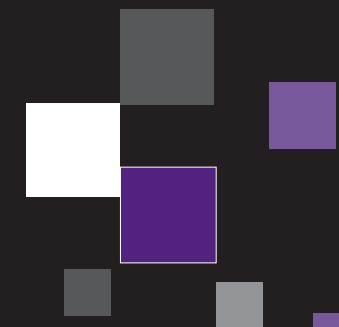


firstquarter

GALLEON ENERGY INC. 2007 INTERIM REPORT



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REPORT TO SHAREHOLDERS

During Q1 2007, a record production level in the history of the company was set. In 2007, Galleon plans to drive production growth by drilling low risk development wells and by taking maximum advantage of the major facilities expansion completed in 2006. Galleon will also aggressively expand exploitation projects at Puskwa – light sweet oil discovery; at Dawson – large Montney natural gas project; and at Eaglesham – multi-zone oil and natural gas project. An exciting exploration program will be layered in with 10 to 15% of the capital budget being committed to new high impact drilling projects. Seven new exploration projects on the Peace River Arch are being worked up with 2 of these having large 3D seismic programs (90 square miles in total) covering them. Multiple high impact locations have been identified and will be drilled in the third and fourth quarters of 2007. The existing opportunity portfolio gives Galleon clear visibility to multiyear drilling which will allow continued growth of production and reserves on a per share basis thereby creating and delivering significant shareholder value.

In the Dawson Montney gas project, production from this project continues to grow and currently exceeds 20 MMcf/d. This is a new production record for this project. Two rigs are contracted to drill continuously for the remainder of 2007. Galleon has over five years drilling inventory or over 300 locations on this project which covers an area 25 miles long and 12 miles wide. Based on the drilling inventory, the project has the potential to grow production to over 50 MMcf/d. Up to 50 wells are planned in 2007.

At Puskwa, Galleon plans to expand the waterflood projects and the Good Production Practice (“GPP”) areas. The first phase of the waterflood injection facility to serve sections 5-72-26W5M and 32-71-26W5M is currently being constructed. This facility is expected to be on stream in June 2007. Galleon plans to gradually ramp up production on the wells which have been granted GPP. To date, Galleon has drilled 15 wells over a 9 mile fairway of Beaverhill lake sand at Puskwa. Based on geological and geophysical interpretation, Galleon expects to drill continuously over the next two to three years to fully exploit the large oil pool at Puskwa. Up to 30 wells are planned in 2007 and 2008.

Two new high impact light oil exploration projects have been identified in the general Puskwa area. Two wildcat deep test wells exceeding 10,000 feet are planned for the third and fourth quarter of 2007.

At Eaglesham, Galleon continues to drive production higher. Current production is over 1,700 BOE/d. Three or four deep test wells are planned in the second half of 2007.



Glenn R. Carley
Executive Chairman

May 14, 2007



Steve Sugianto
President and Chief Executive Officer

MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion & Analysis ("MD&A") is intended to assist in the understanding of the trends and significant changes in the financial condition and results of operations of Galleon Energy Inc. ("Galleon" or the "Corporation") for the three month period ended March 31, 2007 with comparisons to the three months ended March 31, 2006 and as at December 31, 2006. The MD&A has been prepared by management in accordance with Canadian generally accepted accounting principles ("GAAP") and should be read in conjunction with the unaudited interim financial statements as at and for the three month periods ended March 31, 2007 and 2006 and the audited financial statements and MD&A for the year ended December 31, 2006.

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

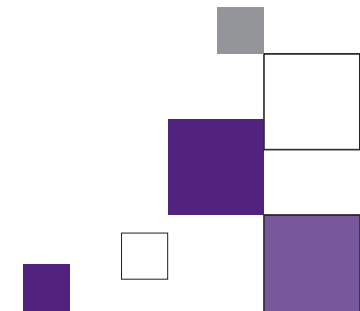
Amounts are shown in Canadian dollars unless otherwise stated. All production volumes disclosed herein are sales volumes.

This MD&A is based on information available as of, and is dated, May 14, 2007.

NON-GAAP MEASUREMENTS

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

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



FORWARD-LOOKING STATEMENTS

Statements that are not historical facts may be considered forward looking statements including management's assessment of future plans and operations, growth expectations within the Corporation, expected production and production increases, effect of pilot waterflood project at Puskwa, expected effect of production increases on operating costs per BOE, effects of new facilities, expected growth areas, expected non taxability of the Corporation in 2007, drilling plans and the timing thereof, commodity prices, expected commodity mix, and capital expenditures, the timing thereof and the method of funding thereof. These forward-looking statements sometimes include words to the effect that management believes or expects a stated condition or result. All estimates and statements that describe the Corporation's objectives, goals or future plans are forward-looking statements. Since forward-looking statements address future events and conditions, by their very nature they involve inherent risks and uncertainties including, without limitation, risks associated with oil and gas exploration, development, exploitation, production, marketing and transportation, loss of markets, volatility of commodity prices, currency fluctuations, imprecision of reserve estimates, environmental risks, competition from other producers, inability to retain drilling rigs and other services, incorrect assessment of the value of acquisitions, failure to realize the anticipated benefits of acquisitions, delays resulting from or inability to obtain required regulatory approvals (including GPP at Puskwa) and ability to access sufficient capital from internal and external sources. As a consequence, Galleon's actual results may differ materially from those expressed in, or implied by, the forward-looking statements. Readers are cautioned that the foregoing list of factors is not exhaustive. Additional information on these and other factors that could affect Galleon's operations and financial results are included elsewhere herein and in reports on file with Canadian securities regulatory authorities and may be accessed through the SEDAR website (www.sedar.com), or at Galleon's website (www.galleonenergy.com). Furthermore, the forward looking statements contained herein are made as at the date hereof and Galleon does not undertake any obligation to update publicly or to revise any of the included forward looking statements, whether as a result of new information, future events or otherwise, except as may be required by applicable securities laws.

FIRST QUARTER 2007 HIGHLIGHTS

- Funds from operations were \$30.2 million (\$0.52 per basic share), an increase of 26% from Q4 2006, and 67% compared to Q1 2006;
- Earnings were \$3.9 million (\$0.07 per basic share), an increase of 106% from Q4 2006, and 125% compared to Q1 2006;
- Daily production averaged 11,888 BOE, an increase of 9% from Q4 2006, and 38% compared to Q1 2006;
- Operating costs of \$8.86/BOE decreased by 8% compared to Q4 2006.
- Drilled 30 gross wells resulting in 17 (15.1 net) natural gas wells and 9 (8.7 net) light oil wells; a success rate of 87%;
- Spent \$61.2 million on exploration and development activities, plus property acquisitions of \$28.7 million;
- Subsequent to March 31, 2007, completed an equity offering of flow-through shares for gross proceeds of \$30.0 million;
- Subsequent to March 31, 2007, increased available credit facilities to \$210 million.

