

CHANGFENG ENERGY INC.
INTERIM CONSOLIDATED FINANCIAL STATEMENTS
FOR THE THREE MONTH PERIOD ENDED MARCH 31, 2008
(Unaudited)
(Expressed in Canadian currency)

CHANGFENG ENERGY INC.
INTERIM CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2008
(Unaudited)
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(Expressed in Canadian currency)	March 31, 2008 (Unaudited) \$	December 31, 2007 (Audited) \$
ASSETS		
CURRENT		
Cash and cash equivalents (Note 4)	7,183,231	2,597,876
Accounts and sundry receivables	991,752	691,372
Prepaid expenses, advances and deposits	113,381	85,947
Inventories (Note 5)	524,814	416,301
	8,813,178	3,791,496
PLANT AND EQUIPMENT (Note 6)	24,286,322	21,547,918
FUTURE INCOME TAX (Note 9)	593,100	585,500
	33,692,600	25,924,914
LIABILITIES		
CURRENT		
Accounts payable and accrued liabilities	1,480,966	1,320,861
Short-term loans	-	200,000
Deferred revenue	1,781,396	1,853,253
Interest payable (Note 7)	2,183,524	1,920,159
Current portion of long-term debt (Note 7)	8,326,880	7,549,740
	13,772,766	12,844,013
LONG-TERM DEBT (Note 7)	5,893,320	5,980,260
DUE TO RELATED PARTIES (Note 10(b))	5,864,000	5,412,000
NON-CONTROLLING INTEREST	20,398	20,398
	25,550,484	24,256,671
SHAREHOLDERS' EQUITY		
CAPITAL STOCK (Note 8(b))	12,121,808	7,430,001
CONTRIBUTED SURPLUS (Note 8(d))	1,057,603	-
WARRANTS (Note 8(e))	321,724	-
ACCUMULATED OTHER COMPREHENSIVE LOSS (Note 13)	(300,589)	(460,613)
DEFICIT	(5,058,430)	(5,301,145)
	8,142,116	1,668,243
	33,692,600	25,924,914

GOING CONCERN (Note 1)
ECONOMIC DEPENDENCE (Note 14)

APPROVED ON BEHALF OF THE BOARD:

Signed "Christopher Harrop", Director

Signed "Jack Duffy", Director

INTERIM CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT
FOR THE THREE MONTHS ENDED MARCH 31,

(Expressed in Canadian currency)	2008 (Unaudited) \$	2007 (Unaudited) \$
REVENUE	2,966,091	2,277,140
COST OF SALES	1,201,416	875,935
GROSS MARGIN	1,764,675	1,401,205
EXPENSES		
General and administrative (Note 10(a))	737,401	561,081
Interest expense on long term debt (Note 7)	289,197	351,727
Travel and promotion	269,602	203,613
Amortization	239,966	320,003
	1,536,166	1,436,424
Income (loss) before the under-noted	228,509	(35,219)
Interest income	53,706	-
	282,215	(35,219)
Income tax expense	39,500	-
NET INCOME (LOSS) FOR THE PERIOD	242,715	(35,219)
DEFICIT, BEGINNING OF PERIOD	(5,301,145)	(5,303,740)
DEFICIT, END OF PERIOD	(5,058,430)	(5,338,959)
NET INCOME (LOSS) PER SHARE – basic and diluted	0.005	(0.001)
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING – basic and diluted	46,717,308	24,405,479

INTERIM UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
FOR THE THREE MONTHS ENDED MARCH 31,

(Expressed in Canadian currency)	2008 (Unaudited) \$	2007 (Unaudited) \$
NET INCOME (LOSS) FOR THE PERIOD	242,715	(35,219)
OTHER COMPREHENSIVE INCOME (LOSS) FOR THE PERIOD		
Currency translation adjustment	160,024	(3,350)
COMPREHENSIVE INCOME (LOSS) FOR THE PERIOD	402,739	(38,569)

Unaudited; See accompanying notes to the interim unaudited consolidated financial statements.

CHANGFENG ENERGY INC.
INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS
 FOR THREE MONTHS ENDED MARCH 31,

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(Expressed in Canadian currency)	2008 (Unaudited) \$	2007 (Unaudited) \$
CASH FLOWS USED IN OPERATING ACTIVITIES		
Net Income (loss) for the period	242,715	(35,219)
Adjustments for:		
Income taxes	39,500	-
Amortization	<u>239,966</u>	<u>320,003</u>
	522,181	284,784
Changes in non-cash working capital balances		
Accounts and sundry receivables	(173,167)	(46,278)
Prepaid expenses, advances and deposits	(19,739)	(17,952)
Inventories	(70,525)	(27,018)
Accounts payable and accrued liabilities	(381,036)	93,086
Deferred revenue	(216,743)	(203,811)
Interest payable	<u>98,500</u>	<u>358,976</u>
Cash flows used in operating activities	<u>(240,529)</u>	<u>441,787</u>
CASH FLOWS USED IN INVESTING ACTIVITIES		
Plant and equipment	<u>(1,137,745)</u>	<u>(137,674)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Short-term loans	-	(39,260)
Payment of interest on convertible debenture (Note 8(b))	(549,797)	-
Long term debt	(420,600)	(181,200)
Cash acquired on RTO (Note 2)	<u>6,718,427</u>	<u>-</u>
	<u>5,748,030</u>	<u>(220,460)</u>
Effects of foreign exchange on cash balances	<u>215,599</u>	<u>(1,823)</u>
INCREASE IN CASH AND CASH EQUIVALENTS	4,585,355	81,830
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	<u>2,597,876</u>	<u>230,677</u>
CASH AND CASH EQUIVALENTS, END OF PERIOD	<u>7,183,231</u>	<u>312,507</u>
SUPPLEMENTAL INFORMATION		
Interest paid	190,503	38,587
Taxes paid	-	-

Unaudited; See accompanying notes to the interim unaudited consolidated financial statements.

NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2008

(Expressed in Canadian currency)

1. BASIS OF PRESENTATION AND GOING CONCERN

Changfeng Energy Inc. (the "Company") was incorporated under the Canada Business Corporation Act on May 4, 2006. The reorganization described in Note 2 was completed on January 29, 2008 and the Company's core business is the distribution of natural gas in Southern China, through its wholly-owned subsidiary, Hainan Energy Limited.

The Company is a rate-regulated natural gas distribution utility, serving residential and commercial customers in Hainan Province, the People's Republic of China ("PRC"). The rights of operation of a gas pipeline infrastructure and provision of piped gas business in PRC are established by permits obtained from the city and provincial governments. The plant and equipment of the Company consist primarily of pipeline, storage and compression facilities used in the transportation, storage and distribution of natural gas.

Substantially all of the assets of the Company, most of which are located in PRC, are subject to the risk of foreign investment, including increases in taxes and royalties, renegotiation of contracts and permits, currency exchange fluctuations and political uncertainty. The Company's operations are subject to government legislation, policies and controls relating to transportation, storage, distribution, pricing, environmental protection, taxes and labour standards. In order for the Company to carry out its distribution activities, the Company is required to hold certain permits. There is no assurance that the Company's existing permits will be renewed or that new permits that have been applied for will be granted.

The accompanying unaudited interim consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and follow the same accounting policies and methods of application as the audited consolidated financial statements of Hainan Energy Limited for the year ended December 31, 2007, except as disclosed in Note 3. They do not include all of the information and disclosures required by Canadian GAAP for annual financial statements. In the opinion of management, all adjustments considered necessary for fair presentation have been included in these financial statements. Operating results for the period ended March 31, 2008 are not necessarily indicative of the results that may be expected for the full year ended December 31, 2008. For further information, see Hainan Energy Limited's consolidated financial statements including the notes thereto for the year ended December 31, 2007.

As at March 31, 2008, the Company had a working capital deficiency of \$4,959,588. These consolidated financial statements have been prepared on the basis of accounting principles applicable to a "going concern", which assume that the Company will continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities in the normal course of operations. There is no guarantee that the Company's current level of operations will yield positive results or that the Company will be able to obtain the necessary financing to support ongoing natural gas distribution operations. If the "going concern" assumption was not appropriate for these interim consolidated financial statements, then adjustments would be necessary to the carrying values of assets and liabilities, the reported revenues and expenses, and the balance sheet classifications used. Such adjustments could be material.

Continued...

NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2008

(Expressed in Canadian currency)

2. REVERSE TAKEOVER TRANSACTIONS

Pursuant to an acquisition agreement dated November 28, 2007, the Company issued 32,750,000 common shares of the Company to CF Energy (BVI) Limited on January 29, 2008 in consideration for all of the issued and outstanding shares of Hainan Energy Limited ("Hainan Energy") not otherwise held by the Company. Hainan Energy holds a 100% interest in Sanya Changfeng Offshore Natural Gas Supply Co. Ltd. ("CF China"), a rate-regulated natural gas distribution utility, serving residential and commercial customers in Hainan Province, the People's Republic of China. Substantially all of the assets of Hainan Energy are located in China.

Following the transaction, the former shareholder of Hainan Energy held more than 50% of the issued and outstanding common shares of the Company. The substance of the transaction was a capital transaction and was accounted for as a reverse takeover in accordance with EIC-10 "Reverse Takeover Accounting" of the CICA Handbook. Hainan Energy, the legal subsidiary is considered to have acquired the assets and liabilities of the Company, the legal parent. Prior to the transaction, the legal parent had outstanding 7,000,000 common shares, 3,750,000 options to purchase common shares at an exercise price of \$0.60 per share valued at \$1,057,603, and 1,000,000 warrants to purchase common shares at an exercise price of \$0.60 valued at \$321,724. The 3,750,000 options and 1,000,000 warrants granted by the legal parent were exchanged for an equivalent number of options and warrants of the legal subsidiary. The options and warrants granted by the legal subsidiary were valued at fair value, and form part of the cost of the acquisition.

