3.83.

18. SHARE BASED PAYMENTS CONTINUED

F	Number of options
Outstanding at 1 January 2006	2,315,000
Exercised during year	–
Outstanding at 31 December 2006	**2,315,000**

The Company granted 2,315,000 options to directors on 22 July 2005. The options had an exercise price of £1.56 and expire on 21 July 2010. The options vest semi-annually over 24 months. Management has estimated the fair value of these options, once vested, to be US$1.40 per option. The value of these options was determined using the Black-Scholes option pricing model with assumptions of a risk free rate of 4.3%, an average term of 4.5 years, a share value at time of granting of £1.56 and a volatility of 56%. The amount of US$1,349,452 was recorded in the consolidated income statement for the year ended 31 December 2006.

G	Number of options
Outstanding at 1 January 2006	1,525,000
Exercised during year	–
Outstanding at 31 December 2006	**1,525,000**

The Company granted 1,525,000 options to directors, employees and consultants on 9 November 2005. The options had an exercise price of £2.068 and expire on 8 November 2010. The options vest semi-annually over 24 months. Management has estimated the fair value of these options, once vested, to be US$1.62 per option. The value of these options was determined using the Black-Scholes option-pricing model with assumptions of a risk free rate of 4.3%, an average term of 5 years, a share value at time of granting of £2.06 and a volatility of 55%. The amount of US$1,684,413 was recorded in the consolidated income statement for the year ended 31 December 2006.

H	Number of options
Outstanding at 1 January 2006	60,000
Exercised during year	–
Outstanding at 31 December 2006	**60,000**

The Company granted 60,000 options to a consultant on 8 December 2005. The options had an exercise price of £2.068 and expire on 8 December 2010. The options vest semi-annually over 24 months. Management has estimated the fair value of these options, once vested, to be US$2.10 per option. The value of these options was determined using the Black-Scholes option-pricing model with assumptions of a risk free rate of 4.3%, an average term of 5 years, a share value at time of granting of £2.24 and a volatility of 55%. The amount of US$91,836 was recorded in the consolidated income statement for the year ended 31 December 2006.

I	Number of options
Outstanding at 1 January 2006	–
Granted during year	75,000
Outstanding at 31 December 2006	**75,000**

The Company granted 75,000 options to employees on 31 January 2006. The options had an exercise price of £3.05 and expire on 31 January 2011. The options vest semi-annually over 24 months. Management has estimated the fair value of these options, once vested, to be US$3.59 per option. The value of these options was determined using the Black-Scholes option-pricing model with assumptions of a risk free rate of 4.5%, an average term of 5 years, a share value at time of granting of £3.59 and a volatility of 55%. The amount of US$200,818 was recorded in the consolidated income statement for the year ended 31 December 2006.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2006

18. **SHARE BASED PAYMENTS** CONTINUED

J	Number of warrants
Outstanding at 1 January 2006	–
Granted during year	6,691,290
Outstanding at 31 December 2006	**6,691,290**

The Company granted 6,691,290 warrants, which may be exercised at any time, to certain lenders under the US$65million Bridge Loan on 4 August 2006. The options had an exercise price of £2.00 and expire on 7 October 2009. The value of these options was determined using the Black-Scholes option-pricing model with assumptions of a risk free rate of 5%, an average term of 38 months, a share value at time of granting of £1.37 and a volatility of 52%. The total value of US$4,902,039 was recorded in the company and consolidated balance sheets at 31 December 2006 as a reduction of the principal amount outstanding under the loan. This amount has been treated as nominal interest and will be amortised over the loan life. At 31 December 2006, the warrants were marked-to-market based on the share price of £0.71 and a profit of US$3,998,715 was accounted for in the income statements of both the company and the group.

K	Number of options
Outstanding at 1 January 2006	–
Granted during year	877,500
Outstanding at 31 December 2006	**877,500**

The Company granted 817,500 options to employees and consultants on 6 October 2006. The options had an exercise price of £1.155 and expire on 6 October 2011. The options vest semi-annually over 24 months but 60,000 were forfeited prior to the first vesting date. Management has estimated the fair value of these options, once vested, to be US$0.50 per option. The value of these options was determined using the Black-Scholes option-pricing model with assumptions of a risk free rate of 5%, an average term of 5 years, a share value at time of granting of £0.74 and a volatility of 49%. The amount of US$77,161 was recorded in the consolidated income statement for the year ended 31 December 2006.

