

Q2

June 30, 2007

TSX.V: PPY.A PPY.B

PAINTED PONY
PETROLEUM LTD.



TO OUR SHAREHOLDERS

Painted Pony Petroleum Ltd. (“Painted Pony” or the “Company”) is pleased to present its first quarterly report to shareholders. We closed our initial public offering and a subsequent private placement on May 17, 2007, raising \$13.475 million before costs into our treasury. Our Class A and Class B shares commenced trading on the TSX Venture Exchange on May 23, 2007 under the symbols PPY.A and PPY.B respectively. Painted Pony was then off to a very quick start, with the spudding of our first operated well within a month and the shooting of a 3D seismic program in SE Saskatchewan before the end of the quarter.

Highlights

- Successful closing of the Company’s financing on May 17, 2007 raised proceeds of \$13.475 million, before costs.
- On May 23, 2007 Painted Pony was listed for trading on the TSX Venture Exchange under the symbols PPY.A and PPY.B.
- Painted Pony has approximately \$19.5 million of tax pools.
- On June 22, 2007 commenced our horizontal drilling program in the Kisbey area of S.E. Saskatchewan targeting light oil in the Bakken formation.
- Gained access to two farm in deals in S.E. Saskatchewan totalling 98.7 gross sections (63,154 gross acres, 55,552 net acres) with multi-zone light oil potential.
- Gained access to over 1,000 kilometers of 3D seismic data and 1,200 kilometers of 2D seismic data in N.E. British Columbia.
- Put in place a full technical team of eight with over 200 years of Western Canada oil and gas experience.

Operations Overview

The Company has two active core areas. In SE Saskatchewan, Painted Pony has assembled opportunities through farm-in arrangements to access over 55,000 net acres of land prospective for oil primarily from the Bakken, Midale and Frobisher formations. In NE British Columbia, the Company has commenced the evaluation of the extensive seismic datasets (over 1,000 square kilometers of 3D and 1,200 kilometers of 2D seismic data) prospective for natural gas.

SE Saskatchewan

During the quarter, Painted Pony commenced the drilling of the first of a two (0.75 net) well horizontal drilling program in the Kisbey area, targeting light sweet oil in the Bakken formation. The first well was rig released on July 11th 2007 and is currently production testing oil. The second well was drilled early during the third quarter and was also successful. The Company is planning to fracture stimulate both wells during the third quarter. The oil is light (44 API) and sweet.

In the Alameda area, Painted Pony participated in the shooting of a 32 square kilometer 3D seismic program over a farm in block of land. The data has resulted in multiple potential drilling locations prospective for light oil.

The Company was also successful at acquiring 1,920 acres gross (940 net) at the Saskatchewan June land sale.

An initial evaluation of the large 90 section (57,390 gross, 51,230 net acres) farm-in along the Midale/Elcott trend in SE Saskatchewan has resulted in the identification of multiple exploratory and development drilling opportunities. Following the first two successful wells, the Company is currently licensing four (2.0 net) wells all targeting light sweet oil. To control access to timing and costs, these wells will be operated by Painted Pony. The Company expects that all four will be drilled during the third quarter, or early in the fourth quarter of this year.

NE British Columbia

The Company has identified numerous potential drilling targets and has started negotiating farm-in deals on prospective lands. With a large 3D seismic data base, Painted Pony has an advantage over other junior oil and gas companies that operate in the area, in that it allows the Company to make drilling commitments, which in turn makes farm-in proposals more likely to be acceptable. Drilling will most likely take place in the first quarter of 2008.

Selected Financial Highlights

For the three months ending and as at June 30, 2007, selected unaudited financial highlights are:

		(unaudited)
Current assets less current liabilities	\$	12,005,429
Net loss	\$	53,661
Net loss per basic and diluted share	\$	0.01
Issuance of share capital for cash	\$	13,475,000
Share issue costs	\$	919,163
Expenditures on property & equipment for cash	\$	497,615

Painted Pony has 11,116,000 Class A Shares and 1,173,600 Class B Shares issued and outstanding which trade on the TSX Venture Exchange under the symbols "PPY.A" and "PPY.B".