RESULTS OF OPERATIONS

Comparative financial results for the quarter are as follows:

<i>Three months ended March 31</i> <i>(\$000s)</i>		<i>2007</i> <i>1,069,915 BOE</i> <i>\$/BOE</i>		<i>2006</i> <i>774,578 BOE</i> <i>\$/BOE</i>
Revenues	52,974	49.51	36,230	46.77
Royalties	(11,016)	(10.30)	(8,861)	(11.44)
ARTC and GCA ¹	2,634	2.46	975	1.26
Transportation costs	(1,587)	(1.47)	(1,106)	(1.43)
Operating costs	(9,478)	(8.86)	(7,065)	(9.12)
Net	33,527	31.34	20,173	26.04
G&A	(1,264)	(1.18)	(1,160)	(1.50)
Interest costs	(2,246)	(2.10)	(740)	(0.95)
Capital and other taxes	(220)	(0.21)	(226)	(0.29)
Realized gain on financial derivative	373	0.35	–	–
Funds from operations ²	30,170	28.20	18,047	23.30

¹ GCA means Gas Cost Allowance

² See “Non-GAAP Measurements”

PETROLEUM AND NATURAL GAS REVENUES

<i>Three months ended March 31</i> <i>(\$000s)</i>		<i>2007</i> <i>%</i>		<i>2006</i> <i>%</i>
Light oil	18,309	35	11,099	31
Heavy oil	6,919	13	3,705	10
NGLs	1,051	2	482	1
Natural gas	26,516	50	20,755	57
Royalty income	179	–	189	1
Total	52,974	100	36,230	100

Revenues for the three months ended March 31, 2007 increased 46% to \$53.0 million from \$36.2 million for the same period of the prior year due to a 38% increase in average production volumes, a 48% increase in heavy

oil prices, and a shift in the product mix towards oil. The oil and liquids to natural gas production ratio for the quarter was 46/54 compared to 41/59 one year ago.

PRODUCTION

<i>Three months ended March 31</i>	<i>BOE/d</i>	<i>2007</i> <i>%</i>	<i>BOE/d</i>	<i>2006</i> <i>%</i>
Light oil (Bbls/d)	3,127	26	1,859	22
Heavy oil (Bbls/d)	2,081	18	1,580	18
NGLs (Bbls/d)	206	2	93	1
Natural gas (Mcf/d)	38,845	54	30,445	59
BOE/d (6:1)	11,888	100	8,606	100

Average production volumes for the quarter of 11,888 BOE/d increased 38% compared to 8,606 BOE/d in the same period of the prior year. By product, production volumes increased as follows: light oil 68%, heavy oil 32%, natural gas 28%, and natural gas liquids 122%.

The light oil production increases represent additions from the drilling activity at Puskwa. On March 23, 2007 Galleon was granted good production practice ("GPP") status from the Alberta Energy and Utilities Board on two sections at Puskwa. Production from the two wells located on these sections will be gradually increased over the spring and summer. A pilot water flood project is expected to be completed by the end of June. Applications are in process for GPP on the remaining sections at Puskwa. Galleon remains optimistic that approval will be received prior to the end of 2007. Heavy oil production increased as a result of optimization techniques and minor workovers at Edam.

Natural gas production increased as a result of pipeline tie-ins of previously drilled wells from the Montney gas project. Drilling success from the Montney gas project was 89% in the first quarter of 2007 with 9 wells drilled and 8 (7.7 net) cased. The drilling program at Eaglesham targeted multi-zone oil and gas from the Dunvegan to Wabamun formations. In the first quarter, 6 wells were drilled and 5 wells (3.7 net) were cased for a success rate of 83%. In total Galleon drilled 30 wells and cased 26 (23.8 net) for production during the quarter, for a success rate of 87%. Wells cased for production include 9 (8.7 net) light oil wells and 17 (15.1 net) natural gas wells.

COMMODITY PRICING AND MARKETING

Petroleum products are sold to major Canadian marketers at spot reference prices based on US WTI for crude oil and AECO for natural gas. As a means of managing the risk of commodity price volatility, Galleon entered into fixed price natural gas contracts. During the first quarter, an average of 14,833 GJ/day (or 38%) of natural gas production was fixed at an average price of \$7.34/GJ. Details of the remaining contracts are disclosed in note 10 to the financial statements.

For crude oil, Galleon entered into a costless collar on 1,000 Bbls a day, fixing a floor price of WTI USD \$61.75/Bbl and a ceiling of WTI USD \$70.00/Bbl for the period January 1, 2007 to December 31, 2007. See "Financial Instruments".

PRICES (NET OF TRANSPORTATION)

<i>Three months ended March 31</i>	<i>2007</i>	<i>2006</i>
Light oil (\$/Bbl)	63.24	65.66
Heavy oil (\$/Bbl)	36.55	24.71
Natural gas (\$/Mcf)	7.36	7.36
NGLs (\$/Bbl)	56.64	57.62

Average heavy oil prices of \$36.55/Bbl increased 48% from the same period of the prior year due to a decrease in differentials. Average natural gas prices were unchanged from the first quarter of 2006 at \$7.36/Mcf. The price calculated for the first quarter of 2007 includes the impact of the fixed price contracts discussed above. Light oil prices decreased 4% to \$63.24/Bbl, not including the impact of the crude oil costless collar.

Including the realized gain on the costless collar of \$373,000, see "Financial Instruments", average crude oil prices received would be \$64.57/Bbl.

Transportation costs of \$1.47/BOE increased 3% over the same period of the prior year due to an increase in contracted firm service on the Nova pipeline to manage expected natural gas production increases in 2007.

PERFORMANCE BY PROPERTY

<i>Three months ended March 31</i>	<i>2007</i>			<i>2006</i>			<i>2007</i>
	<i>Production BOE/d</i>	<i>%</i>	<i>Operating Netbacks/ BOE¹ \$</i>	<i>Production BOE/d</i>	<i>%</i>	<i>Operating Netbacks/ BOE¹ \$</i>	<i>Funds from Operations² %</i>
Puskwa	1,525	13	49.91	175	2	46.22	22
Dawson Montney gas	2,825	24	31.80	590	7	25.33	26
Eaglesham	1,554	13	32.57	–	–	–	15
Dawson	3,038	26	28.48	4,298	50	31.91	25
Edam and other heavy oil	2,082	17	10.23	1,585	18	0.98	6
Calais	477	4	20.80	1,444	17	28.31	3
Other	387	3	23.07	514	6	23.76	3
	11,888	100	28.88	8,606	100	24.78	100

¹ Operating netbacks/BOE exclude ARTC and GCA and are calculated by subtracting royalties and operating costs from revenues.

² See "Non-GAAP Measurements."

At Puskwa, production increased 771% over the same period of the prior year, and the operating netback of \$49.91/BOE improved by 8%. Exploration and development at Puskwa was initiated in the first quarter of 2006 and already contributes 22% of total funds from operations. The production rate for the quarter reflects the allowable rate imposed by the EUB and is not indicative of the production capacity in the area. During the second quarter of 2007, production is expected to increase at Puskwa as a result of GPP granted on two sections. In the third quarter of 2007, it is expected the pilot water flood will further improve recoverability. The strong operating netbacks during the quarter were driven by low operating costs of \$3.47/BOE and high light oil prices, net of transportation, of \$65.03/Bbl. Galleon plans to drill up to 15 wells in the Puskwa area in 2007.

Production of Montney gas at Dawson increased 379% over the same period of the prior year, and the operating netback of \$31.80/BOE improved

by 26%. The operating netback improved with a decrease in operating costs from \$8.29/BOE in the first quarter of 2006 to \$4.27/BOE in the first quarter of 2007. The decrease is a function of control of the facilities in the area. Galleon's 30 MMcf/d gas plant was fully operational in January 2007. The area contributes 26% to total funds from operating activities. Galleon has identified over 300 drilling locations in the Dawson area and plans to drill up to 60 wells in 2007.