L	Number of options
Outstanding at 1 January 2006	–
Granted during year	893,750
Outstanding at 31 December 2006	**893,750**

The Company granted 893,750 options to directors on 6 October 2006. The options had an exercise price of £1.22 and expire on 6 October 2011. The options vest semi-annually over 24 months but 500,000 were forfeited after 31 December 2006 but prior to the first vesting date. Management has estimated the fair value of these options, once vested, to be US$0.48 per option. The value of these options was determined using the Black-Scholes option-pricing model with assumptions of a risk free rate of 5%, an average term of 5 years, a stock value at time of granting of £0.74 and a volatility of 49%. The amount of US$78,590 was recorded in the consolidated income statement for the year ended 31 December 2006.

19. BORROWINGS AND LONG TERM PAYABLES

	2006 US$'000	2005 US$'000
Group		
Loans (note i)	**65,000**	–
Amounts provided as future interest	**(10,182)**	–
Net Borrowings	**54,818**	–
Other Payables	**3,064**	–
Deferred Income (note ii)	**10,902**	–
	68,784	–

	2006 US$'000	2005 US$'000
Company		
Loans (note 1)	**65,000**	–
Amounts provided as future interest	**(10,182)**	–
	54,818	–
Other Payables – warrant obligations	**902**	–
	55,720	–

Note i
On 8 August 2006 the Company entered into a loan agreement with certain of its shareholders for US$65million. The loan has a repayment date of 7 August 2008 and carries interest at rates between 10 per cent per annum and 14 percent per annum payable semi-annually in arrears. In addition the lenders have warrants or conversion rights on up to 17,397,356 ordinary shares at £2.00 per share expiring on 8 October 2009 of which 6,691,290 warrants relating to US$25million of the total borrowings had been issued at the end of 2006. In accordance with IFRS the issued warrants have been marked to market and treated as an adjustment to current year losses. The reduction in the principal amount of the loan has been treated as additional interest and will be amortised over the life of the loan. The effective rate of interest on the loan is 27 per cent per annum.

Note ii
Deferred Income refers to interest accrued on funding provided under the terms of the OML122 Finance and Services Agreement and which is recoverable from future revenues. This will be accounted for as income in due course as revenues commence and this sum represents fair value in the balance sheet.

Loans and deferred income are denominated wholly in US Dollars. Payables are denominated wholly in Pounds Sterling.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED
For the year ended 31 December 2006

20. TRADE AND OTHER PAYABLES

Group	2006 US$'000	2005 US$'000
Trade payables	**533**	14
Accruals	**3,747**	402
	4,280	416

Company	2006 US$'000	2005 US$'000
Trade payables	**515**	–
Accruals	**3,557**	302
	4,072	302

Accruals principally comprise interest due on the US$65million loan due for payment in February 2007 and are denominated in US$. Trade payables are principally denominated in Pounds Sterling.

21. RELATED PARTY TRANSACTIONS

The following transactions were carried out with related parties:

a) Purchases of goods and services.

	2006 US$'000	2005 US$'000
Purchases of services	**145**	213
Recoverable rent deposit	**1,072**	-
	1,217	213

Goods and services are bought from Interbasin Resources (UK) Limited, an entity controlled by key management, which supplies administrative services to the Company on normal commercial terms and conditions.

b) Year end balances arising from sales/purchases of goods services

	2006 US$'000	2005 US$'000
Interbasin Resources (UK) Limited	**1,072**	213
Mart Resources Inc	**599**	–
	1,671	213

c) During the year US$176million (2005: US$35million) was advanced via a wholly-owned subsidiary to fund jointly contracted operations with the owner of the licence in OML 122. The funds were advanced in order to pay for drilling and development services supplied under the terms of the Finance and Service Agreement which sets out the rights and obligations of the parties relating to certain areas within the block OML 122. These amounts are classified as investment in exploration and evaluation assets in the Group accounts and in amounts owed by subsidiary undertakings in the Company accounts.

