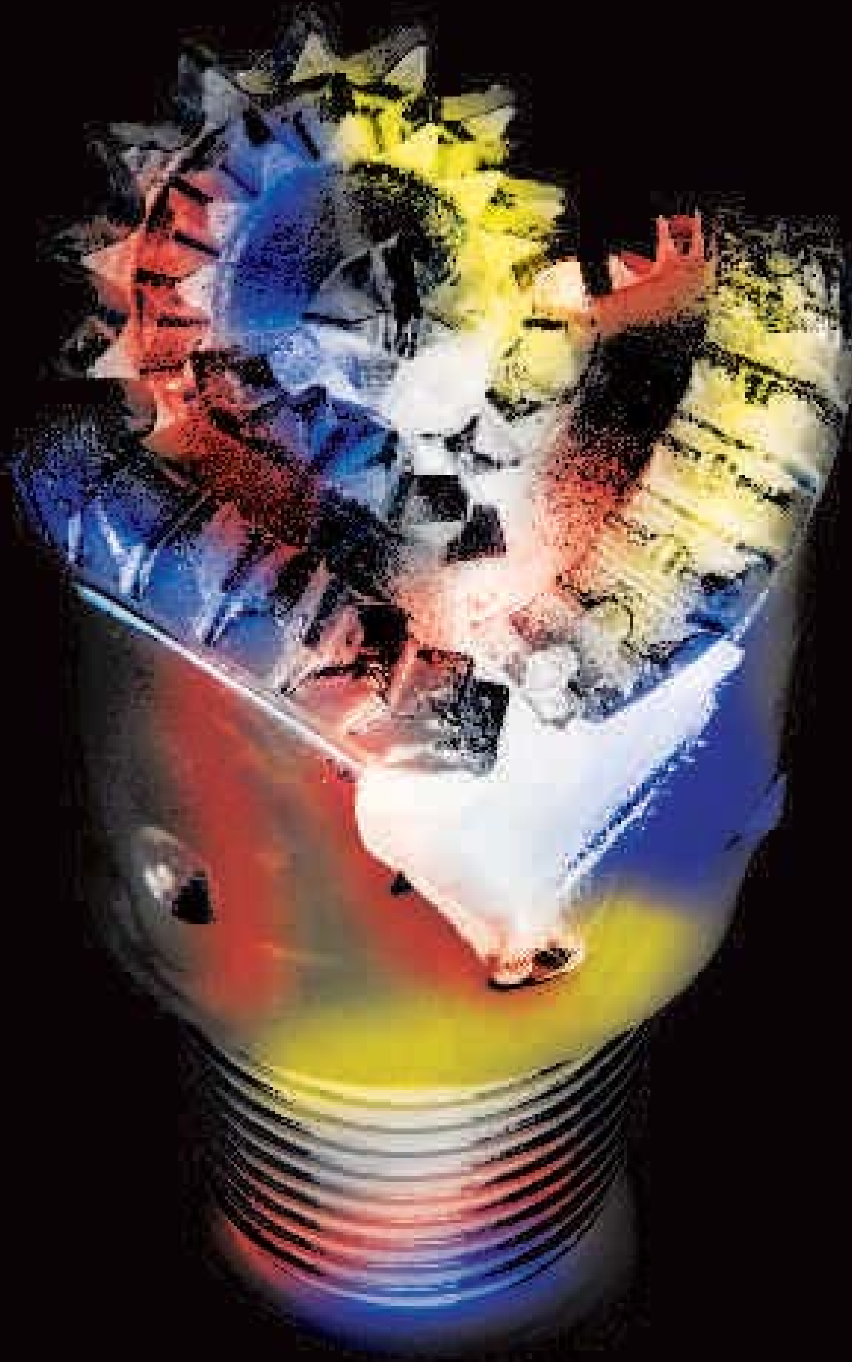
Right Now

Caspian is drilling for oil in Kazakhstan

CASPIAN ENERGY INC. 2007 ANNUAL REPORT



Caspian's Kazakhstan exploratory efforts are an excellent opportunity to create continued value for the Company.

CORPORATE PROFILE

Caspian Energy Inc. (Caspian) is an oil and gas exploration company operating in Kazakhstan where it has a number of targets in the highly prospective Aktobe Oblast of Western Kazakhstan. It holds an exclusive license which entitles it to explore and develop certain oil and gas properties known as the “North Block”, an area of 3,458 km^2. The Company’s license area lies immediately adjacent to various producing fields, including the Alibekmola, Zhanazhol and Kenkiyak fields.

Caspian’s shares are listed on the London Stock Exchange’s special market for growth companies under the symbol: CEK.L and on the Toronto Stock Exchange under the symbol: CEK.TO

President's Message

Caspian Energy is building a robust petroleum and natural gas exploration company based on a solid strategy and business plan. In continuing to pursue our Platform for Growth as a company, we are currently drilling wells in one of the richest resource stockpiles in the Republic of Kazakhstan, whose Caspian Basin is one of the world's largest untapped hydrocarbon reservoirs.

Caspian Energy has been successful in establishing itself as an operating entity in the Republic of Kazakhstan, working with a supportive government that encourages foreign and direct investment in its oil and gas sector. In our exploration work within the North Block in Western Kazakhstan, we continue to increase both production and revenue as we explore new opportunities and drill new wells.

As we move through 2008 and into 2009, evaluating and analyzing seismic data for new areas within the North Block and drilling new wells as our strategy dictates, we expect to continue to see healthy production and revenue growth for the Company and for its shareholders.

HIGHLIGHTS

In many respects, 2007 was a challenging year for us. Caspian is still in an exploratory phase, and challenges are to be expected along the way. In 2007, these challenges took the form of time and mechanical issues, both combining to constrain our development activity.

Despite these challenges, we continued to move forward through 2007. Caspian's work program extension with the Republic of Kazakhstan was extended for an additional two-year period, subject to the terms of the original exploration contract. The East Zhagabulak (EZ) #301 well was put back in production, and re-evaluation and testing resumed on wells EZ #302 and EZ #303. And today, the Company's reserves are more valuable than they were a year ago, thanks to a upward change in market conditions that saw the average price per barrel of oil rise by more than 300%. Caspian is currently in discussions with several different companies interested in a potential farm-in to one of our blocks. Not only will this farm-in give Caspian the cash flow for drilling other wells, but it will also give us the increased capital needed to develop seismic and drill in new areas.

With the stage thus set, 2008 started out strong, and we expect it to remain strong throughout the year. For Caspian, fiscal 2008 will continue to be a year of activity. The Company spudded Baktygaryn #703, our first post-salt well identified from the Baktygaryn 3-D seismic survey, in mid-March, with a target total depth of approximately 2,500 metres. Following the release of the rig from well #703, a second well will be drilled to the eastern side of Baktygaryn, in the Aransay area of the western portion of the North Block.

To assist the financing of these two exploratory tests, Caspian filed a Rights Offering on April 17, 2008. At full subscription, this offering is expected to raise $4,347,635.

Caspian is moving ahead in Kazakhstan's North Block on other projects, as well. Completion of the interpretation work on the Baktygaryn 3-D seismic program and the North Block regional 2-D seismic data, begun in 2006, is expected during June 2008. Later in the year, we plan to begin drilling in the Itisay, Kozdesay and West Kozdesay areas, located in the southwestern portion of the North Block.

Our first-quarter results for 2008 tell the story of the year ahead: we saw an increase in our average production rate to 461 barrels of oil per day (Bopd) from 181 Bopd, as well as an increase in the average price per barrel to $74.98 from $26.86, due to the impact of international oil markets. Revenue has increased, production has increased, and Caspian entered 2008 in a positive cash flow position, active and drilling.

OPPORTUNITY

Caspian faces great opportunities in the Republic of Kazakhstan. This oil-rich nation has projected reserves of 28 billion barrels of oil and condensate and 106 trillion cubic feet of gas. The extraction, production and transportation of oil and gas form a significant part of the Kazakh economy. And, as it is not a member of OPEC, it is not subject to the OPEC system of production quotas, yet another positive aspect of our exploration activities there.

The North Block, where Caspian is currently focusing its exploration efforts, is located on the Eastern margin of the Pre-Caspian basin in the Aktobe Oblast in Western Kazakhstan, and covers an area of 3,458 square kilometres. The North Block area is serviced by excellent infrastructure, including electrical power lines, a good network of all weather roads and an experienced oil industry work force. The area is crossed by the regional rail oil transportation system, and is connected by a new pipeline from Kenkiyak to Atyrau and on to Western European and Russian export markets. This combination of available infrastructure and ease of access to export markets offers Caspian the growth opportunity it needs as the Company's production continues to increase.

OUTLOOK

In the long-term, Caspian's exploratory efforts in these, our development years, are an excellent opportunity to create continued value for the Company, and its shareholders, for many years to come. We will continue to explore and drill as we identify new prospects within the region.

We are very pleased with the strong operational improvements we have made so far this year. We are also excited about the prospects we have identified in the Baktygaryn area, and the new strategy the Company is pursuing. We believe that our latest targets have the potential for highly significant recoverable reserves, relative to those currently booked, and our corporate strategy as a whole presents an attractive risk profile for Caspian.

We are especially grateful for the support and commitment shown by our shareholders, our staff, and our Board of Directors as we continue to grow and develop. We are energized about our Company's future, and we remain committed to delivering sustainable performance to our shareholders over the long-term.

Sincerely,

William A. G. Ramsay
May 23, 2008

The Company has been successful in establishing itself as an operating entity in the ROK and expects to continue with future growth through continued work there.

Prior to the end of the fourth quarter 2005, EZ#301 was drilled to a total depth of 4,846 metres and logged. The well was completed with the drilling rig before the rig was moved to the EZ#302 location. EZ#301 was matrix acidized and the two potentially productive hydrocarbon bearing zones were flow-tested. The lower zone (KT-2) was tested at 2,532 Bopd. The upper zone (KT-1) had difficulty maintaining an independent flow, so it was commingled with the lower zone and the well was tied-in to the Zhagabulak production facility. Subsequently, productions logs were run and it was determined that the KT-1 was producing 100 Bopd. Well 301 was undergoing a government mandated pressure survey in November 2006, when a production logging tool and cable were lost in the hole. During the second quarter, the tool and wire were recovered and the well has resumed production. Well 301 is currently producing 575 BOPD, 14 BWPD, 820 MCFD with a FTP (flowing tubing pressure) of 353 psig and a shut in casing pressure of 1,896 psig on a 12 mm choke.

The second exploration effort, EZ#302, was spud on December 25, 2005. Acidizing and testing of the well were performed following removal of the drilling rig. The well showed indications of hydrocarbons while drilling and logging; however, the stimulation efforts failed to cause the well to flow naturally. In well 302 a workover has been prepared to isolate the KT-II and the lower portions of the KT-I that exhibit higher water saturations on the logs.

The third location, EZ#303 is about 5.2 km southwest of EZ#302. EZ#303 spud on May 28, 2006. The well was permitted to a depth of 5,700 metres. EZ#303 reached a total depth of 4,630 metres in a sidetrack wellbore after the initial wellbore reached a depth of 5,430 metres, but was lost due to a drill string parting, while pulling out of the hole for logging. A total of 70 meters were perforated and acidized in both the KT-1 and KT-2 intervals. A combined test of both intervals yielded water with small amounts of oil, while the separate test on the KT-1 yielded water. In well 303 a workover is being written to isolate intervals and test separately to identify which perforations are producing water.

The original producing well, EZ#213, drilled and completed during the Soviet period, was re-entered in November 2006 and perforations were added in the KT-1 reservoir. Due to different casing weights, problems were encountered with packer setting for the acid operation and consequently, only one-half of the productive zones were acidized. Despite the limits on the acidization, a significant improvement of daily production over the pre-workover rates was achieved. Well 213 is currently producing 180 Bopd, 50 BWPD, 253 MCFD, with a flowing tubing pressure of 397 psig, and a shut in casing pressure of 1,882 psig on an 7.0 mm choke. The choke size was reduced from the previous 8.7 mm choke in order to keep the well flowing at the higher water cut. Artificial lift equipment is currently being designed and quoted and a procedure will be prepared once the design is finalized.

The Company has initiated the development approval process for East Zhagabulak. Caspian has made initial contacts with Kazakhstan design institutes for the preparation of the development program report for the development of the East Zhagabulak field. The preparation of the official State Reserves Report for East Zhagabulak is underway with completion expected by the end of May 2008 and subsequent submission to the government for approval and the resultant issuance of a development contract in late summer 2008. Upon approval of the Reserves Report the Technology Scheme will be prepared and approved, which outlines the detailed plan of development for the field.

Ongoing petrophysical analyses of all wells penetrating the below salt reservoirs is being completed and correlations of these wells will aid in the identification of future drilling locations in the North Block. Identification and acquisition of well data within the extended territory is also be evaluated for inclusion into this process.

The Baktygaryn 3-D seismic program was completed in early November 2005. PGS-GIS, in Almaty, ROK was awarded the processing contract. Due to the presence of large salt bodies in the Baktygaryn Area, the 3-D data set was processed through PSDM (Pre-Stack Depth Migration) and interpretation of this data has been completed. PSTM (Pre-Stack Time Migration) analysis, for the above salt section has also been conducted. The acquisition of the 367 kilometre regional 2-D seismic survey covering the west and north areas of the North Block and tying into the Zhagabulak and Baktygaryn 3-D seismic surveys that was completed in March 2007 has also been processed and interpreted. The Baktygaryn 3-D program and the regional 2-D program were fully interpreted at the end of October 2006. The interpreted data from all new seismic data acquired and from the earlier reprocessed Soviet-era 2-D seismic is being combined to create a geological model and identify additional leads and prospects across the North Block territory.

