

Caspian Energy Inc.

Condensed Interim Consolidated Financial Statements
(Unaudited)

March 31, 2014

Notice of Disclosure of No Auditor Review of Condensed Interim Financial Statements

The accompanying unaudited condensed interim consolidated financial statements of the Company for the three months ended March 31, 2014 have been prepared in accordance with International Financial Reporting Standards (“IFRS”) accounting principles as issued by the IASB and are the responsibility of the Company’s management.

The Company’s independent auditors, MNP LLP, have not performed a review of these unaudited condensed interim consolidated financial statements in accordance with the standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity’s auditor.

Caspian Energy Inc.

Condensed Interim Consolidated Statements of Financial Position (unaudited)

(in thousands of Canadian dollars)

	March 31 2014 \$	December 31 2013 \$
Assets		
Current assets		
Cash and cash equivalents (Note 4)	110	17
Trade and other receivables	7	4
	117	21
Non-current assets		
Investment in Aral (Note 15)	–	–
	117	21
Liabilities		
Current liabilities		
Trade and other payables	1,154	1,950
Promissory note (Note 5)	–	47
Convertible debentures (Note 6)	–	15,949
	1,154	17,946
Non-current liabilities		
Loan payable (Note 7)	7,441	5,656
	8,595	23,602
Equity		
Share capital (Note 8)	159,715	143,559
Warrants (Note 9)	247	247
Contributed surplus	18,260	18,260
Deficit	(186,700)	(185,647)
	(8,478)	(23,581)
Total liabilities and equity	117	21

See accompanying notes to the unaudited condensed interim consolidated financial statements.

Caspian Energy Inc.

Condensed Interim Consolidated Statements of Financial Position (unaudited)

(in thousands of Canadian dollars)

Reporting entity and going concern (Note 1)

Caspian Energy Inc.

Consolidated Statements of Loss and Comprehensive Loss

For the three months ended March 31

(unaudited)

(in thousands of Canadian dollars)

	2014 \$	2013 \$
Revenue		
Oil and natural gas revenue, net	4	2
Expenses		
General and administrative	359	292
Operating expenses	–	2
Share-based compensation	–	337
Depreciation	–	1
	359	632
Operating loss before other items	(355)	(630)
Finance expense (Note 12)	(1,184)	(2,273)
Derivative fair value adjustment (Note 6)	–	208
Gain on convertible debenture (Note 6)	486	–
Loss and comprehensive loss	(1,053)	(2,695)
Loss per share (Note 11)	(0.01)	(0.12)

Caspian Energy Inc.

Condensed Interim Consolidated Statements of Changes in Equity

For the three months ended March 31

(unaudited)

(in thousands of Canadian dollars)

	2014	2013
	\$	\$
Share capital		
Balance, January 1	143,559	143,358
Issuance of shares, net of issue costs (Note 8)	16,156	–
Exercise of warrants	–	103
Balance, March 31	159,715	143,461
Warrants		
Balance, January 1	247	313
Issuance of warrants	–	34
Balance, March 31	247	347
Contributed surplus		
Balance, January 1	18,260	17,660
Share-based compensation	–	337
Balance, March 31	18,260	17,997
Deficit		
Balance, January 1	(185,647)	(177,407)
Loss and comprehensive loss	(1,053)	(2,695)
Balance, March 31	(186,700)	(180,102)
Total Equity	(8,478)	(18,297)

Caspian Energy Inc.

Condensed Interim Consolidated Statements of Cash Flows

For the three months ended March 31

(unaudited)

(in thousands of Canadian dollars)

	2014	2013
	\$	\$
Cash flow provided by (used in)		
Operating activities		
Loss and comprehensive loss	(1,053)	(2,695)
Adjustments for:		
Share-based compensation	–	337
Depreciation	–	1
Finance expense	334	1,980
Derivative fair value adjustment	–	(208)
Gain on convertible debenture	(486)	–
Foreign exchange	812	301
Changes non-cash working capital		
Trade and other receivables	(3)	2
Trade and other payables	(796)	178
Net cash used in operating activities	(1,192)	(104)
Financing activities		
Share issue costs	(92)	–
Repayment of promissory note	(47)	–
Proceeds from loan payable	1,424	154
Net cash provided by financing activities	1,285	154
Change in cash and cash equivalents	93	50
Cash and cash equivalents – January 1	17	19
Cash and cash equivalents – March 31	110	69

Caspian Energy Inc.