22. CONTINGENT LIABILITIES

Seisco Investments Limited

Seisco Investments Limited ('Seisco') is a related company that had a common director and shareholder. During 2002 Seisco provided Equator with US$500,000 to fund Equator's share of the acquisition costs of certain seismic data. The amount borrowed was repaid during 2002 and 2003 from the revenue generated from licensing the seismic data.

In the event that no future seismic revenues can be expected from the majority owner (the 'Majority Owner') of this designated batch of seismic data acquired in 2002, the acquisition cost of which was funded by Seisco, as a result of the Majority Owner of such data entering into liquidation proceedings, Equator will issue Seisco with a maximum of 100,000 common shares. The number of common shares to be issued to Seisco in the event of the cessation of seismic revenues due to the liquidation of the Majority Owner will be dependant upon the extent to which the funds provided by Seisco have been repaid prior to the cessation of seismic revenues as shown below:

Amount of initial investment repaid	Number of shares to be issued
Greater than initial funds provided but less than 1.5 times initial funds provided	100,000
Greater than 1.5 times initial funds provided	50,000

The Company believes that there is a high probability that the lower number of shares will be issued as a sum greater than the initial investment had already been paid to Seisco at the end of 2006.

Contract for Floating Production Vessel ('FPSO')

On 16 October 2006 the Company together with its partner in Block OML 122, Peak Petroleum Industries Nigeria Limited ('Peak'), entered into an agreement with BW Endeavour Limited ('BW'), for the provision of an FPSO for the oil production from the Bilabri Field. Under the terms of this contract, Equator and Peak are jointly and severally liable for certain payments in the event of early termination. The value of the potential payment increases during the period to commencement of oil production and then reduces to zero over the following three years.

At the end of 2006 the early termination contingent liability was US$35million of which US$20million was to be provided by means of a bank guarantee. A bank guarantee for US$10million had already been issued and a further US$10million guarantee was issued on 12 January 2007. The bank guarantees were issued solely by Equator and were secured by means of cash deposit to the issuing bank. The early termination penalty increased to US$52million during 2007 of which US$20million remains covered by bank guarantees in accordance with the terms of the contract.

On 20 August 2007 the Company announced that the FPSO contract had been terminated and that BW might activate the security. The US$20million guarantee was activated in September 2007.

Drilling Rig Contract

On 6 February 2006, Equator entered into a contract for the continued use of the drilling rig being used on the OML122 drilling programme. This contract followed on from the contract entered into jointly by Equator and Peak and would allow for further drilling once the initial 5 exploration, appraisal and development wells had been finished and, where appropriate, were completed for production. The contract had not become effective at 31 December 2006, as the previous contract was still effective. The 6 February 2006 contract became effective on 31 January 2007. Invoices for drilling and ancillary services for approximately US$18million remain outstanding. Many of these invoices are being disputed by Equator due to disagreement over the performance of the rig and the significant additional costs which have resulted.

The rig operator has also invoiced the Company for US$38million for early termination of the contract, which is disputed by the Company because the contract was terminated for prolonged force majeure in accordance with its terms.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2006

22. CONTINGENT LIABILITIES CONTINUED

Restricted Cash Balances

At 31 December 2006 Equator had US$86.7million of cash resources. However some of this cash is not freely available as it is utilized as deposits to secure the issue of bonds and guarantees by its bankers under a group facility to support potential liabilities. The deposits are interest-bearing at market rates. As at 31 December 2006 the following amounts were restricted in use:

	US$'000
Collateral for JDZ Block 2 performance bond	**2,800**
Collateral for guarantee for FPSO early termination penalty	**20,000**

23. SUBSEQUENT EVENTS

On 8 February 2007, Equator agreed terms with a Nigerian bank for the provision of the performance bonds required under the PSC's for OPL 321 and OPL 323 for its share of the agreed work programme. Equator's share of the obligation is US$83million and the bank has provided the guarantees without cash collateral. The bank has taken security over Equator's shares in the two subsidiaries owning the interests in the PSC's – Equator Exploration 321 Nigeria Limited and Equator Exploration 323 Nigeria Limited.

