

TETHYS PETROLEUM LIMITED
(formerly known as Tethys Petroleum Investments Limited)

Consolidated Balance Sheet *(unaudited)*

		As at	
		<u>June 30,</u>	<u>December 31,</u>
Note		<u>2008</u>	<u>2007</u>
(Expressed in 000's United States dollars)			
ASSETS			
Current Assets			
		58,903	26,692
		675	351
		586	219
		34	-
		237	790
		<u>60,435</u>	<u>28,052</u>
Non Current Assets			
		5,129	3,062
		443	318
		2,755	2,752
		47,195	37,472
		<u>55,522</u>	<u>43,604</u>
		<u>115,957</u>	<u>71,656</u>
LIABILITIES AND STOCKHOLDERS' EQUITY			
Current Liabilities			
		991	1,388
		804	-
		1,082	891
		<u>2,877</u>	<u>2,279</u>
Non Current Liabilities			
		4,310	-
		572	776
		729	661
		<u>5,611</u>	<u>1,437</u>
		<u>8,488</u>	<u>3,716</u>
Stockholders' equity			
		145,733	99,483
		5,807	3,527
		17,535	16,555
		(61,606)	(51,625)
		<u>107,469</u>	<u>67,940</u>
		<u>115,957</u>	<u>71,656</u>
		11	

See accompanying notes to these financial statements

TETHYS PETROLEUM LIMITED
(formerly known as Tethys Petroleum Investments Limited)

Consolidated Statement of Operations and Comprehensive Loss (unaudited)

	Note	For three months to		Year to Date	
		June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
		(Expressed in 000's United States dollars except share data)		(Expressed in 000's United States dollars except share data)	
Revenues Net of Royalties					
Oil and gas sales		1,566	-	2,997	-
		<u>1,566</u>	<u>-</u>	<u>2,997</u>	<u>-</u>
Expenses					
Operating		196	-	263	-
Selling, general and administrative		2,974	1,996	6,168	3,421
Stock based compensation	13	1,709	16,339	2,280	16,339
Depreciation, depletion and amortization		1,922	14	3,418	28
		<u>6,801</u>	<u>18,349</u>	<u>12,129</u>	<u>19,788</u>
Operating Loss		<u>(5,235)</u>	<u>(18,349)</u>	<u>(9,132)</u>	<u>(19,788)</u>
Other (Expense):					
Interest, net		124	(1,933)	291	(2,268)
Foreign exchange (losses)		(163)	(9)	(138)	(143)
Finance charges	13	-	-	(980)	(238)
Other		(6)	174	(22)	(2)
Total Other Income/(Expense)		<u>(45)</u>	<u>(1,768)</u>	<u>(849)</u>	<u>(2,651)</u>
Loss Before Income Taxes		<u>(5,280)</u>	<u>(20,117)</u>	<u>(9,981)</u>	<u>(22,439)</u>
Income taxes	12	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Net Loss and Comprehensive Loss for the period		<u><u>(5,280)</u></u>	<u><u>(20,117)</u></u>	<u><u>(9,981)</u></u>	<u><u>(22,439)</u></u>
Weighted average number of common shares outstanding	14	46,051,931	21,235,850	45,586,897	13,119,668
Basic and diluted loss per share		<u>(0.11)</u>	<u>(0.95)</u>	<u>(0.22)</u>	<u>(1.71)</u>

See accompanying notes to these financial statements

TETHYS PETROLEUM LIMITED
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Consolidated Statement of Cash Flows (unaudited)

Note	For three months to		Year to date	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
	(Expressed in 000's United States dollars)		(Expressed in 000's United States dollars)	
Operating activities:				
Net loss for the period	(5,280)	(20,117)	(9,981)	(22,439)
Items not affecting cash				
Stock based compensation	1,709	16,339	2,280	16,339
Accretion	17	-	33	-
Finance costs	-	-	980	-
Non-cash interest expense	-	1,816	-	2,108
Depreciation, depletion and amortization	1,922	14	3,418	28
Net change in non-cash working capital items				
Accounts Receivable	547	(1,053)	(367)	(1,355)
Other current assets	121	-	519	-
Prepayments	(110)	277	(324)	248
Accounts payable	(279)	759	(397)	83
Accrued and other liabilities	337	1,496	191	1,655
Net cash used in operating activities	<u>(1,016)</u>	<u>(469)</u>	<u>(3,648)</u>	<u>(3,333)</u>
Investing activities:				
Capital expenditures	(9,565)	(5,249)	(13,105)	(7,534)
Restricted cash	(20)	(7)	(125)	(12)
Value added tax recoverable	(62)	-	(4)	-
Change in oil & gas suppliers prepayments	(782)	(1,731)	(2,067)	(2,719)
Net cash used in investing activities	<u>(10,429)</u>	<u>(6,987)</u>	<u>(15,301)</u>	<u>(10,265)</u>
Financing activities:				
Proceeds from sale of common stock	50,000	50,000	50,000	67,338
Share issue costs	(3,750)	(4,440)	(3,750)	(5,056)
Proceeds (Repayment) from longterm debt	(186)	(5,010)	5,114	(5,000)
Other non-current liabilities	(182)	32	(204)	32
Net cash provided by financing activities	<u>45,882</u>	<u>40,582</u>	<u>51,160</u>	<u>57,314</u>
Net increase in cash and cash equivalents	34,436	33,126	32,211	43,716
Cash and cash equivalents, beginning of period	<u>24,467</u>	<u>12,353</u>	<u>26,692</u>	<u>1,763</u>
Cash and cash equivalents, end of period	<u><u>58,903</u></u>	<u><u>45,479</u></u>	<u><u>58,903</u></u>	<u><u>45,479</u></u>
Interest paid	157	375	157	375