Based on the unaudited January 29, 2008 balance sheet of the legal parent, the net assets that were acquired by Hainan Energy were as follows:

Cash	\$ 6,718,427
Non-cash working capital (deficiency)	(309,482)
Advances and deferred costs	766,537
Liability component of convertible debentures	<u>(549,797)</u>
Net assets acquired	<u>\$ 6,625,685</u>

Immediately following the Hainan Energy reverse take-over ("RTO"), the Company and McBroom Resources Inc. ("McBroom") completed their previously announced combination to form Amalco. McBroom filed Articles of Continuance effective January 14, 2008 to continue from the Province of Ontario to the federal jurisdiction of Canada, and McBroom and the Company filed Articles of Amalgamation effective January 29, 2008 to complete the combination, with Amalco issuing one common share for each share of the Company and McBroom outstanding on January 29, 2008. In accordance with EIC-10, the substance of the transaction was a capital transaction and was accounted for as a RTO. The Company, the legal subsidiary, was considered to have acquired the assets and liabilities of McBroom, the legal parent.

Based on the unaudited January 29, 2008 balance sheet of McBroom, the net liabilities that were assumed by the Company were as follows:

Non-cash working capital (deficiency)	<u>\$ (28,831)</u>
Net liabilities assumed	<u>\$ (28,831)</u>

As a result of the transactions described above and in accordance with RTO accounting, the interim consolidated financial statements are a continuation of Hainan Energy and the comparative figures presented in the interim consolidated financial statements are those of Hainan Energy.

Costs related to these transactions approximating \$525,720, were charged to equity during the period ended March 31, 2008.

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NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

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(Expressed in Canadian currency)

3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the Company are in accordance with Canadian generally accepted accounting principles and their basis of application is consistent with the prior period, except as disclosed below. Outlined below are those policies considered particularly significant.

Basis of Consolidation

The interim consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries Hainan Energy Limited, Sanya Changfeng Offshore Natural Gas Supply Co. Ltd. ("CF China"), Sanya Changfeng Offshore Natural Gas Engineering Construction Co. Ltd., and Sanya Changfeng Offshore Natural Gas Design Co. Ltd. These interim consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. All material inter-company balances and transactions have been eliminated.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand and balances with banks, cashable guaranteed investment certificates, and short-term investments with original maturities of three months or less.

Inventories

Inventories, including construction materials, gas appliances and meters, consumables and spare parts are stated at the lower of cost and net realizable value, with cost being determined using the weighted average cost basis.

Plant and Equipment, Construction in Progress and Amortization

Construction in progress represents machinery and pipelines under construction and is stated at cost. Cost comprises directly attributable costs of acquisition or construction, which include capitalized borrowing costs. Assets under construction are not depreciated. Completed items are transferred from construction in progress to proper categories of property, plant and equipment when they are ready for their intended use. Plant and equipment are recorded at cost.

Amortization of plant and equipment is provided at the following annual rates:

Pipelines and related equipment	30 - 35 years straight line
Motor vehicles	3 - 8 years straight line
Furniture and office equipment	3 - 5 years straight line
Computer equipment	3 - 5 years straight line

Asset Retirement Obligations

The accounting standard for asset retirement obligations, under normal circumstances, requires companies to recognize the fair value of a liability for an asset retirement obligation in the period in which it is incurred if a reasonable estimate of fair value can be determined. The associated asset retirement cost is capitalized as part of the carrying amount of the long-lived asset. The liability is accreted over the estimated useful life of the asset.

The Company's natural gas distribution network is comprised of mains, service lines, measuring and regulating equipment and storage facilities. The Company estimates that it does not have a material legal retirement obligation with respect to its distribution and supply network.

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NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2008

(Expressed in Canadian currency)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)**Revenue Recognition**

Revenues mainly include revenue from the delivery of natural gas and revenue from the installation and connection of natural gas pipelines for end users. The Company recognizes revenues when gas has been delivered. Gas distribution revenues are recorded on the basis of regular meter readings and estimates of usage since the last meter reading to the end of the reporting period. Revenues and cost of gas are recorded using relatively fixed prices approved by the provincial government.

Gas connection revenue is deferred and only recognized when the outcome of a contract can be estimated reliably and the stage of completion at the balance sheet date can be measured reliably. Revenue from gas connection contracts is recognized on the percentage of completion method, measured by reference to the value of work carried out during the period. When the outcome of a gas connection contract cannot be estimated reliably, revenue is deferred and only recognized to the extent of contract cost incurred that is probable to be recoverable and contract costs are recognized as expenses in the period in which they are incurred. When it is probable that total contract costs will exceed contract revenue, the expected loss is recognized as an expense immediately. Sales of gas appliances are recognized when goods are delivered and title has passed.

As at March 31, 2008, the Company had deferred revenue of \$1,781,396 (December 31, 2007 – \$1,853,253) with respect to deposits received from customers in excess of the value of work carried out during the period.

Income Taxes

The Company uses the asset and liability method of accounting for income taxes. Under this method of tax allocation, future income taxes are determined based on the differences between the financial reporting and tax bases of assets and liabilities. These income tax assets and liabilities are measured using the substantially enacted tax rates in which the income tax assets or liabilities are expected to be settled or realized. A valuation allowance is provided to the extent that it is more likely than not that future income tax assets will not be realized.

Entities Subject to Rate Regulation

In May 2005, the Canadian Institute of Chartered Accountants (“CICA”) issued Accounting Guidelines 19 (“AcG-19”) of the CICA Handbook to establish disclosure guidelines for entities subject to rate regulation. AcG-19 provides guidance for the disclosure of general information regarding the nature and economic effects of rate regulation, as well as additional information on how rate regulation has affected the financial statements. The guideline does not address recognition and measurement issues associated with the accounting for rate-regulated operations.

