



Xcite Energy Limited

Interim consolidated financial statements

For the 3 and 9 month periods ended September 30, 2008

(Unaudited)

Xcite Energy Limited

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Management's Discussion and Analysis

The Management's Discussion and Analysis ("MD&A") of the operating and financial results of Xcite Energy Limited ("XEL" or the "Company") should be read in conjunction with the Company's interim unaudited consolidated financial statements and related notes thereto for the three month period ended September 30, 2008, the audited consolidated financial statements and related notes thereto for the fourteen month period ended December 31, 2007 and the annual MD&A of the Company. This MD&A is dated December 3, 2008. These documents and additional information about XEL are available on SEDAR at www.sedar.com.

XEL is an oil issuer and disclosures pertaining to oil activities are presented in accordance with National Instrument 51-101 ("NI-51-101") of the Canadian Securities Administrators.

This MD&A includes an analysis of the XEL results from January 1, 2008 to September 30, 2008 and from January 1, 2007 to September 30, 2007, which include the results of the operating subsidiary Xcite Energy Resources Limited ("XER"). In this MD&A, XEL and XER are together defined as the "Group". All figures and the comparative figures contained herein are expressed in Pounds Sterling unless otherwise noted.

Certain statements in this MD&A may be regarded as "forward-looking statements" including outlook on oil prices, estimates of future production, estimated completion dates of constructions and development projects, business plans for drilling and exploration, estimated amount and timing of capital expenditures and anticipated future debt levels. Forward-looking statements often, but not always, are identified by the use of words such as "seek", "anticipate", "believe", "plan", "estimate", "expect", "targeting" and "intend" and statements that an event or result "may", "will", "should", "could" or "might" occur or be achieved and other similar expressions.

Information concerning resources may also be deemed to be forward looking statements as such estimates involve the implied assessment that the resources described can be profitably produced in the future. These statements are based on current expectations, estimates and projections that involve a number of risks and uncertainties, which could cause actual results to differ from those anticipated by the Group. The reader should not place undue importance on forward looking statements and should not rely upon this information as of any other date. While the Company may elect to, it is under no obligation and does not undertake to update this information at any particular time, unless required by applicable securities law.

Summary of Results

The following table summarises the Group's performance for the three month periods ended March 31 ("Q1"), June 30 ("Q2") and September 30 ("Q3") of 2008 and the comparatives for the three month periods ended March 31, June 30 and September 30 of 2007. All of these results are unaudited. The Group has no trading revenue in these periods. The interim unaudited consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards (IFRS and IFRIC interpretations) issued by the International Accounting Standards Board (IASB). The interim unaudited consolidated financial statements of the Company have also been prepared in accordance with IFRS's adopted by the European Union and therefore they comply with Article 4 of the EU IAS Regulation.

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	Q3 2008	Q2 2008	Q1 2008	Q3 2007	Q2 2007	Q1 2007
	£'000s	£'000s	£'000s	£'000s	£'000s	£'000s
Net (loss)/profit	(90)	(281)	22	65	(-)	(-)
EPS *	(0.00p)	(0.00p)	0.00p	0.00p	(0.00p)	(0.00p)
Total assets	24,005	25,185	27,787	9,237	11,417	2,288

* (Loss)/earnings per share (basic and diluted) in pence

XEL has seen a disappointing performance in its share price in recent months, which XEL management appreciate is a concern for our shareholders. We believe that the sharp decline in share price has been largely caused by a rapid deterioration in worldwide financial market confidence and not as a result of any deviation from XEL's existing strategy in the commercialisation and development of the Bentley field, one of the largest undeveloped heavy oil fields in the UK continental shelf. Management believe that the current share price does not reflect the underlying value of the Group's assets.

Liquidity and Capital Resources

In June 2007 the Company completed a private placement of new shares, with aggregate proceeds of £10.0 million and associated costs of £0.83 million, resulting in net proceeds of £9.17 million. In November 2007, the Company completed an initial public offering of new shares and dual public listing on AIM in London and the TSX-Venture Exchange in Canada, with aggregate proceeds of £14.92 million and associated costs of £2.0 million, resulting in net proceeds of £12.92 million. The net funds from the private placement and the initial public offering in 2007 were allocated to drilling the appraisal well on Block 9/3b (9/3b-5) to satisfy the work programme obligations to the Department for Business, Enterprise and Regulatory Reform in the UK. XER spudded the 9/3b-5 appraisal well in December 2007 and continued into February 2008 to conduct a successful drill stem test.

The cash balance of the Company as at September 30, 2008 was £2.7 million, compared with £21.07 million as at December 31, 2007. This decrease was attributable to the 9/3b-5 drilling spend, together with the anticipated costs of significant additional work to interpret the successful drill stem test and move forward with the planning for the next stage in the development of the Bentley field. This work includes fluid and reservoir studies, seismic reprocessing and interpretation, field development studies and marketing and refining studies.

The Company has continued to review other business development opportunities and has incurred general corporate working capital costs during the period.