See accompanying notes to these financial statements

TETHYS PETROLEUM LIMITED
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Consolidated Statements of Changes in Stockholders' Equity (unaudited)

	Common Stock		Contributed Surplus	Warrants Reserve	Accumulated Deficit	Total Stockholders Equity
	No of Shares Issued	Share Capital				
	(Expressed in 000's United States dollars except share data)					
Total December 31, 2006	<u>70,000,000</u>	<u>22,315</u>	<u>-</u>	<u>2,220</u>	<u>(9,846)</u>	<u>14,689</u>
Shares Issued pursuant to Private Placement	34,674,390	17,337	-	-	-	17,337
	<u>104,674,390</u>	<u>39,652</u>	<u>-</u>	<u>2,220</u>	<u>(9,846)</u>	<u>32,026</u>
Share restructure 1:5	20,934,878	39,652	-	2,220	(9,846)	32,026
Issue of shares to acquire 30% of BN Munai	6,000,000	15,000	-	-	-	15,000
Initial Public Offering (IPO)	18,181,818	50,000	-	-	-	50,000
Share Warrants and Options	-	-	3,527	14,335	-	17,862
Finance Costs	-	(5,169)	-	-	-	(5,169)
Net loss in 2007	-	-	-	-	(41,779)	(41,779)
Total, December 31, 2007	<u>45,116,696</u>	<u>99,483</u>	<u>3,527</u>	<u>16,555</u>	<u>(51,625)</u>	<u>67,940</u>
Share Warrants and Options	-	-	2,280	980	-	3,260
Public offering	21,276,596	50,000	-	-	-	50,000
Share issue costs	-	(3,750)	-	-	-	(3,750)
Net loss for the period to June 30, 2008	-	-	-	-	(9,981)	(9,981)
Total June 30, 2008	<u>66,393,292</u>	<u>145,733</u>	<u>5,807</u>	<u>17,535</u>	<u>(61,606)</u>	<u>107,469</u>

See accompanying notes to these financial statements
These notes are available in Sedar.

TETHYS PETROLEUM LIMITED
(formerly known as Tethys Petroleum Investments Limited)

NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS – Unaudited

JUNE 30, 2008

NOTE 1 - NATURE OF OPERATIONS AND GOING CONCERN

These interim consolidated financial statements are for the six month period ended June 30, 2008 and should be read in connection with the 2007 annual consolidated financial statements.

As at June 30, 2008 Tethys Petroleum Limited (formerly known as Tethys Petroleum Investments Limited), was incorporated and headquartered in Guernsey, British Isles, but as per the resolution passed at the AGM on April 24, 2008 the process of redomiciling the company to the Cayman Islands was in its final stages. On July 18, 2008 it was announced that the continuance of the Company from the laws of Guernsey to the laws of the Cayman Islands had been completed on July 17, 2008. Tethys Petroleum Limited and its consolidated subsidiaries (collectively “Tethys”), is an oil and gas company operating within the Republic of Kazakhstan and the Republic of Tajikistan. Tethys’ principal activity is the acquisition of interests in and development of crude oil and natural gas fields.

Significant Business Risks and Basis of Presentation

Since inception, the Company has incurred significant losses from operations and negative cash flows from operating activities, and has an accumulated deficit at June 30, 2008. The ability of the Company to successfully carry out its business plan is primarily dependent upon its ability not only to maintain the current level of gas production but also to achieve further production of commercial oil and gas and to control the costs of operating and capital expenditures. While these factors create doubt about the Company’s ability to continue as a going concern management is confident of achieving the Company’s short term plans, including phase two of gas production, and optimistic about the longer term prospects for the Company.

The Company completed an Initial Public Offering of equity securities on the Toronto Stock Exchange on June 27, 2007. The Company issued additional capital on June 27, 2008 that generated sufficient funds to secure its future at least in the short term. In the event the Company is unable to generate significant revenues and cash flows from operations it may need to seek further funding from its shareholders or alternative sources. There can be no assurances that management will be successful with these initiatives.

The financial statements have been prepared on the basis that the Company will continue to operate as a going concern, which contemplates the realisation of assets and the settlement of liabilities and commitments in the normal course of business. These financial statements do not reflect adjustment in the carrying values of assets and liabilities reported, revenue or expenses and the balance sheet classification used that would be necessary if the going concern assumption was not appropriate. Such adjustment could be material.