The Baktygaryn Area presents drilling targets in both the below salt Lower Permian and Carboniferous sections and the above salt Upper Permian and Mesozoic sections with depths ranging from approximately 400 to 2,500 metres and provides a second tier of exploration to the Company's drilling portfolio. These targets are recognized in the forms of channel sands, traps against the Kungurian salt ridges and underneath salt overhangs.

In addition to the ongoing interpretation work on the Baktygaryn 3-D and North Block regional 2-D seismic data and the identification of several post-salt drilling targets in the Triassic and Permian formations, further progress on the interpretation has revealed the presence of additional targets which are being added to the Company's prospect and lead portfolio. Completion of the interpretation work is expected by late May 2008.

The first post-salt well identified from the Baktygaryn 3-D survey, Baktygaryn #703, was spud in mid-March 2008 with a target total depth of approximately 2,500 metres to test the Triassic and Upper Permian horizons. Currently the well has been sidetracked and is drilling ahead in the salt section of the well. The sidetrack hole was the result of a mechanical failure in the lower section of the drill string. The well is drilling at 2000 meters having passed the original hole on May 8th. The well is expected to reach total depth in the Upper Permian by the end of May.

A second drilling location has been prepared, Aransay 711. This well, located approximately 20 kilometers east of Baktygaryn #703, on a parallel salt ridge, and will test Triassic sands at a depth of approximately 800 meters in a fault trap created by salt movement, where Direct Hydrocarbon Indicator's (DHI'S) are seen in seismic data.

Soviet-era seismic data interpretation, mapping and the associated shallow well drilling in the Itisay, Kozdesay and West Kozdesay areas, located in the southwestern portion of the North Block, yielded minor positive tests and shows of oil associated with the post-salt sediments of Jurassic, Triassic and Upper Permian ages. A review of this data has resulted in the identification of several prospects and leads ranging from 600 to 1,800 metres in trapping positions against Permian salt ridges and under-salt overhangs. Several lines from the Company's 2006 2-D seismic program were shot across certain of these leads and prospects to verify this premise. Interpretation of most of the regional 2006 2-D seismic survey covering the west and north areas of the North Block has been completed. The interpreted data from all new seismic data acquired and from the earlier reprocessed Soviet-era 2-D seismic was combined to create a geological model and identify additional leads and prospects across the North Block territory. As a result of this work, some of the earlier leads and prospects in the post-salt sediments identified on vintage maps and seismic in three areas in the south western portion of the North Block, known as Itisay, Kozdesay and West Kozdesay have been confirmed and in addition several new leads and drillable prospects have been identified in trapping positions against Permian salt ridges and under salt overhangs. Drilling for these targets is expected to begin in 2008.

Future seismic activity includes a third 3-D seismic acquisition, pending the results of the upcoming drilling campaign and further ongoing 2-D seismic interpretation.

The relatively shallow post salt targets at Baktygaryn offer a completely new series of opportunities for the Company. The 3-D and 2-D seismic data have enabled several new prospects to be identified and the Company is now in the process of selecting additional drilling locations.

Following the release of the rig from well #703, the first exploration well located in Baktygaryn, the Company intends to move drilling efforts to the eastern side of the Baktygaryn, West Kozdesay, and Aransay areas in the western part of the North Block where it will drill for Triassic and Upper Permian targets ranging from 700 to 1,400 metres.

The Company's work program extension, with the ROK, to December 2007 has now been extended for an additional two-year period, subject to the terms of the original exploration contract. The 2008 work program commits the Company to undertake US$8.6 million of exploration expenditures prior to the close of that calendar year and the 2009 work program – US$10.5 million of exploration expenditures. Additionally, during 2008, Aral is obligated to make-up an additional US$ 7.1 million in cumulative shortfalls under the contract. At March 31, 2008, Aral had expended approximately $US 2.0 million toward discharging this shortfall.

Reserves

All of the Company's reserves are in Kazakhstan. The Company has reserves of light and medium oil.

The Company's reserves were evaluated by McDaniel & Associates Consultants Ltd., independent engineering consultants and qualified reserves evaluators, as at December 31, 2007.

The Company engaged McDaniel to provide an evaluation of proved, probable and possible reserves. The Reserves Data summarizes the oil, liquids and natural gas reserves of the Company and the net present values of future net revenue for these reserves using constant prices and costs and forecast prices and costs. The Reserves Data conforms with the requirements of National Instrument 51-101 Standards of Disclosure for Oil and Gas Activities ("NI 51-101").

The process of estimating reserves is complex. It requires significant judgments and decisions based on available geological, geophysical, engineering and economic data. These estimates may change substantially as additional data from ongoing development activities and production performance becomes available and as economic conditions impacting oil and gas prices and costs change. The reserve estimates contained herein are based on current production forecasts, commodity prices and economic conditions.

The estimated future net revenues presented in the following tables are estimated values and do not represent the fair market value of the reserves. The estimated reserves attributed to the Company described in the Statement are estimates only and the actual reserves may be greater than or less than the estimates provided herein.

National Instrument 51–101

This report was prepared for the purpose of evaluating the Company's P&NG reserves according to Canadian Oil and Gas Evaluation Handbook (COGEH) reserve definitions and standards and by reference in NI 51–101.

Forecast Prices and Costs

Table 1 presents a summary of oil reserves. Table 2 presents a summary of net present values of future net revenue, before and after income taxes. Table 3 presents the total future net revenue (undiscounted) for the total proved and total proved plus probable reserves categories. Table 4 presents the future net revenue by product group. Table #6 is a summary of pricing and inflation rate assumptions.

Reconciliation

Table 5 presents the Reconciliation of the Company's Gross Reserves, by principle product type, using forecast prices and costs, as of December 31, 2007.

Summary of Oil Reserves – Forecast Prices and Costs

(Table #1 – as of December 31, 2007)

	Light and Medium Oil	
Reserves Category (Mbbl)	Gross	Net
Proved		
Developed producing	500	478
Undeveloped	653	640
Total proved	1,153	1,118
Probable	2,893	2,835
Total proved plus probable	4,046	3,953

Summary of Net Present Values of Future Net Revenue – Forecast Prices and Costs

(Table #2 – as of December 31, 2007)

Before income taxes discounted at %/year

Reserves Category	0%	5%	10%	15%	20%
Proved					
Developed producing	8,931	8,278	7,726	7,252	6,842
Undeveloped	4,708	3,180	2,038	1,171	506
Total proved	13,638	11,458	9,763	8,423	7,348
Probable	71,334	51,649	38,564	29,534	23,100
Total proved plus probable	84,972	63,107	48,327	37,957	30,448

After income taxes discounted at %/year

Reserves Category	0%	5%	10%	15%	20%
Proved					
Developed producing	7,568	7,048	6,605	6,223	5,891
Undeveloped	3,909	2,576	1,570	802	208
Total proved	11,477	9,624	8,175	7,025	6,099
Probable	55,337	39,586	29,203	22,095	17,072
Total proved plus probable	66,814	49,209	37,378	29,120	23,171

Total Future Net Revenue (Undiscounted) – Forecast Prices and Costs

(Table #3 – as of December 31, 2007)

Reserves Category (M$US)	Revenue	Royalties	Operating costs	Development costs	Abandonment and reclamation costs	Other expenses [1]	Future net revenue before income taxes	Income taxes	Future net revenue after income taxes
Proved reserves	62,691	1,814	20,677	9,385	88	17,089	13,638	2,161	11,477
Proved plus probable reserves	231,234	5,184	44,467	26,891	172	69,549	84,972	18,159	66,814

[1] Other expenses include export rent tax and payment of commerciality bonus.

Total Future Net Revenue By Production Group – Forecast Prices and Costs

(Table #4 – as of December 31, 2007)

Reserves Category	Production group	Future net revenue before income taxes (discounted at 10%/year) (M$US)	Unit value before income taxes (discounted at 10%/year) ($bbl)
Proved	Light and Medium Crude Oil (including solution gas and other by-products)	9,763	8.74
	Heavy Oil (including solution gas and other by-products)	–	–
	Natural Gas (including by-products but excluding solution gas from oil wells)	–	–
Proved plus probable	Light and Medium Crude Oil (including solution gas and other by-products)	48,327	12.2
	Heavy Oil (including solution gas and other by-products)	–	–
	Natural Gas (including by-products but excluding solution gas from oil wells)	–	–

Reconciliation Of Company Gross Reserves By Principal Product Type – Forecast Prices and Costs

(Table #5 – as of December 31, 2007)

	Light and Medium Oil		
Factors (Mbbl)	Gross proved	Gross probable	Gross proved plus probable
December 31, 2006	1,812	2,897	4,709
Extensions	–	–	–
Improved Recovery	–	–	–
Technical Revisions	(485)	(4)	(489)
Discoveries	–	–	–
Acquisitions	–	–	–
Dispositions	–	–	–
Economic Factors	–	–	–
Production	(174)	–	(174)
December 31, 2007	1,153	2,893	4,046

Summary Of Pricing And Inflation Rate Assumptions – Forecast Prices and Costs

(Table #6– as of December 31, 2007)

Year	WTI crude oil price ($US/bbl)	Brent crude oil price ($US/bbl)	Export field price ($US/bbl)	Domestic field price ($US/bbl)	Inflation forecast (%)
2008	90.00	89.00	59.00	30.00	2.0
2009	86.70	85.70	60.20	30.60	2.0
2010	83.20	82.20	61.39	31.21	2.0
2011	79.60	78.50	59.93	31.84	2.0
2012	78.50	77.40	58.46	32.47	2.0

Management's Discussion & Analysis

FORWARD-LOOKING STATEMENTS AND OTHER INFORMATION

Certain statements contained in this MD&A constitute forward-looking statements. Forward-looking statements are included under "Business Prospects and Outlook" and elsewhere in this MD&A. These statements relate to future events or the Company's future performance. All statements other than statements of historical fact may be forward-looking statements. Forward-looking statements are often, but not always, identified by the use of words such as "seek", "anticipate", "budget", "plan", "continue", "estimate", "expect", "forecast", "may", "will", "project", "predict", "potential", "targeting", "intend", "could", "might", "should", "believe" and similar words suggesting future outcomes or statements regarding an outlook. Forward-looking statements in this MD&A include, but are not limited to, statements with respect to: the performance characteristics of the Company's oil and natural gas properties; drilling plans and the timing and location thereof; plans for the exploration and development of the North Block; plans for seismic acquisition and surveys; production capacity and levels, and the timing of achieving such capacity and levels; the level of expenditures for compliance with environmental regulations; the size of oil and natural gas reserves; projections of market prices and costs; supply and demand for oil and natural gas; expectations regarding the ability to raise capital and to continually add to reserves through acquisitions and development; and capital expenditure programs.

Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements. The Company believes the expectations reflected in those forward-looking statements are reasonable but no assurance can be given that these expectations will prove to be correct and readers are cautioned not to place undue reliance on forward-looking statements contained in this MD&A. Some of the risks and other factors which could cause results to differ materially from those expressed in the forward-looking statements contained in this MD&A include, but are not limited to: volatility of oil and natural gas prices; liabilities inherent in oil and natural gas operations; uncertainties associated with estimating oil and natural gas reserves; competition for, among other things, capital, acquisitions of reserves, undeveloped lands and skilled personnel; geological, technical, drilling and processing problems; fluctuations in currency and interest rates; product supply and demand; risks inherent in the Company's foreign operations; changes in environmental and other regulations or the interpretation of such regulations; political and economic conditions in the Republic of Kazakhstan; and the other factors discussed in this MD&A.

Statements relating to "reserves" are deemed to be forward-looking statements, as they involve the implied assessment, based on certain estimates and assumptions, that the reserves described can be profitably produced in the future. Readers are cautioned that the foregoing lists of factors are not exhaustive. The forward-looking statements contained in this MD&A are made as of the date hereof and the Company undertakes no obligation to update publicly or revise any forward-looking statements, whether as a result of new information, future events or otherwise. The forward-looking statements contained in this MD&A are expressly qualified by this cautionary statement.

Finally, in the presentation of the MD&A, Caspian uses two terms that are universally applied in analyzing corporate performance within the oil and gas industry, but which regulators require that we provide disclaimers.

Barrel of Oil Equivalent (BOE) – The oil and gas industry commonly expresses production volumes and reserves on a "barrel of oil equivalent" basis ("BOE") whereby natural gas volumes are converted at the ratio of six thousand cubic feet to one barrel of oil. The intention is to sum oil and natural gas measurement units into one basis for improved analysis of results and comparisons with other industry participants. Throughout this MD&A Caspian has used the 6:1 BOE measure which is the approximate energy equivalency of the two commodities at the burner tip. BOE does not represent a value equivalency at the plant gate, which is where Caspian sells its production volumes, and therefore may be a misleading measure if used in isolation.

Cash Flow from Operations (cash flow) – This measure is considered critical within the oil and gas industry both in terms of measuring success in our historical operations and being an indicator of funding sources for on-going efforts to replace production volumes and increase reserve volumes. Canadian GAAP requires that "cash flow from operating activities" be the measurement focus. This latter term is derived from "cash flow" as defined by Caspian adjusted for the change in non-cash working capital. Caspian believes "cash flow" and "cash flow per share" to be more meaningful measures of our performance and therefore has used these terms throughout this MD&A. Accordingly, we are required to advise the reader that: (a) these are non-GAAP measure for purposes of Canadian accounting standards and (b) our determinations may not be comparable to those reported by other companies.