On 11 June 2007 Equator announced that it had entered into a conditional Merger Agreement with Camac Energy EP Limited whereby Equator would acquire, by reverse takeover of CEHL, its exploration and production interests in the territorial waters of Nigeria, including participating interests in OML 108, OML 120, OML 121, OPL 278 and OPL 282. On 31 August 2007 Equator and Camac Energy EP Limited agreed to terminate the Merger Agreement.

In June 2007, the Company entered into two working capital loan agreements, one with a shareholder and a second with South African Oil Company, a wholly-owned subsidiary of Camac International Limited. Both loans are for US$5million and carry interest at 8 per cent per annum. The final repayment date is 15 February 2009 for both loans and interest is payable with the repayment. Both lenders have been issued with warrants over 7,326,000 common shares at £0.35 per share, exercisable immediately over a period of 2 years. In addition, the lenders have been given joint security over certain assets of the Company.

In July 2007, the Company entered into a further working capital loan agreement for US$7.5million with a shareholder lender. The loan bears interest at 8 per cent per annum. The final repayment date is 15 February 2009 and interest is payable with the repayment. The lender has been issued with warrants over 10,989,000 common shares at £0.35 per share, exercisable immediately over a period of 2 years. The lender has been given joint security over certain assets of the Company.

In August 2007, the Company entered into a farm-out agreement with BG Exploration and Production Nigeria Limited for two thirds of its 30 percent interest in OPL 323. The total consideration for the farm out could be up to US$75million, comprising a cash consideration payable on completion of the agreement and a carry on the future exploration and appraisal costs. The assignment of the interest to BG is subject to the approval of the Nigerian National Petroleum Corporation.

In September 2007, the Company entered into an unsecured short term working capital loan agreement for US$5million with a shareholder lender. The loan bears interest at 6 per cent per annum. The final repayment date is 15 December 2007 and interest is payable with the repayment. The lender has been issued with warrants over 10,989,000 common shares at the lower of £0.30 per share or the average of the closing share price for the first 15 days of trading following the re-listing of Equator shares in AIM, exercisable immediately over a period of 2 years. If the loan is not repaid by the due date, the principal amount of the loan and accrued interest will be converted into common shares at £0.10 per share.

On 4 May 2007, as a result of unusual activity in Equator's shares, the Company announced that a corporate transaction was being discussed that could lead to Equator acquiring a larger entity in the form of a reverse takeover. As a result, trading in the shares was suspended. The conditional proposed merger with CEHL was announced on 11 June 2007. Following termination of the merger agreement and publication of these financial statements and the interim accounts to 30 June 2007, trading in the shares is expected to recommence.

List of Subsidiaries of Equator Exploration Limited as of 31 December 2006.

PARENT COMPANY

Equator Exploration Limited
British Virgin Islands

WHOLLY OWNED SUBSIDIARIES

Aqua Exploration Limited
Bahamas

Equator Exploration (Congo) Limited
British Virgin Islands

Equator Exploration Nigeria Limited
Nigeria

Equator Exploration JDZ Nigeria Block 2 Limited
Nigeria

Equator Exploration Nigeria 323 Limited
Nigeria

Equator Exploration Nigeria 321 Limited
Nigeria

Equator Exploration (OML 122) Limited
British Virgin Islands

Subsidiary
Equator Exploration Nigeria OML 122 Limited
Nigeria

Interests held by Equator Exploration Limited as of 31 December 2006.

Agreement Type	Country	Block	Equator's %	Operator
PSC	Nigeria (Offshore)	OPL 321	30%	KNOC
PSC	Nigeria (Offshore)	OPL 323	30%	KNOC
Finance & Service Agreement	Nigeria (Offshore)	OML 122	Varying % in contract area	Peak Petroleum Industries Nigeria Limited
PSC	Joint Development Zone	Block 2	9%	Sinopec
Options	São Tomé e Príncipe	2 Blocks	100%	Equator Exploration Ltd.

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