Liquids rich natural gas and light oil production at Eaglesham commenced in August, 2006 and reached 1,554 BOE/day on average in the first quarter of 2007. Operating netbacks of \$32.57/BOE reflect a low operating cost structure of \$5.58/BOE. Control of the facilities in the area has enabled Galleon to control operating costs. Eaglesham contributed 15% of first quarter funds from operating activities. Galleon plans to drill up to 10 wells in this area in 2007.

At Dawson, natural production declines resulted in lower production volumes compared to the prior year. Lower volumes resulted in higher operating costs per barrel of oil equivalent, and a lower operating netback. Although the area was previously Galleon's main contributor to funds from operating activities, for the quarter it represented only 25% due to capital allocations towards Galleon's growth projects.

Heavy oil production grew 31% as a result of exploitation techniques. Operating netbacks of \$10.23/BOE have increased significantly over the same period of the prior year due to a higher heavy oil price. With exit production for 2007 planned to be between 17,000-21,000 BOE/d, it is expected that the heavy oil assets will only account for 10%-12% of total production by the end of 2007.

The decrease in production at Calais relates to natural gas wells at Rycroft, Kakut, and Peoria that were shut-in due to uneconomic conditions, and natural gas declines. Oil production declines were experienced at Peoria due to increasing water cuts. The 27% decrease in operating netbacks is a function of higher operating costs per barrel of oil equivalent due to lower production volumes and higher water handling costs. A lower proportion of oil production resulted in a lower realized price per barrel of oil equivalent.

ROYALTIES

<i>Three months ended March 31 (\$000s)</i>	2007	2006
Crown	10,091	8,255
Freehold	413	186
GORR and other	512	420
Subtotal	11,016	8,861
ARTC and GCA	(2,634)	(975)
Net royalties	8,382	7,886
% of revenue	20.8	24.4
% of revenue net of ARTC and GCA	15.8	21.8

Gross royalties were 20.8% of revenues for the first quarter of 2007 compared to 24.4% for the same period in 2006. By product, gross royalties were 14.7% for light oil, 25.1% for natural gas, 20.2% for heavy oil, and 25.6% for liquids. For the first quarter of 2006 gross royalties were 20.2% for light oil, 29.2% for natural gas, 15.9% for heavy oil, and 29.7% for liquids. Net royalties of 15.8% decreased 28% compared to the prior year as a result of lower gross royalty rates and additional GCA credits attributed to Galleon's new natural gas facilities.

During the first quarter of 2006 Galleon accrued \$125,000 of Alberta Royalty Tax credits (ARTC). For 2007 the ARTC program has been discontinued, therefore no ARTC is included in the first quarter 2007 results.

OPERATING COSTS

<i>Three months ended March 31</i>	<i>Production %</i>	<i>2007 Operating Costs %</i>	<i>Operating Costs \$/BOE</i>
Puskwa	13	5	3.47
Dawson Montney gas	24	11	4.27
Eaglesham	13	8	5.58
Dawson	26	30	10.28
Edam and other heavy oil	17	37	18.85
Calais	4	4	7.27
Other	3	5	13.84
	100	100	8.86

<i>Three months ended March 31</i>	<i>Production %</i>	<i>2006 Operating Costs %</i>	<i>Operating Costs \$/BOE</i>
Puskwa	2	1	2.59
Dawson Montney gas	7	6	8.29
Eaglesham	–	–	–
Dawson	50	38	6.93
Edam and other heavy oil	18	40	19.62
Calais	17	8	4.70
Other	6	7	12.14
	100	100	9.12

Operating costs were \$9.5 million or \$8.86/BOE for the first quarter of 2007 compared to \$7.1 million or \$9.12/BOE for the same period of the prior year. Galleon's operating costs per barrel of oil equivalent excluding the heavy oil was \$6.73/BOE for the first quarter of 2007. Operating costs in Galleon's key areas of Puskwa, Dawson Montney gas, and Eaglesham remain low and below the corporate average due to control of the facilities in

those areas. Sufficient capacity exists at Galleon's facilities to accommodate planned production increases. It is therefore anticipated that production additions in the key areas will be brought on stream at rates similar to those experienced during the first quarter of 2007. It is anticipated that production increases in Galleon's key areas will lower the corporate average operating costs per barrel of oil equivalent.

GENERAL AND ADMINISTRATION EXPENSES

<i>Three months ended March 31 (\$000s)</i>		<i>2007 \$/BOE</i>		<i>2006 \$/BOE</i>
Gross	2,532	2.36	1,959	2.53
Capitalized overhead	(132)	(0.12)	(100)	(0.13)
Overhead recoveries	(1,136)	(1.06)	(699)	(0.90)
	1,264	1.18	1,160	1.50

Net general and administrative (G&A) expenses of \$1.18/BOE for the first quarter of 2007 decreased 21% compared to the same period of the previous year. The decrease is a result of higher production volumes and increased operating activity generating higher operating recoveries. While gross G&A expenses have increased 29% with the growth of the Corporation, gross G&A expenses per barrel of oil equivalent have decreased by 7%. This is indicative of the efficiency of Galleon's growth.

For the three months ended March 31, 2007 G&A expenses by category were: salary and employee – 49%, office – 19%, consulting – 9%, computer – 7%, shareholder costs – 7%, audit, engineering and legal – 5%, and corporate – 4%.

INTEREST

Interest expense of \$2.2 million for the three months ended March 31, 2007 was higher than \$0.7 million in the same period of the prior year due to increased average debt levels and higher interest rates. Subsequent to March 31, 2007 Galleon closed an equity offering for gross proceeds of \$30 million. The funds will initially be used to reduce Galleon's outstanding debt. Galleon monitors its debt levels in relation to equity, and as a ratio of expected annual funds from operating activities.

STOCK BASED COMPENSATION

Stock based compensation was a non-cash expense of \$1.9 million for the first quarter of 2007 compared to \$1.3 million in the same quarter of the prior year. The increase was due to a greater number of options outstanding. During the quarter 250,000 stock options were granted to employees at an average exercise price of \$15.48 and had fair values of between \$4.90 and \$5.62 per option.

At March 31, 2007, 5,374,325 stock options were outstanding at an average exercise price of \$10.72.

DEPLETION, DEPRECIATION AND ACCRETION

Depletion and depreciation ("D&D") charges were \$22.0 million or \$20.58/BOE for the three months ended March 31, 2007 compared to \$12.8 million or \$16.47/BOE for the same period of the prior year. The D&D rate increase was due to significant production facility investments in the second half of 2006 and the increase in future development costs associated with the development of the Montney gas and Puskwa oil projects. Reserve additions for the first quarter of 2007 were estimated internally.

Capital expenditures of \$78.3 million (\$39.2 million – March 31, 2006) related to undeveloped land, seismic, and equipment inventory have been excluded from the depletion and depreciation calculation and \$84.4 million (\$52.0 million – March 31, 2006) of future development costs have been added.

Accretion expense on the Corporation's asset retirement obligation was \$317,000 for the first quarter of 2007 compared to \$144,000 in the same quarter of the prior year. Accretion expense increased due to a greater asset retirement obligation which is driven by the number of wells and facilities in which Galleon has an interest. For the quarter, \$980,000 of asset retirement liabilities were added due to the acquisition of oil and gas assets and \$347,000 of obligations were settled.

CAPITAL AND FUTURE TAXES

The current tax provision of \$220,000 for the first quarter was comprised of Saskatchewan capital and resource taxes, as was the provision for the first quarter of 2006. The provision is calculated based on revenues earned in Saskatchewan. It is not expected that Galleon will pay any income taxes in 2007.

The provision for future income taxes was \$2.5 million for the first quarter of 2007 compared to \$2.1 million for the first quarter of the prior year. The increase in future taxes was a result of higher net earnings before taxes during the period.