Outlook

Painted Pony has already identified in excess of 20 drilling opportunities on existing farm-in lands, and under the 3D seismic. The Company is in a strong financial position to take advantage of available and increasingly less expensive services. Painted Pony has a very experienced and engaged team of oil and gas professionals with access to substantial farm-in deals and a large 3D seismic base; these give the Company a significant competitive advantage. The team at Painted Pony is excited about the potential we see in the existing assets, and is committed to share value growth for investors.

Readers are invited to visit the Company's new website at www.paintedpony.ca.

Respectfully submitted on behalf of the Board of Directors,

(signed) "Patrick Ward"

Patrick Ward
President and Chief Executive Officer
August 22, 2007

MANAGEMENT'S DISCUSSION AND ANALYSIS

INTERM FINANCIAL REPORT – THREE MONTHS ENDED JUNE 30, 2007

The following discussion is management's assessment of Painted Pony Petroleum Ltd. ("Painted Pony" or the "Company") financial condition and operating results for the three months ended June 30, 2007 and has been prepared by management with information up to and as at August 22, 2007.

This Management's Discussion and Analysis ("MD&A") should be read in conjunction with the audited financial statements for the years ended December 31, 2006 and the unaudited interim financial statements for the three months ended June 30, 2007. The MD&A may contain forward-looking statements. This commentary is based on information available to and is dated August 22, 2007.

Painted Pony commenced commercial operations on April 3, 2007 upon completion of a financial reorganization as part of an overall restructuring of the Company. Pursuant to Section 1625 "Comprehensive Revaluation of Assets and Liabilities of the Canadian Institute of Chartered Accountants Handbook, the Company is entitled to use "fresh start" accounting which means that prior or comparative financial information is not required to be presented as it would not be meaningful to the reader. Accordingly, financial information is presented commencing on April 3, 2007. Consequently, comparative financial information for the statements of operations and cash flows is not presented.

These documents and additional information about Painted Pony are available on SEDAR at www.sedar.com.

Forward-looking Statements

This MD&A contains forward-looking statements relating to future events. In some cases, forward-looking statements can be identified by words such as "anticipate", "continue", "estimate", "expect", "forecast", "may", "will", "project", "should", "believe", or similar expressions. These statements represent management's best projections but undue reliance should not be placed upon them as they are derived from numerous assumptions. These assumptions are subject to known and unknown risks and uncertainties, including the business risks discussed in the MD&A, which may cause actual performance and financial results to differ materially from any projections of future performance or results expressed or implied by such forward-looking statements.

These risks and uncertainties include, but are not limited to, the following:

- Normal risks common to the oil and natural gas industry, including various operational risks in the carrying out of exploration, development and production operations,
- Risks and uncertainty of oil and gas geological deposits,
- Revisions, amendments or changes to capital expenditure plans including exploration, development and exploitation projects,
- Risks as to the availability and pricing of appropriate financing alternatives, and
- Potential changes in income tax regulations, governmental policies, rules, practise or approval processes changes, or delays, or enhancements.

Accordingly, readers are cautioned that events or circumstances could cause results to differ materially from those predicted. From time to time, Painted Pony's management make estimates and form opinions on which the forward-looking statements are based. The Company assumes no obligation to update forward-looking statements if circumstances, management's estimates or opinions change.

Overview

From incorporation on August 12, 1999, the Company was a provider of web, logistics, financial and marketing services to U.S. merchants servicing the international market. In October 2002, a partnership agreement was entered into with Canada Post to jointly operate the Company's merchant activities. This partnership interest was disposed of in 2005. In November 2005, the auction business was sold. Since then, the Company did not carry on active business as it was reorganizing its affairs. The Company, a private company, was not a reporting issuer and did not prepare quarterly financial statements; consequently quarterly information for the eight most recently completed quarters is not presented.