The following Management's Discussion and Analysis ("MD&A") of financial results as provided by the management of Caspian Energy Inc. ("Caspian" or the "Company") should be read in conjunction with the audited consolidated financial statements and notes for the years ended December 31, 2007 and 2006. This commentary is based upon information available to March 28, 2008.

The intention of this Management's Discussion and Analysis (MD&A) is for Caspian to explain to its shareholders and the investment community three analyses from management's perspective:

1. **Caspian's performance in fiscal 2007;**
2. **Caspian's current financial condition; and**
3. **Caspian's future prospects.**

This MD&A complements and supplements the disclosures in our audited financial statements which have been prepared according to Canadian generally accepted accounting principles ("GAAP").

References to "we", "us" and "our" in this MD&A are to the Company and all references to dollars are in Canadian dollars, unless otherwise indicated. Additional information relating to the Company, including its annual information form, is available on SEDAR at www.sedar.com.

BUSINESS OF THE COMPANY

Caspian has a 50% interest in Aral Petroleum Capital LLP ("Aral"), which is held by Caspian Energy Ltd. ("Caspian Ltd."), the Company's wholly-owned subsidiary, through which it has the right to explore and develop certain oil and gas properties in the Republic of Kazakhstan ("ROK") known as the North Block, a 3,458 square kilometre area located in the vicinity of the Kazakh pre-Caspian basin. The Company's strategy is to focus on the operations of Aral and the significant opportunity it presents in the North Block.

Aral's exploration and development rights in the North Block were granted pursuant to an exploration contract dated December 29, 2002 between Aral and the Ministry of Energy and Mineral Resources of the ROK (the "Exploration Contract"). Under the terms of the Exploration Contract, Aral agreed to spend at least US$20.8 million under a minimum work program in respect of the North Block, during the initial three-year term of the contract. Eligible expenditures include such things as processing and reinterpretation of geological and geophysical data of prior years, two dimensional and three dimensional seismic surveys, drilling exploration wells, well reactivations and well surveys and testing. As discussed below, funds raised by the Company are used to discharge the obligations of Aral relating to the minimum work program. As at December 31, 2005, Aral's financial obligation under the minimum work program had been discharged in full. Further, Aral undertook to expend US$12.2 million by the close of calendar 2006, which undertaking was also discharged. The initial term of the Exploration Contract was extended for a two-year period through to December 2007, and has now been extended for an additional two-year period, subject to the terms of the exploration contract. The work program extension to December 2007 included drilling three wells to a combined total of 8,500 metres with a monetary obligation of US$20.6 million. The 2008 work program commits the Company to undertake US$8.6 million of exploration expenditures prior to the close of the calendar year and the 2009 work program – US$10.5 million. As at December 31, 2007, Aral had incurred US$119.7 million in charges related to the work commitments of the Minimum Working Program agreed with the ROK competent bodies. Shortfalls under the Work Commitments aggregated US$7.1 million. Management of Aral believes the Company is in compliance with its commitments under the Minimum Working Program and has received authorization from the Ministry of Energy and Natural Resources and other competent bodies to carry over fulfillment of the above shortfalls to the year ending December 31, 2008.

Under the terms of a shareholders' agreement dated June 25, 2004 among Caspian Ltd., Azden Management Limited ("Azden") and Aral, Caspian is obligated to fund Aral's initial work program. Further, under the terms of the shareholders' agreement, Caspian was committed to use all reasonable commercial efforts to raise financing of US$84.0 million (to be loaned to Aral) to fund

the first stage of Aral's exploration program under the Exploration Contract. Funds are transferred to Aral via monthly instalments. Caspian discharged this undertaking and has advanced further funds to Aral to prosecute the exploration program. These additional capital advances are being matched by Azden, the other shareholder in the Aral joint venture. Pursuant to the Credit Agreement among Aral and Caspian, Caspian has begun charging interest at a rate equal to Canada Treasury Bills + 0.25% on its initial advance. This inter-company charge eliminates upon consolidation of the two entities.

Terms of the Exploration Contract include a 3% royalty during the pilot phase, a 10% fee, based upon sales, after VAT (value-added tax), a 30% corporate income tax and the liability for an excess profits tax based upon a sliding scale.

In accordance with Kazakhstani tax legislation Aral is required to pay royalties in relation to the volume of oil produced. However, management of Aral believes that in accordance with the Exploration Contract the test production phase is not subject to royalties and that Aral will be liable to pay royalties only at the experimental-industrial phase or when the Production Contract is signed. Should tax authorities consider Aral's position as incorrect, additional taxes and fines may be imposed. Accordingly, at December 31, 2007 no provision for royalties had been recorded by Aral.

Caspian accesses western capital markets and utilizes western technology to explore and exploit its Kazakh assets. The proceeds from its financing activities are used to fund the exploration program and support pilot production in the North Block. The operational strategy of the Company is as follows:

- **To prove-up the maximum amount of reserves with the minimum number of wells**
- **To utilize 3-D seismic and international standards and evaluation technology**
- **To focus initially on the Zhagabulak area in the North Block, where the pilot production exists, then move to the Baktygaryn area and subsequently, other areas within the North Block**
- **To position the Company to maximize value to the investor through development and/or sale – farmout of the North Block**
- **To be aware of competitive efforts and resultant opportunities that may manifest themselves in the form of reserves/production acquisitions**

While there have been improvements in the economic situation in Kazakhstan in recent years, its economy continues to display some characteristics of an emerging market. These characteristics include, but are not limited to, the existence of a currency that is not freely convertible outside of the Country, a low level of liquidity of debt and equity securities in the markets and relatively high inflation. Additionally, the oil and gas Kazakhstan is impacted by political, legislative, fiscal and regulatory developments. The prospects for future economic stability are largely dependent upon the effectiveness of economic measures undertaken by the Government, together with legal, regulatory and political developments, which are beyond the Company's control. The financial condition and future operations of the Company may be adversely affected by continued uncertainties in the business environment of Kazakhstan. Management is unable to predict the extent and duration of these uncertainties, nor quantify the impact, if any, on the financial statements. Tax legislation and practice in Kazakhstan are in the developmental stage and therefore are subject to varying interpretations and frequent changes, which may be retroactive.

Further, the interpretation of tax legislation by tax authorities as applied to the transactions and activities of the Company may not coincide with that of Management. As a result, transactions may be challenged by tax authorities and the Company may be charged additional taxes, penalties and interest. Tax periods remain open to review by the tax authorities for three to five years; however, under certain circumstances a tax year may remain open longer.

The Company's common shares trade on the Alternative Investment Market (AIM) of the London Stock Exchange and the Toronto Stock Exchange under the symbol CEK.

East Zhagabulak (EZ)

The Zhagabulak Area is located in the southeastern corner of the North Block. The Government of Kazakhstan has estimated that this Area contains 642 million barrels of oil in place with 193 million barrels classified as recoverable. These Kazakh estimates were based upon the results of Soviet era 2-D seismic data and stratigraphic test wells. Caspian neither accepts nor denies these estimates, but expects to validate this data through its exploration program.

The initial 3-D seismic program covering 406 square kilometres has been completed, processed and interpreted, indicating significant structures. Processing through Pre-Stack Time Migration (PSTM) of the Zhagabulak 3-D seismic data set was completed at the end of August 2005. The processing was performed by PGD-Dank (a division of Paradigm Geophysical) in Almaty, ROK. Following processing, the data set was transferred to Halliburton's Landmark Geophysical office in Moscow, Russia for interpretation. Processing through Pre-Stack Depth Migration (PSDM) was completed in December 2005 and transferred to Landmark for interpretation. The presence of a broad, extensive structure separating Zhagabulak from neighboring producing fields has been noted and several potential drilling locations have been identified. The original producing well, EZ#213, drilled and completed during the Soviet period, was re-entered in November 2006 and perforations were added in the KT-1 reservoir. Due to different casing weights, problems were encountered with packer setting for the acid operation and consequently, only one-half of the productive zones were acidized. Despite the limits on the acidization, a significant improvement of daily production over the pre-workover rates was achieved. Well 213 is currently producing 300 BOPD, 43 BWPD, 428 MCFD with a flowing tubing pressure of 375 psig and a shut-in casing pressure of 1,705 psig on an 8.7 mm choke. A production survey to determine the reservoir pressures and production contribution from the KT-1 and KT-2 intervals was completed during October 2007 that showed approximately 30 BOPD from the KT-1 with the remaining production from the KT-2.

The location for the first well on the block, EZ#301, 1.1 km southwest of well EZ#213, was chosen from an earlier fast-track interpretation of the 3-D seismic data set. A contract with Nabors Drilling International was concluded in April 2005 and the well spud on July 16, 2005. The well reached a total depth of 4,846 metres on November 7, 2005, logs were run, production casing was set and testing began in mid-December. Acid treatment of the perforated intervals occurred during February 2006. Well 301 was undergoing a government mandated pressure survey in November 2006, when a production logging tool and cable were lost in the hole. During the second quarter 2007, the tool and wire were recovered and the well has resumed production. Well 301 is currently producing 588 BOPD, 14 BWPD, 837 MCFD with a FTP (flowing tubing pressure) of 382 psig and a shut in casing pressure of 1,838 psig on a 12 mm choke. A pressure buildup was successfully completed in August 2007 and a xylene cleanout was pumped in November 2007 to clean out the suspected asphaltene buildup in the production tubing.

A second well location, EZ#302, was drilled approximately 3.6 km southwest of EZ#301 and is structurally updip to that well. EZ#302 spud on December 25, 2005. Acidizing and testing of the well were performed following removal of the drilling rig. The well showed all indications of hydrocarbons while drilling and logging; however, the stimulation efforts failed to cause the well to flow naturally. In well 302, a workover is being evaluated to isolate the KT-2 and the lower portions of the KT-1 that exhibit higher water saturations on the logs.

The third drilling location, EZ#303, located 5.2 km southwest of EZ#302, was permitted to a depth of 5,700 metres and was spud on May 28, 2006. EZ#303 reached a total depth of 4,630 metres in a sidetrack wellbore after the initial wellbore reached a depth of 5,430 metres, but was lost due to a drill string parting, while pulling out of the hole for logging. A total of 70 meters were perforated and acidized in both the KT-1 and KT-2 intervals. A combined test of both intervals yielded water with small amounts of oil, while the separate test on the KT-1 yielded water. In well 303 a workover is being evaluated to isolate intervals and test separately to identify which perforations are producing water.

The Company has initiated the development process for East Zhagabulak. Caspian has made initial contacts with Kazakhstan design institutes for the preparation of the development program report for the development of the East Zhagabulak field.

Modifications to our pilot processing plant in Zhagabulak were made to increase its throughput and to improve its reliability and safety. These modifications were completed in August 2006.

Baktygaryn

The Baktygaryn Area is located in the northwestern corner of the North Block. The Government of Kazakhstan has estimated that this Area contains 863 million barrels of oil in place with 259 million barrels classified as recoverable. These Kazakh estimates were based upon the results of Soviet era 2-D seismic data and stratigraphic test wells. Caspian neither accepts nor denies these estimates, but expects to validate this data through its exploration program.

In September 2005, Azimut Energy Services began seismic acquisition work in the Baktygaryn Area. The acquisition program of 235 square kilometres of 3-D seismic data was completed during November 2005 and the data transferred to PGS-GIS in Almaty for processing.

The data was fully processed through Pre-Stack Time Migration for the above salt section and through Pre-Stack Depth Migration for the below salt section and full interpretation of this data was completed by the end of October 2006. The acquisition of the regional 2-D seismic survey covering the west and north areas of the North Block and tying into the Zhagabulak and Baktygaryn 3-D seismic surveys that was completed in March 2006 has been processed and interpreted. The interpreted data from all new seismic data acquired and from the earlier reprocessed Soviet-era 2-D seismic has been combined to create a geological model and identify additional leads and prospects across the North Block territory.

The Baktygaryn Area presents drilling targets in both the below salt Lower Permian and Carboniferous sections and the above salt Upper Permian and Mesozoic sections with depths ranging from approximately 400 to 2,500 metres and provides a second tier of exploration to the Company's drilling portfolio. These targets are recognized in the forms of channel sands, traps against the Kungurian salt ridges and underneath salt overhangs.

Interpretation work on the Baktygaryn 3-D and North Block regional 2-D seismic data identified several post-salt drilling targets in the Triassic and Permian formations. Four of these targets have been permitted and locations prepared. Problems with rig preparation have delayed drilling, however, the first of these wells, located in the Baktygaryn area, spud on March 20, 2008, and will target both the Triassic and Upper Permian clastics in structures related to a salt diaper, with a total depth of 2,500 meters.

The remaining permitted locations will be drilled on schedule as the rig is released from each well. The identified locations are located in two areas in the western portion of the North Block, known as Aransay and West Kozdesay. Ongoing interpretation of the seismic data is creating a growing list of other drillable prospects and leads.

Itisay, Kozdesay and West Kozdesay

These three Areas are located in the southwestern portion of the North Block and collectively, are viewed as one prospect. The Government of Kazakhstan has estimated that these Areas contain 567 million barrels oil in place and 170 million barrels recoverable. These Kazakh estimates were based upon the results of Soviet era 2-D seismic data and stratigraphic test wells. Caspian neither accepts nor denies these estimates, but expects to validate this data through its exploration program.

