Velo Energy Inc.
Consolidated Financial Statements
2nd Quarter 2008
Interim Report

SECOND QUARTER FINANCIAL STATEMENTS

INTERIM UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

In accordance with National Instrument 51-102 released by the Canadian Securities Administrators, Velo Energy Inc. (the Company) discloses that its auditors have not reviewed the unaudited consolidated financial statements for the period ended June 30, 2008.

NOTICE TO READER OF THE CONSOLIDATED FINANCIAL STATEMENTS

The consolidated financial statements of the Company, comprising the accompanying interim unaudited consolidated balance sheet as at June 30, 2008 and the interim unaudited consolidated statements of operations and deficit and cash flows for the six month period then ended are the responsibility of the Company's management.

These consolidated financial statements have not been reviewed on behalf of the shareholders by the independent external auditors of the Company, MacKay LLP. The interim consolidated financial statements have been prepared by management and include the selection of appropriate accounting principles, judgments and estimates necessary to prepare these consolidated financial statements in accordance with Canadian generally accepted accounting principles.

"Rick Wlodarczak"

Rick Wlodarczak
Director

"John Muir"

John Muir
Director

Velo Energy Inc.
Consolidated Balance Sheets

	June 30 2008 (unaudited)	December 31 2007 (audited)
Assets		
Current		
Cash	**$1,402**	$83,258
Receivables	**44,880**	82,745
Prepaid expenses and deposits (note 8)	**342,110**	359,735
	$388,392	$525,738
Liabilities		
Current		
Accounts payable and accrued liabilities (note 5)	**$1,393,378**	$1,501,091
Indemnity payable (note 6)	**452,133**	452,133
Loan payable (note 7)	**20,000**	-
Asset retirement obligations (note 8)	**133,985**	140,000
	1,999,496	2,093,224
Shareholders' Equity (Deficiency)		
Share Capital (note 9(a))	**5,583,466**	5,583,466
Contributed Surplus (note 10)	**240,394**	240,394
Warrants	**48,700**	48,700
Deficit	**(7,483,664)**	(7,440,046)
	(1,611,104)	(1,567,486)
	$388,392	$525,738

See note 1 for going concern

See note 14 for commitment and contingency

See Note 15 for subsequent events

See accompanying notes to consolidated financial statements

Velo Energy Inc.
Consolidated Statements of Operations and Deficit

(unaudited)

	Three months June 30, 2008	Three Months June 30, 2007	**Six months June 30, 2008**	Six months June 30, 2007
Natural gas revenue	**-**	$9,565	**-**	$9,613
Expenses				
General and administrative	**31,751**	181,497	**50,230**	273,696
Interest	-	31,082	**3,763**	31,082
Operations	**-**	39,668	**(6,572)**	64,009
Stock based compensation (note 5(c))	**-**	-	**-**	30,724
Impairment of oil and gas properties (note 4)	**-**	349,163	**-**	4,204,838
Goodwill impairment (note 3)	**-**	-	**-**	1,026,400
Depreciation and accretion	**-**	2,757	**-**	6,076
	31,751	604,167	**47,421**	5,636,825
Interest income	**3,183**	2,653	**3,803**	10,916
Net loss and comprehensive loss	**(28,241)**	(591,949)	**(43,618)**	(5,616,296)
Deficit, beginning of period	**(7,455,423)**	(5,791,145)	**(7,440,046)**	(766,798)
Deficit, end of period	**$(7,483,664)**	$(6,383,094)	**$(7,483,664)**	$(6,383,094)
Loss per share (basic and diluted)	**$(0.00)**	$(0.02)	**$(0.00)**	$(0.19)
Weighted average number of shares outstanding	**29,618,334**	29,618,334	**29,618,334**	29,618,334

See note 1 for going concern

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Velo Energy Inc.