On May 23, 2007, subsequent to completion of an initial public offering on May 17, 2007, the Class A shares and Class B shares of Painted Pony Petroleum Ltd. began trading on the TSX Venture under the symbols "PPY.A" and "PPY.B" respectively.

Results of Operations

The Company currently has no producing properties and consequently no oil and gas sales or revenue. Expenses consist primarily of general and administrative expenses. For the three months ended June 30, 2007, revenue was comprised of interest on term deposits of \$64,322. Management expect that as the funds obtained through the placement of Class A and Class B shares in May of 2007 is expended, the interest income will diminish.

General and administrative expenses for the three months ended June 30, 2007 are inclusive of \$56,756 of costs assumed pursuant to the Financing Agreement, as set out in the May 8, 2007 long form prospectus (a copy of which can be viewed at SEDAR.com, or by contacting the Company). Total general and administrative costs, prior to capitalization of \$112,096 of those costs directly relating to the exploration for and development of hydrocarbons, were \$229,211. Salaries and consulting costs, which commenced on May 16, 2007 for six full-time and three part-time people, totalled \$101,358. Other significant general and administrative items were computer software licenses and rentals (\$14,851) and office rent and parking (\$13,898).

Depreciation expense of \$868 was incurred on office equipment, computer hardware and software and office furniture determined on a 20% per annum declining balance basis. For purposes of the depletion and depreciation calculation for the three months ended June 30, 2007, all the costs of unproved petroleum properties have been excluded from the cost pool for the purpose of calculating depletion, pending assignment of reserves or determination the costs are impaired.

Sales of crude oil are anticipated to commence during the third quarter of 2007, as the first two wells complete the production testing phase and are then placed on production after fracing operations are completed.

Debt

During 2006 and 2007, certain officers and other individuals advanced funds in return for promissory notes totalling \$120,000. The promissory notes are unsecured, have no fixed terms of repayment and bear interest at a rate of 5% per annum beginning on the first anniversary of the date they were issued.

As at June 30, 2007 and August 22, 2007, Painted Pony has no long term debt or credit facilities.

Share Capital

In February, 2007, the Company entered into a series of agreements whereby it reorganized itself. The Company was continued into Alberta under the ABCA, and articles of amendment were filed effecting name changes. All of the assets and liabilities were sold or assigned, and a private placement consisting of 240,000 Common Voting Shares and a convertible debenture in the principal amount of \$347,500 was completed. The convertible debenture was secured, bore interest at the rate of 5% per annum during the first two years of its term and at bank prime rate plus 3% thereafter and was convertible into Common Non-Voting Shares of the Company at a price of \$0.15625 per Common Non-Voting Share. The Company created an unlimited number of non-voting common shares and consolidated the issued common shares on the basis that up to 2,500 of such shares became one common share. The Company then had 196 issued and outstanding common voting shares outstanding.

On March 27, 2007, the Company entered into a financing agreement (“Financing Agreement”) pursuant to which the Company reconstituted the Company's board of directors, reorganized the share capital of the Company and filed articles of amendment to change the name to Painted Pony Petroleum Ltd., all of which were approved by the shareholders of the Company on March 29, 2007 and which were effected on April 3, 2007.

The 196 issued and outstanding common voting shares were exchanged for:

- (i) 29,400 issued and outstanding Class A shares on the basis of 150 Class A shares for each existing common voting shares, and
- (ii) 6,615 issued and outstanding Class B shares on the basis of 33.75 Class B shares for each existing common voting share.

Completion of the reorganization of the Company, as contemplated in the Financing Agreement was conditional upon the closing of the initial public offering, which occurred on May 17, 2007.