CAPITAL EXPENDITURES

(\$000s)

Property & equipment balance at December 31, 2006	577,758
Additions to property and equipment	61,934
Change in equipment inventory	(725)
Acquisition of property and equipment	29,870
Asset retirement obligation acquired	980
Asset retirement obligation incurred	792
Depletion and depreciation	(22,022)
Property & equipment balance at March 31, 2007	648,587

Three months ended March 31

(\$000s)

		2007		2006
		%		%
Land	3,633	6	6,728	10
Geological and geophysical	2,930	5	12,322	19
Drilling and completion	40,553	66	26,110	40
Plant and facilities	14,048	23	20,135	31
Other assets	45	—	(133)	—
Exploration and Development Expenditures	61,209	100	65,162	100

Capital expenditures during the first quarter of 2007 included the cash consideration of \$28.7 million for the acquisition of oil and gas properties in the Dawson area. The table above shows \$29.9 million of acquired properties and \$1.0 million of acquired asset retirement obligations relating to this acquisition. The difference between the cash consideration of \$28.7 million and \$30.9 million added to the property and equipment balance relates to the allocation of the purchase price reflecting related asset retirement obligation, future income taxes, and goodwill. See Note 3 to the consolidated financial statements for further details.

Exploration and development expenditures during the first quarter of 2007 were \$61.9 million, less \$0.7 million of equipment inventory purchased in previous quarters, for net expenditures of \$61.2 million. Drilling and completions expenditures comprised 66% of exploration and development activity. Galleon drilled 30 wells and cased 26 (23.8 net) for a success rate of 87%. Galleon completed 36 (32.4 net) wells during the quarter.

Facilities expenditures comprised 23% of activity, and included the construction of pipelines and tie-in of wells. Land and seismic expenditures were incurred to expand Galleon's key areas and initiate exploration activity in new areas. Management has established a capital budget of between \$170 to \$220 million for 2007.

LIQUIDITY AND CAPITAL RESOURCES

Three months ended March 31
(\$000s)

	<i>2007</i>	<i>2006</i>
Bank debt	189,414	60,086
Working capital deficiency	21,096	26,219
Total net debt	210,510	86,305

FUNDING OF CAPITAL PROGRAM

Three months ended March 31
(\$000s)

	<i>2007</i>	<i>2006</i>
Issuance of shares, net of costs	796	53,486
Funds from operations	30,170	18,047
Change in bank debt	66,418	(15,215)
Change in working capital and other	(7,469)	8,845
	89,915	65,163

During the quarter option exercises of \$0.8 million, funds from operations of \$30.2 million, and an additional \$58.9 million in bank debt and working capital were used to fund \$89.9 million of acquisition and exploration and development expenditures.

At March 31, 2007, the Corporation has \$180 million extendible revolving term credit facilities with a syndicate of Canadian chartered banks and a \$28.5 million non-revolving credit facility with a Canadian chartered bank. The facilities are secured by a first floating charge demand debenture in the amount of \$500 million over property and equipment of the Corporation. At March 31, 2007, \$189.4 million was drawn on the credit facilities.

Subsequent to March 31, 2007 the banks renewed Galleon's \$180 million extendible revolving term credit facility and added an additional \$30 million revolving facility for acquisition purposes.

On April 19, 2007 the Corporation closed an equity offering of flow-through Class A shares for total proceeds of \$30.0 million. For further information see note 12 b) to the financial statements. It is expected that the Corporation's capital expenditures and operating activities for 2007 will be funded from this offering, the Corporation's current bank line, and from funds from operations.

COMMITMENTS

Drilling Rig

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

<i>Year</i>	<i>Amount (\$000s)</i>
2007	2,660
2008	4,554
2009	1,894

Minimum Lease Payments

At March 31, 2007 the Corporation has committed to future minimum payments under operating leases that cover office space as follows:

<i>Year</i>	<i>Amount (\$000s)</i>
2007	355
2008	280

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

Flow-through Shares

In connection with the Corporation's flow-through share offerings in 2006, Galleon is obligated to spend \$40.0 million on qualifying exploration expenses prior to December 31, 2007. As at March 31, 2007, it is estimated that \$4.2 million remains to be incurred.

FINANCIAL INSTRUMENTS

As a means of managing the risk of commodity price volatility, in December 2006, Galleon entered into a financial contract with a Canadian chartered bank, setting a floor price of USD WTI \$61.75/Bbl and a ceiling of USD WTI \$70.00/Bbl on 1,000 Bbl per day of crude oil for the period January 1, 2007 to December 31, 2007. The contract will protect base line revenues if the WTI crude oil benchmark falls below \$61.75/Bbl. The contract is a costless collar, therefore no premium was paid by Galleon upon entering into the contract. The contract will be settled monthly based on the average USD WTI benchmark price. Galleon will receive payments on the contract if the benchmark USD WTI price falls below \$61.75/Bbl and will be required to make payments if the price rises above \$70.00/Bbl. Galleon has recognized this financial instrument on its balance sheet at fair value, and is accounting for the instrument using mark to market accounting. As at March 31, 2007 Galleon had realized gains of \$373,000 and an unrealized gain of \$479,000 related to this derivative instrument.

BUSINESS RISKS

Environmental Regulation and Risk

All phases of the oil and natural gas business present environmental risks and hazards and are subject to environmental regulation pursuant to a variety of federal, provincial and local laws and regulations. Compliance with such legislation can require significant expenditures and a breach may result in the imposition of fines and penalties, some of which may be material. Environmental legislation is evolving in a manner expected to result in stricter standards and enforcement, larger fines and liability and potentially increased capital expenditures and operating costs. In 2002, the Government of Canada ratified the Kyoto Protocol (the "Protocol"), which calls for Canada to reduce its greenhouse gas emissions to specified levels. There has been much public debate with respect to Canada's ability to meet these targets and the Government's strategy or alternative strategies with respect to climate change and the control of greenhouse gases. Implementation of strategies for reducing greenhouse gases whether to meet the limits required by the Protocol or as otherwise determined, could have a material impact on the nature of oil and natural gas operations, including those of the Corporation.

The Federal Government released on April 26, 2007, its Action Plan to Reduce Greenhouse Gases and Air Pollution (the "Action Plan"), also known as ecoACTION and which includes the Regulatory Framework for Air Emissions. This Action Plan covers not only large industry, but regulates the fuel efficiency of vehicles and the strengthening of energy standards for a number of energy-using products. Regarding large industry and industry related projects the Government's Action Plan intends to achieve the following: (i) an absolute reduction of 150 megatonnes in greenhouse gas emissions by 2020 by imposing mandatory targets; and (ii) air pollution from industry is to be cut in half by 2015 by setting certain targets. New facilities using cleaner fuels and technologies will have a grace period of three years. In order to facilitate the companies' compliance of the Action Plan's requirements, while at the same time allowing them to be cost-effective, innovative and adopt cleaner technologies, certain options are provided. These are: (i) in-house reductions; (ii) contributions to technology funds; (iii) trading of emissions with below-target emission companies; (iv) offsets; and (v) access to Kyoto's Clean Development Mechanism.