The Company is a rate-regulated, natural gas distribution utility and operates within Hainan Province, PRC. The utility operation of the Company is subject to regulation. Rate schedules are approved periodically by the PRC government and are designed to permit a fair and reasonable return on the utility investment.

The Company follows Canadian GAAP, which may differ for regulated operations from those otherwise expected in non-regulated businesses. As a result, the Company may record assets and liabilities that result from the regulated rate making process that would not have been recorded under GAAP for non-regulated entities. Regulatory assets generally represent incurred costs that have been deferred because they are probable of future recovery in customer rates. Regulatory liabilities generally represent obligations to make refunds to customers for previous collections for costs that are not likely to be incurred. The Company did not have any rate-regulated assets or liabilities as at December 31, 2007 and March 31, 2008.

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3. **SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Interest Income

Interest income is recorded on an accrual basis.

Foreign Currency Translation

The Canadian dollar is the functional currency of the parent Company's operations, and the Chinese Renminbi or ("RMB") is the functional currency of the Company's subsidiaries. The Canadian dollar has been chosen as the reporting currency of the Company.

Monetary assets and liabilities are translated into Canadian dollars at exchange rates in effect at the balance sheet date. Non-monetary assets and liabilities are translated at historical exchange rates, unless such items are carried at market, in which case they are translated at the exchange rates in effect on the balance sheet date. The Company's foreign subsidiaries are defined as self-sustaining. Assets and liabilities denominated in RMB are translated into Canadian dollars using exchange rate in effect on the balance sheet date. Operating revenues and expenses are translated at the average exchange rates during the period. Foreign exchange gains and losses arising from translation of the balances are disclosed separately as comprehensive income or loss. The accumulated foreign exchange gains or losses are reported as a separate component of shareholders' equity as the accumulated other comprehensive income or loss.

Stock-based Compensation

The Company records compensation cost based on the fair value method of accounting for stock-based compensation. The fair value of stock options is determined using the Black-Scholes option-pricing model. The fair value of the options is recognized over the vesting period as compensation expense and contributed surplus. When options are exercised, the proceeds received, together with any related amount in contributed surplus, will be credited to share capital. The Company's stock option plan is described in Note 8(c).

Loss Per Share

Basic loss per share is calculated using the weighted average number of shares outstanding. Diluted loss per share is calculated using the treasury stock method. In order to determine diluted loss per share, the treasury stock method assumes that any proceeds from the exercise of dilutive stock options and warrants would be used to repurchase common shares at the average market price during the period, with the incremental number of shares being included in the denominator of the diluted loss per share calculation. The diluted loss per share calculation excludes any potential conversion of options and warrants that would increase earnings per share or decrease loss per share.

NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2008

(Expressed in Canadian currency)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)**Measurement Uncertainty**

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the related reported amounts of revenue and expense during the report period. Such estimates and assumptions affect the carrying value and useful lives of assets and affect the valuation of investments, the debt and equity components of convertible debentures, stock-based compensation and income tax accounts. Actual results could differ from those estimates. Management believes that the estimates are reasonable.

Government Assistance

Government assistance related to current expenses is recorded as a reduction of these expenses in the period incurred.

Financial Instruments - Recognition and Measurement

This standard prescribes when a financial asset, financial liability, or non-financial derivative is to be recognized on the balance sheet and whether fair value or cost-based methods are used to measure the recorded amounts. It also specifies how financial instrument gains and losses are to be presented. All derivatives are recorded on the balance sheet at fair value. Mark-to-market adjustments on these instruments are included in net income, unless the instruments are designated as part of a cash flow hedge relationship.

All other financial instruments will be recorded at cost or amortized cost, subject to impairment reviews. The criteria for assessing other than temporary impairment remain unchanged. Transaction costs incurred to acquire financial instruments are included in the underlying balance.

Comprehensive Income

This standard requires the presentation of a statement of comprehensive income and its components. Comprehensive income includes both net earnings and other comprehensive income. Other comprehensive income includes holding gains and losses on available for sale investments, gains and losses on certain derivative instruments and foreign currency gains and losses relating to self-sustaining foreign operations, all of which are not included in the calculation of net earnings until the period that the related asset or liability affects income.

Hedges

This standard is applicable when a company chooses to designate a hedging relationship for accounting purposes. It builds on the previous AcG-13 "Hedging Relationships" and Section 1650 "Foreign Currency Translation", by specifying how hedge accounting is applied and what disclosures are necessary when it is applied. The Company currently does not have any instruments that are covered in this standard.

Transaction Costs

On June 1, 2007, the Emerging Issues Committee of the CICA issued Abstract No. 166 "Accounting Policy Choice for Transaction Costs ("EIC-166"). This EIC addresses the accounting policy choice of expensing or adding transaction costs related to the acquisition of financial assets and financial liabilities that are classified as other than held-for-trading. Specifically, it requires that the same accounting policy choice be applied to all similar financial instruments that are not similar. The Company has evaluated the impact of EIC-166 on adoption and determined that no adjustments were required.

Continued...

NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2008

(Expressed in Canadian currency)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)**Accounting Changes**

This standard requires that: a) a voluntary change in accounting policies can be made if, and only if, the changes result in more reliable and relevant information; b) changes in accounting policies are accompanied with disclosures of prior period amounts and justification for the change; and c) for changes in estimates, the nature and amount of the change should be disclosed. The Company has not made any voluntary change in accounting policies since the adoption of the revised standard.

New Accounting Policies

On December 1, 2006, the CICA issued the following new accounting standards: Capital Disclosures (Handbook Section 1535), Financial Instruments - Disclosures (Handbook Section 3862), Financial Instruments - Presentation (Handbook Section 3863), and Inventories (Handbook Section 3031). These new standards became effective for the Company on January 1, 2008.

Capital Disclosures

CICA Handbook Section 1535 "Capital Disclosures", issued in December 2006, establishes standards for disclosures about capital that are effective for fiscal periods beginning on or after October 1, 2007. It requires an entity to disclose its objectives, policies and processes for managing capital and to disclose quantitative data about what it considers to be capital. It also requires an entity to disclose whether it has complied with any externally imposed capital requirements and, if not, the consequences of such non-compliance. The Company has included disclosures recommended by the new Handbook section in Note 15 to these interim consolidated financial statements.

Financial Instruments

In December 2006, the Canadian Accounting Standards Board (AcSB) issued two new Sections in relation to financial instruments: Section 3862, Financial Instruments - Disclosures, and Section 3863, Financial Instruments - Presentation. The Company adopted both sections, effective January 1, 2008. The Company has included disclosures recommended by the new Handbook section in Note 11 to these interim consolidated financial statements.

Inventories

In June 2007, the CICA issued section 3031, Inventories, which requires inventory to be measured at lower of cost and net realizable value. The standard also provides guidance on costs that can be capitalized. In addition, previous inventory write-downs must be reversed if the economic circumstances have changed to support an increase in the previously impaired inventory value. The adoption of this standard did not have a material impact on the interim consolidated financial statements.

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NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2008

(Expressed in Canadian currency)

4. CASH AND CASH EQUIVALENTS

	March 31, 2008 (Unaudited) \$	December 31, 2007 (Audited) \$
Cash	7,166,927	2,597,876
Cashable guaranteed investment certificate, bearing interest of 3%	16,304	-
	<u>7,183,231</u>	<u>2,597,876</u>

5. INVENTORIES

	March 31, 2008 (Unaudited) \$	December 31, 2007 (Audited) \$
Construction materials	360,033	225,887
Gas appliances, meters, and spare parts	164,781	190,414
	<u>524,814</u>	<u>416,301</u>

6. PLANT AND EQUIPMENT

	March 31, 2008 Cost \$	Accumulated Amortization \$	March 31, 2008 Net \$
Pipelines and related equipment	25,416,820	4,268,251	21,148,569
Motor vehicles	605,675	59,085	546,590
Furniture and office equipment	256,088	30,848	225,240
Computer equipment	46,711	22,192	24,519
	<u>26,325,294</u>	<u>4,380,376</u>	<u>21,944,918</u>
Construction in progress	2,341,404	-	2,341,404
	<u>28,666,698</u>	<u>4,380,376</u>	<u>24,286,322</u>
	December 31, 2007 Cost (Audited) \$	Accumulated Amortization (Audited) \$	December 31, 2007 Net (Audited) \$
Pipelines and related equipment	22,907,876	3,720,088	19,187,788
Motor vehicles	279,948	47,925	232,023
Furniture and office equipment	223,300	24,149	199,151
Computer equipment	39,358	18,994	20,364
	<u>23,450,482</u>	<u>3,811,156</u>	<u>19,639,326</u>
Construction in progress	1,908,592	-	1,908,592
	<u>25,359,074</u>	<u>3,811,156</u>	<u>21,547,918</u>

Continued...

NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2008

(Expressed in Canadian currency)

7. LONG-TERM DEBT

	March 31, 2008 (Unaudited) \$	December 31, 2007 (Audited) \$
a) Term Loan Facility – China Development Bank RMB 44,800,000 (December 31, 2007 – RMB 47,800,000), advanced from the China Development Bank to Sanya Assets Management Corporation (an intermediary company controlled by the municipality of Sanya City, see Note 7(b)), and re- loaned to the Company, bearing interest at the prescribed rate of the People’s Bank of China (7.83% at March 31, 2008) due quarterly, principal repayments commencing February 2008, due November 2012, secured by pipelines of the Company with an estimated net book value as at March 31, 2008 of \$21,148,569 (December 31, 2007 of \$ 19,187,788).	6,567,680	6,467,340
b) Term Loan Facility – Sanya State Assets Management Corporation RMB 42,200,000 (December 31, 2007 – RMB 42,200,000), representing principal repayments of the term loan facility described in Note 7(a) made by Sanya State Assets Management Co. on behalf of the Company, unsecured, non-interest bearing, with no fixed terms of repayment.	6,186,520	5,709,660
c) Term Loan Facility – Bank of China RMB 10,000,000 (December 31, 2007 - RMB 10,000,000), bears interest (8.415% at March 31, 2008) at a rate of 110% of the prescribed rate of the People’s Bank of China prime lending rate due monthly, repayable in 20 monthly principal payments of RMB 500,000 (\$67,650) commencing April 30, 2011. This loan is secured by gas connection fees.	1,466,000	1,353,000
	14,220,200	13,530,000
Less: current portion	(8,326,880)	(7,549,740)
	5,893,320	5,980,260

Principal payments over successive periods ended March 31 are as follows:

	RMB	\$
2009	56,800,000	8,326,880
2010	12,600,000	1,847,160
2011	10,100,000	1,480,660
2012	11,000,000	1,612,600
2013	6,500,000	952,900
	97,000,000	14,220,200

Continued...

NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

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7. LONG-TERM DEBT (Continued)

As at March 31, 2008, the Company had accrued interest of \$2,150,931 (RMB 14,672,109) (December 31, 2007 - \$1,894,592; RMB 14,002,900) with respect to the loan facilities described in Notes 7(a) and (b), and accrued interest of \$32,593 (RMB 222,326) with respect to the loan facility described in Note 7(c) (December 31, 2007 - \$3,437, RMB 25,400).

The entire balance of the loan described in Note 7(b) has been classified as current due to the fact that no fixed terms of repayment have been established. Management believes that Sanya State Management Company will not require repayment in full during the next twelve months.

8. CAPITAL STOCK**a) Authorized**

Unlimited number of common shares

b) Issued

66,025,000 common shares

Transactions during the period are as follows:

	Number of Shares	Amount
	#	\$
Balance, December 31, 2006	50,000	1,630,001
Issue of shares (i)	<u>50,000</u>	<u>5,800,000</u>
Balance, December 31, 2007	100,000	7,430,001
Adjustments to give effect to RTO transactions (Note 2)		
Adjust number of common shares outstanding to that of the legal parent immediately prior to the RTO	6,900,000	-
Share exchange to effect RTO and conversion of subscription receipts (ii) and convertible debentures (iii)	59,025,000	5,217,527
RTO transaction costs	<u>-</u>	<u>(525,720)</u>
Balance, March 31, 2008	<u>66,025,000</u>	<u>12,121,808</u>

(i) On July 6, 2007, Hainan Energy issued 50,000 shares of Hainan Energy to the Company for cash consideration of \$5,800,000.

(ii) Prior to the RTO described in Note 2, the legal parent completed a private placement and issued 12,500,000 subscription receipts for gross proceeds of \$7,500,000. These subscription receipts were subsequently converted into 12,500,000 common shares for no additional consideration. The legal parent paid cash commission of \$600,000 and issued 1,000,000 agent's warrants valued at \$321,724 (see Note 8(e)). The legal parent also incurred additional costs of \$585,000 relating to the private placement.

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NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

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(Expressed in Canadian currency)

8. CAPITAL STOCK (Continued)**b) Issued (Continued)**

(iii) In 2007, the legal parent issued 12,000,000 common shares upon the conversion of convertible debentures (the "Debentures") at a conversion price of \$0.50 per common share. The Debentures were issued by the legal parent during the year ended December 31, 2006 for gross proceeds of \$6,000,000 less related costs of \$314,530. The Debentures bore simple interest at an annual rate of 12% of the principal amount payable upon the earlier of:

- i. the conversion of the Debentures; and
- ii. May 19, 2012.

On January 29, 2008, the Company paid interest of \$549,797 to the Debenture holders in full settlement of the interest payable, upon conversion of the Debentures.

c) Stock Options

The Company has a stock option plan to assist the Company in attracting, retaining and motivating directors, key officers, employees and consultants of the Company and to closely align the personal interests of such parties with those of the shareholders by providing them with the opportunity, through options, to acquire common shares of the Company. The maximum number of shares reserved for issuance under the stock option plan was increased to 6,000,000. The options are non-assignable and may be granted for a term not exceeding ten years. The exercise price is fixed by the board of directors of the Company at the time of grant, subject to all applicable regulatory requirements.

On January 22, 2008 prior to the RTO transactions described in Note 2, the Company granted options to directors, officers and consultants of the Company to acquire 3,750,000 common shares of the Company at an exercise price of \$0.60 per share on or before January 22, 2013. The options vested immediately. The fair value of the options granted was estimated as \$1,057,603 at the date of grant using the Black-Scholes option pricing model with the following assumptions:

Expected dividend yield	0%
Expected volatility	50%
Risk-free interest rate	3%
Expected life	60 months

A continuity of stock options is as follows:

	<u>Number of Stock Options</u>	<u>Weighted Average Exercise Price</u>	<u>Expiry Date</u>
	#	\$	
Balance, December 31, 2007	-	-	
Options granted by legal parent prior to RTO	<u>3,750,000</u>	<u>0.60</u>	January 22, 2013
Balance, March 31, 2008	<u>3,750,000</u>	<u>0.60</u>	

As at March 31, 2008, 2,437,500 options were exercisable (see Note 8(f)).