On May 17, 2007, the Company sold 12,000 units at a price of \$1,000 per unit for gross proceeds of \$12,000,000 (the “Offering”). Each unit is comprised of 400 Class A shares and 90 Class B shares issued on a “flow-through” basis. Share issue costs were \$919,163.

Subsequent to the closing of the Offering, Painted Pony issued on a non-flow through basis, 386,600 Class A shares and 86,985 Class B shares to a third party in satisfaction of the \$347,500 convertible debenture and other debt in the amount of \$619,000 (the “Debt Satisfaction”).

Immediately after the closing of both the Offering and the Debt Satisfaction, a non-brokered private placement (the “Private Placement”) was completed of 5,900,000 Class A Shares at a price of \$0.25 per share to the new Directors, Officers, employees and certain of their associates and affiliates.

In accordance with the policies of the TSXV, the 5,900,000 Class A Shares which were issued pursuant to the Private Placement were placed in escrow. Under the terms of the Escrow Agreement, ten percent (10%) of such Class A Shares were released from escrow upon receipt of notice from the TSXV confirming the listing of the Class A Shares on the TSXV (the "Listing Notice"), which was dated on May 22, 2007. The remaining ninety percent (90%) of such Class A Shares will be released from escrow in fifteen percent (15%) tranches during consecutive six month intervals over the following 36 months. The above escrow release schedule is subject to acceleration in accordance with NP 46-201 Escrow for Initial Public Offerings and the policies of the TSXV in the event that the Company subsequently meets certain listing requirements.

After giving effect to the Offering, the Debt Satisfaction and the Private Placement, and at June 30, 2007 and August 22, 2007, 11,116,000 Class A shares and 1,173,600 Class B shares were issued and outstanding. As at June 30, 2007 and August 22, 2007, no Common Voting, Common Non-Voting or Preferred Shares were outstanding.

The Company has a Stock Option Plan whereby options to purchase Class A Shares may be granted by the board of directors to directors, officers, employees of, and consultants to the Company. The Plan has reserved for issuance a number of Class A shares equal to ten percent of the aggregate number of Class A Shares and Class B Shares issued and outstanding from time to time. As at the date hereof, no options are issued and outstanding.

Income Taxes

The Company has a tax loss carry forward of approximately \$19.5 million. No tax asset for the value of these losses has been recorded for accounting purposes as the Company does not believe that it currently meets the criteria of the losses being utilized being more likely than not.

On May 2007, the Company issued 12,000 units at \$1,000 per unit for total proceeds of \$12,000,000, committing to spend these funds on qualified exploration and development expenditures by December 31, 2008. The Company intends to renounce the full \$12,000,000 effective December 31, 2007. The tax effect of the tax benefits renounced to subscribers will be recognized in the financial statements when the renouncement documents are filed in February, 2008. As at June 30, 2007, the Company had expended approximately \$433,922 of funds on qualified expenditures related to this financing. The remaining commitment of \$11,566,078 as at June 30, 2007 is to be incurred by December 31, 2008.

Dividends

The Company has not declared or paid any dividends. Any decision to pay dividends on its shares will be made by the board of directors on the basis of earnings, financial requirements and other conditions existing at such future time.

Outlook

During the third quarter of 2007, the Company is planning to fracture stimulate the two horizontal light oil wells drilled to date. Painted Pony is currently licensing four (2.0 net) wells in Saskatchewan, targeting light sweet oil, which are expected to be drilled with partners during the third quarter, or early in the fourth quarter of this year. Within the NE British Columbia area of interest, the Company anticipates potentially drilling the first well during early 2008, pending successful farm-in negotiations.

Comprehensive Income

As Painted Pony does not have any comprehensive income, being net earnings and other comprehensive income, the interim financial statements do not include a Statement of Comprehensive Income describing the components nor is a section needed in shareholder's equity, nor is a Statement of Accumulated Other Comprehensive Income which would provide a continuity of the balance.