The use of cash was offset by additional investment in share capital of £0.48 million in the first quarter of 2008, resulting from the exercising of warrants over the ordinary shares of the Company.

Lease and Contractual Commitments

At September 30, 2008 the Company had no material lease commitments or contractual obligations.

Operations and Administrative Expenses

The Group is in the development phase and as such no revenue is yet being generated from the Group's assets. Certain key milestones as set out in the original prospectus for the initial public offering have been achieved in the nine months ended September 30, 2008, principally being the successful testing of the 9/3b-5 appraisal well.

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In the nine months ended September 30, 2008, total costs of £14.7 million (nine months ended September 30, 2007: £1.0 million) have been capitalised as Exploration and Evaluation (“E&E”) Assets in Intangible Assets relating to Block 9/3b. The costs capitalised in this way to E&E Assets in the three months ended September 30, 2008 amount to £1.0 million (three months ended September 30, 2007: £0.7 million). These costs have been capitalised in accordance with the Group’s accounting policies and will be amortised against the revenue from production, if any, from the Bentley field.

This aggregate nine months’ expenditure reflects the work that has been done by XER in the period in bringing forward Block 9/3b, both technically and commercially, through the drilling of the 9/3b-5 appraisal well and the anticipated significant subsequent study work. The expenditure in this latest three month period to September 30, 2008 comprises the costs of this significant additional study work to interpret the successful drill stem test and move forward with the planning for the next stage in the development of the Bentley field. This work includes fluid and reservoir studies, seismic reprocessing and interpretation, field development studies and marketing and refining studies.

The Group has not incurred any additional material research and development costs or deferred development costs over and above those costs capitalised as E&E assets. XEL has incurred costs of operating as a public company amounting to £0.56 million for the nine months ended September 30, 2008, including investor relations, Non-Executive Director fees and Stock Exchange fees (nine months ended September 30, 2007: £0.01 million). The comparative costs for the three months to September 30, 2008 amounted to £0.1 million (three months ended September 30, 2007: £0.05 million).

Share Options, Warrants and Rights

On June 19, 2008 the Company issued 450,000 share options over the Company’s ordinary share capital to three members of the XER Management Team. All such options vested immediately with an exercise price of CAD\$1.60 (£0.805) and a term of five years.

No new share warrants or other rights over the Company’s ordinary share capital were issued in the nine month period ended September 30, 2008. See Note 12 to the interim unaudited consolidated financial statements for details of share warrants exercised during the nine month period to September 30, 2008.

Income

Interest income earned on funds invested during the nine months ended September 30, 2008 amounted to £0.31 million (nine months to September 30, 2007: £0.12 million). Interest income earned on funds invested during the three months ended September 30, 2008 amounted to £0.03 million (three months to September 30, 2007: £0.12 million). This interest income earned is consistent with the funds held on deposit during the relevant periods.

During the uncertainties of the financial markets during the three months ended September 30, 2008, management has maintained its policy of keeping cash deposits with banks with “AA” rating or better. The policy of the group is to ensure that all cash balances earn a market rate of interest and that interest rate exposures are regularly reviewed and managed.

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Disclosure Controls and Procedures

In conformance with the Canadian Securities Administrators Multilateral Instrument 52-109, the Company has filed certificates signed by the Chief Executive Officer and the Chief Financial Officer that, amongst other things, deal with the matter of disclosure controls and procedures.

Outstanding Share Capital

The following table outlines the issuances of ordinary shares of the Company during the nine months ended September 30, 2008.

	Ordinary Shares
As at December 31, 2007	60,550,000
Issue of shares through Broker warrant exercise	812,500
Issue of shares through warrant exercise	51,300
As at September 30, 2008	61,413,800

During the nine months ended September 30, 2008, the Company received additional funds of £0.48 million through the exercise of certain warrants over the ordinary shares of the Company.

As at the date of signing this MD&A, the number of shares in issue was 61,413,800 as set out in Note 12 to the interim unaudited consolidated financial statements and the total number of outstanding share options and warrants over the ordinary share capital of the Company was 4,350,000 and 11,824,700 respectively, which would be equal to 16,174,700 further ordinary shares upon full conversion of these options and warrants.

Risk Management

The principal risk factors facing the Group are as follows:

Exploration and development

The nature of oil exploration is such that there is no assurance that exploration activities will be successful. Industry statistics show that few properties that are explored go on to being fully developed. Operations can also be adversely affected by weather conditions and drilling rig and other operating equipment availability outwith the control of the Group.

Commodity pricing

The Group has no control over the market price of crude oil. Suitable hedging arrangements will be considered to mitigate the volatility of oil prices when the Group enters into the production phase.

Financing

Future field development will depend upon the ability of the Group to secure financing, whether this is by joint venture projects, farm down arrangements, public financing or other means. The unprecedented deterioration in credit markets in recent months may limit the funding sources available to the Group.

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Currency

The Group's reporting and functional currency is Pounds Sterling. However, the market for heavy crude is in US Dollars. The Group does not currently engage in active hedging to minimise exchange rate risk although this will remain under review as the Group approaches the production phase.