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NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

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8. CAPITAL STOCK (Continued)**d) Contributed Surplus**

	<u>Balance</u>
	\$
Balance, December 31, 2006 and 2007	-
Options granted by legal parent prior to RTO (Note 8(c))	<u>1,057,603</u>
Balance, March 31, 2008	<u><u>1,057,603</u></u>

e) Warrants

Pursuant to the private placement mentioned in Note 8(b)(ii) and prior to the RTO described in Note 2, the legal parent granted 1,000,000 warrants to the Agent to acquire 1,000,000 common shares of the Company at an exercise price of \$0.60 per share on or before January 29, 2013. The fair value of warrants granted was estimated as \$321,724 at the date of grant using the Black-Scholes option pricing model with the following assumptions:

Expected dividend yield	0%
Expected volatility	50%
Risk-free interest rate	3%
Expected life	24 months

f) Shares and Options Held in Escrow

Pursuant to Escrow Agreements entered into during the three month period ended March 31, 2008, 36,350,000 common shares of the Company and 1,750,000 options issued to certain officers and directors of the Company will be held in escrow and released as follows: one quarter were released on February 4, 2008, the date on which the common shares are listed on a Canadian stock exchange; one third of the remaining securities will be released six months following the listing date; one half of the remaining securities will be released twelve months following the listing date; and the remaining securities will be released 18 months following the listing date.

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9. INCOME TAXES

The Company utilizes the asset and liability method of accounting for incomes taxes.

Provision for Income Taxes

Major items causing the Company's income tax rate to differ from the federal statutory rate of 34% (2007 – 36%) were as follows:

	<u>2008</u>
	\$
Income before taxes:	<u>282,215</u>
Expected income tax provision based on statutory rate	96,000
Change in expected tax rates	(50,800)
Share issue and transaction costs	(609,500)
Other	(73,900)
Change in valuation allowance	<u>677,700</u>
	<u>39,500</u>

Future Tax Balances

The tax effects of temporary differences that give rise to future income tax assets are as follows:

	<u>March 31,</u>	<u>December 31,</u>
	<u>2008</u>	<u>2007</u>
	\$	\$
Future income tax assets:		
Non-capital losses	465,000	309,400
Plant and equipment	283,800	276,100
Share issue and transaction costs	522,000	-
Valuation allowance	<u>(677,700)</u>	<u>-</u>
	<u>593,100</u>	<u>585,500</u>

Tax Loss Carry-Forwards

As at March 31, 2008, the Company has approximately \$537,800 of non-capital losses, which can be used to reduce taxable income in Canada in future periods, of which \$9,200 expire in 2026, \$381,100 expire in 2027 and \$147,500 expire in 2028. The Company also has approximately \$1,545,000 (RMB10,538,900) of non-capital losses in China, which can be used to reduce taxable income in China in future periods, of which \$666,900 (RMB4,549,500) expire in 2010, \$869,800 (RMB5,933,600) expire in 2011, and \$8,300 (RMB55,800) expire in 2012.

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10. RELATED PARTY TRANSACTIONS

(a) During the three months ended March 31, 2008, the Company incurred consulting fees of \$37,500 (2007 - \$Nil) charged by two entities controlled by directors and officers of the Company, of which \$12,500 (2007 - \$Nil) was incurred prior to the RTO transactions described in Note 2. The above transactions were in the normal course of operations and were measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

(b) Due to related parties

A significant shareholder, who is also an officer and director of the Company advanced loans in the aggregate amount of RMB 40,000,000 (\$5,864,000) (December 31, 2007 – RMB 40,000,000 \$5,412,000) to the Company, through wholly owned corporations, in accordance with a Subordination and Forbearance Agreement dated April 27, 2007, Consignment Loan Agreements dated May 23, 2007 and June 26, 2007, and other ancillary documentation.

These loans are unsecured, non-interest bearing, are subordinate to the claims of all other creditors, including unsecured creditors, of the Company, and are due on demand; however, the loans cannot be demanded at any time until April 27, 2010. These corporations and the Company have entered into Loan Renewal Agreements whereby the parties have agreed to enter into further loan agreements upon the same terms and conditions as the Consignment Loan Agreements every three years, in perpetuity.

(c) Subscription receipts

Pursuant to the financing described in Note 8(b)(ii), four directors and officers of the Company subscribed for an aggregate of 1,559,000 subscription receipts for gross proceeds of \$935,400.

11. FINANCIAL INSTRUMENTS**Fair Value**

Canadian generally accepted accounting principles require that the Company disclose information about the fair value of its financial assets and liabilities. Fair value estimates are made at the balance sheet date based on relevant market information and information about the financial instrument. These estimates are subjective in nature and involve uncertainties in significant matters of judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect these estimates.

The carrying amounts for cash and cash equivalents, accounts and sundry receivables, advances, accounts payable and accrued liabilities, short-term loans, and interest payable on the balance sheet approximate fair value because of the limited term of these instruments. It is not practicable to estimate the fair value of the amounts of due to related parties.

Financial Risk Factors

The Company's risk exposures and the impact on the Company's financial instruments are summarized below:

(a) Foreign Exchange Risk

Certain of the Company's expenses and notes receivable are incurred in United States currencies and are therefore subject to gains or losses due to fluctuations in these currencies.

Substantially all of the assets, liabilities and operations of the Company are denominated in Chinese RMB. RMB is not a freely convertible currency. Future exchange rates of RMB could vary significantly from the current or historical exchange rates as a result of controls that could be imposed by the PRC government. The exchange rates may also be affected by economic developments and political changes domestically and internationally, and supply and demand of RMB. The appreciation or devaluation of RMB against the Canadian dollar may have positive or negative impact on the results of operations of the Company.