Foreign Operations

Tethys’ future operations and earnings will depend upon the results of Tethys’ operations in the Republics of Kazakhstan and Tajikistan. There can be no assurance that Tethys will be able to successfully conduct such operations, and a failure to do so would have a material adverse effect on Tethys’ financial position, results of operations and cash flows. Also, the success of Tethys’ operations will be subject to numerous contingencies, some of which are beyond management control. These contingencies include general and regional economic conditions, prices for crude oil and natural gas, competition and changes in regulation. Since Tethys is dependent on international operations, specifically those in Kazakhstan, Tethys will be subject to various additional political, economic and other uncertainties. Among other risks, Tethys’ operations may be subject to the risks and restrictions on transfer of funds, import and export duties, quotas and embargoes, domestic and international customs and tariffs, and changing taxation policies, foreign exchange restrictions, political conditions and regulations.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The unaudited interim consolidated financial statements and notes thereto are prepared in accordance with accounting principles generally accepted in the United States of America using accounting policies consistent with those adopted by the Company in its consolidated financial statements for the year ended December 31, 2007. All tabular amounts are in thousands of U.S. dollars.

The interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the USA (US GAAP) which in most respects conform to accounting principles generally accepted in Canada (Canadian GAAP). The differences between US GAAP and Canadian GAAP that apply to the Company are explained in Note 17.

Recently Adopted Pronouncements

Fair Value Measurements

In September 2006, the FASB issued SFAS No. 157, "*Fair Value Measurements*." This Statement replaces multiple existing definitions of fair value with a single definition, establishes a consistent framework for measuring fair value and expands financial statement disclosures regarding fair value measurements. This Statement applies only to fair value measurements that already are required or permitted by other accounting standards and does not require any new fair value measurements. SFAS No. 157 is effective for fiscal years beginning subsequent to November 15, 2007. The Company adopted this Statement in the first two quarters of 2008 and it did not have a material impact on its financial position or results of operations.

The Fair Value Option for Financial Assets and Financial Liabilities

In February 2007, the FASB issued SFAS No. 159, "*The Fair Value Option for Financial Assets and Financial Liabilities*," which permits an entity to measure certain financial assets and financial liabilities at fair value. The objective of SFAS No. 159 is to improve financial reporting by allowing entities to mitigate volatility in reported earnings caused by the measurement of related assets and liabilities using different attributes, without having to apply complex hedge accounting provisions. Under SFAS No. 159, entities that elect the fair value option (by instrument) will report unrealized gains and losses in earnings at each subsequent reporting date. The fair value option election is irrevocable, unless a new election date occurs. SFAS No. 159 establishes presentation and disclosure requirements to help financial statement users understand the effect of the entity's election on its earnings, but does not eliminate disclosure requirements of other accounting standards. Assets and liabilities that are measured at fair value must be displayed on the face of the balance sheet. The Company adopted this statement in the first two quarters of 2008 and it did not have a material impact on its financial position or results of operations.

Recently Issued Accounting Pronouncements

In December 2007, the FASB issued SFAS No. 141 (revised 2007), —Business Combinations (—SFAS No. 141R), which replaces FASB Statement No. 141. SFAS No. 141R will change how business acquisitions are accounted for and will impact financial statements both on the acquisition date and in subsequent periods. SFAS No. 141R requires the acquiring Company to measure almost all assets acquired and liabilities assumed in the acquisition at fair value as of the acquisition date. SFAS No. 141R is effective for fiscal years beginning on or after December 15, 2008 (fiscal 2009 for the Company) and should be applied prospectively with the exception of income taxes which should be applied retrospectively for all business combinations. Early adoption is prohibited. The Company is in the process of evaluating the impacts, if any, of adopting this pronouncement.

In March 2008, the FASB issued SFAS No. 161, —Disclosures about Derivative Instruments and Hedging Activities, (—SFAS No. 161), an amendment to SFAS No. 133, —Accounting for Derivative Instruments and Hedging Activities.

SFAS No. 161 requires enhanced disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under Statement 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. This Statement will be effective for the Company's interim and annual consolidated financial statements beginning in fiscal year 2010. This Statement encourages, but does not require, comparative disclosures for earlier periods at initial adoption. The Company is in the process of evaluating the impacts, if any, of adopting this pronouncement.

NOTE 3 – PREPAYMENTS

Prepayments consisted of the following:

	June 30, 2008	December 31, 2007
Contractors	5,129	3,062
Other	675	351
Balance	<u>5,804</u>	<u>3,413</u>

Prepaid contractors relate to suppliers who were paid in advance for materials and services in relation to the drilling of two wells on the Kul Bas contract, initial and stage payments on compressors and pipes that will constitute phase 2 of the Company's gas production from the Akkulka contract and the initial payment for transport of the rig that will drill the first deep well on Akkulka. Other prepayments primarily relate to prepaid insurance and other operating expense items.

NOTE 4 – RESTRICTED CASH

Restricted cash at June 30, 2008 consisted of bank deposits that have been placed to satisfy local Kazakhstan requirements in respect of asset retirement obligations.

NOTE 5 – VALUE ADDED TAX RECOVERABLE

Non-current VAT recoverable represents VAT on capital expenditures in Kazakhstan that is allowed as an offset against VAT on revenues.