Condensed Interim Consolidated Statements of Cash Flows

For the three months ended March 31

(unaudited)

(in thousands of Canadian dollars)

Caspian Energy Inc.

Notes to Condensed Interim Consolidated Financial Statements

For the three months ended March 31, 2014

(unaudited)

All tabular amounts are in thousands of Canadian dollars except as otherwise indicated.

1. Reporting entity and going concern

Caspian Energy Inc. (“Caspian” or the “Company”) is a publicly traded company on the NEX, a separate board of TSX Venture Exchange under the stock symbol CKZ.H. Caspian is engaged in the exploration for and development and production of oil and gas in the Republic of Kazakhstan (“ROK”). Its primary operating activities are carried out through its wholly-owned subsidiary, Caspian Energy Ltd. (“CEL”). Caspian’s registered office is located at 396 11th Avenue S.W., Calgary, Alberta, Canada.

The Company’s principal assets are a 40% interest in Aral Petroleum Capital LLP (“Aral”), held by CEL. The remaining 60% of Aral is held by Asia Sixth Energy Resources Limited (“ASER”) and its subsidiary Groenzee BV (collectively “Asia Sixth”).

Through its interest in Aral, the Company has the right to explore and develop certain oil and gas properties in Kazakhstan, known as the North Block, a 2,200 square kilometre area located in the vicinity of the Kazakh pre-Caspian basin. The Company also has minor resource interests in Canada.

Going concern

These consolidated financial statements have been presented on a going concern basis. For the year ended December 31, 2013, the Company reported a loss of \$1.1 million and used funds for operating activities of \$1.2 million. As at March 31, 2014, the Company had a net working capital deficiency of \$1.0 million (December 31, 2013 – \$17.9 million) and a cumulative deficit of \$186.7 million (December 31, 2013 – \$185.6 million).

As at March 31, 2014, Caspian management performed an assessment of the value of the Company’s 40% interest in certain assets of Aral reduced its share of the carrying amount of property, plant and equipment to \$nil (Note 15(b)).

The Company’s ability to continue as a going concern is in significant doubt and is dependent upon obtaining financing to fund exploration and development activities and general and administrative expenses and on Aral achieving profitable operating results from its Kazakhstan operations. There are no assurances that these initiatives will be successful.

On February 19, 2014, the Company’s shareholders approved:

- The one-for-ten consolidation of the Company’s common shares.
- The January 15, 2014 agreement to amend the Company’s convertible debentures (Note 10) that amends the conversion price such that an aggregate of 108,319,091 (post-consolidated) common shares would be issued to the debenture holders on conversion.

The accompanying consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded assets and classification of liabilities that might be necessary should the Company be unable to continue its operations. Such adjustments could be material.

All common share, warrant, stock option and performance share figures presented herein are on a post-consolidated basis.

2. Basis of presentation

These unaudited condensed interim consolidated financial statements have been prepared in accordance with International

Caspian Energy Inc.

Notes to Condensed Interim Consolidated Financial Statements

For the three months ended March 31, 2014

(unaudited)

Financial Reporting Standards (“IFRS”), including International Accounting Standard (“IAS”) 34 – Interim Financial Reporting.

The Company has consistently applied the same accounting policies throughout all periods presented. These unaudited condensed interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto for the year ended December 31, 2013.

These unaudited condensed interim consolidated financial statements were authorized for issue by the Board of Directors on May 29, 2014.

3. Changes in accounting policies

On January 1, 2014, the Company adopted amendments to IAS 24 Related Party Disclosures, IAS 32 Financial Instruments: Presentation, IAS 36 Impairment of Assets and IAS 39 Financial Instruments: Recognition and Measurement. The adoption of these amendments had no impact on the Company’s unaudited condensed interim consolidated financial statements.

4. Cash and cash equivalents

	March 31	December 31
	2014	2013
Cash in CAD	(5)	13
Cash in USD	67	3
Cash in Pounds Sterling	48	1
	110	17

5. Promissory note

On April 1, 2013, the Company entered into a promissory note agreement with an officer of the Company in the principal amount of \$41,127. The promissory note is unsecured, matures on December 31, 2013 and bears interest at 20% per annum. As at December 31, 2013, the \$47,296 balance was comprised of \$41,127 of principal plus \$6,169 of accrued interest. The balance of principal plus accrued interest was repaid in full in January 2014.