Liquidity

As at June 30, 2007, Painted Pony had current assets of \$13,363,205 and current liabilities of \$1,357,776. Management believe they have sufficient financial resources with which to carry out the planned capital expenditure program for the year. The cash has been and is currently on deposit in a major Canadian financial institution.

The Company is committed to spending \$12,000,000 on qualifying exploration and development expenditures prior to December 31, 2008 relating to a flowthrough agreement, of which \$433,922 has been expended as at June 30, 2007.

Capital Resources

All of the property and equipment of the original business operations of the Company were sold in 2005. Subsequent to the sale of the Company's auction business in November, 2005, the Company had no continuing operations until completion of the initial public offering on May 17, 2007. On June 22, 2007 the Company commenced active operations with the drilling of its first crude oil well in the Kisbey area of Saskatchewan.

Costs of petroleum properties reflect the estimated costs incurred for eight days of drilling operations for the Company's first well, preliminary preparatory costs for the second Kisbey well and \$11,626 of costs for participating in a land sale.

In addition, the Company has invested \$52,067 in other assets, specifically office furniture, computer hardware and software and office furniture and fixtures. Of these, \$30,189 of other assets was assigned to the Company pursuant to the Financing Agreement whereby all of the asset and liabilities were transferred to the Company immediately prior to closing of the initial public offering.

For the three month period ending June 30, 2007, the Company capitalized general and administrative expenses in the amount of \$112,096 relating to exploration and development activities.

Off Balance Sheet Arrangements

In addition to the land purchased, the Company has also entered into an agreement with an independent company whereby Painted Pony will be carried for approximately \$35,050 of land costs in exchange for carrying the company for an equivalent value in the drilling of a well expected to be incurred during the first half of 2008.

The Company also participated in a three dimensional seismic program on a carried basis by an independent company. In exchange, the Company will carry an equivalent value (being approximately \$150,000) for the benefit of the company in the drilling of a well, expected to be drilled during the third quarter of 2007.

Related Party Transactions

The Company utilizes the services of a law firm in which the Corporate Secretary is an Associate. During the three months ended June 30, 2007, the Company incurred \$111,815, excluding reimbursement of costs, on services obtained from the firm, which charges for fees and services.

For the three months ended June 30, 2007, a family member of the President provided computer consulting services entered into on normal commercial terms valued at \$2,302 to the Company.

All related party transactions are in the normal course of business and have been measured at the agreed to terms and exchange values, being the consideration established and agreed to by the parties and on normal commercial terms comparable to those negotiated with third parties.

Financial Instruments and Other Instruments

The fair values of the Company's term deposits, accounts receivables, accounts payables and accrued liabilities approximate their carrying values due to the short-tem nature of these financial instruments. The carrying value of the promissory notes payable approximate their fair value due to the capacity of prompt liquidation.

The Company's accounts receivables are primarily with industry competitors and are subject to normal industry credit risks. As the Company extends unsecured credit to these entities, therefore, the collection of any receivables may be affected by changes in the economic environment or other conditions. Management believe the risk is mitigated by the financial position of the entities, and the Company's practice of requesting cash call advances for funds estimated to be incurred.

To date, the Company has not participated in any hedges.

Internal Controls

As of June 30, 2007 the Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO") have evaluated the design and effectiveness of the Company's disclosure controls and procedures. The small size of the current organization contributes in a large part to senior management being fundamentally aware of material information that would require disclosure by the Company and this, in part, supports management's assessment that its disclosure controls are adequate and effective to ensure accurate and complete disclosure except as described below.

The Chief Executive Officer and Chief Financial Officer of Painted Pony are responsible for designing internal controls over financial reporting or causing them to be designed under their supervision in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian generally accepted accounting principles. Painted Pony management has assessed the design of internal controls over financial reporting. During this process, certain material weaknesses in internal controls over financial reporting were identified as follows:

- Due to the limited number of staff at Painted Pony, it is not economically feasible to achieve segregation of incompatible duties. Painted Pony currently only has six full time employees, two part-time employees and one part-time consultant. The limited number of staff may also result in identifying weaknesses with respect to accounting for complex and non-routine accounting transactions that may arise as the Company does not have a sufficient number of finance personnel with technical accounting knowledge to address all complex and non-routine accounting matters that may arise, and
- Many of Painted Pony's information systems are subject to general control deficiencies including a lack of effective controls over spreadsheets, access and documentation.