NOTE 6 - CAPITAL ASSETS

Capital assets, net of accumulated depletion, depreciation and amortization ("DD&A") and impairment, include the following at June 30, 2008:

	Cost	Accumulated DD&A	Net Capital Assets
Oil and Gas Properties			
Proved properties	43,856	(16,296)	27,560
Unproved properties	8,654	-	8,654
	<u>52,510</u>	<u>(16,296)</u>	<u>36,214</u>
Plant and Equipment			
Oil & Gas Equipment	9,812	-	9,812
Vehicles	896	(74)	822
Office equipment, furniture, fixtures and other	426	(79)	347
	<u>11,134</u>	<u>(153)</u>	<u>10,981</u>

63,644	(16,449)	47,195
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Capital assets, net of accumulated DD&A, include the following at December 31, 2007:

	Cost	Accumulated DD&A	Net Capital Assets
Oil and Gas Properties			
Proved properties	39,727	(12,975)	26,752
Unproved properties	7,749	-	7,749
	<u>47,476</u>	<u>(12,975)</u>	<u>34,501</u>
Plant and Equipment			
Oil & Gas Equipment	2,057	-	2,057
Vehicles	579	(19)	560
Office equipment, furniture, fixtures and other	386	(32)	354
	<u>3,022</u>	<u>(51)</u>	<u>2,971</u>
	<u>50,498</u>	<u>(13,026)</u>	<u>37,472</u>

Proved properties consist of both the Kyzylloi and Akkulka contracts. Following the commencement of gas production from the Kyzylloi gas field on December 19, 2007 the Kyzylloi costs, included in the proved properties, have been depreciated on a unit of production basis.

Unproved property additions relate to activity being carried out in properties where as yet there are no proved reserves and at June 30, 2008 this consisted of the Kul Bas Exploration and Production Contract. In the period to June 30, 2008 US\$198,811 was capitalized from G&A while in the year ended December 31, 2007 the amount was US\$316,200.

Oil & gas equipment primarily relates to the construction in progress of a drilling rig and as such this was not subject to depreciation.

In addition to the depreciation charge on proved properties of US\$175,000 in the December 31, financial statements an impairment adjustment of US\$12,800,000 was required under the US GAAP ceiling test which was calculated on proved reserves only at the constant prices. The prices used in valuing the reserves were US\$0.90 per Mcf for the existing Kyzylloi gas sales contract and US\$3.38 per Mcf for future gas sales, both prices are net of VAT.

NOTE 7 – ACCOUNTS PAYABLE

Accounts payable consisted of the following at:

	June 30, 2008	December 31, 2007
Trade payables	785	1,182
Education fund obligations	206	206
	<u>991</u>	<u>1,388</u>

Each of the Kyzylloi, Akkulka and Kul Bas contracts in Kazakhstan require that a sum equivalent to 1% of the capital expenditure incurred on the respective work programs is provided for the professional education of its Kazak personnel.

NOTE 8 – LONG TERM DEBT

	June 30, 2008	December 31, 2007
	<u> </u>	<u> </u>
Long term debt	5,114	-
Current portion of long term debt	(804)	-
	<u> </u>	<u> </u>
Balance	<u>4,310</u>	<u>-</u>

On March 19, 2008 the Company announced that it had completed a financing arrangement for funds of US\$5,300,000 to assist with the purchase of a drilling rig by means of a 3-year loan with monthly payments of interest and capital and a final balloon payment. The interest payable on the borrowed funds was 12% per annum. In addition 795,000 warrants to purchase Tethys shares were also issued to the lenders with a term of 3 years and an exercise price of CAD\$3.25. Fair value of these warrants at US\$980,394 was recognized as a finance charge in Q1 and was unchanged at the end of Q2. Lenders have security over the shares of Tethys Petroleum Inc. which has no other assets except the drilling rig. No corporate guarantees or security are being provided by Tethys. To June 30, 2008 Tethys has incurred US\$5,949,850 of costs with respect to this rig and a further \$2,922,000 on drill strings, BOP and other ancillary equipment.

The loan is to be repaid with monthly payments of interest and capital over a 36 month period and a final balloon payment at the end of this period. The balance of US\$4,310,000 represents total payments due beyond June 2009.

Principal due within each of the next three years:

To June 30,	2009	804
	2010	906
	2011	<u>3,404</u>
		<u>5,114</u>

NOTE 9 – NON CURRENT LIABILITIES

Other non current liabilities relates to the accrual of Historic Costs due to the Government of Kazakhstan on the Kyzylol contract in Kazakhstan. The total amount outstanding at June 30, 2008 was US\$994,586 and this is to be paid in quarterly instalments between July 2008 and March 2014. The net present value of the US\$994,586 using an interest rate of 10% is US\$729,000 of which US\$157,000 is current leaving a balance of US\$572,000.

NOTE 10 – ASSET RETIREMENT OBLIGATION

The asset retirement obligation is comprised of the following:

	June 30, 2008	December 31, 2007
	<u> </u>	<u> </u>
Balance at beginning of the period	661	451
New obligations incurred	35	175
Accretion of expense	33	35
	<u> </u>	<u> </u>
Balance at end of the period	<u>729</u>	<u>661</u>

NOTE 11 - COMMITMENTS AND CONTINGENCIES

Kazakhstan

For full details of the contract commitments in Kazakhstan please refer to the Notes to the 2007 annual consolidated financial statements.