Soviet-era seismic data interpretation, mapping and the associated shallow well drilling in these Areas yielded minor positive tests and shows of oil associated with the post-salt sediments of Jurassic, Triassic and Upper Permian ages. A review of this data has resulted in the identification of several prospects and leads ranging from 600 to 1,800 metres in trapping positions against Permian salt ridges and under-salt overhangs. Several lines from the Company's 2006 2-D seismic program were shot across certain of these leads and prospects to verify this premise. Interpretation of most of the regional 2006 2-D seismic survey covering the west and north areas of the North Block has been completed. The interpreted data from all new seismic data acquired and from the earlier reprocessed Soviet-era 2-D seismic was combined to create a geological model and identify additional leads and prospects across the North Block territory. As a result of this work, some of the earlier leads and prospects in the post-salt sediments identified on vintage maps and seismic in three areas in the south western portion of the North Block, known as Itisay, Kozdesay and West Kozdesay have been confirmed and in addition several new leads and drillable prospects have been identified in trapping positions against Permian salt ridges and under salt overhangs. Drilling for these targets is expected to begin in 2008.

Future seismic activity includes a third 3-D seismic acquisition, pending the results of the upcoming drilling campaign and further ongoing 2-D seismic interpretation.

Other Areas Within The North Block

Following are some of the other exploration areas within the North Block and their reserve estimates as put forth by the Government of Kazakhstan. Again, Caspian neither accepts nor denies these estimates, but expects to validate this data through its exploration program: Tashir – 126 million barrels oil in place and 38 million barrels recoverable, Bulash – 116 million and 35 million, respectively, and Shegelshy – 90 million and 31 million, respectively. The grand totals estimated by the Kazakh Government for all prospects in the North Block are 899 million barrels oil in place and 274 million barrels oil recoverable.

Beginning in the fourth quarter of calendar 2004, the Company undertook to reprocess and interpret approximately 3,000 kilometres of Soviet age 2-D seismic data in other areas of the original concession. From this effort the Company identified the Baktygaryn Area for acquiring additional 3-D seismic.

During March 2005, Aral was awarded the exploration rights over an additional 1,110 square kilometre area adjacent to the north and west portions of the North Block. This new territory contains additional seismic and well data and efforts to identify that data for incorporation into the electronic database have begun. Evaluation of the North Block extension, the preliminary identification of potential drilling areas and plans on how to explore are in process.

Digitization and calibration of the existing Soviet age well log data across the entire North Block territory for those wells penetrating into the formations below the Permian salt complex have been completed and petrophysical analysis of these wells commenced during December 2005 and continues to present.

Annual Analysis

Period	Jan. 1– Dec. 31 2007	Jan. 1– Dec. 31 2006	Feb. 1– Dec. 31 2005
Sales volumes			
Oil and gas (boe/day)	**414**	291	329
Average selling price (US$/boe)	**41.52**	34.14	20.86
Revenues ($000s)	**6,567**	5,423	3,674
Cash flow ($000s)	**(8,562)**	442	(1,506)
Per share – basic	**(0.08)**	0.00	(0.02)
Per share – diluted	**(0.07)**	0.00	(0.02)
Net and comprehensive loss ($000s)	**(13,209)**	(6,438)	(8,408)
Per share – basic & diluted	**(0.13)**	(0.07)	(0.10)
Capital expenditures ($000s)	**8,991**	52,155	27,868
Total assets ($000s)	**133,123**	139,104	80,377
Total indebtedness ($000s)	**17,669**	18,683	–

Summary of Selected Quarterly Financial Results [$]

Period	1Q-06	2Q-06	3Q-06	4Q-06	1Q-07	2Q-07	3Q-07	4Q-07
Oil and gas revenues	751,911	1,358,550	1,421,381	664,396	357,997	1,889,400	2,074,923	**1,946,798**
Operating and transportation	280,216	343,981	412,875	1,678,027	394,838	717,081	779,677	**759,658**
Operating income	471,695	1,014,569	1,008,506	(1,013,631)	(36,841)	1,172,319	1,295,246	**1,187,140**
Interest and other, net	105,308	489,540	418,131	213,312	196,092	1,454,585	980,996	**(2,333,920)**
General & administrative	687,371	731,052	830,002	1,025,985	604,320	984,878	866,105	**1,128,982**
Realized Foreign exchange loss (gain)	276,498	(1,150,430)	999,494	(1,133,198)	(92,329)	1,021,691	325,822	**7,638,484**
Cash flow	(386,866)	1,923,487	(402,859)	(729,403)	(352,740)	620,335	1,084,315	**(9,914,246)**
Interest charged on debentures	–	602,823	449,324	470,387	457,383	468,409	461,454	**384,395**
Depletion, depreciation & accretion (debentures)	80,302	129,060	137,632	2,199,984	137,662	838,668	649,858	**1,184,542**
Stock-based compensation	305,689	305,689	1,182,872	590,651	595,914	1,877,803	217,906	**(254,584)**
Unrealized Foreign exchange (gain) loss	(378,134)	447,866	(158,997)	(283,326)	(169,974)	2,324,801	1,289,389	**(6,557,452)**
Gain on disposal	–	–	–	(83,332)	–	–	–	**–**
Future income taxes (recovery)	–	1,408,619	(500,612)	(604,431)	–	448,569	215,186	**76,423**
Net and comprehensive loss	(397,309)	(974,273)	(1,514,083)	(3,596,534)	(1,373,725)	(5,337,915)	(1,749,478)	**(4,747,570)**
Net and comprehensive loss per share – basic and diluted	(0.01)	(0.01)	(0.01)	(0.04)	(0.01)	(0.05)	(0.02)	**(0.05)**

Until the beginning of the first quarter of calendar 2006, Caspian had a temporary 100% beneficial interest in the producing well (EZ#213) of Aral until such time as Caspian Ltd.'s indirect ownership of 50% of the Exploration Contract (excluding well EZ#213) had proved developed reserves of at least $3,000,000 (before income tax, discounted cash flow @ 20%, constant dollar pricing). Subsequent to December 31, 2005, concurrent with the inclusion of well EZ#301 in the Company's reserve study, this threshold was reached and the 100% beneficial ownership reverted to a 50% indirect interest. Both wells in East Zhagabulak (#213 and #301) were producing during the second and third quarters of 2006. During November 2006, the scheduled workover for acidization on 213 began. Difficulties in acquiring a workover rig and acid equipment for the job due to a high level of industry activity were experienced, so that work was not completed until late December 2006. Subsequently, an operation to swab the well to recover the spent acid water resulted in re-establishing the flow during January 2007. Also, during November 2006, well 301 was due for its quarterly "pressure and flow" testing as per local regulation, but while running a PLT (production logging tool) on wireline, the line broke and the tool was lost and then, recovered during 2Q 07. The average production rate for the first quarter 2007 was 362 Bopd (181 Bopd, net) and the March 2007 rate was 435 Bopd (218 Bopd, net). During 2Q 07, the gross production rates, were April – 902 Bopd, May – 1,383 Bopd and June – 1,375 Bopd, while corresponding sales rates were 150, 895 and 1,747 Bopd, respectively. During 3Q 07, the gross production rates, were July – 1311 Bopd, August – 1,196 Bopd and September – 1,179 Bopd, while corresponding sales rates were 1,226, 979 and 1,010 Bopd, respectively. During 4Q 07, the gross production rates, were October – 1,021 Bopd, November – 1,027 Bopd and December – 1,012 Bopd, while corresponding sales rates were 981, 1,013 and 979 Bopd, respectively. Net rates are 50% of the gross rates.

Interest and other, net has decreased due to the consumption of cash by the Company's exploration program and the elimination upon consolidation of 100% of the interest expense charged to Aral pursuant to the Credit Agreement, executed between Caspian and Aral concerning the funds advanced to Aral by Caspian. Caspian Energy Ltd. began charging interest during 2Q 07 on the advance and eliminated the cumulative amount during the fourth quarter. Interest expense on the convertible debentures of $384,395 was accrued during the fourth quarter. Depletion, depreciation and accretion expense includes $159,992 relating to the accretion of the discount on the convertible debentures. Stock-based compensation expense was reduced by $254,584 due to compilation errors. The Canadian dollar continues to fluctuate versus the British Pound Sterling and the US dollar, resulting in foreign exchange gains and/or losses.

CONTRACTUAL OBLIGATIONS

In accordance with the shareholders' agreement in respect of Aral, Caspian was obligated to fund the initial work program of Aral pursuant to the Exploration Contract.

The minimum work program was US$20.8 million and matured at the end of calendar 2005. As at December 31, 2005, this financial obligation was fully discharged. The work program was extended to December 2007 and included drilling three wells to a combined total of 8,500 metres with a monetary obligation of US$20.6 million. No additional seismic is required. The Company's calendar 2006 minimum work program with the ROK was approved for US$12.2 million and was discharged during the first quarter 2006. During the third quarter of this fiscal year, the work program was extended to December 2009 and contains an exploration commitment which aggregates US$19.0 million. As at December 31, 2007, Aral had incurred US$119.7 million in charges related to the work commitments of the Minimum Working Program agreed with the ROK competent bodies. Shortfalls pursuant to the Work Commitments aggregated US$7.1 million. Management of Aral believes the Company is in compliance with its commitments under the Minimum Working Program and has received authorization from the Ministry of Energy and Natural Resources and other competent bodies to carry over fulfillment of the above shortfalls to the year ending December 31, 2008.

Year	USD (millions)
2008	15.6
2009	10.5
Total contractual obligations	26.1

CASH PROVIDED BY (USED IN) OPERATIONS AND NET LOSS AND COMPREHENSIVE LOSS FOR THE YEAR

Cash Provided by (Used in) Operations

Caspian's operations used $8,562,336 of cash for the year ended December 31, 2007 and provided $442,173 of cash for the year ended December 31, 2006. The large decrease in cash flow over the 2006 fiscal year is attributable to realized foreign exchange losses of 8,893,668.

[$]	Year-ended Dec. 31, 07	Year-ended Dec. 31, 06
Cash provided by (used in) operations	**(8,562,336)**	442,173
Basic	**(0.08)**	0.00
Diluted	**(0.07)**	0.00

Net Loss and Comprehensive Loss

For 2007, net loss and comprehensive loss was $13,208,688 (2006 – $6,437,812). Stock-based compensation charges for 2007, a non-cash item equal to $2,437,039 (2006 – $2,384,901), and foreign exchange losses of $5,780,432 (2006 – a gain of $813,575) together with accrued interest of $1,771,641 (2006 – $1,522,534) on the convertible debentures contribute to the loss – the remaining components being primarily operating costs and general and administrative expenses.

[$]	Year-ended Dec. 31, 07	Year-ended Dec. 31, 06
Net and comprehensive loss	**13,208,688**	6,437,812
Basic	**0.13**	0.07
Diluted	**0.13**	0.07

Sales Volumes

Presently, our oil is shipped by rail to Kaliningrad, due to its inability to meet pipeline specifications, a consequence of the lack of facilities that can desalt our feedstock and remove the mercaptans. The Company sold an average 411 Bopd (2006 – 288 Bopd) at a price of $41.48 (2006 – $39.49), per barrel, net of ROK takes, during the year ended December 31, 2007.

Under the Exploration Contract, Aral is required to pay royalties at a rate of 3% of the volume of hydrocarbons produced and sold based upon the average selling price (less transportation expenses) of the production. Aral is also obligated to allocate 10% of produced hydrocarbons to the ROK. The government is paid in cash (rather than in kind) after the production has been sold.

Gas sales from Caspian's Canadian non-operated production totaled $49,184 (2006 – $48,752) or $46.43 per Boe (2006 – $48.76 per Boe) and contributed an average 2.9 Boepd during the year ended December 31, 2007. The production rate was 2.9 Boepd for the 2006 fiscal period.

Revenues

For 2007, revenues before transportation costs were $6,269,118. For 2006, revenues before transportation costs were $4,196,238. During 2007, not only did the average production rate increase from 291 Bopd in 2006 to 414 Bopd, but the average price per barrel increased from $34.14 to $41.52, due to the impact of international oil markets.

Interest has decreased due to the consumption of cash by the Company's exploration program and the elimination upon consolidation of 100% of the interest expense charged to Aral pursuant to the Credit Agreement, executed between Caspian and Aral concerning the funds advanced to Aral by Caspian. Caspian Energy Ltd. began charging interest during 2Q 07 on the advance and eliminated the cumulative amount during the fourth quarter upon consolidating Aral with Caspian Energy Ltd. Interest of $282,139 (2006 – $1,216,890) was earned from the short-term investment of the Company's cash reserves. None of the Company's cash reserves is invested in Asset Backed Commercial Paper (ABCP).

Operating Expenses

For 2007, operating costs were $2,163,997 (2006 – $2,509,396) and transportation costs were $487,257 (2006 – $205,704). Operating costs aggregated $14.31 (2006 – $17.13) per barrel. Approximately $1.2 million, included in operating expenses, was expended on well workovers during 2006. Transportation costs were $3.22 (2006 – $1.40) per barrel and increased dramatically from 2006 as our oil is no longer sold at the lease line.

Operating Netbacks

Operating netback for the year ended December 31, 2007 was $3,617,864.

[$]	Total	Per Boe
Sales, net	**6,269,118**	**41.46**
Operating costs	**2,163,997**	**14.31**
Transportation	**487,257**	**3.22**
Netback	**3,617,864**	**23.93**

Operating netback for the year-ended December 31, 2006 was $1,481,138.