Resource estimation

Oil reserve estimation techniques are inherently judgemental and involve a high degree of technical interpretation and modelling techniques. Incorrect resource estimation may result in inappropriate capital investment decisions being made.

Significant Accounting Judgements and Estimates

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual costs. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying value of assets and liabilities within the next financial period are discussed below.

(a) Income taxes

There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Group recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

(b) Fair value of share options and warrants

The Company has valued the fair value of outstanding share options and warrants over the Company's shares using the Black-Scholes valuation methodology. The Company uses judgement to derive such valuation model assumptions that are mainly based on market conditions existing at the Balance Sheet date.

(c) Impairment of Exploration and Evaluation ("E&E") assets

A review is performed at the end of each financial period for any indication that the value of the Group's E&E assets may be subject to impairment. In the event of any such indication, an impairment test is carried out and, if necessary, an impairment representing the surplus of capitalised cost over estimated recoverable value of the related commercial oil reserves is charged. Estimated recoverable value is based upon anticipated discounted net cash flows attributable to such reserves.

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Financial Instruments and Other Derivatives

Details regarding the Group's policies in respect of financial instruments are disclosed in Notes 1 and 11 to the interim unaudited consolidated financial statements.

Outlook for the Remainder of 2008

The nine months ended September 30, 2008 was a period of high investment by the Company in the Bentley field, with the three months ended September 30, 2008 being focused on the anticipated significant additional study work to interpret the successful drill stem test and move forward with the planning for the next stage in the development of the Bentley field. This work includes fluid and reservoir studies, seismic reprocessing and interpretation, field development studies and marketing and refining studies. The Group will continue this programme of study work for the balance of 2008 and management believes that it has sufficient funds to enable it to continue with the planning of the next stage of the programme to commercialise the Bentley field.

Following the successful drilling and testing of the appraisal well at the start of 2008, the Group's long term prospects are dependent on the investment of significant capital sums for the commercialisation of the Bentley field. Deterioration in the financial and credit market during 2008 is likely to make the securing of new funding more difficult.

Recent financial market turmoil has resulted in a significant reduction in the UK base rate since June 30, 2008, which will reduce the overall financial income generated by the Group on its cash balances.

The Company expects to be able to update its shareholders on the results of the study work noted above, together with a progress report on the planning for the next stage in the development of the Bentley field during the first quarter of 2009.

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Consolidated Income Statement

		9 months ended September 30 2008 (unaudited) £	3 months ended September 30 2008 (unaudited) £	9 months ended September 30 2007 (unaudited) £	3 months ended September 30 2007 (unaudited) £
	Note				
Administrative expenses		(654,573)	(124,020)	(53,732)	(53,145)
Operating loss	3	(654,573)	(124,020)	(53,732)	(53,145)
Finance income - bank interest		314,294	33,543	118,061	117,753
(Loss)/profit before tax		(340,279)	(90,477)	64,329	64,608
Tax expense	5	(9,443)	-	-	-
(Loss)/profit for the period	13	(349,722)	(90,477)	64,329	64,608
(Loss)/earnings per share:					
Basic and diluted	6	(0.01p)	(0.00p)	0.00p	0.00p

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Consolidated Statement of Recognised Income and Expense

	9 months ended September 30 2008 (unaudited) £	3 months ended September 30 2008 (unaudited) £	9 months ended September 30 2007 (unaudited) £	3 months ended September 30 2007 (unaudited) £
(Loss)/profit for the period	(349,722)	(90,477)	64,329	64,608
Total recognised income and expense for the period	(349,722)	(90,477)	64,329	64,608
Attributable to:				
Equity shareholders	(349,722)	(90,477)	64,329	64,608

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Consolidated Balance Sheet

		September 30 2008	December 31 2007
		£	£
	Note	(unaudited)	(audited)
Assets			
<i>Non-current assets</i>			
Intangible assets	7	21,260,650	6,582,176
Property, plant and equipment	8	23,422	-
<i>Current assets</i>			
Trade and other receivables	9	29,492	82,789
Cash and cash equivalents		2,691,370	21,067,134
Total current assets		2,720,862	21,149,923
Total assets		24,004,934	27,732,099
Liabilities			
<i>Current liabilities</i>			
Trade and other payables	10	1,104,684	5,042,672
Total liabilities		1,104,684	5,042,672
Net assets		22,900,250	22,689,427
Equity			
Share capital	12	22,252,625	21,774,150
Retained earnings	13	(978,370)	(730,422)
Merger reserve	13	218	218
Other reserves	13	1,625,777	1,645,481
Total equity		22,900,250	22,689,427

These interim unaudited consolidated financial statements were approved by the Board of Directors and authorised for issue on December 3, 2008 and were signed on its behalf by:

Richard Smith
Chief Executive Officer

Rupert Cole
Chief Financial Officer

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Consolidated Cash Flow Statement