Tajikistan

On June 13, 2008 the Company announced that its subsidiary Kulob Petroleum Limited (KPL) had signed a production sharing contract with the government of the Republic of Tajikistan. Under the Production Sharing Contract KPL will recover 100% of its costs from up to 70% of total production (the maximum allowed under the newly approved production sharing legislation of Tajikistan) and the remaining production (termed "Profit Oil and Gas") will be shared 70% to KPL and 30% to the Government whose share includes all taxes, levies and duties. The terms are fixed over the life of the PSC which is a minimum of twenty-five years.

Pursuant to the PSC, KPL has agreed to fund a work program which has been designed to provide data for a focused exploration of the Contract Area and which will be carried out in two stages (the "**Work Program**"). During the first phase of the Work Program ("**Phase I**"), planned activities will include geological studies, reprocessing of existing seismic and other geophysical data, acquisition of seismic and other geophysical data and the commencement of initial rehabilitation activities on the Beshtentak and Khoja Sartez fields. The total minimum cost of Phase I is estimated to be approximately US\$3,000,000. After completion of Phase I, KPL would make a determination as to whether it will proceed with the second phase of the Work Program ("**Phase II**") or terminate the PSC. Phase II, which is to be completed within 18 months of the completion of Phase I, is expected to involve the commencement of the drilling of an exploration well to determine the oil and gas potential of the Bukhara formation and to perform additional rehabilitation activities if economically justified. The total minimum cost of the activities planned in Phase II is estimated to be approximately US\$5,000,000. Tethys, through its planned indirect 51% holding in KPL, would be expected to fund its share of these costs.

Drilling Rig Telesto

On October 16, 2007 Tethys placed an order for a new 2,000 horsepower (1,470 kN) ZJ70/4500L drilling rig from a Chinese supplier. The rig has a nominal drilling depth of 23,000 feet (7,000 metres). Transportation of the rig to Akkulka commenced in June 2008 for use on the Akkulka deep exploration program which is anticipated to commence in October 2008. It is planned that the rig will be operated by Tethys' current Kazakh drilling contractor under a management agreement. The rig would also be suitable for drilling on the potentially large prospects Tethys has identified in the Kulob area of Tajikistan that would be within the scope of the recently signed production sharing contract. The cost of the rig is US\$6,263,000 and support equipment including drill strings and BOP is anticipated to be in the region of a further US\$3,700,000 of which \$2,922,000 had been incurred to June 30, 2008. The Company paid the rig deposit of US\$1,878,900 in October 2007 and a stage payment of the same amount in January 2008. The third installment of US\$2,192,050 was paid in May 2008. The final payment will be made upon completion of the transportation of the rig to the drilling site.

NOTE 12 – SHAREHOLDERS' EQUITY

On June 27, 2008 Tethys successfully completed a public offering having placed 21,276,596 shares at a price of US\$2.35 (C\$2.39) raising US\$ 50 million (gross). The Ordinary Shares are listed on the Toronto Stock Exchange.

At the AGM on April 24, 2008 the authorized share capital of the Company was increased by an additional 200,000,000 Ordinary Shares and 50,000,000 Preference Shares. The Preference Shares have the rights as set out in the Memorandum and Articles of Association approved at the AGM on April 24, 2008. Significant terms related to preference shares are summarized below:

1. may be issued in one or more series;
2. are entitled to any dividends in priority to the Ordinary Shares;
3. confer upon the holders thereof rights in a winding-up in priority to the Ordinary Shares;
4. and may have such other rights, privileges and conditions (including voting rights) as the Board may determine prior to the first allotment of any series of Preference Shares, provided that if a series of Preference Shares has no or limited voting rights it shall be designated as such by the Board.

NOTE 13 – STOCK BASED COMPENSATION

The Company has adopted a stock incentive plan referred to as the “2007 Long Term Stock Incentive Plan” pursuant to which the Company may grant stock options to any director, employee or consultant of the Company, or any subsidiary or Vazon Energy Limited (collectively, “Service Providers”). The purpose of the plan is to secure for the Company and its shareholders the benefits of incentives inherent in share ownership by Service Providers who, in the judgment of the Board of Directors, will be largely responsible for its future growth and success.

The maximum number of Ordinary Shares reserved for issuance under the plan equals 10% of the outstanding Ordinary Shares after giving effect to the Treasury Offering. The plan is administered by the Compensation and Nomination Committee of the Board of Directors. Options may be granted pursuant to recommendations of the Compensation and Nomination Committee. The Compensation and Nomination Committee may determine the vesting schedule and term, provided that options may not have a term exceeding ten years. Subject to any resolution passed by the Compensation and Nomination Committee, options will terminate three months after an optionee ceases to be a Service Provider.