[$]	Total	Per Boe
Sales, net	4,196,238	28.64
Operating costs	2,509,396	17.13
Transportation	205,704	1.40
Netback	1,481,138	10.11

General and Administrative Expenses

[$]	2007	2006
Office expenses	**98,533**	109,419
Travel and entertainment	**379,601**	333,270
Salaries/benefits	**1,182,370**	1,051,864
Professional fees	**577,284**	679,428
Capital taxes/interest	**19,617**	35,220
Public listing	**568,429**	379,456
Aral	**673,451**	596,053
Insurance	**85,000**	89,700
Total expense	**3,584,285**	3,274,410

Significant travel expenses are incurred as the operations of the Company are centered in the ROK, a Calgary, Alberta office is maintained for financial reporting and investor relations, the CEO is resident in Portugal, the COO is an American citizen and financing activities span North America, the British Isles, Asia and Europe. Salaries and benefits relate to the remuneration packages of the Chief Executive Officer, Chief Operating Officer and the Chief Financial Officer, while professional fees are legal, audit, taxation and engineering services. Administrative expenses of $673,451 for the period ending December 31, 2007 and $596,053 for the period ending December 31, 2006 relating to Aral operations have been included upon consolidation. During the fiscal year, Caspian segregated the duties of its Nominated Advisor (NOMAD) and Broker of Record on the LSE which has resulted in the large increase in the Public listing category of expense.

CAPITAL EXPENDITURES

Capital expenditures of $8,991,257 for 2007 (2006 – $52,154,798) were incurred. Capital expenditures are composed of advances to Aral and the expenditure of funds by Aral.

Since capital expenditures are composed of advances to Aral and the expenditure of funds by Aral, whose carrying value is denominated in US dollars, the CAD:USD exchange rate has also served to reduce the application of funds to this category of assets.

DEPLETION, DEPRECIATION AND ACCRETION

Depletion, depreciation and accretion expense was $2,411,418 ($15.95 per Boe) for the year ended December 31, 2007 and $2,265,810 ($21.32 per Boe) for the year ended December 31, 2006. The per Boe decrease in this expense is due an increase in the volume of proven reserves assigned to the Company by its independent reservoir engineers. The majority of the Company's property, plant and equipment is in the pre-development stage.

LIQUIDITY AND CAPITAL RESOURCES

The Company operates within several parameters affecting its liquidity and capital resources:

- **Its business is capital intensive, requiring cash infusions on a regular basis as it seeks to grow its business.**
- **Its inventory of product for sale – its reserves – needs to be constantly replenished and augmented.**
- **It is a price taker when selling its inventory of oil and natural gas reserves.**

Given these constraints, Caspian finances its operations through equity sources and cash flows.

Caspian's working capital at December 31, 2007 was $4.6 million.

Dramatic growth, enhanced by the acquisition of 50% of the shares of Aral is projected for the future of Caspian. Aral has operated in Kazakhstan since December 2002 and has assembled a team of both Kazakh and international executives who have extensive experience in the Kazakh operating and regulatory environment. See "Business of the Company".

The Company expects to be able to fund its capital expenditure program to the end of 2008 using cash flow from operations, working capital and, to the extent required or desirable, through funds raised in the capital markets.

On March 1, 2006, Caspian announced the closing of a private placement of U.S. $16 million principal amount, 10% interest rate, convertible debentures which mature on March 2, 2011.

On April 5, 2006, Caspian announced that it had closed an underwritten private placement to issue 19,609,000 common shares at a price of $2.55 per share for total gross proceeds of $50 million. Also, on this date, 50,000 common shares stock options at $1.75 per share were exercised resulting in proceeds of $87,500.

Caspian must rely on access to debt and capital markets to supplement internally generated cash flow to fund its capital commitments and to finance its growth plans. There can be no assurance that Caspian will be successful in obtaining the funds required to meet its capital needs on a timely basis or, if successful, that the terms will be advantageous to Caspian.

The Company reported a net loss of $13,208,688 and a cash flow deficiency of $8,562,336 for the year ended December 31, 2007. There is doubt regarding the Company's ability to continue as a going concern as it is dependent upon the ability to raise capital and the success of its exploration and development program. Plans to address this circumstance include a potential rights offering. There can be no assurance that the Company will be successful with these initiatives.

OUTSTANDING SHARE DATA

At March 28, 2008, the number of common shares of the Company outstanding and the number of common shares issuable pursuant to other securities of the Company outstanding are as follows:

Common Shares	Number
Outstanding	104,343,263
Issuable under options	13,328,777
Issuable under warrants	588,270
Issuable pursuant to convertible debentures	6,413,127
Issuable pursuant to debentures interest	4,095,528

BUSINESS PROSPECTS AND OUTLOOK

The Company has been successful in establishing itself as an operating entity in the ROK and expects to continue with future growth through continued work there.

Prior to the end of the fourth quarter 2005, EZ#301 was drilled to a total depth of 4,846 metres and logged. The well was completed with the drilling rig before the rig was moved to the EZ#302 location. EZ#301 was matrix acidized and the two potentially productive hydrocarbon bearing zones were flow-tested. The lower zone (KT-2) was tested at 2,532 Bopd. The upper zone (KT-1) had difficulty maintaining an independent flow, so it was commingled with the lower zone and the well was tied-in to the Zhagabulak production facility. Subsequently, productions logs were ran and it was determined that the KT-1 was producing 100 Bopd. Well 301 was undergoing a government mandated pressure survey in November 2006, when a production logging tool and cable were lost in the hole. During the second quarter, the tool and wire were recovered and the well has resumed production. Well 301 is currently producing 588 BOPD, 14 BWPD, 837 MCFD with a FTP (flowing tubing pressure) of 382 psig and a shut in casing pressure of 1,838 psig on a 12 mm choke. A pressure buildup was successfully completed in August 2007 and a xylene cleanout was pumped in November 2007 to clean out the suspected asphaltene buildup in the production tubing.

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The third location, EZ#303 is about 5.2 km southwest of EZ#302. EZ#303 spud on May 28, 2006. The well was permitted to a depth of 5,700 metres. EZ#303 reached a total depth of 4,630 metres in a sidetrack wellbore after the initial wellbore reached a depth of 5,430 metres, but was lost due to a drill string parting, while pulling out of the hole for logging. A total of 70 meters were perforated and acidized in both the KT-1 and KT-2 intervals. A combined test of both intervals yielded water with small amounts of oil, while the separate test on the KT-1 yielded water. In well 303 a workover is being evaluated to isolate intervals and test separately to identify which perforations are producing water.

The original producing well, EZ#213, drilled and completed during the Soviet period, was re-entered in November 2006 and perforations were added in the KT-1 reservoir. Due to different casing weights, problems were encountered with packer setting for the acid operation and consequently, only one-half of the productive zones were acidized. Despite the limits on the acidization, a significant improvement of daily production over the pre-workover rates was achieved. Well 213 is currently producing 300 BOPD, 43 BWPD, 428 MCFD with a flowing tubing pressure of 375 psig and a shut-in casing pressure of 1,705 psig on an 8.7 mm choke. A production survey to determine the reservoir pressures and production contribution from the KT-1 and KT-2 intervals was completed during October 2007 that showed approximately 30 BOPD from the KT-1 with the remaining production from the KT-2.

The Company has initiated the development process for East Zhagabulak. Caspian has made initial contacts with Kazakhstan design institutes for the preparation of the development program report for the development of the East Zhagabulak field.

Ongoing petrophysical analyses of all wells penetrating the below salt reservoirs is being completed and correlations of these wells will aid in the identification of future drilling locations in the North Block. Identification and acquisition of well data within the extended territory is also be evaluated for inclusion into this process.

The Baktygaryn 3-D seismic program was completed in early November 2005. PGS-GIS, in Almaty, ROK was awarded the processing contract. Due to the presence of large salt bodies in the Baktygaryn Area, the 3-D data set was processed through PSDM (Pre-Stack Depth Migration) and interpretation of this data has been completed. PSTM (Pre-Stack Time Migration) analysis, for the above salt section has also been conducted. The acquisition of the 367 kilometre regional 2-D seismic survey covering the west and north areas of the North Block and tying into the Zhagabulak and Baktygaryn 3-D seismic surveys that was completed in March 2007 has also been processed and interpreted. The Baktygaryn 3-D program and the regional 2-D program were fully interpreted at the end of October 2006. The interpreted data from all new seismic data acquired and from the earlier reprocessed Soviet-era 2-D seismic is being combined to create a geological model and identify additional leads and prospects across the North Block territory.

The Baktygaryn Area presents drilling targets in both the below salt Lower Permian and Carboniferous sections and the above salt Upper Permian and Mesozoic sections with depths ranging from approximately 400 to 2,500 metres and provides a second tier of exploration to the Company's drilling portfolio. These targets are recognized in the forms of channel sands, traps against the Kungurian salt ridges and underneath salt overhangs.

Interpretation work on the Baktygaryn 3-D and North Block regional 2-D seismic data identified several post-salt drilling targets in the Triassic and Permian formations. Four of these targets have been permitted and locations prepared. Problems with rig preparation have delayed drilling, however, the first of these wells, located in the Baktygaryn area, spud on March 20, 2008, and will target both the Triassic and Upper Permian clastics in structures related to a salt diaper, with a total depth of 2,500 meters.

The remaining permitted locations will be drilled on schedule as the rig is released from each well. The identified locations are located in two areas in the western portion of the North Block, known as Aransay and West Kozdesay. Ongoing interpretation of the seismic data is creating a growing list of other drillable prospects and leads.

Soviet-era seismic data interpretation, mapping and the associated shallow well drilling in the Itisay, Kozdesay and West Kozdesay areas, located in the southwestern portion of the North Block, yielded minor positive tests and shows of oil associated with the post-salt sediments of Jurassic, Triassic and Upper Permian ages. A review of this data has resulted in the identification of several

prospects and leads ranging from 600 to 1,800 metres in trapping positions against Permian salt ridges and under-salt overhangs. Several lines from the Company's 2006 2-D seismic program were shot across certain of these leads and prospects to verify this premise. Interpretation of most of the regional 2006 2-D seismic survey covering the west and north areas of the North Block has been completed. The interpreted data from all new seismic data acquired and from the earlier reprocessed Soviet-era 2-D seismic was combined to create a geological model and identify additional leads and prospects across the North Block territory. As a result of this work, some of the earlier leads and prospects in the post-salt sediments identified on vintage maps and seismic in three areas in the south western portion of the North Block, known as Itisay, Kozdesay and West Kozdesay have been confirmed and in addition several new leads and drillable prospects have been identified in trapping positions against Permian salt ridges and under salt overhangs. Drilling for these targets is expected to begin in 2008.

Future seismic activity includes a third 3-D seismic acquisition, pending the results of the upcoming drilling campaign and further ongoing 2-D seismic interpretation.

The relatively shallow post salt targets at Baktygaryn offer a completely new series of opportunities for the Company. The 3-D and 2-D seismic data have enabled several new prospects to be identified and the Company is now in the process of selecting additional drilling locations.

Following the release of the rig from well #703, the first exploration well located in Baktygaryn, the Company intends to move drilling efforts to the eastern side of the Baktygaryn, West Kozdesay, and Aransay areas in the western part of the North Block where it will drill for Triassic and Upper Permian targets ranging from 700 to 1,400 metres. The Company is awaiting the outcome of permitting constraints and current weather conditions before it confirms the precise location of the second well.

The Company's work program extension, with the ROK, to December 2007 has now been extended for an additional two-year period, subject to the terms of the original exploration contract. The 2008 work program commits the Company to undertake US$8.6 million of exploration expenditures prior to the close of that calendar year and the 2009 work program – US$10.5 million of exploration expenditures. Additionally, during 2008, Aral is obligated to make-up an additional US$ 7.1 million in cumulative shortfalls under the contract.

ADDITIONAL DISCLOSURES

Critical Accounting Estimates

In the preparation of the financial statements, it was necessary for Caspian to make certain estimates that were critical to determining our assets, liabilities and net income. None of these estimates affect the determination of cash flow but do have a significant impact in the determination of net income. The most critical of these estimates is the reserves estimations and the resulting effect on various income statement and balance sheet measures.

Caspian engaged an independent engineering firm to evaluate 100% of our oil and natural gas reserves and prepare a report thereon. Their report was utilized in: a) the calculations of depletion and depreciation expense, b) the application of the ceiling test, and c) the calculation of asset retirement obligations. The estimation of the reserve volumes and future net revenues set out in the report is complex and subject to uncertainties and interpretations. Judgments are based upon engineering data, projected future rates of production, forecasts of commodity prices, and the timing of future expenditures. Inevitably the estimates of reserve volumes and future net revenues will vary over time as new data becomes available and estimates of future net revenues do not represent fair market value. The impact of such revisions in 2007 was not significant.

The significant accounting policies used by the Company are disclosed in the notes to the Company's audited consolidated financial statements. Certain accounting policies require that management make appropriate decisions with respect to the formulation of estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. The following discussion outlines such accounting policies and is included in this MD&A to aid the reader in assessing the critical accounting policies and practices of the Company and the likelihood of materially different results being reported. The Company's management reviews its estimates regularly.

The following significant accounting policies outline the major policies involving critical estimates.

Proved Oil and Gas Reserves

Proved reserves are those reserves that can be estimated with a high degree of certainty to be recoverable. It is likely that the actual remaining quantities recovered will exceed the estimated proved reserves. The estimated quantities of proved crude oil, natural gas liquids and natural gas are derived from geological and engineering data that demonstrate with reasonable certainty the amounts that can be recovered in future years from known reservoirs under existing economic and operating conditions. Reserves are considered proved if they can be produced economically as demonstrated by either actual production or conclusive formation tests. The oil and gas reserve estimates are made using all available geological and reservoir data as well as historical production data. Estimates are reviewed and revised as appropriate. Revisions occur as a result of changes in prices, costs, fiscal regimes, reservoir performance or a change in the Company's plans.