6. Convertible debentures

As at December 31, 2013, the Company had USD 12.5 million principal amount of 10% per annum convertible debentures (the “Debentures”) with a maturity date of June 2, 2013 and secured with Caspian shares issued and outstanding.

The Company was not able to repay the Debentures on the maturity date. The terms of the Debentures provide that a default occurs if there is a failure to pay principal on maturity and such failure to pay is not remedied within 30 days after receipt of written notice from the debenture holders (the “Holders”). In late June of 2013, the Company received notices from each of the Holders providing the Company with written notice of payment defaults.

The Company and the Holders entered into a remedial period extension agreement dated July 26, 2013 (the “Extension Agreement”) pursuant to which, among other things, the Holders agreed to extend the remedial period to August 26, 2013 during which time the Company could remedy the payment defaults before such payment defaults would constitute defaults under the Debenture agreements. Such remedial period was further extended pursuant to amendments to the Extension Agreement dated August 26, 2013, September 26, 2013, October 26, 2013, November 26, 2013 and December 17, 2013.

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Notes to Condensed Interim Consolidated Financial Statements

For the three months ended March 31, 2014

(unaudited)

The December 17, 2013 amendment extended the remedial period to February 20, 2014. On January 15, 2014, the Company entered into a further extension agreement (the “Amended Extension Agreement”) with the Holders, pursuant to which the Company and Holders executed the Debenture Amendment which provides for the conversion (the “Conversion”) of the outstanding Debentures, and the obligations owing thereunder, into an aggregate of 108,319,092 shares, representing approximately 82.5% of the Company’s outstanding common shares on the business day following the receipt of shareholder approval for, among other things, the one-for-ten share consolidation (Note 8) and the Conversion.

The Company received shareholder approval on February 19, 2014 and on February 20, 2014, following approval by the NEX board of the TSX Venture Exchange, the Debentures were converted to 108,319,091 common shares.

A continuity of the Debentures is as follows:

Balance, December 31, 2013	15,949
Interest	179
Foreign exchange	606
Balance, February 20, 2014	16,734
Conversion to 108,319,091 common shares (Note 8)	(16,248)
Gain on conversion of Debentures	(486)
Balance, March 31, 2014	–

Interest continued to accrue on the debenture principal amount at 10% per annum during the remedial period and extensions. Upon conversion of the Debentures, the Company recognized a gain in the amount of \$485,758 in the consolidated statement of loss and comprehensive loss for the three months ended March 31, 2014.

7. Loan payable

In connection with the Company’s sale of a 10% interest in Aral to Asia Sixth in 2011, the Company entered into a facility agreement with Asia Sixth pursuant to which Asia Sixth will advance up to USD 6 million in loans to Caspian, of which USD 2 million remained available as at June 3, 2013.

On June 3, 2013, the terms of the facility agreement were amended to the following terms, which represent a refinement of the original terms:

- Amounts advanced under the facility will bear interest at a rate of 10% per annum until December 28, 2016 and 18% per annum, compounded annually, thereafter until November 1, 2020.
- The Company is permitted to draw up to USD 100,000 during each calendar month until November 2013 at which time, until expiry, the Company may draw the undrawn balance of the remaining USD 2,000,000.
- The ability to draw under the facility expires after 12 months from the amendment date.
- The loan is to be repaid with all proceeds received by the Company by way of dividends from Aral or from the sale of any asset by the Company.
- The balance of all principal and interest still owing on November 1, 2020 must be repaid on such date.
- The Company provided a pledge of all of its interest in Aral in favour of Asia Sixth as security for the Company’s obligations under the facility.

As at March 31, 2014, the Company had received total draws under the facility of USD 6 million (December 31, 2013 – USD 4.7 million).

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As at March 31, 2014, the \$7,441,329 balance owing Asia Sixth is comprised of \$6,634,860 of principal plus \$806,469 of accrued interest (December 31, 2013 – \$5,656,041 balance comprised of \$5,026,321 of principal plus \$629,720 of accrued interest).

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Notes to Condensed Interim Consolidated Financial Statements

For the three months ended March 31, 2014

(unaudited)

8. Share capital

On February 19, 2014, the Company's shareholders approved the one-for-ten consolidation of the Company's common shares.

