

CONSOLIDATED BALANCE SHEETS

	March 31, 2007	December 31, 2006
<i>(\$000s)(unaudited)</i>		
Assets		
Current assets		
Accounts receivable	56,205	54,944
Prepaid expenses and deposits	2,973	2,928
Financial instruments <i>(notes 2 and 7)</i>	-	3,194
	59,178	61,066
Property, plant and equipment <i>(note 3)</i>	1,003,086	972,599
Long-term investment, at cost <i>(notes 2 and 8)</i>	1,150	1,150
Goodwill	358,096	358,096
	1,421,510	1,392,911
Liabilities and Shareholders' Equity		
Current liabilities		
Accounts payable and accrued liabilities	102,410	88,552
Financial instruments <i>(notes 2 and 7)</i>	3,441	-
	105,851	88,552
Long-term debt <i>(note 4)</i>	157,870	138,890
Future income taxes	149,412	151,802
Asset retirement obligations <i>(note 5)</i>	11,281	11,258
Deferred lease inducements	387	408
Shareholders' equity		
Share capital <i>(note 6)</i>	957,403	957,186
Contributed surplus <i>(note 6)</i>	10,859	9,962
Retained earnings	28,447	34,853
	996,709	1,002,001
Subsequent event <i>(note 4)</i>	1,421,510	1,392,911

See accompanying notes to the interim consolidated financial statements.

CONSOLIDATED STATEMENTS OF OPERATIONS, COMPREHENSIVE INCOME AND RETAINED EARNINGS

	Three months ended March 31,	
	2007	2006
<i>(\$000s, except per share amounts)(unaudited)</i>		
Revenues		
Oil and natural gas revenues	90,751	61,806
Royalties, net of ARTC	(26,718)	(19,994)
Financial instruments <i>(note 7)</i>		
Realized gains	1,795	468
Unrealized (losses) gains	(6,635)	2,142
	59,193	44,422
Expenses		
Operating costs	14,374	6,895
Transportation costs	1,592	518
General and administrative	3,355	1,995
Depletion, depreciation and accretion	45,610	29,160
Interest and finance costs	1,856	1,125
Stock-based compensation <i>(note 6)</i>	1,121	1,520
	67,908	41,213
Earnings (loss) before taxes	(8,715)	3,209
Taxes (reduction)		
Current	-	180
Future	(2,309)	1,738
	(2,309)	1,918
Net earnings (loss) and comprehensive income	(6,406)	1,291
Retained earnings, beginning of period	34,853	27,900
Retained earnings, end of period	28,447	29,191
Net earnings (loss) per share <i>(note 6)</i>		
Basic	\$ (0.09)	\$ 0.03
Diluted	\$ (0.09)	\$ 0.03

See accompanying notes to the interim consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three months ended March 31,	
	2007	2006
<i>(\$000s)(unaudited)</i>		
Cash provided by (used in):		
Operating Activities		
Net earnings (loss)	(6,406)	1,291
Items not involving cash:		
Depletion, depreciation and accretion	45,610	29,160
Future income taxes (reduction)	(2,309)	1,738
Stock-based compensation	1,121	1,520
Unrealized losses (gains) on financial instruments	6,635	(2,142)
Amortization of deferred lease inducements	(21)	(21)
Abandonment expenditures	(516)	-
Change in non-cash operating working capital	1,631	(16,121)
	45,745	15,425
Financing Activities		
Common shares issued for cash	-	100,620
Share issue costs	-	(4,339)
Proceeds on exercise of stock options	176	998
Increase (decrease) in bank indebtedness	18,980	(74,821)
	19,156	22,458
Investing Activities		
Property, plant and equipment additions	(75,822)	(46,559)
Property acquisitions	-	(210)
Purchase of investments	-	(150)
Net cash paid on business combination	-	(527)
Deferred charges	-	251
Change in non-cash investing working capital	10,921	9,312
	(64,901)	(37,883)
Change in cash	-	-
Cash, beginning of period	-	-
Cash, end of period	-	-
Cash interest paid	2,207	748
Cash taxes paid	1,025	280

See accompanying notes to the interim consolidated financial statements.

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS

Three months ended March 31, 2007 and 2006
(tabular amounts in thousands of dollars, unless otherwise noted)

1. Significant Accounting Policies

The interim consolidated financial statements of Highpine Oil & Gas Limited (the "Company") have been prepared by management in accordance with Canadian generally accepted accounting policies and follow the same accounting policies as the most recent audited annual consolidated financial statements, except as noted below. Certain disclosures normally required to be included in the notes to the annual consolidated financial statements have been condensed or omitted. The interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the notes thereto for the years ended December 31, 2006 and 2005.