Depletion Expense

The Company uses the full cost method of accounting for exploration and development activities. In accordance with this method of accounting, all costs associated with exploration and development are capitalized whether successful or not. The aggregate of net capitalized costs and estimated future development costs less estimated salvage values is amortized using the unit-of-production method based upon proved oil and gas reserves. An increase in estimated proved oil and gas reserves would result in a corresponding reduction in depletion expense. A decrease in estimated future development costs would result in a corresponding reduction in depletion expense.

Withheld Costs

Certain costs related to unproved properties may be excluded from costs subject to depletion until proved reserves have been determined or their value is impaired. These properties are reviewed quarterly and any impairment is transferred to the costs being depleted.

Impairment of Long Lived Assets

The Company is required to review the carrying value of all property, plant and equipment, including the carrying value of oil and gas assets, for potential impairment.

The carrying value of the Company's petroleum and natural gas properties must not exceed their fair value. The fair value is equal to the estimated future cash flows from proved and probable reserves using future price forecasts and costs discounted at a risk-free rate. If impairment is indicated, the amount by which the carrying value exceeds the estimated fair value of the long lived asset is charged to income.

Asset Retirement Obligations

Asset retirement obligations are initially measured at fair value when they are incurred, which is the discounted future value of the estimated liability. This requires an estimate to be made of the future costs of retiring the asset at the point in time the asset is acquired.

Changes in Accounting Policies

Comprehensive Income

This standard introduces a new "Statement of comprehensive income" and establishes accumulated other comprehensive income as a separate component of shareholders' equity. Comprehensive income is defined as the change in equity from transactions and other events from non-owner sources and includes all changes in equity during a period except those resulting from investments

by owners and distributions to owners. Other comprehensive income comprises revenues, expenses, gains and losses that, in accordance with GAAP, are recognised in comprehensive income but excluded from net income. Amounts included in accumulated other comprehensive income are reclassified to net income when realised.

Financial Instruments

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

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

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

Credit Risk Management

We are exposed to credit risk on our commodity contracts due to the potential for non-performance by the counter parties. We mitigate this risk by only dealing with well established marketing companies.

Fair Value Measurement

The carrying values of cash, cash equivalents, accounts receivable, accounts payable and accrued liabilities approximate their fair values due to their short term to maturity.

Related Party Transactions

There were no related party transactions during the period.

Critical Accounting Disclosure

As at the year ended December 31, 2007, an evaluation was carried out under the supervision of and with the participation of the Company's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the design and operation of these disclosure controls and procedures were effective as at December, 2007, to provide reasonable assurance that material information relating to the Company would be made known to them by others within the Company.

As at the financial year ended December 31, 2007, the Chief Executive Officer and Chief Financial Officer evaluated the design of the Company's internal control over financial reporting. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the design of internal control over financial reporting was effective as at December 31, 2007 to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP.

Consolidated Financial Statements

December 31, 2007 and 2006

Consolidated Financial Statements

December 31, 2007 and 2006

MANAGEMENT'S REPORT TO THE SHAREHOLDERS

Management is responsible for the preparation of the financial statements and for the consistency of all other financial and operating data presented in this annual report. Management maintains a system of internal controls to provide reasonable assurance that all assets are safeguarded and to facilitate the preparation of relevant, reliable and timely financial information.

PricewaterhouseCoopers LLP, Chartered Accountants, appointed by the shareholders, has audited the financial statements. The Audit Committee has reviewed the financial statements with management and the auditors and has reported to the Board of Directors. The Board of Directors has subsequently approved the financial statements.

William A. G. Ramsey
Chief Executive Officer
March 28, 2008

Brian D. Korney
Vice-President, Finance,
Chief Financial Officer and Secretary
March 28, 2008

AUDITORS' REPORT

We have audited the consolidated balance sheets of Caspian Energy Inc. (the "Company") as at December 31, 2007 and 2006 and the consolidated statements of loss, comprehensive loss and deficit and cash flows for the each of the years in the two year period ended December 31, 2007. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2007 and 2006 and the results of its operations and its cash flows for each of the years in the two year period ended December 31, 2007 in accordance with Canadian generally accepted accounting principles.

Chartered Accountants, Calgary
March 28, 2008

Consolidated Balance Sheets

As at December 31, 2007 and 2006

[$]	2007	2006
ASSETS		
Current Assets		
Cash and cash equivalents	**4,373,919**	17,022,285
Accounts receivable	**935,773**	672,879
Prepaids and other deposits	**2,310,302**	2,713,994
Inventory (note 3)	**454,302**	177,055
	8,074,296	20,586,213
Restricted cash (note 5)	**253,132**	194,412
Property, plant and equipment (note 4)	**124,795,793**	118,323,038
	133,123,221	139,103,663
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities	**3,458,427**	5,305,085
Asset retirement obligation (note 5)	**252,279**	156,255
Loan payable (note 6)	**6,947,055**	–
Future income taxes (note 8)	**967,400**	358,848
Convertible debentures (note 7)	**17,669,238**	18,683,004
	29,294,399	24,503,192
SHAREHOLDERS' EQUITY		
Share capital (note 9)	**121,470,892**	121,470,892
Warrants to purchase common shares (note 9)	**946,508**	946,508
Contributed surplus (note 11)	**14,467,311**	12,030,272
Deficit	**(33,055,889)**	(19,847,201)
	103,828,822	114,600,471
	133,123,221	139,103,663

Going concern (note 1)

See accompanying notes to consolidated financial statements.

Approved by the Board of Directors

(signed) "Gord Harris"
Director

(signed) "William Ramsay"
Director

Consolidated Statements of Loss, Comprehensive Loss and Deficit

For the years ended December 31, 2007 and 2006

[$]	2007	2006
REVENUE		
Oil and gas revenue, net	**6,269,118**	4,196,238
Interest	**282,139**	1,216,890
Other	**15,614**	9,401
	6,566,871	5,422,529
EXPENSES		
General and administrative	**3,584,285**	3,274,410
Accretion of convertible debentures (note 7)	**393,312**	281,168
Interest (note 7)	**1,777,641**	1,532,103
Operating	**2,163,997**	2,509,396
Transportation	**487,257**	205,704
Stock-based compensation (notes 10 and 11)	**2,437,039**	2,384,901
Foreign exchange loss (gain)	**5,780,432**	(813,575)
Depletion, depreciation and accretion	**2,411,418**	2,265,810
Gain on disposal of mining interest (note 14)	**–**	(83,332)
	19,035,381	11,556,585
Loss before income taxes	**(12,468,510)**	(6,134,056)
Future income taxes	**740,178**	303,756
Net loss and comprehensive loss for the year	**(13,208,688)**	(6,437,812)
Deficit – Beginning of year	**(19,847,201)**	(13,409,389)
Deficit – End of year	**(33,055,889)**	(19,847,201)
Basic and diluted loss per share (note 9)	**(0.13)**	(0.07)

Going concern (note 1)

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

For the years ended December 31, 2007 and 2006

[$]	2007	2006
Cash provided by (used in)		
OPERATING ACTIVITIES		
Net loss and comprehensive loss for the year	**(13,208,688)**	(6,437,812)
Items not affecting cash		
Stock-based compensation	**2,437,039**	2,384,901
Unrealized foreign exchange (gain) loss	**(3,113,236)**	194,061
Depletion, depreciation and accretion	**2,411,418**	2,265,810
Interest on convertible debentures	**1,777,641**	1,522,534
Accretion of convertible debentures	**393,312**	281,168
Future income taxes	**740,178**	303,756
Gain on disposal of mining interest	**–**	(83,332)
Loss on disposal of fixed assets	**–**	11,087
	(8,562,336)	442,173
Changes in non-cash working capital balances	**(262,893)**	(167,064)
	(8,825,229)	275,109
FINANCING ACTIVITIES		
Convertible debentures	**–**	18,240,640
Loan payable	**6,947,055**	(6,872,279)
Restricted cash	**(58,720)**	(57,528)
Issuance of common shares and warrants	**–**	50,804,650
Share issue expenses	**–**	(3,782,317)
	6,888,335	58,333,166
INVESTING ACTIVITIES		
Acquisition of property, plant and equipment	**(8,991,257)**	(52,154,798)
Proceeds on disposal of mining interest	**–**	81,219
Changes in non-cash working capital balances	**(1,720,215)**	393,503
	(10,711,472)	(51,680,076)
(Decrease) increase in cash and cash equivalents	**(12,648,366)**	6,928,199
Cash and cash equivalents – Beginning of year [1]	**17,022,285**	10,094,086
Cash and cash equivalents – End of year [1]	**4,373,919**	17,022,285
Interest received	**385,076**	1,216,890

[1] Cash and cash equivalents consist of cash and short term investments with a maturity date of less than three months.

See accompanying notes to consolidated financial statements.

1 NATURE OF OPERATIONS AND GOING CONCERN

Caspian Energy Inc. ("Caspian" or the "Company") is engaged in the exploration for and development and production of oil and gas in the Republic of Kazakhstan. Its primary operating activities are carried out through its wholly-owned subsidiary, Caspian Energy Ltd. ("Caspian Ltd.").

Caspian's principal assets are a 50% interest in Aral Petroleum Capital LLP ("Aral"), held by Caspian Ltd. Through its interest in Aral, Caspian has the right to explore and develop certain oil and gas properties in Kazakhstan, known as the North Block, a 3,458 square kilometre area located in the vicinity of the Kazakh pre-Caspian basin. The Company also has minor resource interests in Canada.

Aral's exploration and development rights to the North Block were granted pursuant to the terms of an exploration contract between the government of Kazakhstan and Aral (the "Exploration Contract"). The initial three-year term of the Exploration Contract was extended for a two-year period (expiring in December 2007) and a further extension of two years to December 31, 2009 with a minimum work commitment of US $19.1 million has now been placed into effect.

Under the terms of the Exploration Contract, Aral was obligated to spend at least US $20.8 million under a minimum work program in respect of the North Block during the initial three-year term of the contract. The expenditures include processing and reinterpretation of geological and geophysical data of prior years, two dimensional and three dimensional seismic shoots and surveys, drilling exploration wells, well reactivations and well surveys and testing. The minimum work program matured at the end of calendar 2005. As of December 31, 2005, Aral's financial obligation under the minimum work program had been discharged. The work program extension to December 2008 includes drilling three wells to a combined total of 8,500 metres with a monetary obligation of US $20.15 million. At December 31, 2007, Aral had contract shortfalls aggregating US $7.1 million. Management of Aral believes the Company is in compliance with its commitments under the Minimum Working Program and has received authorization from the Ministry of Energy and Natural Resources and other competent bodies to carry over fulfillment of the above shortfalls to the year ending December 31, 2008.

Under terms of a shareholders' agreement dated June 25, 2004, among Caspian Ltd., Azden Management Limited ("Azden") and Aral, Caspian was committed to fund Aral's US $20.8 million obligation under the initial work program. This financial commitment was satisfied, in full, by the Company. In addition, Caspian Ltd. has undertaken, on a best efforts basis, to raise financing of US $84.0 million to fund Aral's operations pursuant to the Exploration Contract. At March 31, 2007, Caspian Ltd. had discharged this undertaking.

Going concern

These financial statements have been prepared in accordance with Canadian generally accepted accounting policies ("GAAP") applicable to a going concern, which contemplates the realization of assets and the payment of liabilities in the ordinary course of business. Should the Company be unable to continue as a going concern, it may be unable to realize the carrying value of its assets and to meet its liabilities as they become due.

The Company reported a net loss of $13,208,688 and negative funds generated from operations of $8,825,229 for the year ended December 31, 2007. The Company had net working capital of $4,615,869. As a result, there is substantial doubt about the Company's ability to continue as a going concern. The Company's continuation is dependent upon the ability to raise capital and the success of its drilling and exploration program. The Company plans a potential rights offering, however, there can be no assurance that the Company will be successful with this offering or other initiatives it undertakes.

The accompanying financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts and classification of liabilities that might be necessary should the Company be unable to continue in existence. Such adjustments could be material.

2 SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements of Caspian are stated in Canadian dollars and have been prepared in accordance with Canadian GAAP.

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates.

Cash and cash equivalents

Cash and cash equivalents are comprised of cash and short-term investments with an initial maturity date of three months or less.

Inventory

Inventory is recorded at the lower of cost calculated using the weighted average method, and net realizable value. Cost comprises direct materials and where applicable direct labour costs and those overheads which have been incurred in bringing the inventories to their present location and condition. Net realizable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

Joint ventures

The Company's oil and gas exploration and development activities are conducted mainly in Kazakhstan through its 50% interest in Aral and, accordingly, these consolidated financial statements reflect only the Company's proportionate interest in such activities.

Property, plant and equipment

a) *Capitalized costs*

The Company follows the full cost method of accounting for oil and natural gas operations, whereby all costs related to the acquisition, exploration and development of petroleum and natural gas reserves are capitalized. Such costs include lease acquisition costs, geological and geophysical costs, carrying charges on non-producing properties, costs of drilling both productive and non-productive wells, the cost of petroleum and natural gas production equipment and overhead charges directly related to exploration and development activities. Proceeds from the sale of oil and gas properties are applied against capital costs, with no gain or loss recognized, unless such a sale would change the rate of depletion and depreciation by 20% or more, in which case, a gain or loss would be recorded.

b) *Depletion, depreciation and amortization*

The capitalized costs are depleted and depreciated using the unit-of-production method based on proven petroleum and natural gas reserves, as determined by independent consulting engineers. Oil and natural gas liquids reserves and production are converted into equivalent units of natural gas based on relative energy content on a ratio of six thousand cubic feet of gas to one barrel of oil. Significant development projects and expenditures on exploration properties are excluded from calculation of depletion prior to assessment of the existence of proved reserves.