	Number of shares	Amount
Balance, December 31, 2013	23,021,777	143,559
Conversion of Debentures (Note 6)	108,319,091	16,248
Share issue costs	—	(92)
Balance, March 31, 2014	131,340,868	159,715

9. Warrants

As at December 31, 2013 and March 31, 2014, the Company had 317,835 warrants outstanding. Information about warrants as at March 31, 2014 is summarized in the following table:

Exercise price	Number of warrants outstanding	Weighted average exercise price	Weighted average remaining contractual life (years)
\$ 0.57	98,721	\$ 0.57	1.03
\$ 0.64	64,334	0.64	0.78
\$ 1.41	39,361	1.41	0.51
\$ 1.84	31,818	1.84	0.27
\$ 1.91	83,601	1.91	0.04
	317,835	\$ 1.17	0.58

10. Share-based compensation

(a) Stock options

A continuity of options outstanding as at March 31, 2014 is summarized as follows:

	Number of options	Weighted average exercise price
Opening	2,634,162	\$ 1.43
Expired	(157,000)	1.59
Closing	2,477,162	\$ 1.42
Exercisable	2,477,162	\$ 1.42

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(unaudited)

Information about options outstanding and exercisable as at March 31, 2014 is summarized in the following table:

Exercise price	Number of options outstanding	Weighted average exercise price	Weighted average remaining contractual life (years)	Number of options exercisable
\$ 0.50	75,000	\$ 0.50	4.01	75,000
\$ 0.70	500,000	0.70	3.82	500,000
\$ 0.95	450,000	0.95	3.61	450,000
\$ 1.80	707,162	1.80	2.24	707,162
\$ 1.90	550,000	1.90	3.03	550,000
\$ 2.00	195,000	2.00	1.17	195,000
	2,477,162	\$ 1.42	2.83	2,477,162

(b) Performance shares

The Company entered into an agreement on August 18, 2012 and amended in January 2013, (“the Amended Consulting Agreement”) with a petrophysicist (the “Consultant”) for the provision of consulting services in connection with the exploitation, development and completion of eight Aral wells in the Republic of Kazakhstan. Pursuant to the amended Consulting Agreement, remuneration for consulting services is performance based and the Consultant will be compensated with common shares of the Company according to certain performance criteria.

If all performance criteria are met, the Consultant would be entitled to a maximum of 2.6 million common shares of the Company comprised of 2 million Consideration Shares and 600,000 Bonus Shares. At the Company’s option, the Company can elect to satisfy all or a portion of consideration payable in cash. Any amounts elected to be paid in cash would be determined by the number of Consideration Shares or Bonus Shares payable multiplied by the market price of the Company’s common shares at the close of trading on the date the particular Consideration Shares or Bonus Shares became payable.

The fair value of performance shares was estimated to be a negligible amount and therefore no amount has been recognized in the consolidated financial statements in respect of the consulting services performed to date. As of March 31, 2014, no performance shares had been issued.

11. Per share amounts

For the three months ended March 31	2014	2013
Net loss for the period	(1,053)	(2,695)
Weighted average number of shares (in thousands) – basic:		
Issued common shares at January 1	23,022	22,696
Effect of shares issued during the period	61,381	116
	84,403	22,812
Net loss per share – basic and diluted	(0.01)	(0.12)

Caspian Energy Inc.

Notes to Condensed Interim Consolidated Financial Statements

For the three months ended March 31, 2014

(unaudited)

The effect of stock options, performance shares, Debentures and warrants is anti-dilutive in loss periods.

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For the three months ended March 31, 2014

(unaudited)

12. Finance expense

For the three months ended March 31	2014	2013
Interest on convertible debentures	179	396
Accretion of convertible debentures	–	1,478
Interest expense on loan payable	158	106
Net foreign exchange loss	847	293
Net finance expense	1,184	2,273

13. Supplemental cash flow disclosure

During the three months ended March 31, 2014, the Company paid \$nil (March 31, 2013 – \$nil) of interest in cash and settled \$nil (March 31, 2013 – \$81,000) of interest through the issuance of common shares and warrants.

14. Guarantee in favour of Asia Sixth

In connection with the Transaction Agreements signed on June 3, 2013 (Note 1), the Company agreed to provide a guarantee of its 40% share of the obligations owed by Aral to Asia Sixth under the Aral Loan Agreement.