	9 months ended September 30 2008 (unaudited) £	3 months ended September 30 2008 (unaudited) £	9 months ended September 30 2007 (unaudited) £	3 months ended September 30 2007 (unaudited) £
Net cash flow from operating activities				
(Loss)/profit for the period after tax	(349,722)	(90,477)	64,329	64,608
Adjustment for share based payments	82,070	-	-	-
Adjustment for interest received	(314,294)	(33,543)	(118,061)	(117,753)
Adjustment for depreciation	3,887	2,276	-	-
Movement in working capital				
- Trade and other receivables	53,297	16,508	(21,697)	(19,180)
- Trade and other payables	(3,937,988)	(1,089,236)	(19,237)	(16,536)
Net cash flow from operations	(4,462,750)	(1,194,472)	(94,666)	(88,861)
Cash flow from investing activities				
Exploration and evaluation assets	(14,678,474)	(974,546)	(997,381)	(702,170)
Purchase of fixed assets	(27,309)	-	-	-
Contribution to costs received	-	-	257,683	-
Interest received	314,294	33,543	118,061	117,753
Net cash flow from investing	(14,391,489)	(941,003)	(621,637)	(584,417)
Cash flow from financing activities				
Net proceeds from issue of new shares	478,475	-	9,172,330	-
Cash flow from financing	478,475	-	9,172,330	-
Net (decrease)/increase in cash and cash equivalents	(18,375,764)	(2,135,475)	8,456,027	(673,278)
Cash and cash equivalents as at January 1/July 1	21,067,134	4,826,845	44,702	9,174,007
Cash and cash equivalents as at September 30	2,691,370	2,691,370	8,500,729	8,500,729
Cash and cash equivalents				
Cash available on demand	2,691,370	2,691,370	8,500,729	8,500,729

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Notes to the Interim Consolidated Financial Statements

1 Accounting Policies

Basis of preparation

The interim unaudited consolidated financial statements for the three months ended September 30, 2008 have been prepared in accordance with IAS 34 Interim Financial Reporting. However, the interim unaudited consolidated financial statements for the three and nine months ended September 30, 2008 have not been reviewed or audited by the Company's auditors.

These interim unaudited consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards following the same accounting policies and methods of computation as the audited consolidated financial statements for the financial period ended December 31, 2007. These interim unaudited consolidated financial statements do not include all the information and footnotes required by generally accepted accounting principles for annual financial statements and therefore should be read in conjunction with the audited consolidated financial statements and the notes thereto in the Xcite Energy Limited ("XEL" or "the Company") annual report for the fourteen month period ended December 31, 2007.

Basis of consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, Xcite Energy Resources Limited ("XER"). XEL and XER together comprise the "Group". All inter-company balances and transactions have been eliminated upon consolidation.

Property, plant and equipment

Property, plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. All repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Depreciation on assets is calculated using the straight-line method to allocate their cost over their estimated useful life, as follows:

- Furniture, fittings and equipment 3-5 years

New accounting standards adopted during the period

During the period the Group has adopted no new standards for the first time.

New standards and interpretations not yet applied

The following new standards and interpretations, which have been issued by the IASB and the IFRIC, have yet to be endorsed by the European Union and/or are effective for future periods and thus have not been adopted in these interim unaudited consolidated financial statements. A description of these standards and interpretations, together with (where applicable) an indication of the effect of adopting them, is set out below. None are expected to have a material effect on the reported results or financial position of the Group.

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The IASB issued a revised IAS 1 ‘Presentation of Financial Statements’ in September 2007 effective for accounting periods beginning on or after January 1, 2009.

The IASB published revisions to IAS 32 ‘Financial Instruments: Presentation’ and consequential revisions to other standards in February 2008 to improve the accounting for and disclosure of puttable financial instruments. The revisions are effective for accounting periods beginning on or after January 1, 2009 but together they may be adopted earlier.

The IASB published amendments to IFRS 1 and IAS 27 “Cost of an Investment in a Subsidiary, Jointly-Controlled Entity or Associate” in May 2008. A first-time adopter now may use as deemed cost of an investment in a subsidiary, jointly-controller entity or associate either the fair value at the entity’s transition to IFRS or the previous GAAP carrying amount at that date. Investors no longer need to determine whether dividends received have been paid from pre or post-acquisition profits, all such dividends now being treated as income in the income statement. The amendments also clarify how to determine the cost of an investment in accordance with IAS 27 when a parent reorganises the operating structure of its group by establishing a new entity as its parent and this new parent obtains control of the original parent by issuing equity instruments in exchange for existing equity instruments of the original parent. Entities are required to apply these amendments for annual periods beginning on or after January 1, 2009, and earlier adoption is permitted.

The IASB issued in May 2008 as part of its Annual Improvements Project an Exposure Draft discussing proposed improvements to existing IFRSs. The Annual Improvements Project has the intention of dealing with a relatively high number of small amendments to existing standards. Most amendments will be effective January 1, 2009.