Other property, machinery and equipment are recorded at historical cost. Depreciation is calculated on a straight-line basis at the following annual rates:

Buildings	8%
Machinery and equipment	8%
Vehicles	7%
Other fixed assets	10%

c) Ceiling test

The Company follows the Canadian accounting guideline on full cost accounting. In applying the full cost guideline, Caspian calculates its ceiling test for each cost centre by comparing the carrying value of oil and natural gas properties and production equipment to the sum of undiscounted cash flows expected to result from Caspian's proved reserves. If the carrying value is not fully recoverable, the amount of impairment is measured by comparing the carrying value of oil and gas properties and production and equipment to the estimated net present value of future cash flows from proved plus probable reserves using a risk-free interest rate and expected future prices. Any excess carrying value above the net present value of the future cash flows is recorded as a permanent impairment.

d) Unproved property

Costs of acquiring and evaluating unproven properties are initially excluded from costs subject to depletion, until it is determined whether or not proved reserves are attributable to the properties or, in the case of major development projects, commercial production has commenced, or impairment has occurred. Impairment occurs whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. When proven reserves are determined or the property is considered to be impaired, the cost of the property or the amount of the impairment is added to the costs subject to depletion for that country's cost centre.

e) Asset retirement obligation

Caspian records the fair value of asset retirement obligations ("ARO") as a liability in the period in which it incurs a legal obligation to restore an oil and gas property, typically when a well is drilled or other equipment is put in place. The associated asset retirement costs are capitalized as part of the carrying amount of the related asset and depleted using a unit-of-production method over the life of the proved reserves. Subsequent to initial measurement of the obligations, the obligations are adjusted at the end of each reporting period to reflect the passage of time and changes in estimated future cash flows underlying the obligation. Actual costs incurred on settlement of the ARO are charged against the ARO.

Income taxes

Income taxes are calculated using the liability method of tax accounting. Temporary differences arising from the difference between the tax basis of an asset or liability and its carrying value amount on the balance sheet are used to calculate future income tax assets and liabilities. Future income tax assets and liabilities are calculated using tax rates anticipated to apply in the periods that the temporary differences are expected to reverse.

Stock-based compensation

The Company grants options to purchase common shares to employees and directors under its stock option plan. Under this standard, future awards are accounted for using the fair value of accounting for stock-based compensation. Under the fair value method, an estimate of the value of the option is determined at the time of grant using a Black-Scholes option-pricing model. The fair value of the option is recognized as an expense and contributed surplus over the vesting period of the option. Proceeds received on exercise of stock options, along with amounts previously included in contributed surplus, are credited to share capital.

Revenue recognition

Revenue from the sale of oil and natural gas is recognized based on volumes delivered to customers at contractual delivery points and rates. The costs associated with the delivery, including operating and maintenance costs, transportation, and production-based royalty expenses will be recognized in the same period in which the related revenue is earned and recorded.

Measurement uncertainty

The amounts recorded for depletion and depreciation of property, plant and equipment, the provision for asset retirement obligations and the amounts used for ceiling test calculations are based on estimates of reserves and future costs. The Company's reserve estimates are reviewed annually by an independent engineering firm. The amounts disclosed relating to fair values of stock options issued are based on estimates of future volatility of the Company's share price, expected lives of options, and other relevant assumptions. By their nature, these estimates are subject to measurement uncertainty.

Loss per share

Basic per share amounts are calculated using the weighted average number of shares outstanding during the period. Diluted per share amounts are calculated based on the treasury stock method whereby the weighted average number of shares is adjusted for the dilutive effect of options. The Company applies the treasury stock method for the calculation of diluted net loss per share whereby the effect of the "in the money" instruments such as stock options and warrants affect the calculation. The treasury stock method assumes that the proceeds from the exercise are used to repurchase common shares of the Company at the weighted average market price during the year.

Financial instruments

Fair values

The fair values of accounts receivable, accounts payable and accrued liabilities, and loan payable approximate their carrying values due to their short-term maturity.

Credit risk

Substantially all of the Company's accounts receivable are due from companies in the oil and gas industry and are subject to the normal industry credit risks. The carrying value of accounts receivable reflects management's assessment of the associated credit risks.

Foreign currency

All operations are considered financially and operationally integrated. Results of operations are translated to Canadian dollars, using average rates for revenues and expenses, except depreciation which is translated at the rate of exchange applicable to the related assets. Monetary items denominated in foreign currency are translated to Canadian dollars at exchange rates in effect at the balance sheet date and non-monetary items are translated at rates of exchange in effect when the assets were acquired or obligations incurred. Foreign exchange gains and losses are recorded in the statement of loss.

Adoption of new accounting policies

On January 1, 2007, the Company adopted the Canadian Institute of Chartered Accountants (CICA) handbook Sections 1506 "Accounting Changes", 1530 "Comprehensive Income", Section 3251 "Equity", Section 3855 "Financial Instruments – Recognition and Measurement", Section 3861 "Financial Instruments – Disclosure and Presentation" and Section 3865 "Hedges".

CICA Section 1530, "Comprehensive Income" – Comprehensive income is comprised of net earnings or loss and other comprehensive income (OCI). OCI is the change in a company's net assets that results from transactions, events and circumstances from non owner sources and includes items that would not normally be included in net earnings such as unrealized gains and losses on available-for-sale investments. The Company currently does not have any OCI.

CICA Section 3251, "Equity" establishes new standards for presentation of equity and changes in equity during the period. Application of this section did not result in changes to the presentation of equity for the Company.

CICA Section 3855, "Financial Instruments – Recognition and Measurement", prescribes when a financial instrument is to be recognized on the balance sheet and at what amount. It also specifies how financial instrument gains and losses are to be presented. All financial instruments are classified into one of the following five categories: held for trading, held-to-maturity, loans and receivables, available-for-sale financial assets and other financial liabilities. Initial and subsequent measurement and recognition of changes in the value of financial instruments depends on their classification.

a) Held for trading financial instruments are measured at fair value. All gains and losses are included in net earnings in the period in which they arise.

b) Loans and receivables are accounted for at amortized cost using the effective interest method. Any gain or loss on the realization of the loans and receivables are recorded into earnings.

Future accounting changes

The CICA issued three new accounting standards: Section 1535, Capital Disclosures, Section 3862, Financial Instruments – Disclosures, and Section 3863, Financial Instruments – Presentation. These new standards will be effective for fiscal years beginning on or after October 1, 2007 and the Company will adopt them on January 1, 2008. The Company is in the process of evaluating the disclosure and presentation requirements of the new standards, however it is not anticipated that the earnings or financial position of the Company will be affected.

Section 1535 establishes disclosure requirements about an entity's capital and how it is managed. The purpose will be to enable the users of the financial statements to evaluate the entity's objectives, policies and processes for management capital.

Sections 3862 and 3863 will replace Section 3861, Financial Instruments – Disclosure and Presentation, revising and enhancing its disclosure requirements, and carrying forward unchanged its presentation requirements. These new sections will place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks.

In March 2006, the Accounting Standards Board of the CICA released its new strategic plan which proposes to abandon Canadian GAAP for public companies and effect a complete convergence to the International Financial Reporting Standards, at the end of a transitional period Canadian GAAP will cease to exist as a separate distinct basis of financial reporting for public companies. The Company will convert to these new standards according to the timetable set with these new rules. The Company will closely monitor changes arising from this convergence.

3 INVENTORY

[$]	2007	2006
Oil inventory	**187,300**	24,742
Fuel	**25,748**	3,522
Construction materials	**2,742**	4,342
Spare parts	**5,004**	3,4258
Other materials	**233,508**	141,024
	454,302	177,055

4 PROPERTY, PLANT AND EQUIPMENT

[$]	2007	2006
Petroleum and natural gas assets	**126,806,121**	118,334,595
Other assets	**3,122,928**	2,508,707
	129,929,049	120,843,302
Accumulated depletion and depreciation	**(5,133,256)**	(2,520,264)
	124,795,793	118,323,038

Excluded from the depletable base of oil and gas assets at December 31, 2007 are unproved properties of $72,049,847 (2006 – $65,707,839).

The Company applied the ceiling test to its capitalized assets at December 31, 2007 and 2006 and determined that there was no impairment of such carrying costs.

	WTI Crude oil price $US/bbl
2008	90.00
2009	86.70
2010	83.20
2011	79.60
2012	78.50

The prices increase by 2% for years thereafter.

During the year ended December 31, 2007, the Company capitalized $269,548 (2006 – $506,317) of general and administrative expenses related directly to exploration and development activities.

5 ASSET RETIREMENT OBLIGATION

The Company records the fair value of asset retirement obligations as a liability in the period in which it incurs the legal obligation.

The asset retirement obligation results from net ownership interests in petroleum and natural gas assets including well sites, gathering systems and processing facilities. The Company estimates the total undiscounted amount of cash flows required to settle its asset retirement obligations at December 31, 2007 is $261,394, which will be incurred between 2014 and 2019. A credit-adjusted risk-free rate of 16.5% was used to calculate the fair value of the asset retirement obligations, and an inflation factor of 19.0%.

A reconciliation of the asset retirement obligation is provided below:

[$]	2007	2006
Opening balance	**156,255**	88,900
Liabilities incurred	**94,490**	38,382
Accretion	**19,574**	4,760
Change in estimate	**(18,040)**	24,213
Closing balance	**252,279**	156,255

Under the terms of the Exploration Contract (note 1), the Company is required to create a fund to finance actual future restoration costs, equal to 1% of the capital costs of exploration. At December 31, 2007 and 2006, $253,132 and $194,412, respectively have been placed in a restricted bank account related to the funding requirement.

6 LOAN PAYABLE

Pursuant to the Participants Agreement By and Among Azden Management Limited and Caspian Energy Ltd. and Aral Petroleum Capital Limited Liability Partnership, subsequent to reaching the US $84 million threshold on advances by Caspian to Aral, Caspian and Azden shall jointly finance, in equal proportions, the next stages of exploration by Aral. As at December 31, 2007, $6,947,055 had been advanced by Azden to Aral and is recorded as a loan payable in Aral's accounts.

7 CONVERTIBLE DEBENTURES

On March 1, 2006, the Company received US $16 million and issued 10% per annum, convertible debentures in a like amount secured with Caspian Ltd. shares. The debentures mature on March 2, 2011 and are convertible at any time and from time to time into common shares of the Company at a conversion price of $2.45 per share. The Company may repay the principal amount of the debentures, in whole or in part, or require conversion into common shares of the Company if the volume-weighted average trading price of the common shares, for 40 consecutive trading days, is at least $4.08.

[$]	Face amount	Fair value of conversion option	Accretion	Interest	Carrying value
Debentures issued, opening balance	18,320,884	(1,483,805)	281,168	1,564,757	18,683,004
Accretion of discount	–	–	393,312	–	393,312
Translation adjustment	(2,608,884)	–	–	1,201,806	(1,407,078)
Balance – December 31, 2007	15,712,000	(1,483,805)	674,480	2,766,563	17,669,238

8 INCOME TAXES

Future income taxes reflect the net tax effects of temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for tax purposes. The Company has provided for certain taxes based upon statutory regulations of Kazakhstan. The Company is subject to permanent tax differences due to the fact that certain expenses are not deductible for income tax purposes under Kazakh laws.

The provision for taxes differs from that computed using the combined Canadian federal and provincial statutory rate as follows:

[$]	2007	2006
Loss before income taxes	**(12,468,510)**	(6,134,056)
Expected recovery at statutory tax rate of 32.10% (2006 – 34.50%)	**(4,002,392)**	(2,116,249)
Tax rate difference of foreign jurisdiction	**261,839**	291,699
Non-deductible stock-based compensation	**782,290**	822,791
Losses for which no benefit is being recognized	**3,698,441**	1,128,924
Non-deductible expenses	**–**	176,591
Future income taxes	**740,178**	303,756

The tax effects on major temporary differences that give rise to the future tax liability are as follows:

[$]	2007	2006
Future tax asset		
Tax losses available for carry forward	**307,790**	936,012
Other	**47,244**	8,562
Difference in the tax bases and carrying values of property, plant and equipment	**904,103**	143,939
	1,259,137	1,088,513
Future tax liability		
Geological and geophysical expense	**(2,226,537)**	(1,433,712)
Other	**–**	(13,649)
Net future tax liability	**(2,226,537)**	(1,447,361)
	(967,400)	(358,848)

9 SHARE CAPITAL

Authorized

Unlimited number of voting common shares, without stated par value.

Issued

	Number of shares	Amount $
Issued and outstanding as at December 31, 2005	**84,327,163**	75,220,762
Exercise of warrants [1]	**357,100**	888,505
Private placement [2]	**19,609,000**	49,056,442
Exercise of options [3]	**50,000**	87,500
Share issue costs [4]	–	(3,782,317)
Issued and outstanding as at December 31, 2007 and 2006	**104,343,263**	121,470,892

(1) During the year, 357,100 broker warrants were exercised. The warrants had an exercise price of $2.00 per common share.
(2) On April 5, 2006 a private placement of 19,609,000 common shares were issued at $2.55 per share.
(3) On April 10, 2006, 50,000 common shares at $1.75 per, were issued pursuant to the Company's stock option plan.
(4) Share issue costs have not been tax-effected.

Stock options

The Company has a stock option plan (the "Plan") under which it may grant options to directors, officers and employees for the purchase of up to 15% of the number of common shares from time to time. Options are granted at the discretion of the board of directors. The exercise price, vesting period and expiration period are also fixed at the time of grant at the discretion of the Board of Directors in accordance with terms of the Plan.