Consolidated Statements Of Cash Flows

(unaudited)

	Three Months June 30, 2008	Three Months June 30, 2007	**Six Months June 30, 2008**	Six Months June 30, 2007
Cash Provided By (Used In)				
Operating Activities				
Net loss	**$(28,241)**	$(591,949)	**$(43,618)**	$(5,616,296)
Add non-cash items:				
Stock-based compensation	**-**	-	**-**	30,724
Goodwill impairment	**-**	-	**-**	1,026,400
Impairment of oil and gas properties	**-**	349,163	**-**	4,204,838
Depreciation and accretion	**-**	2,757	**-**	6,076
	(28,241)	(240,029)	**(43,618)**	(348,258)
Net change in non-cash working capital	**19,862**	-	**17,360**	(55,491)
	(8,379)	(240,029)	**(26,258)**	(403,749)
Financing Activities				
Share issue costs	**-**	(554)	**-**	(20,884)
Loan payable	**-**	-	**20,000**	-
Net change in non-cash working capital	**-**	-	**3,750**	(31,064)
	-	(554)	**23,750**	(51,948)
Investing Activities				
Additions to property, plant and equipment	**-**	(350,972)	**-**	(991,039)
Net change in non-cash working capital	**(10,342)**	371,964	**(79,348)**	(1,191,772)
	(10,342)	20,992	**(79,348)**	(2,182,811)
Increase (Decrease) in cash during period	**(18,721)**	(219,591)	**(81,856)**	(2,638,508)
Cash, beginning of period	**20,123**	775,996	**83,258**	3,194,913
Cash, end of period	**$1,402**	$556,405	**$1,402**	$556,405

See note 1 for going concern

See note 14 for commitment and contingency

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See accompanying notes to consolidated financial statements

1. Nature of Operations and Going Concern

Velo Energy Inc. ("Velo" or the "Company") was incorporated on July 8, 2004 and was originally classified as a Capital Pool Corporation as defined in Policy 2.4 of the TSX Venture Exchange Corporate Finance Manual and Policies. Effective May 31, 2006 The Company. purchased all of the outstanding shares of Velo Energy Ltd. by the issuance of 3,333,334 common shares of the Company. This was an arm's length transaction and constituted the Company's Qualifying Transaction under the rules of the TSX Venture Exchange. As a result of that transaction the Company is in the business of exploration, development and production of crude oil, natural gas and natural gas liquids in Western Canada.

At June 30, 2008, the Company had incurred a cumulative loss of $7,483,664 and has no revenue producing oil and gas properties. The Company's ability to continue operations will depend upon future profitable operations from their oil and gas ventures and the raising of additional capital.

The financial statements have been prepared using generally accepted accounting principles that are applicable to a going concern. There are no assurances that the Company will achieve profitable operations. The financial statements do not reflect adjustments in the carrying value of the assets and liabilities, the reported revenue and expenses, and the balance sheet classifications used, that would be necessary if the going concern assumption were not appropriate, and that such adjustments could be material (See note 15).

2. Significant Accounting Policies

The unaudited interim period consolidated financial statements were prepared by management in accordance with Canadian generally accepted accounting principles ("GAAP") and follow the same accounting policies and methods of application as those used in the preparation of the audited annual consolidated financial statements for the year ended December 31, 2007 except as described below. Under Canadian GAAP, additional disclosure is required in annual financial statements and accordingly the unaudited interim period consolidated financial statements should be read together with the audited annual consolidated financial statements for the year ended December 31, 2007 and the accompanying notes included thereto.

The consolidated financial statements include the accounts of Velo Energy Inc. and its subsidiary collectively referred to as the "Company". The Company's interest in the voting share capital of its subsidiary is 100%.

Accounting Changes

The CICA amended Handbook Section 1400 "General standards of financial presentation" effective for periods beginning on or after January 1, 2008 to include requirements to assess and disclose the Company's ability to continue as a going concern. The adoption of this new section did not have an impact on the Company's financial statements.

In December 2006, the CICA issued Handbook section 1535 "Capital disclosures" which is effective for years beginning on or after October 1, 2007. The Company manages its capital to ensure it will be able to continue as a going concern while maximizing the return to shareholders largely through equity sales. These stock issues depend on numerous factors including a positive oil and gas environment, positive stock market conditions, a company's track record, and the experience of management. The capital structure of the Company consists of shareholder's equity, comprising issued capital and deficit.