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NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

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(Expressed in Canadian currency)

11. FINANCIAL INSTRUMENTS (Continued)**(b) Regulatory Risks and Uncertainties**

The price of natural gas charged by CF China for the supply of natural gas to its customers is fixed by the local state price bureau. Any increase in gas usage charges exceeding the original approved charge requires the approval of the local state price bureau. There is no assurance that any increases, except for an increase to offset the rise in the Company's purchase price of natural gas, will be approved.

Connection fees chargeable by CF China require the approval of the local state price bureau. There is no assurance that CF China will be able to obtain approvals from the relevant state price bureau for an increase in connection fees, which may in turn adversely affect the profits of CF China.

(c) Interest Rate Risk

The Company has cash balances and interest-bearing debt. The Company's current policy is to invest excess cash in investment-grade short-term deposit certificates issued by its banking institutions. The Company periodically monitors the investments it makes and is satisfied with the credit ratings of its banks. The Company's interest rate on its debt is based upon the prescribed rate of the Peoples Bank of China which is subject to fluctuations and may result in an increase in interest expense. The Company does not use derivative instruments to reduce its exposure to interest rate risk.

(d) Credit Risk

The Company's credit risk is primarily attributable to its long-term debt. The Company has no significant concentration of credit risk arising from operations. Management believes that the credit risk concentration with respect to financial instruments included in other assets is remote.

(e) Liquidity Risk

The Company's approach to managing liquidity risk is to ensure that it will have sufficient liquidity to meet liabilities when due. As at March 31, 2008, the Company had a cash and cash equivalent balance of \$7,183,231 (December 31, 2007 - \$2,597,876) to settle current liabilities of \$13,772,766 (December 31, 2007 - \$12,844,013). Management believes that the loan currently classified as a current liability and more fully described in Note 7(b) in the amount of \$6,186,520 will not require repayment in full during the next twelve months.

(f) Sensitivity Analysis

The Company has designated its cash and cash equivalents as held-for-trading, which are measured at fair value. Financial instruments included in other assets are classified as loans and receivables, which are measured at amortized cost. Accounts payable and accrued liabilities are classified as other financial liabilities, which are measured at amortized cost. As at March 31, 2008, the carrying and fair value amounts of the Company's financial instruments are approximately the same.

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NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2008

(Expressed in Canadian currency)

12. SEGMENTED INFORMATION

For management purposes, the Company is currently organized into three operating divisions: gas connection, piped gas sales, and other. These principal operating activities are the basis on which the Company reports its primary segment information. The gas connection and piped gas sales operating divisions are based in the PRC.

FOR THE PERIOD ENDED MARCH 31, 2008

	Gas Connection	Piped Gas Sales	Other	Consolidated
	\$	\$	\$	\$
REVENUE	1,201,480	1,764,611	-	2,966,091
COST OF SALES	<u>766,695</u>	<u>434,721</u>	-	<u>1,201,416</u>
	<u>434,785</u>	<u>1,329,890</u>	-	<u>1,764,675</u>
EXPENSES				
General and administrative	250,018	352,571	134,812	737,401
Interest on long-term debt	-	289,197	-	289,197
Travel and promotion	133,368	136,234	-	269,602
Amortization	<u>4,019</u>	<u>235,947</u>	-	<u>239,966</u>
	<u>387,405</u>	<u>1,013,949</u>	<u>134,812</u>	<u>1,536,166</u>
Income (loss) before the under-noted	47,380	315,941	(134,812)	228,509
Interest income	<u>-</u>	<u>-</u>	<u>53,706</u>	<u>53,706</u>
	47,380	315,941	(81,106)	282,215
Income tax expense	<u>315</u>	<u>39,185</u>	-	<u>39,500</u>
NET INCOME (LOSS) FOR THE PERIOD	<u><u>47,065</u></u>	<u><u>276,756</u></u>	<u><u>(81,106)</u></u>	<u><u>242,715</u></u>

Substantially all of the Company's assets are located in the PRC.

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NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

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(Expressed in Canadian currency)

13. ACCUMULATED OTHER COMPREHENSIVE LOSS

	<u>March 31,</u> <u>2008</u> \$	<u>December 31,</u> <u>2007</u> \$
Balance, at the beginning of the period	(460,613)	(331,563)
Currency translation adjustment during the period	<u>160,024</u>	<u>(129,050)</u>
Balance, at the end of the period	<u>(300,589)</u>	<u>(460,613)</u>

14. ECONOMIC DEPENDENCE

Currently, one gas field in the South China Sea supplies all of the Company's natural gas. There is no alternative supply in the short-term. Interruption of this gas field would affect The Company's ability to operate. Currently, the Company has a contract to purchase 24 million M³ gas a year from this supplier until December 31, 2015. There is no certainty that the Company will be able to purchase gas in excess of this amount from this gas field.

The Company is currently exploring other possible sources of natural gas.

15. CAPITAL MANAGEMENT

The Company manages its capital structure and makes adjustments to it, based on the funds available to the Company, in order to support the ongoing operations of the business. The Board of Directors does not establish quantitative return on capital criteria for management, but rather relies on the expertise of the Company's management to sustain future development of the business.

Management reviews its capital management approach on an ongoing basis and believes that this approach, given the relative size of the Company, is reasonable.

There were no changes in the Company's approach to capital management during the three months ended March 31, 2008.