On March 8, 2007, the Alberta Government introduced Bill 3, the Climate Change and Emissions Management Amendment Act, which intends to reduce greenhouse gas emission intensity from large industries. Bill 3 states that facilities emitting more than 100,000 tonnes of greenhouse gases a year must reduce their emissions intensity by 12% starting July 1, 2007; if such reduction is not initially possible the companies owning the large emitting facilities will be required to pay \$15 per tonne for every tonne above the 12% target. These payments will be deposited into an Alberta-based technology fund that will be used to develop infrastructure to reduce emissions or to support research into innovative climate change solutions. As an alternate option, large emitters can invest in projects outside of their operations that reduce or offset emissions on their behalf, provided that these projects are based in Alberta. Prior to investing, the offset reductions, offered by a prospective operation, must be verified by a third party to ensure that the emission reductions are real.

Given the evolving nature of the debate related to climate change and the control of greenhouse gases and resulting requirements, it is not possible to predict the impact of those requirements on the Corporation and its operations and financial condition.

Review of Alberta Royalty and Tax Regime

On February 16, 2007, the Alberta Government announced that a review of the province's royalty and tax regime (including income tax and freehold mineral rights tax) pertaining to oil and gas resources, including oil sands, conventional oil and gas and coalbed methane, will be conducted by a panel of experts, with the assistance of individual Albertans and key stakeholders. The review panel is to produce a final report that will be presented to the Minister of Finance by August 31, 2007.

CHANGES IN ACCOUNTING POLICIES

Financial Instruments

Galleon adopted the following new Handbook Sections effective January 1, 2007:

- Section 1530, "Comprehensive Income";
- Section 3251, "Equity";
- Section 3855, "Financial Instruments- Recognition and Measurement";
- Section 3861, "Financial Instruments- Disclosure and Presentation";
- Section 3865, "Hedges"

These new accounting standards provide requirements for the recognition and measurement of financial instruments and the use of hedge accounting. The standards have been adopted prospectively and the comparative interim consolidated financial statements have not been restated.

Accounting Changes

Effective January 1, 2007 the Corporation adopted the revised recommendations of CICA Section 1506, "Accounting Changes". These standards are effective for all changes in accounting policies, changes in accounting estimates and corrections of prior period errors initiated in periods beginning on or after January 1, 2007. There was no effect on the current or prior period financial statements as a result of this adoption.

CONTROLS AND PROCEDURES OVER FINANCIAL REPORTING

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

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

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

SHARE INFORMATION

The following table summarizes the outstanding shares of Galleon Energy as of March 31:

	2007	2006 ¹
Class A shares outstanding		
Basic	57,898,077	51,874,815
Diluted ²	63,272,402	56,144,190
Class B shares outstanding	922,500	922,500
Class A shares issuable on conversion of Class B shares ³	545,535	406,925

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

² Includes outstanding options of 5,374,325 (March 31, 2006 – 4,269,375).

³ Assumes a conversion at the March 31, 2007 closing price of \$16.91 per Class A share (March 31, 2005 - \$22.67). The actual conversion rate varies based on a formula related to the trading price of the Class A shares.

At March 31, 2007, the market value of Galleon's class A and class B shares was \$987.3 million based on the March 31, 2007 closing price of \$16.91 per class A share and \$8.95 per class B share. As of May 14, 2007, the number of class A shares, class B shares, and options outstanding is 59,387,077, 922,500, and 5,491,825 respectively.

ADDITIONAL INFORMATION

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

OUTLOOK

Looking forward to Q2 and Q3 2007:

- Expansion of the waterflood/GPP areas at Puskwa;
- Production increases between 5-15% per quarter on average;
- Additional consolidation acquisitions are being considered; and
- Update key high impact exploration drilling projects in several new areas and at Puskwa.

Estimated 2007 exit production is targeted between 17,000 and 21,000 BOE/d (based on obtaining regulatory approvals removing restrictions on production at Puskwa during 2007).

Galleon has a dominant land position that will sustain strong multiyear growth, repeatable low risk drilling opportunities and control of infrastructure in its operating areas. Galleon has a portfolio of 3D defined high impact exploration projects, access to over 1 million gross acres land and has an inventory of over 500 locations. Galleon plans to drill approximately 125 wells in 2007 based on a capital program of \$170 to \$220 million.

QUARTERLY HIGHLIGHTS

	2007 <i>Q1</i>	<i>Q4</i>	<i>Q3</i>	2006 <i>Q2</i>	<i>Q1</i>	2005 <i>Q4</i>	<i>Q3</i>	<i>Q2</i>
PRODUCTION								
Light oil (Bbl/d)	3,127	2,419	1,823	1,753	1,859	2,271	2,213	1,393
Heavy oil (Bbl/d)	2,081	2,100	1,984	1,705	1,580	1,135	1,205	594
Natural Gas (Mcf/d)	38,845	36,733	33,068	30,014	30,445	32,212	27,452	21,813
Liquids (Bbl/d)	206	230	102	100	93	99	71	21
BOE/d	11,888	10,869	9,420	8,560	8,606	8,874	8,064	5,643
Total BOE produced	1,069,915	999,982	866,646	778,992	774,578	816,420	741,917	513,535
Daily BOE of production per million Class A shares – basic ¹	206	191	172	165	173	186	169	130
PRICES (net of transportation)								
Light oil (\$/Bbl)	63.24	61.12	75.65	75.63	65.66	67.44	73.64	65.35
Heavy oil (\$/Bbl)	36.55	31.16	47.01	42.69	24.71	29.31	48.19	32.21
Crude oil (\$/Bbl)	52.57	47.19	53.35	59.39	46.78	54.73	62.54	54.86
Natural Gas (\$/Mcf)	7.36	6.84	5.58	5.97	7.36	11.16	9.13	6.99
NGLs (\$/Bbl)	56.64	56.02	69.83	65.71	57.62	58.84	56.64	53.94
PER BOE (\$)								
Revenues	49.51	45.26	46.06	46.88	46.77	63.68	59.99	48.18
Royalties, net of ARTC & GCA	(7.84)	(6.02)	(7.20)	(4.34)	(10.18)	(15.01)	(11.69)	(11.11)
Transportation costs	(1.47)	(1.37)	(1.25)	(1.22)	(1.43)	(1.48)	(1.64)	(1.37)
Operating costs	(8.86)	(9.65)	(10.66)	(9.91)	(9.12)	(7.73)	(6.98)	(5.31)
Net	31.34	28.22	26.95	31.41	26.04	39.46	39.68	30.39
Other revenue	-	-	-	-	-	-	-	0.03
G&A	(1.18)	(2.67)	(0.80)	(1.37)	(1.50)	(1.82)	(1.58)	(2.01)
Interest	(2.10)	(1.49)	(1.39)	(1.41)	(0.95)	(0.91)	(0.90)	(1.09)
Capital and other taxes	(0.21)	(0.21)	(0.33)	(0.30)	(0.29)	(0.40)	(0.38)	(0.49)
Realized gain on financial derivative	0.35	-	-	-	-	-	-	-
Funds from operations²	28.20	23.85	24.43	28.33	23.30	36.33	36.82	26.83

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

² See “Non-GAAP Measurements”

QUARTERLY FINANCIAL HIGHLIGHTS (unaudited)

	<i>2007</i> <i>Q1</i>	<i>Q4</i>	<i>2006</i> <i>Q3</i>	<i>Q2</i>
FINANCIAL (\$000s)				
Revenues	52,974	45,264	39,921	36,517
Operating costs	(9,478)	(9,651)	(9,243)	(7,716)
General & Administrative expenses	(1,264)	(2,670)	(692)	(1,068)
Interest expense	(2,246)	(1,487)	(1,202)	(1,098)
Funds from operations ²	30,170	23,857	21,178	22,069
Per share, basic ^{1, 2}	0.52	0.42	0.39	0.42
Per share, diluted ^{1, 2}	0.50	0.40	0.37	0.40
EARNINGS	3,921	1,906	2,196	7,985
Per share, basic ¹	0.07	0.03	0.04	0.15
Per share, diluted ¹	0.07	0.03	0.04	0.15
Total assets	692,749	614,565	540,980	477,967
Weighted average outstanding Class A shares-basic ¹	57,800,899	56,761,415	54,854,334	52,003,462
Weighted average outstanding Class A shares-diluted ¹	59,947,494	59,234,229	57,447,555	54,838,259