2. Significant Accounting Policies (continued)

Accounting Changes (continued)

In December 2006, the CICA issued Handbook Section 3862, “Financial Instruments – Disclosures” and Handbook Section 3863, “Financial Instruments – Presentation” to replace Handbook Section 3861, “Financial Instruments – Disclosure and Presentation”. Section 3862 expands on the disclosures previously required under Section 3861 that establishes standards for disclosures about financial instruments and non-financial derivatives and identifies the information that should be disclosed about them. Section 3863 is consistent with the presentation requirements of Section 3861 that establishes standards for presentation of financial instruments and non-financial derivatives. These sections apply to interim and annual financial statements for fiscal periods beginning on or after October 1, 2007. The effect on the Company's financial statements was not material.

Recent accounting pronouncements

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 impact of the transition to IFRS on the Company’s financial statements has not yet been determined.

3. Business Acquisitions

On May 31, 2006 the Company acquired all of the shares of Velo Energy Ltd., a private oil and gas company. The acquisition was accounted for by the purchase method and the excess of the purchase price over the net assets acquired was allocated to goodwill.

Goodwill	$	1,081,759
Total purchase price	**$**	**1,081,759**

Consideration was comprised of:

Issue of 3,333,334 common shares	$	1,000,000
Costs related to the acquisition		81,759
Total consideration	**$**	**1,081,759**

The results of operations for Velo Energy Ltd. have been included in the consolidated financial statements since May 31, 2006.

At March 31, 2007, the Company tested goodwill for impairment and determined that based on the impairment of the oil and gas properties, further described in note 4, that the goodwill was impaired. As a result, a goodwill impairment charge of $1,026,400 was recorded in that quarter.

4. Property, Plant and Equipment

	June 30, 2008		
	Cost	Accumulated Amortization	Net
Petroleum and natural gas properties and equipment	$ -	$ -	$ -
Furniture, fixtures and equipment	-	-	-
Total	**$ -**	**$ -**	**$ -**

	June 30, 2007		
	Cost	Accumulated Amortization	Net
Petroleum and natural gas properties and equipment	$ 453,000	$ -	$ 453,000
Furniture, fixtures and equipment	24,578	14,864	9,654
Total	**$ 477,518**	**$ 14,864**	**$ 462,654**

Included in the Company's 2007 period expenses is a non-cash charge of $4,204,838 related to an impairment of the carrying value of petroleum and natural gas properties. The impairment is the result of applying what is commonly known as the ceiling test which is prescribed under generally accepted accounting principles for exploration and production companies that use the full cost accounting method.

An impairment loss is recognized when the carrying value of a cost centre is not recoverable and exceeds its fair value. The carrying amount is not recoverable if the carrying amount exceeds the sum of the undiscounted cash flows expected from its use and eventual disposition.

An impairment loss is then measured as the amount by which the carrying amount of the petroleum and natural gas assets capitalized in a cost centre exceeds the sum of the fair value of proved and probable reserves and the costs of unproved properties that have been subject to a separate test for impairment and contain no probable reserves.

In the first quarter of 2007, $21,000 of general and administrative expenses were capitalized to petroleum and natural gas properties.

5. Accounts Payable

During 2007 the Company made an informal proposal to its unsecured creditors. The basic terms of the proposal included an initial payment of 23% of the amount payable with a final payment of 17%. Creditors representing $1,031,980 in unsecured payables have agreed to the proposal. Forgiveness of the amounts agreed to will be recorded when the Company fulfills its obligations under the proposal.

6. Indemnity Payable

The Company issued $1,977,000 of flow through shares in December, 2006. The Company failed to spend the full $1,977,000 on qualifying expenditures as at December 31, 2007, the final day for qualification. As part of the subscription agreement the Company agreed to indemnify the

6. Indemnity Payable (continued)

subscribers of the flow through shares in the event of such an occurrence. The shortfall of $990,536 of qualified expenditures resulted in the indemnity payable of $452,133. The highest marginal tax rate of a subscriber's province of residence was used to calculate the payable.