Changes to the Company's stock options are summarized as follows:

	Number of options	Weighted average option price $
Balance – December 31, 2005	9,166,499	1.72
Granted	1,943,433	1.29
Exercised	(50,000)	1.75
Balance – December 31, 2006	11,059,932	1.64
Granted	2,668,845	0.88
Expired	(400,000)	2.15
Balance – December 31, 2007	**13,328,777**	**1.47**
Exercisable – December 31, 2007	**12,895,444**	**1.48**

The following is a summary of stock options outstanding and exercisable as at December 31, 2007:

	Options outstanding			Options exercisable
Range of exercise price	Options outstanding	Weighted average remaining contractual life in years	Weighted average exercise price	Options exercisable
$0.75	2,079,090	1.7	$0.75	2,079,090
$0.86	800,000	4.1	$0.86	666,667
$0.89	1,868,845	4.3	$0.89	1,868,845
$1.25	1,043,433	3.7	$1.25	1,043,433
$1.34	900,000	4.0	$1.34	600,000
$1.61	843,271	2.5	$1.61	843,271
$1.75	1,100,000	2.5	$1.75	1,100,000
$2.00	1,050,000	2.0	$2.00	1,050,000
$2.15	3,644,138	1.7	$2.15	3,644,138
	13,328,777		$1.48	12,895,444

Per share amounts

The weighted average number of common shares outstanding during the period ended December 31, 2007 of 104,343,263 (2006 – 99,146,605 shares) was used to calculate loss per share amounts.

In computing diluted loss per share, no shares were added to the weighted average number of common shares outstanding during the year ended December 31, 2007 (2006 – nil) as they are anti-dilutive.

Warrants

588,270 broker warrants are outstanding at December 31, 2007 and all have vested. These warrants entitle the holder to purchase one common share at a price of $2.77 until April 5, 2008. The fair value of the outstanding warrants using the Black-Scholes method was $946,508 (2006 – $946,508).

10 STOCK-BASED COMPENSATION

Options granted to both employees and non-employees are accounted for using the fair value method. The fair value of common share options granted in the year ended December 31, 2007 was estimated to be $1,638,489 as at the grant date using a Black-Scholes option-pricing model and the following assumptions:

Risk free interest rate	4.11 – 4.27%
Expected life	5 year average
Expected volatility	84 – 89%
Expected dividend yield	0%

The estimated fair value of the options is amortized to expense and credited to contributed surplus over the option vesting period on a straight-line basis.

11 CONTRIBUTED SURPLUS

[$]	2007	2006
Balance – Beginning of year	**12,030,272**	7,668,133
Stock options issued to employees, officers and directors	**2,437,039**	2,384,901
Fair value of debentures conversion option	**–**	1,483,805
Fair value of warrants expired	**–**	493,433
Balance – End of year	**14,467,311**	12,030,272

The term and vesting conditions of each option may be fixed by the board when the option is granted, but the term cannot exceed 5 years from the date upon which the option is granted.

The options granted to directors, officers and employees may be exercised over five years from the date of granting and expire from time to time to April 2012.

The debentures are convertible into common shares of the Company at a price of $2.45 per share and mature on March 31, 2011.

12 COMMITMENTS

In accordance with the shareholders' agreement in respect of Aral, Caspian was obligated to fund the initial work program of Aral pursuant to the Exploration Contract. The minimum work program was US $20.8 million and matured at the end of calendar 2005. As at December 31, 2005, this obligation was fully discharged. The work program extension to December 2007 includes drilling three wells to a combined total of 8,500 metres with a monetary obligation of US $20.15 million. No additional seismic is required. The work program extension to December 2009 includes drilling seven wells to a combined total of 8,500 metres with a monetary obligation of US $19.085 million. The Company's calendar 2006 minimum work program with the Republic of Kazakhstan was approved for US $12.2 million and was discharged during 2006. The Company's calendar 2007 work program was approved for US $8.4 million with amendment for another US $23.7 million). At December 31, 2007, Aral had contract shortfalls aggregating US $7.1 million. Management of Aral believes the Company is in compliance with its commitments under the Minimum Working Program and has received authorization from the Ministry of Energy and Natural Resources and other competent bodies to carry over fulfillment of the above shortfalls to the year ending December 31, 2008.

13 FINANCIAL INSTRUMENTS

Caspian's financial instruments included in the consolidated balance sheet are comprised of cash and cash equivalents, accounts receivable, other deposits and, accounts payable. The fair values of these financial instruments approximate their carrying amounts due to the short-term nature of the instruments. A substantial portion of Caspian's accounts receivable are with customers in the oil and gas industry and are subject to normal industry credit risks.

A substantial portion of Caspian's activities are settled in foreign currencies and consequently, the Company is subject to fluctuations in currency translation rates.

The liability and equity components of the convertible debentures are presented separately in accordance with their substance. The liability component is accreted to the amount payable at maturity by way of a charge to earnings using the effective interest method.

14 DISPOSAL OF MINING INTEREST

On November 1, 2006, the Company executed a Letter of Intent to dispose of its interest in a mining property located in Noyon Township, Quebec, Canada for consideration of $150,000. The property was not consistent with the Company's business objective. The transaction was completed in December 2006 and resulted in a book gain of $83,332.

15 SEGMENTED INFORMATION

The Company's activities are conducted in two geographic segments: Canada and Kazakhstan. All activities relate to exploration for and development of petroleum and natural gas.

[$]	Canada	Kazakhstan	Total
Revenue			
Oil and gas revenue, net	40,249	6,228,869	6,269,118
Interest	282,139	–	282,139
Other	–	15,614	15,614
	322,388	6,244,483	6,566,871
Expenses			
General and administrative	2,910,834	673,451	3,584,285
Accretion of convertible debentures	393,312	–	393,312
Interest	1,777,641	–	1,777,641
Operating	12,075	2,151,922	2,163,997
Transportation	342	486,915	487,257
Stock-based compensation	2,437,039	–	2,437,039
Foreign exchange loss (gain)	14,763,369	(8,982,937)	5,780,432
Depletion, depreciation and accretion	5,000	2,406,418	2,411,418
Future income taxes	–	740,178	740,178
	22,299,612	(2,524,053)	19,775,559
Net (loss) income for the year	(21,977,224)	8,768,536	(13,208,688)
Assets			
Current assets	3,557,712	4,516,584	8,074,296
Restricted cash	–	253,132	253,132
Property, plant and equipment, net	29,173	124,766,620	124,795,793
	3,586,885	129,536,336	133,123,221
Liabilities	18,130,131	10,720,986	28,851,117

16 RECONCILIATION OF INTERNATIONAL FINANCIAL REPORTING STANDARDS

Accounting practices under Canadian GAAP and International Financial Reporting Standards ("IFRS") are, as they affect these financial statements, substantially the same except for the following:

Property and equipment

Under Canadian GAAP, an impairment loss should be recognized when the carrying amount of a cost centre is not recoverable and exceeds its fair value. The carrying amount is not recoverable if the carrying amount exceeds the sum of the undiscounted cash flows expected to result from its use and eventual disposition. Unproved properties and major development projects are included in this recoverability test. A cost centre impairment loss should be measured as the amount by which the carrying amount of assets capitalized in a cost centre exceeds the sum of:

- **the fair value of proved and probable reserves; and**
- **the costs (less any impairment) of unproved properties that have been subject to a separate test for impairment and contain no probable reserves**

For costs beyond the exploration and evaluation stage, IFRS requires (i) an impairment to be recognized when the recoverable amount of an asset (cash generating unit) is less than the carrying amount; (ii) the impairment loss to be determined as the excess of the carrying amount above the recoverable amount (the higher of fair value less costs to sell and value in use, calculated as the present value of future cash flows from the asset), rather than the excess of the carrying amount above the undiscounted future cash flows of the asset; and (iii) the reversal of an impairment loss when the recoverable amount changes. A ceiling test based on cash generating units did not reveal the need for an impairment charge.

For exploration and evaluation costs, IFRS 6 has been adopted effective January 1, 2005. IFRS 6 allows for continued application of an entity's existing policy with respect to accounting for exploration and evaluation costs.

Impairment of long-lived assets

Under Canadian GAAP, a long-lived asset should be tested for recoverability whenever events or changes in circumstances indicate that its carrying amount may not be recoverable. An impairment loss should be recognized when the carrying amount of a long-lived asset is not recoverable and exceeds its fair value. Under IFRS, the carrying amounts of the Company's assets, other than oil and gas properties, inventories and deferred tax assets, are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the assets' recoverable amounts are estimated. An impairment loss is recognized when the carrying amount of an asset exceeds its recoverable amount. Impairment losses, if any, are recognized in the income statement. This difference in accounting policy has no impact on these financial statements.

In respect of impairment of assets other than oil and gas properties, under Canadian GAAP, an impairment loss is not reversed if the fair value subsequently increases. For IFRS, an impairment loss may be reversed if there has been a change in the estimates used to determine the recoverable value.

An impairment loss, on assets other than oil and gas properties, is only reversed to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized. This difference in accounting policy has no impact on these financial statements.

Asset retirement obligation

In re-measuring an asset retirement obligation for the passage of time, Canadian GAAP requires re-measurement based on the risk-free rate that existed when the liability was initially measured. IFRS requires the use of current market assessed interest rates in each estimate. This difference did not result in a material reconciling item.

Inventory

Under Canadian GAAP, the Company measures its supplies inventory at the lower of historical cost or net replacement cost. Under IFRS, the lower of cost or net realizable value principle would apply. This difference did not result in a material reconciling item.

Directors and Advisors

William A. G. Ramsay
Chief Executive Officer & Director
Cascais, Portugal

Chief Executive Officer of the Company from September 2004 to present. President of the Company from September 2004 to April 2007. President and Chief Executive Officer of Caspian Energy Ltd. from April 2004 to present. Prior thereto and since 1997, engaged in private equity investments primarily in Kazakhstan.

Charles J. Summers
President, Chief Operating Officer & Director
Texas, U.S.A.

President of the Company from April 2007 to present. Chief Operating Officer of the Company from September 2004 to present and Chief Operating Officer of Caspian Energy Ltd. from June 2004 to present. Prior thereto, he was general manager for Kerr-McGee Oil & Gas Corporation (an oil and gas exploration and production company) for eight years in Kazakhstan.

Brian D. Korney
Vice-President Finance, Chief Financial Officer & Secretary
Alberta, Canada

Vice-President, Finance, Chief Financial Officer and Secretary of the Company from December 2004 to present. Chief Financial Officer and Secretary of Caspian Energy Ltd. from December 2004 to present. Prior thereto, he was Vice-President, Finance, and Chief Financial Officer of Innova Exploration Corporation for four years and Chief Financial Officer of Genoil Inc.

Robert S. Pollock [1]
Director
Ontario, Canada

Financial Consultant (2006 to present). Senior Vice-President of Quest Capital Corporation (a merchant banking organization) from 2003 to 2006. Prior thereto, he was Vice-President of Investment Banking for Dundee Securities Corporation (an investment dealer).

Robert D. Cudney [1] [2] [3]
Director
Ontario, Canada

President and Chief Executive Officer of Northfield Capital Corporation (an investment company).

Gordon D. Harris [1] [2] [3]
Director
Alberta, Canada

President and Chief Executive Officer of Choice Resources Corp. (an oil and gas company) from February 2004 to date. From 1999 to 2003, he was President of Roseland Resources Ltd. (an oil and gas company).

John McBride [1] [2] [3]
Director
Ontario, Canada

Managing Director of CC Capital Partners Group (a merchant bank) from 1988 to present.

Adil Mukhamedzhanov
Director
Almaty, Kazakhstan

Vice-President of Economics and Finance of Aral from March 2004 to present. Specialist at Kaz Trans Oil from January 1, 2003 to March 2004. Prior thereto, he was a student.

Notes:

[1] Member of Audit Committee.
[2] Member of the Nominating and Compensation Committee.
[3] Member of the Corporate Governance Committee.
[4] Mr. Cudney was a director of Aspen Group Resources Corporation which became subject to a management cease trade order in May 2003 and in May 2004, in each case for failing to file financial statements. The cease trade orders were lifted in July 2003 and July 2004, respectively.

Corporate Information

Nominated Advisor and Broker
Jefferies International Limited

Legal Advisors to the Company
As to English law: Denton Wilde Sapte
As to Canadian law: Cassels Brock
As to Kazakh law: Denton Wilde Sapte

Registrar
Equity Transfer Services

Reporting Accountants
PricewaterhouseCoopers LLP

Auditors to the Company and CEL
PricewaterhouseCoopers LLP

Independent Engineers
McDaniel & Associates Consultants Ltd.

Banker
CIBC

Trading
London Stock Exchange
Symbol: CEK.L

Toronto Stock Exchange
Symbol: CEK.TO

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Notice to Shareholders

The annual meeting of the shareholders of Caspian Energy Inc. will be held at: The National Club, 303 Bay Street, Toronto, Ontario on Tuesday, June 24, 2008, at 3:30 p.m. (Toronto time).

FORWARD-LOOKING STATEMENTS

This document contains forward-looking statements that involve risks and uncertainties. These statements relate to the Corporation's future plans, objectives, expectations and intentions. These statements are identified by the use of words such as "may", "will", "expect", "anticipate", "intend", "plan", "estimate", "believe", "continue" or other similar expressions. These forward-looking statements reflect management's current expectations and assumptions as to future events that may not prove to be accurate. Actual results are subject to a number of risks and uncertainties and could differ materially from those discussed in these statements. In light of the many risks and uncertainties surrounding our business and operations, you should keep in mind that the forward-looking statements described in this document may not transpire. The Corporation undertakes no obligation, and does not intend to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as otherwise required under applicable securities laws.

The terms used throughout our Annual Report are defined, and summarized on the tables.

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