QUARTERLY FINANCIAL HIGHLIGHTS (unaudited)

	2006 <i>Q1</i>	<i>Q4</i>	2005 <i>Q3</i>	<i>Q2</i>
FINANCIAL (\$000s)				
Revenues	36,230	51,989	44,506	24,743
Operating costs	(7,065)	(6,311)	(5,179)	(2,727)
G&A	(1,160)	(1,489)	(1,171)	(1,030)
Interest	(740)	(742)	(668)	(558)
Funds from operations ²	18,047	29,662	27,325	13,782
Per share, basic ^{1, 2}	0.36	0.62	0.57	0.32
Per share, diluted ^{1, 2}	0.35	0.59	0.54	0.30
EARNINGS	1,740	9,324	9,112	689
Per share, basic ¹	0.04	0.20	0.19	0.02
Per share, diluted ¹	0.03	0.18	0.18	0.02
Total assets	399,269	352,619	312,523	290,883
Weighted average outstanding Class A shares-basic ¹	49,661,598	47,698,056	47,640,620	43,467,068
Weighted average outstanding Class A shares-diluted ¹	52,220,178	50,599,782	50,268,840	45,474,116

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

² See "Non-GAAP Measurements".

CONSOLIDATED BALANCE SHEETS

(\$000s)

March 31, 2007
(unaudited)

December 31, 2006

ASSETS

CURRENT

Accounts receivable	26,069	24,639
Deposits and prepaid expenses	1,411	1,839
Fair value of financial derivative (note 11)	669	190
	28,149	26,668
Goodwill (note 3)	16,013	10,139
Property and equipment (notes 3,4 and 6)	648,587	577,758
	692,749	614,565

LIABILITIES

CURRENT

Accounts payable and accrued liabilities	48,576	54,695
Bank loan (note 6)	189,414	122,996
	237,990	177,691
Asset retirement obligation (note 5)	23,174	21,432
Future income taxes (note 8)	53,543	32,287
	314,707	231,410

SHAREHOLDERS' EQUITY

Share capital (note 7)	329,234	339,869
Contributed surplus (note 7)	13,220	11,619
Retained earnings	35,588	31,667
	378,042	383,155
	692,749	614,565

See accompanying notes

CONSOLIDATED STATEMENTS OF EARNINGS

COMPREHENSIVE INCOME AND RETAINED EARNINGS

Three months ended March 31

(\$000s, except per share amounts) (unaudited)

	2007	2006
REVENUE		
Petroleum and natural gas revenue	52,974	36,230
Royalties, net of ARTC and GCA	(8,382)	(7,886)
	44,592	28,344
EXPENSES		
Operating	9,478	7,065
Transportation	1,587	1,106
General and administration	1,264	1,160
Interest	2,246	740
Stock-based compensation (note 7)	1,861	1,292
Accretion	317	144
Depletion and depreciation	22,022	12,760
Realized gain on financial derivative (note 11)	(373)	–
Unrealized gain on financial derivative (note 11)	(479)	–
	37,923	24,267
EARNINGS BEFORE TAXES		
	6,669	4,077
Income taxes		
Capital and other taxes	220	226
Future income taxes	2,528	2,111
	2,748	2,337
NET EARNINGS AND COMPREHENSIVE INCOME		
	3,921	1,740
RETAINED EARNINGS, BEGINNING OF PERIOD		
	31,667	17,841
RETAINED EARNINGS, END OF PERIOD		
	35,588	19,581
NET EARNINGS PER SHARE (note 7)		
Basic	\$0.07	\$0.04
Diluted	\$0.07	\$0.03
Weighted average Class A shares – basic	57,800,899	49,661,598
– diluted	59,947,494	52,220,178

See accompanying notes

CONSOLIDATED STATEMENTS OF CASH FLOWS

Three months ended March 31
(\$000s) (unaudited)

	2007	2006
Cash provided by (used in):		
OPERATING ACTIVITIES		
Net earnings	3,921	1,740
Items not requiring cash:		
Future income taxes	2,528	2,111
Depletion and depreciation	22,022	12,760
Accretion	317	144
Stock-based compensation	1,861	1,292
Unrealized gain on financial derivative	(479)	—
Abandonment costs	(347)	—
Change in non-cash working capital	(2,063)	7,442
	27,760	25,489
FINANCING ACTIVITIES		
Issue of common shares	800	56,945
Share issue costs	(4)	(3,459)
Bank loan	66,418	(15,215)
	67,214	38,271
INVESTING ACTIVITIES		
Additions to equipment inventory		(1,389)
Additions to oil and gas properties	(61,209)	(65,162)
Acquisition of oil and gas properties (note 3)	(28,706)	(1)
Change in non-cash working capital	(5,059)	2,792
	(94,974)	(63,760)
Change in cash	—	—
Cash, beginning and end of period	—	—
SUPPLEMENTARY INFORMATION		
Cash interest paid	2,235	740
Cash taxes paid	165	226
<i>See accompanying notes</i>		

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the three month periods ended March 31, 2007 and 2006 (unaudited)

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

1 ACCOUNTING POLICIES

Nature of Business and Basis of Presentation

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

These unaudited interim consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"), and follow the same accounting policies as the financial statements for the year ended December 31, 2006, except as noted below. These notes do not include all disclosures required in annual financial statements and are incremental to, and should be read in conjunction with, the audited financial statements for the year ended December 31, 2006.

2 CHANGES IN SIGNIFICANT ACCOUNTING POLICIES

As of January 1, 2007, Galleon adopted the Canadian Institute of Chartered Accountants ("CICA") Handbook Section 1506 "Accounting Changes;" Section 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 1506, "Accounting Changes," provides expanded disclosures for changes in accounting policies, accounting estimates and corrections of errors. Under the new standard, accounting changes should be applied retrospectively unless otherwise permitted or where impracticable to determine. As well, voluntary changes in accounting policy are made only when required by a primary source of GAAP or the change results in more relevant and reliable information.

CICA Section 1530 introduces a new requirement to temporarily present certain gains and losses from changes in fair value outside net income.

It includes unrealized gains and losses, such as: changes in the currency translation adjustment relating to self-sustaining foreign operations; unrealized gains or losses on available-for-sale investments; and the effective portion of gains or losses on derivatives designated as cash flow hedges. The application of this revised standard did not result in comprehensive income being different from the net earnings for the periods presented.

CICA Section 3855 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, or other financial liabilities. Initial and subsequent measurement and recognition of changes in the value of financial instruments depends on their initial classification. All derivative financial instruments are classified as held for trading financial instruments and are measured at fair value, even when they are part of a hedging relationship. All gains and losses are included in net earnings in the period in which they arise. The application of CICA Section 3855 did not have an impact on Galleon's consolidated financial statements.

CICA Section 3865 provides alternative treatments to Section 3855 for entities which choose to designate qualifying transactions as hedges for accounting purposes. It replaces and expands on Accounting Guideline 13 "Hedging Relationships", and the hedging guidance in Section 1650 "Foreign Currency Translation" by specifying how hedge accounting is applied and what disclosures are necessary when it is applied. Galleon has not designated its derivative instrument as a hedge, therefore this section does not have an impact on Galleon's consolidated financial statements.