In March, 2008 the Company mailed a proposal to the flow through share indemnity claimants. The offer proposed to extinguish the indemnity claims for common shares of the Company. The issue price of the shares is $.075 per share, resulting in a maximum of 6,028,440 shares issued if all claimants accept the proposal. As at June 30, 2008, 99% of the claimants had accepted the proposal.

7. Loan Payable

The loan is repayable on demand and bears interest at prime plus five percent.

8. Asset Retirement Obligations

At June 30, 2008, the Company had recorded $133,985 for future asset retirement obligations.

The asset retirement obligation was determined using the following assumptions:

- The total amount of undiscounted future cash flows to settle the liability is estimated to be $133,985.
- The liability is estimated to be settled within a year.

Deposits are being held by the Energy Resources Conservation Board as collateral for these obligations.

9. Share Capital

a) Authorized and Issued Common Shares

<u>Authorized</u>

An unlimited number of common voting shares (the "Common Shares") without nominal or par value and an unlimited number of preferred shares issuable in series, rights and restrictions to be determined by the board of directors upon issuance.

<u>Issued Share Capital</u>

The issued share capital is as follows:

9. Share Capital (continued)

	Number of Common Shares		Amount
Balance December 31, 2005	10,063,000	$	1,783,048
Issued to acquire Velo Energy Ltd.	3,333,334		1,000,000
Issued for cash	5,000,000		1,500,000
Issued on exercise of warrants	537,000		134,250
Issued on exercise of options	800,000		200,000
Flow-though share issuance	9,885,000		1,977,000
Share issuance costs	-		(520,387)
Transfer from contributed surplus on exercised options	-		104,000
Balance December 31, 2006	29,618,334	$	6,177,911
Share issue costs	-		(20,330)
Indemnity on unspent flow through funds	-		(452,133)
Tax effect of flow-through common shares	-		(128,313)
Balance, December 31, 2007 and June 30, 2008	29,618,334	$	5,583,466

In May 2006, the Company issued 5,000,000 common shares at $0.30 per share for gross proceeds of $1,500,000. In December 2006, the Company issued 9,885,000 flow-through common shares at $0.20 per share for gross proceeds of $1,977,000. Under the terms of the flow-through share agreement, the Company is committed to spend 100% of the gross proceeds on qualifying exploration and development expenditures prior to December 31, 2007, which it did not do. An indemnity payable was recorded for the short fall (see note 6).

b) Escrowed Shares

The 4,000,000 common shares issued to the founders (the “Seed Capital Shares”) for a total consideration of $500,000 were deposited with a trustee under an escrow agreement. In accordance with TSX Venture Exchange (the “Exchange”) Policy 2.4., 10% of the Seed Capital Shares were released from escrow on the issuance of the Final Exchange Bulletin on June 5, 2006 (the “Initial Release”) and an additional 15% will be or have been released on each of the dates which are 6 months, 18 months, 24 months, 30 months, and 36 months following the Initial Release.

The 3,333,334 common shares issued to purchase Velo Energy Ltd. are Value Escrow Shares. Under the Value Escrow Agreement and Exchange Policy 5.4, 10% of the Value Escrow Shares were released from escrow at the Initial Release and an additional 15% will be or have been released on each of the dates which are 6 months, 12 months, 18 months, 24 months, 30 months, and 36 months following the Initial Release.

All common shares of the Company acquired in the secondary market prior to the completion of a Qualifying Transaction by a control Person, as defined in the policies of the Exchange, are required to be deposited in escrow.

9. Share Capital (continued)

All Common Shares deposited in escrow and to be released subject to the completion of a Qualifying Transaction will be cancelled upon the issuance of a TSX Venture Exchange bulletin delisting the Common Shares of the Company.

c) Incentive Stock Options

On February 15, 2007 the Company granted 350,000 incentive stock options of the Company to purchase common shares at an exercise price of $0.20 per share. These options expire on four years from the date of grant and vest equally at the date of grant, June 15, 2007, October 15, 2007 and February 15, 2008.