The IASB published a revised IFRS 3 ‘Business Combinations’ and related revisions to IAS 27 ‘Consolidated and Separate Financial Statements’ following the completion in January 2008 of its project on the acquisition and disposal of subsidiaries. The standards improve convergence with US GAAP and provide new guidance on accounting for changes in interests in subsidiaries. The cost of an acquisition will comprise only consideration paid to vendors for equity; other costs will be expensed immediately. Groups will only account for goodwill on acquisition of a subsidiary; subsequent changes in interest will be recognised in equity and only on a loss of control will there be a profit or loss on disposal to be recognised in income. The changes are effective for accounting periods beginning on or after July 1, 2009, but both standards may be adopted together for accounting periods beginning on or after July 1, 2007.

The Exposure Draft “Proposed Amendments to IFRS 2 - Vesting Conditions and Cancellations” was issued in February 2006, with the final standard being issued in January 2008. The amendment requires that vesting conditions be restricted to service conditions and non-market performance conditions. Cancellations by parties other than the entity will be accounted for in the same way as cancellations by the entity. The amendments will be applied retrospectively in annual periods beginning on or after January 1, 2009.

Amendment to IAS 23 ‘Borrowing Costs’ was issued in May 2007 and is effective for accounting periods beginning on or after January 1, 2009. The amendment requires borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset to be added to the cost of that asset.

IFRIC 12 ‘Service Concession Arrangements’ was issued in November 2006 and is effective for annual periods beginning on or after January 1, 2008. IFRIC 12 prohibits private sector operators from recognising as their own those infrastructure assets which are owned by the grantor.

IFRIC 13 ‘Customer Loyalty Programmes’ was issued in June 2007 and is effective for annual periods beginning on or after July 1, 2008. IFRIC 13 requires the fair value of revenue relating to customer loyalty rewards to be deferred until all related obligations to the customer have been fulfilled.

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IFRIC 14 'IAS 19 - The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction' was issued in June 2007 and is effective for annual periods beginning on or after January 1, 2008. IFRIC 14 clarifies how any asset to be recognised should be determined, in particular where a minimum funding requirement exists.

IFRIC 15 'Agreements for the Construction of Real Estate' and IFRIC 16 'Hedges of a Net Investment in a Foreign Operation' were both issued in July 2008 but their impact are not considered of relevance to XEL.

IFRS 8 'Operating Segments' was issued in November 2006 and is effective for annual periods beginning on or after January 1, 2009. It requires reportable operating segments to be based on the entity's own internal reporting structure. It also extends the scope and disclosure requirements of IAS 14 Segmental Reporting, the standard which it is replacing. IFRS 8 will require the publication of segment reports, which will, as a minimum, disclose net result and total assets on a segment by segment basis based on management's own internal accounting information.

The IASB published amendments to IAS 39 'Financial Instruments: Recognition and Measurement: Eligible Hedged items' in July 2008 to clarify when inflation can be designated as a hedged item in a financial instrument under the hedge accounting provisions of IAS 39 and how hedge accounting can be applied to hedges when a hedging instrument is an option contract.

Status of EU endorsement

Entities in EU Member States which report in accordance with EU-endorsed IFRS can only apply IFRSs and IFRICs where the endorsement process has been completed at the date of approval of their financial statements. Of the standards and interpretations listed above, the following had not yet been endorsed by the European Union at the date these interim consolidated financial statements were authorised for issue:

- IFRIC 12 'Service Concession Arrangements';
- IFRIC 13 'Customer Loyalty Programmes';
- IFRIC 14 'IAS 19 - The limit on a defined benefit asset';
- IFRIC 15 'Agreements for the Construction of Real Estate';
- IFRIC 16 'Hedges of a Net Investment in a Foreign Operation';
- IFRS 3 'Business Combinations (revised)';
- Amendment to IAS 23 'Borrowing Costs';
- Amendments to IAS 1 'Presentation of Financial Statements: A Revised Presentation';
- Amendments to IAS 27 'Consolidated and Separate Financial Statements';
- Amendment to IFRS 2 'Share-Based Payment: Vesting Conditions and Cancellations';
- Amendments to IAS 32 and IAS 1 'Puttable Financial Instruments and Obligations Arising on Liquidation';
- Improvements to IFRS;
- Amendments to IFRS 1 and IAS 27 'Cost of an investment in a subsidiary, jointly-controlled entity or associate'; and
- Amendments to IFRS 39 'Financial Instruments: Recognition and Measurement: Eligible Hedged Items'.

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2 Segment Information

The Group only operates in a single business and geographical segment. The Group's single line of business is the appraisal and evaluation of oil and gas reserves and the geographical segment in which it currently operates is the North Sea.

3 Operating Loss

The operating loss on ordinary activities is stated after charging the following:

	9 months ended September 30 2008 (unaudited)	3 months ended September 30 2008 (unaudited)	9 months ended September 30 2007 (unaudited)	3 months ended September 30 2007 (unaudited)
	£	£	£	£
Share based payment charges	12,072	-	-	-

The Company incurred total charges in respect of share based payments in the six month period to June 30, 2008 of £82,070 (2007: £nil). Of this, £74,115 (2007: £nil) was in respect of employees (see Note 4). In accordance with the Company accounting policy, £69,998 (2007: £nil) has been capitalized within E&E assets and the balance of £12,072 expensed within operating loss. There were no such charges in the three month period to September 30, 2008 (2007: £nil).