In addition, the Company has assessed new and revised accounting pronouncements that have been issued that are not yet effective and determined that the following may have a significant impact on the Company:

As of January 1, 2008, Galleon will be required to adopt two new CICA standards, Section 3862 "Financial Instruments – Disclosures" and Section 3863 "Financial Instruments – Presentation," which will replace Section 3861 "Financial Instruments – Disclosure and Presentation." The new disclosure standard increases the emphasis on the risks associated with both recognized and unrecognized financial instruments and how those risks are managed.

The new presentation standard carries forward the former presentation requirements. The new financial instruments presentation and disclosure requirements were issued in December 2006 and the Company is assessing the impact on its consolidated financial statements.

As of January 1, 2008, Galleon will be required to adopt Section 1535 "Capital Disclosures," which will require companies to disclose their objectives, policies and processes for managing capital. In addition, disclosures are to include whether companies have complied with externally imposed capital requirements. The new capital disclosure requirements were issued in December 2006 and the Company is assessing the impact on its consolidated financial statements.

In January 2006, the CICA Accounting Standards Board ("AcSB") adopted a strategic plan for the direction of accounting standards in Canada. As part of that plan, accounting standards in Canada for public companies are expected to converge with International Financial Reporting Standards ("IFRS") by the end of 2011. The Company continues to monitor and assess the impact of convergence of Canadian GAAP and IFRS.

3 ACQUISITION OF PARTNERSHIP

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

Allocation of Purchase Price	\$
Property and equipment	30,854
Goodwill	5,874
Asset retirement obligation	(980)
Future income taxes	(7,037)
	<u>28,711</u>

Calculation of Purchase Price	
Cash for purchase of interest	28,664
Transaction costs	47
	<u>28,711</u>

4 PROPERTY AND EQUIPMENT

As at March 31, 2007, \$78.3 million (March 31, 2006 - \$39.2 million) of undeveloped land, seismic and equipment inventory have been excluded from and \$84.4 million (March 31, 2006 - \$52.0 million) in future

development costs have been added into the full cost pool for depletion purposes. For the three months ended March 31, 2007, \$132,000 (March 31, 2006 - \$100,000) of exploration salaries have been capitalized.

<i>As at March 31, 2007</i>	<i>Cost</i> \$	<i>Accumulated depletion and depreciation</i> \$	<i>Net book value</i> \$
Petroleum and natural gas properties & equipment	781,884	(135,595)	646,289
Equipment inventory	1,811	-	1,811
Office furniture and equipment	716	(229)	487
	784,411	(135,824)	648,587

<i>As at December 31, 2006</i>	<i>Cost</i> \$	<i>Accumulated depletion and depreciation</i> \$	<i>Net book value</i> \$
Petroleum and natural gas properties & equipment	688,354	(113,605)	574,749
Equipment inventory	2,536	-	2,536
Office furniture and equipment	671	(198)	473
	691,561	(113,803)	577,758

5 ASSET RETIREMENT OBLIGATION

The Corporation's asset retirement obligation results from net ownership interests in petroleum and natural gas assets including well sites, gathering systems and processing facilities. The Corporation estimates the total

undiscounted amount of cash flows required to settle its asset retirement obligation is approximately \$51.9 million, which will be incurred over the next 19 years. Credit adjusted risk free rates of 5% and 8% and an inflation rate of 2% were used to calculate the fair value of the asset retirement obligation.

	<i>Three months ended March 31, 2007</i> \$	<i>Year ended December 31, 2006</i> \$
Balance, beginning of period	21,432	11,186
Accretion expense	317	631
Liabilities incurred	792	6,149
Liabilities acquired (note 3)	980	1,200
Revision of liabilities	-	2,880
Settlement of liabilities	(347)	(614)
Balance, end of period	23,174	21,432

6 AVAILABLE CREDIT FACILITY

The Corporation has a \$180 million extendible revolving term credit facility in place with a bank syndicate and a \$28.5 million non-revolving credit facility with a Canadian chartered bank. The facilities bear interest at rates ranging from the bank's prime rate to prime plus 0.75% per annum based on the Corporation's debt to cash flow ratio. The Corporation may also borrow at the prevailing Banker's Acceptance rate. The borrowing base is subject to semi-annual review, the next review date being April 30, 2007 (see note 12). Collateral for the facilities consists of a demand debenture for \$500 million secured by a first floating charge over all of the property and equipment of the Corporation.

7 SHARE CAPITAL

Authorized

Unlimited number of preferred shares with no par value

Unlimited number of voting Class A shares with no par value

Unlimited number of voting Class B shares with no par value, convertible (at the option of the Corporation) at any time after December 31, 2006 and before December 31, 2008, into Class A shares. The conversion factor is calculated by dividing \$10 by the greater of \$1 and the then current market price of Class A shares. If conversion has not occurred by the close of business on December 31, 2008, the Class B shares become convertible (at the option of the shareholder) into Class A shares on the same basis. Effective February 1, 2009, all remaining Class B shares will be deemed to be converted to Class A shares.

Issued and outstanding

	<i>Number of Shares</i>	<i>Amount \$</i>
CLASS A SHARES		
Balance at December 31, 2005 (a)	47,740,326	169,256
Issued for cash (b)	7,415,700	135,196
Issue of flow-through shares for cash (b)	1,580,000	40,046
Issued for cash on exercise of stock options	976,051	3,058
Tax effect of flow through shares	–	(6,800)
Share issue costs, net of tax of \$3,148	–	(6,944)
Transfer from contributed surplus	–	850
Balance at December 31, 2006	57,712,077	334,662
Issued for cash on exercise of stock options	186,000	800
Tax effect of flow through shares	–	(11,692)
Share issue costs, net of tax of \$1	–	(3)
Transfer from contributed surplus	–	260
Balance at March 31, 2007	57,898,077	324,027
CLASS B SHARES		
Balance at March 31, 2007 and December 31, 2006	922,500	5,207
Total share capital at March 31, 2007	58,820,577	329,234

- a) On June 7, 2006, the shareholders of the Corporation approved a three-for-two Class A share split. The number of Class A shares above has been restated to reflect the share split.
- b) On February 14, 2006, the Corporation issued 3,405,000 Class A shares at \$16.17 per share by way of private placement for gross proceeds of \$55.0 million.

On July 25, 2006, the Corporation issued 2,985,000 Class A shares at \$20.15 per share and 780,000 flow-through Class A shares at \$25.70 per share pursuant to a public offering for gross proceeds of \$80.2 million.

On November 16, 2006 the Corporation issued 1,025,700 Class A shares at a price of \$19.50 per share and 800,000 flow-through Class A shares at a price of \$25.00 per share pursuant to a public offering for gross proceeds of \$40.0 million.

Share options

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

	<i>Three months ended March 31, 2007</i>	<i>Year ended December 31, 2006</i>
	\$	\$
Contributed surplus, beginning of period	11,619	4,756
Stock based compensation expense	1,861	7,713
Transfer to share capital on exercise of options	(260)	(850)
Contributed surplus, end of period	13,220	11,619

The fair value of options granted was estimated at the date of grant using a Black-Scholes Option Pricing Model with the following assumptions: risk-free interest rates of 2.00-3.28%; dividend yield of 0%; volatility factors of the market price of the Corporation's common shares of 40-46%; and, an average expected life of the options of 3 years.