2. Change in Accounting Policy

Effective January 1, 2007, the Company adopted the Canadian Institute of Chartered Accountants ("CICA") section 3855, "Financial Instruments - Recognition and Measurement," section 1530 "Comprehensive Income," section 3865 "Hedges" and section 3861 "Financial Instruments – Disclosure and Presentation." These standards have been adopted prospectively. Adoption of these standards did not impact January 1, 2007 opening balances.

i) *Financial instruments*

All financial instruments must initially be recognized at fair value on the balance sheet date. The Company has classified each financial instrument into the following categories: held for trading financial assets and financial liabilities, loans or receivables, held to maturity investments, available for sale financial assets, and other financial liabilities. Subsequent measurement of the financial instruments is based on their classification. Unrealized gains and losses on held for trading financial instruments are recognized in earnings. Gains and losses on available for sale financial assets are recognized in other comprehensive income and are transferred to earnings when the asset is derecognized. The other categories of financial instruments are recognized at amortized cost using the effective interest rate method.

Upon adoption and with any new financial instrument, an irrevocable election is available that allows entities to classify any financial asset or financial liability as held for trading, even if the financial instrument does not meet the criteria to designate it as held for trading. The Company has not elected to classify any financial assets or financial liabilities as held for trading unless they meet the held for trading criteria. A held for trading financial instrument is not a loan or receivable and includes one of the following criteria:

- it is a derivative, except for those derivatives that have been designated as effective hedging instruments;
- it has been acquired or incurred principally for the purpose of selling or repurchasing in the near future; or
- it is part of a portfolio of financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit taking.

ii) *Derivative instruments and hedging activities*

The Company may enter into derivative instrument contracts to manage its commodity price exposure, foreign exchange exposure and interest rate exposure. The Company does not enter into derivative instrument contracts for trading or speculative purposes. The Company may choose to designate derivative instruments as hedges. Hedge accounting continues to be optional.

iii) *Comprehensive income*

Comprehensive income consists of net earnings and other comprehensive income ("OCI"). OCI comprises the change in the fair value of the effective portion of the derivatives used as hedging items in a cash flow hedge and the change in fair value of any available for sale financial instruments. Amounts included in OCI are shown net of tax. Accumulated other comprehensive income is a new equity category comprised of the cumulative amounts of OCI.

3. Property, Plant and Equipment

	March 31, 2007		December 31, 2006	
	Cost	Accumulated depletion and depreciation	Net book value	Net book value
Petroleum and natural gas properties	\$ 1,245,837	\$ 245,516	\$ 1,000,321	\$ 969,784
Land, buildings and leaseholds	2,389	268	2,121	2,170
Office equipment and computers	1,033	389	644	645
	<u>\$ 1,249,259</u>	<u>\$ 246,173</u>	<u>\$ 1,003,086</u>	<u>\$ 972,599</u>

At March 31, 2007, approximately \$155.9 million (December 31, 2006 – \$152.2 million) of unproved property costs and unevaluated seismic costs were excluded from the depletion calculation. Future development costs of \$39.7 million (December 31, 2006 – \$56.4 million) were included in the depletion calculation. Salvage value of \$23.9 million (December 31, 2006 – \$23.9) was excluded from the depletion calculation. During the three months ended March 31, 2007, cash general and administrative expenses of \$0.8 million (three months ended March 31, 2006 – \$0.6 million) were capitalized. The Company also capitalized \$0.4 million of stock based compensation expense for the three months ended March 31, 2007 and recovered \$0.6 million of stock based compensation which had been capitalized in 2006 as a result of the cancellation of options.

4. Long-Term Debt

At March 31, 2007, the Company had available a \$205 million revolving term credit facility with a syndicate of Canadian financial lenders and a \$20 million demand operating credit facility with a Canadian financial lender.

The revolving term credit facility has a 364-day extendable revolving period plus a one-year maturity. The revolving term credit facility bears interest within a range of the lenders' prime rate to prime plus 0.25 percent depending on financial ratios of the Company. The demand operating facility bears interest at the lenders' prime rate.

The lenders review the credit facilities semi-annually. The facilities are secured by a general security agreement and a first floating charge over all of the Company's assets.