The exercise price of options granted under the plan may not be less than the closing price of Ordinary Shares on the principal stock exchange where the Ordinary Shares are listed as of the date of the option grant. The plan contains amendment provisions which allow amendments to the plan by the Board of Directors, without shareholder approval, for amendments of a “housekeeping” nature, changes to vesting or termination provisions, and discontinuance of the plan. The plan also provides that outstanding options will vest immediately on the occurrence of a “change of control” (as defined in the plan). Options granted under the plan are only assignable to certain related entities of an optionee or otherwise with the consent of the Company.

The plan does not contain any restriction on the number of Ordinary Shares which may be reserved for issuance in respect of options granted to insiders under the plan or pursuant to any other share compensation arrangement. Accordingly, amendments to the plan and other compensation arrangements of the Company which require approval of shareholders will require approval of disinterested shareholders for as long as the number of Ordinary Shares reserved for issuance under the options or other share compensation arrangements exceeds 10% of the outstanding Ordinary Shares and the plan or share compensation arrangements do not limit the participation of insiders to 10% of outstanding Ordinary Shares.

The Company has approved the grant to its executive officers of warrants (the “Performance Warrants”) to acquire 6,767,504 Ordinary Shares. The Performance Warrants will be exercisable at US\$4.125 through the period ending December 25, 2009 in respect of 1,353,501 Ordinary Shares, US\$5.50 through the period ending June 25, 2011 in respect of 2,255,835 Ordinary Shares, and US\$6.875 through the period ending December 25, 2012 in respect of 3,158,168 Ordinary Shares.

Quarterly Activity

Stock options – The following table summarizes the stock option activity under the 2007 Long Term Stock Incentive Plan for the six months ended June 30, 2008.

	Number of Options	Weighted average Exercise Price	Aggregate Intrinsic value Thousands	Weighted Average Remaining Term (in years)
Outstanding at December 31, 2007	4,497,000	\$2.76		
Granted	2,274,000	\$2.51		
Forfeited	(36,000)	\$2.75		
Exercised	-	N/A		
Expired	-	N/A		
<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
Outstanding at June 30, 2008	6,735,000	\$2.67	\$429	6.33
Exercisable at June 30, 2008	3,622,000	\$2.70	\$143	6.20

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (the difference between the Company's stock price on June 30, 2008 and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders if all option holders had exercised their options on June 30, 2008. This amount changes based on the fair market value of the Company's stock.

For options granted during the six months ended June 30, 2008, the weighted average fair value on the date of grant, estimated using the Black-Scholes option pricing model was US\$1.5493 per option, using the following weighted average assumptions: dividend yield of 0%; expected term of 4.0 years; a risk free interest rate of 3.32%; and an expected volatility of 73.5%.

For the six months ended June 30, 2008, there was US\$1,708,000 of pre-tax compensation expense for options granted under the 2007 Long Term Stock Incentive Plan. As of June 30, 2008, there was US\$4,500,000 of total unrecognized compensation expense related to unvested stock options granted under the plan. The Company expects to recognize the expense over a weighted-average period of 1.49 years.

Warrants - The following table summarizes the warrant activity, including Performance Warrants, for the six months ended June 30, 2008.

	Number of Warrants	Weighted average Exercise Price	Aggregate Intrinsic value (thousands)	Weighted Average Remaining Term (in years)
Outstanding at December 31, 2007	8,857,504	\$5.07		
Granted	795,000	\$3.25		
Forfeited	-	N/A		
Exercised	-	N/A		
Expired	-	N/A		
<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
Outstanding at June 30, 2008	9,652,504	\$4.92	\$418	4.53
Exercisable at June 30, 2008	9,652,504	\$4.92	\$418	4.53

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (the difference between the Company's stock price on June 30, 2008 and the exercise price, multiplied by the number of in-the-money warrants) that would have been received by the warrant holders if all warrant holders had exercised their warrants on June 30, 2008. This amount changes based on the fair market value of the Company's stock.

During the six months ended June 30, 2008, there were 795,000 warrants issued in connection with loan financing. These warrants were noncompensatory. As of June 30, 2008, there was no unrecognized compensation expense related to unvested warrants.

NOTE 14 - NET LOSS PER COMMON SHARE

Basic net loss per common share is computed by dividing the net loss attributable to common stockholders by the weighted average number of shares of common stock outstanding during the applicable period. Diluted per share information is calculated, including the dilutive effect of stock options which are determined using the treasury stock method. The treasury stock method assumes that the proceeds that would be obtained upon exercise of "in the money" options would be used to purchase common shares at the average market price during the period. No adjustment to diluted earnings per share is made if the result of this calculation is anti-dilutive.

NOTE 15- RELATED PARTY TRANSACTIONS

Vazon Energy Limited ("Vazon") is a corporation organized under the laws of the Bailiwick of Guernsey, of which Dr. David Robson, Chief Executive Officer, is the sole owner and managing director. Tethys has a management services contract with Vazon that came into effect from June 27, 2007 whereby the services of Dr. Robson, Ms. Landles (Corporate Secretary and Executive Vice President) and other Vazon employees are provided to the Company. A monthly fee is paid for the services of Dr. Robson, a separate monthly fee for other Vazon employees and an invoice for all other services and costs is to be issued to Tethys at the end of each month. The total cost charged to Tethys for services from Vazon in the six months to June 30, 2008 was US\$455,355.