As at March 31, 2014, obligations owed by Aral to Asia Sixth under the Aral Loan Agreement totalled USD 29.4 million comprised of USD 21.1 million of existing loans (as defined by the Aral Loan Agreement) and USD 8.3 million of amounts advanced under the USD 20 million of “New Loan” portion of the Aral Loan Agreement.

15. Selected financial information for Aral Petroleum Capital LLP

As at March 31, 2014 and December 31, 2013, the Company held a 40% interest in Aral, recognized in these consolidated financial statements using the equity method of accounting. As the investment is in a negative net asset position, there is no representation of the investment in the Company’s consolidated financial statements. To date, the Company has not received any dividends from Aral.

(a) Aral’s results of operations, assets and liabilities

A summary of Aral’s results of operations for the three months ended March 31, 2014 and 2013 and Aral’s assets and liabilities as at March 31, 2014 and December 31, 2013 is presented below:

For the three months ended March 31	2014	2013
Oil and natural gas revenue, net	3,085	95
General and administrative expenses	(409)	(365)
Operating and transportation expenses	(2,294)	(620)
Depletion and depreciation expense	(1,210)	(183)
Interest and finance expense	(37,006)	(742)
Loss and comprehensive loss	(37,834)	(1,815)

Caspian Energy Inc.

Notes to Condensed Interim Consolidated Financial Statements

For the three months ended March 31, 2014

(unaudited)

As at	March 31 2014	December 31 2013
Cash and cash equivalents	12	161
Other current assets	2,429	5,626
Total current assets	2,441	5,787
Exploration and evaluation assets	76,664	83,259
Property, plant and equipment (Note 15(b)(i))	47,536	52,529
Other non-current assets	8,932	9,943
Total non-current assets	133,132	145,731
Total assets	135,573	151,518
Trade and other payables	56,569	65,821
Current loans payable	175,519	164,047
Total current liabilities	232,088	229,868
Long-term loans payable	40,867	37,226
Other non-current liabilities	1,091	1,237
Total non-current liabilities	41,958	38,463
Total liabilities	274,046	268,331

(b) Caspian's 40% interest in Aral's results of operations, assets and liabilities

A summary of the Company's 40% interest in Aral's results of operations for the three months ended March 31, 2014 and 2013 and Aral's assets and liabilities as at March 31, 2014 and December 31, 2013 is presented below:

For the three months ended March 31	2014	2013
Oil and natural gas revenue, net	1,234	38
General and administrative expenses	(164)	(146)
Operating and transportation expenses	(917)	(248)
Depletion and depreciation expense	(484)	(73)
Impairment of property, plant and equipment (i)	(1,202)	–
Interest and finance expense	(11,604)	(297)
Loss and comprehensive loss	(13,137)	(726)

Caspian Energy Inc.

Notes to Condensed Interim Consolidated Financial Statements

For the three months ended March 31, 2014

(unaudited)

	March 31 2014	December 31 2013
Current assets	977	2,314
Exploration and evaluation assets	30,666	33,304
Property, plant and equipment (i)	–	–
Total assets	35,215	39,595
Current liabilities	92,836	91,947
Total liabilities	109,619	107,332

- (i) Based on the uncertainty surrounding the economic recoverability of Aral's proved and probable reserves given the current market and cost structure, Caspian management reduced the carrying amount of its share of Aral's property, plant and equipment by \$19,014 to a carrying amount of \$nil comprised of \$1,202 of impairment recognised in the three months ended March 31, 2014, \$21,012 of impairment recognized in the year ended December 31, 2013 and a \$3,200 credit to accumulated other comprehensive income for the effects of foreign exchange translation on property, plant and equipment. This adjustment has no impact on Caspian's consolidated financial position as at March 31, 2014 and December 31, 2013 and consolidated financial performance for the periods then ended as the carrying amount of the Company's investment in Aral has already been reduced to zero.
- (ii) As at March 31, 2014, the Company's unrecognized 40% interest of Aral's cumulative losses recognized by Aral was \$61,463 (December 31, 2013 – \$46,328). The Company's unrecognized 40% interest of Aral's cumulative losses as at March 31, 2014, including the impairments recognized by the Company as noted above, increased to \$83,667.