	<i>Number of Shares⁽¹⁾</i>	<i>Weighted Average Exercise Price⁽¹⁾</i>
		\$
Outstanding, December 31, 2005	4,638,876	5.63
Granted	1,647,500	19.13
Exercised	(976,051)	(3.13)
Outstanding, December 31, 2006	5,310,325	10.28
Granted	250,000	15.48
Exercised	(186,000)	(4.30)
Outstanding, March 31, 2007	5,374,325	10.72

(1) Restated to reflect the three-for-two Class A share split in June 2006.

Earnings per share

The Corporation utilizes the treasury stock method in the determination of diluted per share amounts. Under this method, the diluted weighted average number of shares is calculated assuming the proceeds that arise from the exercise of outstanding and in the money options are used to purchase common shares of the Corporation at their average market price for the period. For the three months ended March 31, 2007, 1,460,000 options have been excluded from the diluted earnings per share calculation as they are anti-dilutive. The diluted weighted average number of Class A shares outstanding after deemed conversion of the Class B shares is 60,516,002 (March 31, 2006 – 52,751,549). The prior year amounts have been restated to reflect the three-for-two Class A share split in June 2006.

8 INCOME TAXES

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

	<i>March 31, 2007</i>	<i>December 31, 2006</i>
	\$	\$
Property and equipment	55,002	38,740
ACRI benefit	(870)	(870)
Share issue costs	(3,721)	(4,031)
Asset retirement obligation	(278)	(286)
Non-capital losses	(5,702)	(1,321)
Partnership income tax deferral	8,916	–
Financial derivative	196	55
Future income tax liability	53,543	32,287

9 COMMITMENTS

Drilling Rig

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

<i>Year</i>	<i>Amount</i> \$
2007	2,660
2008	4,554
2009	1,894

10 COMMODITY CONTRACTS

The Corporation has the following fixed price physical contracts in place:

Natural Gas:

April 1, 2007 – October 31, 2007	5,000 GJ/day	CDN \$6.64 GJ
April 1, 2007 – October 31, 2007	5,000 GJ/day	CDN \$6.50 - \$8.12 GJ
April 1, 2007 – October 31, 2007	5,000 GJ/day	CDN \$7.50 GJ

The Corporation's fixed price physical contracts qualify as a non-financial derivative for accounting purposes. As the above physical contracts were entered into for the purpose of selling the Corporation's natural gas production and were based on Galleon's expected natural gas production volumes, the contracts are considered to be within the scope of normal sales contracts for accounting purposes.

Minimum Lease Payments:

At March 31, 2007 the Corporation has committed to future minimum payments under operating leases that cover office space as follows:

<i>Year</i>	<i>Amount</i> \$
2007	355
2008	280

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

Flow-through Shares:

In connection with the Corporation's flow-through share offerings in 2006, Galleon is obligated to spend \$40.0 million on qualifying exploration expenses prior to December 31, 2007. As at March 31, 2007, it is estimated that \$4.2 million remains to be incurred.

As such, natural gas production sold based on physical contracts is included within the petroleum and natural gas revenue caption in the statement of earnings.

11 FINANCIAL INSTRUMENTS

Fair value of financial assets:

The Corporation's financial instruments recognized in the balance sheet consist of accounts receivable, accounts payable, bank loan and financial derivative ("financial instruments"). The fair value of these instruments, excluding the financial derivative, approximates their carrying amounts due to their short term nature or the indexed rate of interest on the bank loan. The fair value of the financial derivative is recognized on the balance sheet as described below.

Credit risk:

A substantial portion of the Corporation's accounts receivable are with customers in the energy industry and are subject to normal industry credit risk. Galleon generally grants unsecured credit but routinely assesses the financial strength of its customers.

Interest rate risk:

The Corporation is exposed to interest rate cash flow risk to the extent that changes in market interest rates will impact the Corporation's debts that have a floating interest rate.

Financial derivative contracts:

Galleon has entered into the following financial derivative contract for the purpose of protecting its funds generated from operations from the volatility of crude oil prices. For the three months ended March 31, 2007, the contract had a realized gain of \$373,000. As described in note 2, the Corporation recognizes the fair value of its financial derivatives on the

balance sheet each reporting period with the change in fair value recognized as an unrealized gain or loss on the statement of earnings. The fair value is based on quoted market prices. At March 31, 2007 the fair value was an asset of \$669,000, resulting in an unrealized gain for the three months ended March 31, 2007 of \$479,000.

The Corporation has the following costless collar financial derivative in place:

Crude Oil:

January 1, 2007 – December 31, 2007 1,000 Bbl/d WTI USD \$61.75-\$70.00/Bbl

12 SUBSEQUENT EVENTS

- a) Subsequent to March 31, 2007, the Corporation renewed its existing extendible revolving credit facility of \$180 million and added an additional \$30 million revolving facility for acquisition purposes.
- b) Subsequent to March 31, 2007 the Corporation closed a private placement of 1,481,500 flow-through Class A shares at a price of \$20.25 per share for total proceeds of \$30.0 million. Galleon is obligated to spend \$30.0 million on qualifying exploration expenses prior to December 31, 2008. Galleon will recognize the associated future income tax liability upon renunciation of the exploration expenses.

13 COMPARATIVE FIGURES

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

CORPORATE INFORMATION

HEAD OFFICE

500, 311 – 6th Avenue SW
Calgary, Alberta T2P 3H2

p (403) 261-6012

f (403) 262-5561

www.galleonenergy.com

BOARD OF DIRECTORS

John A. Brussa ^{2 3}

Glenn R. Carley, Executive Chairman²

Fred C. Coles ^{1 2}

William L. Cooke ^{1 3}

Brad R. Munro ¹

Steve Sugianto

¹ Member of the Audit and Reserves Committee

² Member of the Compensation Committee

³ Member of the Corporate Governance Committee

OFFICERS

Steve Sugianto, *President and Chief Executive Officer*

Glenn R. Carley, *Executive Chairman*

Shivon M. Crabtree, *VP Finance & Chief Financial Officer*

Tom Greschner, *VP Production*

Brent Lacey, *VP Exploration*

Dale Orton, *VP Engineering West*

Devin Sundstrom, *VP Engineering East*

C. Steven Cohen, *Secretary*

AUDITOR

Ernst & Young LLP

Calgary, Alberta

BANK

The Bank of Nova Scotia

Calgary, Alberta

ATB Financial

Calgary, Alberta

HSBC

Calgary, Alberta

TD Canada Trust

Calgary, Alberta

LEGAL COUNSEL

Burnet, Duckworth & Palmer LLP

Calgary, Alberta

EVALUATION ENGINEERS

DeGolyer and MacNaughton

Canada Limited

Calgary, Alberta

REGISTRAR AND TRANSFER AGENT

Valiant Trust Company

Calgary, Alberta

STOCK EXCHANGE LISTING

Toronto Exchange

Trading Symbols GO.A and GO.B

COMPANY DEFINITION

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

VOLUME REPORTING

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

FORWARD-LOOKING STATEMENT

Certain information regarding Galleon Energy Inc. including management’s assessment of future plans and operations, may constitute forward-looking statements under applicable securities laws and necessarily involve risks associated with oil and gas exploration, production, marketing and transportation such as loss of market, volatility of prices, currency fluctuations, imprecision of reserve estimates, environment risks, competition from other producers and ability to access sufficient capital from internal and external sources. As a consequence, actual results may differ materially from those anticipated in the forward-looking statements.



TSX: GO.A