Changes in the number of stock options, with their weighted average exercise prices, are summarized below:

	June 30, 2008		
	Number of Options		Weighted average exercise price
Outstanding, beginning of period	1,150,000	$	0.27
Exercised	-		-
Forfeited	(50,000)		0.30
Granted	-		-
Outstanding, end of the period	**1,100,000**	**$**	**0.27**
Exercisable	1,100,000	$	0.27

During the period, stock-based compensation expense was Nil (2007-$30,724) with a credit recorded to contributed surplus. The weighted average fair value of the options granted during the first quarter 2007 was $0.049 per share. The fair value of the options was estimated using the Black-Scholes option pricing model, using a risk-free interest rate of 4.0%, expected volatility of 60%, expected life of four years and no expected dividends.

d) Agent's Warrants

A summary of the status of the Company's warrants as of June 30, 2008 and changes during the period then ended is as follows:

	Number of Warrants		Weighted average exercise price
Balance, beginning of period	798,500	$	0.20
Issued in the period	-		-
Expired	(798,500)		0.20
Exercised in the period	-		-
Balance, end of the period	**-**	**$**	**-**

9. Share Capital (continued)

In December 2006, the Company granted the agents of the flow-through equity offering, warrants to purchase 798,500 common shares at a price of $0.20 per common share. The warrants to purchase the 798,500 common shares expired in June 2008.

10. Contributed Surplus

		June 30, 2008
Balance, beginning of year	$	240,394
Stock-based compensation		-
Exercised of stock options		-
Balance, end of period	**$**	**240,394**

11. Income Taxes

The Company has the following deductions available at June 30, 2008:

Undepreciated capital cost	$	908,057
Canadian development expenses	$	2,017,962
Canadian exploration expenses	$	801,065

12. Related Party Transactions

During the quarter the Company borrowed $20,000 from a corporation controlled by three directors of the Company. The loan is repayable upon demand and bears interest at prime plus 5%.

The above-noted related party transaction was in the normal course of business and was measured at the exchange value which was the amount of consideration established and agreed to by the related parties.

13. Financial instruments:

(a) Fair values:

At June 30, 2008, the fair values of all financial instruments approximated their carrying values due to their short-term maturity.

(b) Credit risk

The Company believes there is no unusual exposure as regular credit assessments are performed.

14. Commitment and Contingency

The President of the Company was dismissed during the second quarter of 2007. He has filed a wrongful dismissal action against the Company's wholly owned subsidiary, Velo Energy Ltd. The subsidiary will aggressively defend its position. The maximum potential exposure to the subsidiary is $60,000.

14. Commitment and Contingency (continued)

The Energy Utility Board has required a letter of credit be established with them for abandonment of wells. The letter of credit totals $342,187. This amount of cash is securing the letter of credit and is included in prepaid expenses and deposits.

15. Subsequent Events

Settlement of December 2006 Flow-Through Obligation

Having obtained the conditional approval of the TSX Venture Exchange (“TSX-V”), on July 24, 2008 the Company issued 5,990,554 shares from treasury at a price of $0.075 per share settling the indemnity obligation of $449,292. These shares are subject to a 4 month hold period in Canada.

New Joint Venture

Velo has entered into a confidential joint venture and participation agreement (the “Agreement”) with a private Alberta company, to jointly participate in a drilling, completion, seismic, recompletion of wells located on certain lands in Southern Alberta. The Company has committed up to a maximum of $1,000,000 to be expended by the end of 2009 on qualifying Canadian Exploration Expenses or Canadian Development Expenses. Generally, Velo will pay 100% of costs to earn 50% of the private company’s working interest in each well.

Other

Final payments to trade creditors of Velo Ltd. have been made and the restructuring completed. In July, 2008, Velo Ltd. was sold to Daran Energy Services Corp., a private Alberta company, for nominal consideration. The sale includes the shares of Velo Ltd. and the debt owing from Velo Ltd. to the Company.

Private Placement

Velo completed a private placement raising $1.5 million by issuing 30 million common shares at $0.05 per share. The Company paid finders fees of $57,500 (5%) in connection with $1,150,000 of the financing.