4 Staff Costs and Directors' Emoluments

- a) The average number of persons employed by the Group (including Executive Directors) during the period was as follows:

	9 months ended September 30 2008 (unaudited)	3 months ended September 30 2008 (unaudited)	9 months ended September 30 2007 (unaudited)	3 months ended September 30 2007 (unaudited)
Technical and administration	7	8	3	3

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The aggregate payroll costs of staff and Executive Directors were as follows:

	9 months ended September 30 2008 (unaudited)	3 months ended September 30 2008 (unaudited)	9 months ended September 30 2007 (unaudited)	3 months ended September 30 2007 (unaudited)
	£	£	£	£
Wages and salaries	757,614	287,635	419,545	156,990
Social security costs	93,406	35,424	65,507	23,416
Share based payments	74,115	-	-	-
	925,135	323,059	485,052	180,406

b) Executive Directors' emoluments

	9 month period ended September 30 2008 (unaudited)	3 month period ended September 30 2008 (unaudited)	9 month period ended September 30 2007 (unaudited)	3 month period ended September 30 2007 (unaudited)
	£	£	£	£
Wages and salaries	479,025	159,675	419,545	156,990
Social security costs	59,762	19,916	65,507	23,416
	538,787	179,591	485,052	180,406

The Executive Directors comprise the key management personnel of the Group.

In addition to the above, during the three month period ended September 30, 2008, the Group paid to Roger Ramshaw and Scott Cochlan in their capacity as Non-Executive Directors of the Company fees of £6,000 and £1,500 respectively. There were no such equivalent payments for the three month period ended September 30, 2007.

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5 Taxation

	9 months ended September 30 2008 (unaudited) £	3 months ended September 30 2008 (unaudited) £	9 months ended September 30 2007 (unaudited) £	3 months ended September 30 2007 (unaudited) £
Overseas tax charges	9,443	-	-	-

Current tax is calculated at the rates prevailing in the respective jurisdictions. XEL is incorporated in the British Virgin Islands, a jurisdiction subject to a tax exemption. XER is incorporated in the UK, is considered a company which profits from oil extraction and oil rights, and is therefore subject to current tax on taxable profits at a rate of 30% (September 30, 2007: 30%).

6 (Loss)/earnings per Share

The basic (loss)/earnings per share is calculated by dividing the (loss)/profit attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the period. The calculation of basic (loss)/earnings per ordinary share for the nine month period ended September 30, 2008 is based on a nine month period loss of £349,722 (nine months to September 30, 2007: profit of £64,329) and on 61,313,091 (nine months to September 30, 2007: 28,858,824), being the weighted average number of ordinary shares in issue during the period.

For the three month period to September 30, 2008 the calculation of basic (loss)/earnings per ordinary share is based on a loss of £90,477 (three months to September 30, 2007: profit of £64,608) and on 61,413,800 (three months to September 30, 2007: 41,800,000), being the weighted average number of ordinary shares in issue during the period.

Details of potentially dilutive financial instruments are given in Note 12 to these financial statements.

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7 Intangible Assets

<i>Exploration and Evaluation Assets</i>	Licence Fees	
	September 30 2008 (unaudited)	December 31 2007 (audited)
	£	£
Cost and carrying value:		
At January 1, 2008 / November 1, 2006	126,567	66,297
Additions during period	-	60,270
At September 30, 2008 / December 31, 2007	126,567	126,567

	Appraisal and Exploration Costs	
	September 30 2008 (unaudited)	December 31 2007 (audited)
	£	£
Cost and carrying value:		
At January 1, 2008 / November 1, 2006	6,455,609	2,036,813
Additions during period	14,678,474	4,676,479
Contributions to costs received	-	(257,683)
At September 30, 2008 / December 31, 2007	21,134,083	6,455,609

	Total	
	September 30 2008 (unaudited)	December 31 2007 (audited)
	£	£
Cost and carrying value:		
At January 1, 2008 / November 1, 2006	6,582,176	2,103,110
Additions during period	14,678,474	4,736,749
Contributions to costs received	-	(257,683)
At September 30, 2008 / December 31, 2007	21,260,650	6,582,176

The costs associated with the appraisal of the Bentley field have been capitalised in accordance with the Group's accounting policy in Note 1.

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Based on the Group's success in drilling its appraisal well on Bentley, and in view of the forecast revenue streams and cash flows of this project, management is satisfied that the carrying amount of the related intangible assets as disclosed above will be recovered in full and that there is no need for any impairment provision. The situation will be monitored by management and adjustments made in future periods if future events indicate that such adjustments are appropriate.