These weaknesses in internal controls over financial reporting result in a more than remote likelihood that a material misstatement would not be prevented or detected. Management and the Board of Directors try to mitigate the risk of material mis-statement; however, reasonable assurance does not exist that this risk can be reduced to a remote likelihood of a material misstatement. Painted Pony has no current plans to remediate these weaknesses.

Because of their inherent limitations, disclosure controls as well as internal controls over financial reporting may not prevent or detect fraud, misstatements, or errors. Control systems can provide only reasonable and not absolute assurance that the objectives of the control system and the Company are achieved.

PAINTED PONY PETROLEUM LTD.

(Formerly 1300873 Alberta Ltd.)

INTERIM FINANCIAL STATEMENTS

(UNAUDITED)

JUNE 30, 2007

REVIEW OF INTERIM FINANCIAL STATEMENTS

The accompanying unaudited interim financial statements of the Company have been prepared by and are the responsibility of the Company's management.

The Company's independent auditor has not performed a review of these financial statements in accordance with standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

PAINTED PONY PETROLEUM LTD.
(Formerly 1300873 Alberta Ltd.)
Interim Balance Sheets

Unaudited

	June 30, 2007	December 31, 2006
ASSETS		
Current assets		
Cash and cash equivalents	\$ 12,901,591	\$ 51,470
Holdback receivable	-	1,051,872
Accounts receivable	356,191	-
Prepaid expenses	105,423	-
	<u>13,363,205</u>	<u>1,103,342</u>
Property and equipment (note 5)	501,828	-
	<u>\$ 13,865,033</u>	<u>\$ 1,103,342</u>
LIABILITIES and SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable and accrued liabilities	\$ 1,237,776	\$ 261,510
Promissory notes (note 6)	120,000	-
Due to parent company	-	1,777,741
	<u>1,357,776</u>	<u>2,039,251</u>
Asset retirement obligations (note 7)	5,081	-
	<u>1,362,857</u>	<u>2,039,251</u>
Capital stock (note 4 & 8)	13,559,837	5,000
Contributed surplus (note 4)	-	15,690,266
Deficit (note 4)	(1,057,661)	(16,631,175)
	<u>12,502,176</u>	<u>(935,909)</u>
	<u>\$ 13,865,033</u>	<u>\$ 1,103,342</u>

Basis of Presentation (notes 2 & 4)

Commitments (note 11)

See accompanying notes to the interim financial statements.

PAINTED PONY PETROLEUM LTD.
(Formerly 1300873 Alberta Ltd.)
Interim Statement of Operations and Deficit

(unaudited)

	Three months ended June 30, 2007
Revenue	
Interest	\$ 64,322
Expenses	
General and administrative	117,115
Depreciation and accretion	868
	117,983
Net loss for the period	(53,661)
Deficit, beginning of period (note 4)	(1,004,000)
Deficit, ending of period	\$ (1,057,661)
Net loss per share (note 9)	
Basic and diluted	\$ (0.01)

See accompanying notes to the interim financial statements.