Upon completion of the loan referred to in Note 8 in March 2008 Kraken Financial Group, which has one common director with the company, was entitled to receive 6% commission of the funds it was responsible for introducing to be taken in the form 81,447 shares. Kraken Financial Group also acted as broker for Tethys in the placement of various insurance policies, including D&O, for which the combined annual premiums were US\$112,000.

Transactions with affiliates or other related parties including management of affiliates are to be undertaken on the same basis as third party arms-length transactions. Transactions with affiliates are reviewed and voted on solely by non-interested directors.

NOTE 16 – SUBSEQUENT EVENTS

On July 18 2008 the Company announced that the re-domiciliation from Guernsey to the Cayman Islands had been completed on July 17, 2008. The continuance, which had been approved by the shareholders of the Company at the annual meeting on April 24, 2008, is described in the management information circular dated March 20, 2008 ("the management information circular") available on [sedar.com](http://www.sedar.com).

NOTE 17 – CANADIAN ACCOUNTING PRINCIPLES AND REPORTING

The interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the USA (US GAAP) which in most respects conform to accounting principles generally accepted in Canada (Canadian GAAP). The differences between US GAAP and Canadian GAAP that apply to the Company are explained in this note.

Reconciliation between US GAAP and Canadian GAAP

Under US GAAP regulations only proved reserves are included in the ceiling test and consequently the Company had to record an impairment in its 2007 accounts of US\$12,800,000. Under Canadian GAAP where probable reserves can also be included in the ceiling test this impairment would not have been necessary.

RECONCILIATION OF NET EARNINGS BETWEEN US GAAP AND CANADIAN GAAP

	For three months to		For six months to	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Net Loss and Comprehensive Loss for the period under US GAAP	(5,280)	(20,117)	(9,981)	(22,438)
Additional DD&A on Proved Properties	(535)	-	(1,074)	-
Loss for the period before income taxes under Canadian GAAP	(5,815)	(20,117)	(11,055)	(22,438)
Basic and diluted loss per share under Canadian GAAP	(0.12)	(0.95)	(0.24)	(1.71)

CONSOLIDATED STATEMENT OF OPERATIONS, COMPREHENSIVE LOSS AND DEFICIT – CANADIAN GAAP

	For three months to		For six months to	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Operating Revenue	1,566	-	2,997	-
Expenses				
Operating expenses	196	-	263	-
Selling, general & admin expense	2,974	1,996	6,168	3,421
Stock based compensation	1,709	16,339	2,280	16,339
Depreciation, depletion & amortization	2,457	14	4,492	28
Other	45	1,768	849	2,650
Loss before income tax for the period under Canadian GAAP	(5,815)	(20,117)	(11,055)	(22,438)
Income Tax	-	-	-	-
Net Loss and Comprehensive Loss after tax for the period under Canadian GAAP	(5,815)	(20,117)	(11,055)	(22,438)
Deficit – Beginning of the period	(44,065)	(12,167)	(38,825)	(9,846)
Deficit – End of period	(49,880)	(32,284)	(49,880)	(32,284)

CONDENSED CONSOLIDATED BALANCE SHEET

	June 30, 2008	December 31, 2007
Assets		
Current Assets	60,435	28,052
Non Current Assets	8,327	6,132
Plant & Equipment	63,644	50,498
Depreciation, depletion & amortization	(4,723)	(226)
Total Assets	<u>127,683</u>	<u>84,456</u>
Liabilities and Stockholder Equity		
Current Liabilities	2,877	2,279
Non Current Liabilities	5,611	1,437
Total stockholder equity	119,195	80,740
Total liabilities and stockholder equity	<u>127,683</u>	<u>84,456</u>

RECENTLY ADOPTED STANDARDS – CANADIAN GAAP

“Inventories”, Section 3031. This new standard replaces the previous standard in Section 3030 and establishes standards for the measurement and disclosure of inventories. The adoption of this standard has had no material effect on the Company’s consolidated financial statements.

“Capital Disclosures”, Section 1535. This new standard requires the Company to disclose its objectives, policies and processes for managing capital.

“Financial Instruments – Presentation”, Section 3863 and “Financial Instruments – Disclosures”, Section 3862, which replaced Section 3861.

RECENT ACCOUNTING PRONOUNCEMENTS – CANADIAN GAAP

In January 2006 the Accounting Standards Board (“AcSB”) adopted a strategic plan for accounting standards in Canada. In February 2008 the AcSB confirmed that International Financial Reporting Standards (“IFRS”) will replace Canadian GAAP effective January 1, 2011. The Company is assessing the potential impacts of this transition and developing a plan accordingly.

In February 2008 the CICA issued Section 3064, “Goodwill and Intangible Assets” which will replace Section 3062 and be effective January 1, 2009. This new standard revises the criteria for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. The Company is currently assessing the impact of these new recommendations.