8 Property, Plant and Equipment

	Furniture, fittings and computing equipment
At November 1, 2006 (audited)	£
Cost and net book amount	-
Period ended December 31, 2007 (audited)	
Opening and closing net book amount	-
At December 31, 2007 (audited)	
Cost and net book amount	-
Period ending September 30, 2008 (unaudited)	
Opening net book amount	-
Additions	27,309
Depreciation charge	3,887
Closing net book amount	23,422
At September 30, 2008 (unaudited)	
Cost or valuation	27,309
Accumulated depreciation	3,887
Net book amount	23,422

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9 Trade and Other Receivables

	September 30 2008 (unaudited) £	December 31 2007 (audited) £
Indirect taxes receivable	25,817	79,114
Other receivables	3,675	3,675
	29,492	82,789

10 Trade and Other Payables

	September 30 2008 (unaudited) £	December 31 2007 (audited) £
Trade payables	171,198	2,857,762
Social security and other taxes payable	47,821	33,919
Accruals and other creditors	885,665	2,150,991
	1,104,684	5,042,672

11 Financial Instruments

The Group's principal financial instruments are other receivables, trade and other payables and cash, which are denominated in various currencies. The main purpose of these financial instruments is to finance the Group's ongoing operational requirements.

The Group does not currently trade in derivative financial instruments. The principal financial risks faced by the Group are credit risk, liquidity and foreign currency risk. Policies for the management of these risks, which have been consistently applied throughout the period, are shown below.

Non-market risk

a) Credit risk

Receivables relate to VAT recoverable and an office rent deposit. As such, they are regarded as low risk.

b) Liquidity risk

Group management has responsibility for reducing exposure to liquidity risk and for ensuring that adequate funds are available to meet anticipated requirements. It operates according to the policies and guidelines established by the Board. Cash management is carried out centrally.

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	Carrying Amount	
	September 30 2008 (unaudited) £	December 31 2007 (audited) £
Financial assets – loans and receivables		
- Cash	2,691,370	21,067,134
- Receivables (current)	29,492	82,789
	2,720,862	21,149,923
Financial liabilities – measured at amortised cost		
- Payables (current)	1,104,684	5,042,672

The management believes that as all financial instruments are short term, the fair values for all such items equate to their carrying amount.

The accounting policies for financial assets and financial liabilities are disclosed in Note 1.

Market risk

c) Interest rate and foreign currency risks

The currency and interest profile of the Group's financial assets and liabilities are as follows:

	Interest Free Liabilities	
	September 30 2008 (unaudited) £	December 31 2007 (audited) £
Sterling	1,104,575	2,807,605
CAD\$	109	62,947
USD\$	-	2,172,120
	1,104,684	5,042,672

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	Floating rate assets	Interest free assets	Total
	September 30 2008 (unaudited)	September 30 2008 (unaudited)	September 30 2008 (unaudited)
	£	£	£
Sterling	2,654,943	29,492	2,684,435
CAD\$	34,081	-	34,081
USD\$	2,346	-	2,346
	2,691,370	29,492	2,720,862

	Floating rate assets	Interest free assets	Total
	December 31 2007 (audited)	December 31 2007 (audited)	December 31 2007 (audited)
	£	£	£
Sterling	16,460,016	82,789	16,542,805
USD\$	4,607,118	-	4,607,118
	21,067,134	82,789	21,149,923

Sterling floating rate assets earn interest at circa 25 basis points below the Bank of England Base Rate per annum. US\$ floating rate assets earn interest at circa 25 basis points below the Federal Reserve Rate per annum. CAD\$ floating rate assets earn interest at circa 25 basis points below the Canadian Overnight Rate per annum. Cash deposits are only kept with banks with “AA” rating or better. The policy of the group is to ensure that all cash balances earn a market rate of interest and that interest rate exposures are regularly reviewed and managed.

(d) Interest rate sensitivity analysis

Interest rate sensitivity analysis has been determined based on the exposure to interest rates for financial instruments during the financial period.

Based on the Group’s cash balances during the period, if interest rates had been 50 basis points higher/lower and all other variables were held constant, the Group’s loss for the nine month period ended September 30, 2008 would decrease/increase by £41,450 (September 30, 2007; the Group’s profit would increase/decrease by £11,906). Using the same parameters, the Group’s loss for the three month period ended September 30, 2008 would decrease/increase by £4,385 (September 30, 2007; the Group’s profit would increase/decrease by £11,875).

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12 Share Capital

	September 30 2008 (unaudited)	December 31 2007 (audited)
	Number of shares	Number of shares
<hr/>		
Authorised		
- Ordinary shares of no par value each	Unlimited	Unlimited
Issued and fully paid up		
- Ordinary shares of no par value each	61,413,800	60,550,000
<hr/>		

	September 30 2008 (unaudited)	December 31 2007 (audited)
	£	£
<hr/>		
Authorised		
- Ordinary shares of no par value	Unlimited	Unlimited
Issued and fully paid up		
- Ordinary shares of no par value	22,252,625	21,774,150
<hr/>		

Shares issued

During the nine month period ended September 30, 2008 the Company issued a further 863,800 ordinary shares for a total consideration of £478,475 following the exercise of certain warrants (nine month period ended September 30, 2007; 20,000,000 ordinary shares for a total consideration of £10,000,000). No ordinary shares were issued in the three month period ended September 30, 2008 (three month period ended September 30, 2007; nil).