On May 3, 2007, the revolving term credit facility was increased from \$205 million to \$230 million and the term date was extended to May 28, 2008.

Interest expense includes \$1.9 million (three months ended March 31, 2006 - \$1.1 million) in respect of debt repayable for a period exceeding one year.

5. Asset Retirement Obligations

At March 31, 2007, the estimated total undiscounted cash flows required to settle asset retirement obligations were \$18.1 million (December 31, 2006 – \$17.9 million). Expenditures to settle asset retirement obligations will be incurred between 2007 and 2027. Estimated cash flows have been discounted using an annual credit-adjusted risk-free interest rate of 8.0 percent per annum and have been inflated using an inflation rate of 2.0 percent per annum.

Changes to asset retirement obligations were as follows:

	Three months ended March 31, 2007	Year ended December 31, 2006
Asset retirement obligations, beginning of period	11,258	5,898
Liabilities acquired	-	3,980
Liabilities incurred	314	1,069
Liabilities settled	(516)	(368)
Accretion expense	225	679
Asset retirement obligations, end of period	11,281	11,258

6. Share Capital

Authorized:

- (i) an unlimited number of class A common shares without par value; and
- (ii) an unlimited number of class B common shares without par value issuable in series. The class B common shares are non-voting and are not entitled to the receipt of dividends.

	Three months ended March 31, 2007		Year ended December 31, 2006	
	Shares	Amount	Shares	Amount
	<i>(thousands)</i>	<i>(\$thousands)</i>	<i>(thousands)</i>	<i>(\$thousands)</i>
Class A common shares				
Balance, beginning of period	67,648	957,186	44,250	479,496
Issued to acquire White Fire	-	-	4,089	95,480
Issued to acquire Kick	-	-	14,831	283,269
Issued for cash	-	-	4,300	100,620
Stock options exercised	13	176	178	1,202
Contributed surplus transferred on exercise of stock options	-	41	-	225
Share issue costs less tax effect of (2007 - nil; 2006 – \$1,500)	-	-	-	(3,106)
Balance, end of period	67,661	957,403	67,648	957,186

Per Share Amounts

	Three months ended March 31,	
	2007	2006
	(thousands)	(thousands)
Weighted average number of common shares outstanding		
Basic	67,657	47,796
Dilutive effect of stock options	-	421
Diluted	67,657	48,217

Anti-dilutive options excluded from the calculation of diluted earnings per share were 5.8 million (2006 – 30,000).

Stock Options

The Company has a stock option plan pursuant to which options to purchase class A common shares of the Company may be granted to directors, officers, employees and consultants. The outstanding stock options of the Company are exercisable for a period of six years and vest over a period of four years.

In March 2007, 1,850,500 stock options previously granted to non-officer employees at exercise prices ranging from \$14.92 to \$23.25 were repriced. The new exercise price was set at \$12.05 which was the closing price of the Company's class A common shares on the day preceding the repricing. The vesting period of the repriced stock options, including vested stock options, was reset. As a result of the stock options repricing, the fair value of the stock options, calculated using the Black-Scholes model, increased by \$5.1 million. The increase in the fair value of the stock options will be amortized over the four year vesting period of the repriced options. All other characteristics of the repriced options, including the expiry date, remain unchanged.

A summary of changes is as follows:

	Three months ended		Year ended	
	March 31, 2007		December 31, 2006	
	Class A		Class A	
	Common Shares	Weighted	Common Shares	Weighted
	Issuable Upon	Average	Issuable Upon	Average
	Exercise	Exercise	Exercise	Exercise
	of Options	Price	of Options	Price
	(thousands)	(\$/share)	(thousands)	(\$/share)
Balance, beginning of period	5,077	15.80	3,652	13.06
Granted	1,368	12.16	2,016	20.42
Exercised	(13)	(13.79)	(178)	(6.75)
Cancelled	(637)	(19.29)	(413)	(18.06)
Repriced	(1,851)	(19.67)	-	-
Repriced	1,851	12.05	-	-
Balance, end of period	5,795	12.13	5,077	15.80
Exercisable, end of period	1,169	7.81	1,271	9.44

Details of the exercise prices and expiry dates of options outstanding at March 31, 2007 are as follows:

Range of Exercise price	Options Outstanding			Options Exercisable	
	Common Shares Issuable	Weighted Average Years to Expiry	Weighted Average Exercise Price	Common Shares Issuable	Weighted Average Exercise Price
	<i>(thousands)</i>	<i>(years)</i>	<i>(\$/share)</i>	<i>(thousands)</i>	<i>(\$/share)</i>
\$2.60 - \$3.50	554	1.92	\$ 2.76	513	\$ 2.73
\$4.50 - \$5.00	469	3.16	\$ 4.76	235	\$ 4.76
\$8.10 - \$9.00	303	3.67	\$ 8.38	151	\$ 8.38
\$12.05 - \$14.00	3,228	5.93	\$ 12.09	30	\$ 14.00
\$18.00 - \$21.65	1,241	4.79	\$ 20.14	240	\$ 20.53
	5,795	4.96	\$ 12.13	1,169	\$ 7.81

The fair value of stock options granted is estimated using the Black-Scholes option pricing model with the following assumptions.

	Three months ended March 31, 2007
Weighted average expected volatility (%)	51
Risk-free rate of return (%)	4.2
Expected option life (years)	4
Weighted average fair value (\$/share)	5.37

The Company does not anticipate paying any dividends during the expected life of the options.

Contributed Surplus

	Three months ended March 31, 2007	Year ended December 31, 2006
Balance, beginning of period	9,962	3,627
Stock-based compensation expense, net of recovery	1,121	5,677
Capitalized stock-based compensation expense	443	883
Recovery of capitalized stock-based compensation expense	(626)	-
Transferred to share capital on exercise of stock options	(41)	(225)
Balance, end of period	10,859	9,962

Deferred Share Units Plan

In 2006, the Company implemented a deferred share unit ("DSU") plan for non-management directors. Under the terms of the plan, DSUs awarded will vest immediately and will be settled with cash in the amount equal to the closing price of the Company's class A common shares on the date the Director specifies upon tendering their resignation from the Board.

The Company has recorded a liability of \$140,000 relating to DSUs and there are 10,220 DSUs outstanding at March 31, 2007.

7. Commodity Price Risk Management

The Company uses a variety of derivative instruments to reduce its exposure to fluctuations in commodity prices. Derivative instruments are classified as held for trading and recorded at fair value on the consolidated balance sheet. No derivative instruments were designated as hedges during the three months ended March 31, 2007.

Realized Financial Instrument Gain

The realized hedging gain of \$1.8 million for the three months ended March 31, 2007 relates to the cash settlement of derivative instruments.

Unrealized Financial Instrument Gain (Loss)

The unrealized financial instrument loss of \$6.6 million for the three months ended March 31, 2007 represents the change in fair value of the Company's financial risk management agreements from December 31, 2006 to March 31, 2007. The loss is calculated as follows:

	Three months ended March 31, 2007
Balance, beginning of period	3,194
Change in fair value of derivative instrument contracts	(6,635)
Balance, end of period	(3,441)

The following commodity price risk management agreements were in place as at March 31, 2007.

Financial WTI Crude Oil Contracts

Term	Contract	Volume (bbls/d)	Fixed Price (\$/bbl)	Unrealized Gain (Loss) As at March 31, 2007 (CDN \$000s)
Jan 07 to Dec 07	Collar	1,750	US \$55.00 to \$86.15	7
Jan 07 to Dec 07	Collar	1,750	US \$60.00 to \$80.70	126
Jan 07 to Dec 07	Swap	500	Cdn \$73.00	(793)
Jan 07 to Dec 07	Swap	500	Cdn \$73.70	(688)
Jan 07 to Dec 07	Swap	500	Cdn \$74.70	(537)
Jan 07 to Dec 07	Swap	500	Cdn \$75.82	(369)

Financial AECO Natural Gas Contracts

Term	Contract	Volume (GJs/d)	Fixed Price (\$/GJ)	Unrealized Gain (Loss) As at March 31, 2007 (CDN \$000s)
Jul 06 to Mar 08	Collar	5,000	Cdn \$6.00 to \$11.10	(413)
Jan 07 to Dec 07	Swap	2,500	Cdn \$7.55	(196)
Jan 07 to Dec 07	Swap	2,500	Cdn \$7.62	(149)
Feb 07 to Mar 08	Swap	1,250	Cdn \$7.68	(229)
Feb 07 to Mar 08	Swap	1,250	Cdn \$7.70	(200)

8. Long-term Investment

At March 31, 2007, the Company's long-term investment of \$1.2 million was comprised of 1,080,000 common shares of In-Depth Resources Ltd. ("In-Depth"), a privately held oil and natural gas company. The investment in In-Depth has been classified as available for sale and recorded at cost.