Capital Disclosures

The Company’s objectives when managing capital is to maintain adequate financial flexibility to preserve its ability to meet financial obligations, both current and long term. The capital structure of the Company is managed and adjusted to reflect changes in economic conditions. In order to maintain or adjust the capital structure in the future, adjustments may be made to the amount of distributions (if any) to shareholders and the amount of capital returned to shareholders, in addition to the amount of new units issued. Financing decisions are set based on the timing and extent of expected operating and capital cash outlays. Factors considered when determining whether to take on new debt or to issue equity

include the amount of cash sought, the availability of these sources and their terms and to overall balance creation of value for shareholders with the management of risk associated with debt.

The Company's capital structure is comprised of shareholders' equity and a loan from a number of accredited private investors (including the current portion) and is monitored by using a non-GAAP financial metric of Net Debt to Capitalization. Net Debt is calculated as the sum of the loan (including the current portion) less cash and cash equivalents. There was no Net Debt at June 30, 2008 as the cash and cash equivalents significantly exceeded the loan. The Company had no loans at December 2007.

Financial Instruments and Risk Management

Financial Risks

The Company is exposed to a number of financial risks in the normal course of its business operations, including market risks, credit risks and liquidity risks. The nature of these risks has not changed significantly from the prior period ended December 31, 2007.

Market Risk

Market risk is the risk that changes in market prices such as interest rates and commodity prices will affect the Company's operating income or the value of its financial instruments.

Interest Rate Risk

Interest rate risk is the risk that the value of a financial instrument will be affected by changes in market interest rates. The loan from private investors is a fixed rate facility and so has no exposure to changes in market interest rates.

Commodity Price Risk

Commodity price risk is the risk that fluctuations in oil or natural gas prices could materially adversely affect the Company's financial condition. The commodity prices affect the levels of drilling activity, particularly with respect to natural gas. The current contract for existing sales with Kazakhstani Petrochemical Company Kemikal LLP is a fixed price contract and so there is no current exposure to Price Risk.

Foreign Currency Exchange

The Company's operations and expenditures are to some extent paid in foreign currencies. As a result, the Company is exposed to market risks resulting from fluctuations in foreign currency exchange rates. A material drop in the value of any such foreign currency could result in a material adverse effect on the Kazakhstan cash flow and revenues. Currently, there are no significant restrictions on the repatriation of capital and distribution of earnings from Kazakhstan to foreign entities. There can be no assurance, however, that restrictions on repatriation of capital or distributions of earnings from Kazakhstan will not be imposed in the future. Amendments to current taxation laws and regulations which alter tax rates and/or capital allowances could have a material adverse impact on Tethys.

To the extent revenues and expenditures denominated in or strongly linked to the U.S. dollar are not equivalent; the Company is exposed to exchange rate risk. The Company is exposed to the extent U.S. dollar revenues do not equal U.S. dollar expenditures. In addition, a portion of expenditures in Kazakhstan are denominated in Tenge, which are difficult to hedge. The Company is not currently using exchange rate derivatives to manage exchange rate risks but is attempting to negotiate exchange rate stabilization conditions in new local Tenge denominated service and supply contracts in Kazakhstan. As at June 30, 2008 had the United States dollar changed by 1% against the Kazakhstan Tenge, with all other variables held constant, the Company's foreign exchange gain or loss would have been affected by \$67,556.

In addition, the Company's results will be reported in U.S. dollars and foreign currency denominated monetary balances could result in gains and losses that may increase the variability of earnings. Moreover, the Company's ordinary shares trade in Canadian dollars on the TSX.

Credit Risk

Credit risk is the risk that the counterparty to a financial instrument fails to meet its contractual obligations, resulting in a financial loss to the Company. This relates primarily to the Company's trade accounts receivable.

The Company has only recently commenced production and revenue generation and currently has only one customer, which is unlikely to change in the immediate future. While this customer is considered credit worthy the level of debt will be carefully monitored and appropriate action taken if the debt exceeds sixty days.

Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. This risk relates to the Company's ability to generate or obtain sufficient cash or cash equivalents to satisfy these financial obligations as they become due. The Company's processes for managing liquidity risk include preparing and monitoring capital and operating budgets, coordinating and authorizing project expenditures, and authorization of contractual agreements. The Company seeks additional financing based on the results of these processes. The budgets are updated when required as conditions change.

The only liabilities the Company had at June 30, 2008 that exceeded one year are the loan of US\$5,114,000 payable over three years and other non-current liabilities on the Kyzylol contract of US\$994,586 payable in quarterly instalments up to March 2014.

Fair Value of Financial Assets and Liabilities

The Company's cash and cash equivalents are designated as held-for-trading and are measured at carrying value, which approximates fair value due to the short-term nature of these instruments. Accounts receivable are designated as loans and receivables and recorded at amortized cost, which approximates fair value due to the short term nature of the instrument. Accounts payable, accrued liabilities and the loan from accredited private investors are designated as other liabilities and are recorded at cost. The fair value of accounts payable and accrued liabilities approximate their carrying values due to the short term nature of these instruments. The fair value of obligations under the loan approximate their carrying values as the interest rates applicable to these instruments reflect current market rates. Financing costs relating to all financial instruments are expensed as incurred.

NOTE – 18 COMPARATIVES

Certain prior periods' amounts have been reclassified to conform to the current period's presentation.