Stock Option Plan

An element of the Group's reward strategy is the implementation of the Stock Option Plan, the purpose of which is to provide an incentive to the Directors, officers and key employees of the Group to achieve the objectives of the Group; to give suitable recognition to the ability and industry or such persons who contribute materially to the success of the Group; and to attract and retain persons of experience and ability, by providing them with the opportunity to acquire an increased proprietary interest in the Company. The Stock Option Plan is administered by the Remuneration and Nominating Committee.

No new share options were issued under the Company's Stock Option Plan during the three month period ended September 30, 2008 (three month period ended September 30, 2007; nil).

At September 30, 2008 there were 4,350,000 options outstanding (December 31, 2007: 3,800,000).

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Share warrants

The Company had the following outstanding warrants over the ordinary share capital of the Company at September 30, 2008:

Security	Holder	Number of ordinary shares	Exercise price	Market price at grant date	Expiry date
Warrants ⁽¹⁾	Shareholders of the company	9,948,700	US\$1.50	US\$1.00	May 7, 2009
Broker warrants ⁽²⁾	Thomas Weisel Partners (UK) Limited	700,000	US\$1.00	US\$1.00	June 26, 2009
Broker warrants ⁽³⁾	Various	1,012,500	CAD\$1.60	CAD\$1.60	Nov 15, 2009
Warrants ⁽⁴⁾	Ammonite	163,500	US\$1.00	US\$1.00	Nov 15, 2009

- (1) On June 26, 2007, pursuant to the Private Placement, XEL issued 20,000,000 units consisting of ordinary shares and 20,000,000 half-warrants at US\$1.00 per unit. Each whole warrant entitles the holder to purchase one ordinary share in XEL at an exercise price of US\$1.50 per share at any time until May 7, 2009. On February 15, 2008 the Company received consideration of US\$75,000 in respect of the exercise of 50,000 of such warrants and on March 12, 2008 the Company received consideration of US\$1,950 in respect of the exercise of 1,300 of such warrants.
- (2) Pursuant to the Private Placement, the Company issued to Thomas Weisel Partners (UK) Limited (formerly Westwind Partners (UK) Limited) 1,400,000 broker warrants to purchase 1,400,000 ordinary shares at an exercise price of US\$1.00 at any time until June 26, 2009. On January 31, 2008 Thomas Weisel Partners (UK) Limited exercised a total of 700,000 of these warrants for a consideration of US\$700,000.
- (3) Pursuant to the Initial Public Offering, XEL issued a total of 1,125,000 broker warrants to the following institutions: Thomas Weisel Partners (UK) Limited 843,750 (75%); Mirabaud Securities Limited 112,500 (10%); Wellington West Capital Markets Inc. 112,500 (10%); and MGI Securities 56,250 (5%), with each warrant entitling the holder to purchase one ordinary share in XEL at an exercise price of CAD\$1.60 at any time until November 15, 2009. On February 7, 2008, Wellington West Capital Markets Inc. exercised a total of 112,500 of these warrants for a consideration of CAD\$180,000.
- (4) XER entered into an agreement with Ammonite Capital Partners L.P. ("Ammonite") in January 2007 in connection with its proposed funding activities. The agreement contained provisions for XER to award Ammonite warrants over ordinary shares in XER under certain circumstances. XEL assumed responsibility for this agreement at the time that XEL acquired XER. The agreement provided for Ammonite to receive a total of 163,500 warrants, each over one ordinary share in XEL (the "Ammonite Warrants"), with each warrant entitling the holder to purchase one ordinary share in XEL at an exercise price of US\$1.00 at any time until November 15, 2009.

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13 Retained earnings and other reserves

	Retained Earnings	Merger Reserve	Other Reserves	Total
	£	£	£	£
At November 1, 2006	(133)	218	-	85
Loss for the period to December 31, 2007	(730,289)	-	-	(730,289)
Fair value of share warrants and options	-	-	1,645,481	1,645,481
At January 1, 2008 (audited)	(730,422)	218	1,645,481	915,277
Transfer upon exercise of share warrants	101,774	-	(101,774)	-
Fair value of share warrants and options	-	-	82,070	82,070
Loss for the period to September 30, 2008	(349,722)	-	-	(349,722)
At September 30, 2008 (unaudited)	(978,370)	218	1,625,777	647,625

The following explains the nature and purpose of each reserve within owners' equity:

Retained Earnings	Cumulative net gains and losses recognised in the Group Balance Sheet.
Merger Reserve	The difference between the nominal value of the shares issued to acquire a subsidiary and the nominal value of the shares acquired.
Other Reserves	The fair value of share based payment instruments and warrants in respect of ordinary shares granted by the Company at the date of grant and still outstanding.

14 Commitments and contingencies

The Group had no commitments or contingencies as at September 30, 2008 other than as accounted for in these interim unaudited consolidated financial statements.