PAINTED PONY PETROLEUM LTD.
(Formerly 1300873 Alberta Ltd.)
Interim Statement of Cash Flows

(unaudited)

	Three months ended June 30, 2007
Cash provided by (used for)	
Operating activities	
Net loss for the period	\$ (53,661)
Add items not affecting cash	
Depreciation and accretion	868
	(52,793)
Change in non-cash working capital	(88,900)
	(141,693)
Financing activities	
Issuance of share capital	13,475,000
Share issue costs	(919,163)
Issue of promissory notes (note 6)	120,000
Change in non-cash working capital	35,796
	12,711,633
Investing activities	
Expenditures on property and equipment	(497,615)
Change in non-cash working capital	829,266
	331,651
Increase in cash and cash equivalents	12,901,591
Cash and cash equivalents, beginning of period	-
Cash and cash equivalents, end of period	\$ 12,901,591
Cash and cash equivalents is comprised of:	
Balances with banks	\$ 26,591
Short term deposits	12,875,000
	\$ 12,901,591

See accompanying notes to the interim financial statements.

PAINTED PONY PETROLEUM LTD.
(Formerly 1300873 Alberta Ltd.)
NOTES TO INTERIM FINANCIAL STATEMENTS

(UNAUDITED)
June 30, 2007

1. Nature of Operations

Painted Pony Petroleum Ltd. (“the Company”) had no operations since November 2005 until the Company was recapitalized in May 2007. The Company’s principal business activity is the exploration, development and production of petroleum and natural gas resources in western Canada.

2. Basis of Presentation

The interim unaudited financial statements of Painted Pony Petroleum Ltd., (“the Company”) have been prepared by management in accordance with Canadian generally accepted accounting principles.

The Company commenced commercial operations on April 3, 2007 upon completion of the financial reorganization (see note 4). Consequently, comparative financial information for the statements of operations and cash flows is not presented.

3. Significant Accounting Policies

Use of Estimates

The preparation of financial statements in accordance 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 balance sheet date and the reported amounts of revenue and expenses during the reporting period. The financial statements have, in management’s opinion, been properly prepared using careful judgment with reasonable limits of materiality and within the framework of the significant accounting policies summarized below. Actual results could differ from those estimates.

Property and Equipment

(i) Capitalized Costs

The Company follows the Canadian full cost method of accounting for its petroleum and natural gas operations. Under this method, all costs related to the exploration, development and production of petroleum and natural gas reserves are capitalized in a single Canadian cost centre. Costs include lease acquisition costs, geological and geophysical expenses, costs of drilling both productive and non-productive wells, production equipment costs, general and administrative costs and stock-based compensation directly related to exploration and development activities. Proceeds from the sale of properties are applied against capitalized costs, without any gain or loss being realized, unless such sale would alter the rate of depletion and depreciation by more than 20%. Office equipment is recorded at cost.

(ii) Depletion and Depreciation

Petroleum and natural gas properties, net of estimated salvage or residual value, and estimated costs of future development of proved undeveloped reserves are depleted and amortized using the unit-of-production method based on estimated gross proved petroleum and natural gas reserves as determined by independent engineers. For depletion and amortization purposes, relative volumes of petroleum and natural gas production and reserves are converted at the energy equivalent conversion rate of six thousand cubic feet of natural gas to one barrel of crude oil.

Costs of unproved properties and seismic costs on undeveloped land are initially excluded from petroleum and natural gas properties for the purpose of calculating depletion. When proved reserves are assigned or the property or seismic is considered to be impaired, the costs of the property or seismic or the amount of the impairment is added to costs subject to depletion.

Office equipment is depreciated over its estimated useful life at declining-balance rates between 20% and 50%.

(iii) Ceiling Test

In applying the full cost method, the Company calculates a ceiling test whereby the carrying amount of property and equipment is compared to the sum of the undiscounted cash flows expected to result from the future production of proved reserves and the sale of unproved properties. Cash flows are based on third party quoted forward prices, adjusted for transportation and quality differentials. Should the ceiling test result in an excess of carrying value, the Company would then measure the amount of impairment by comparing the carrying amounts of property and equipment to an amount equal to the estimated net present value of future cash flows from proved plus probable reserves and the sale of unproved properties. The Company's risk-free interest rate is used to arrive at the net present value of the future cash flows. Any excess carrying amount would be recorded as a permanent impairment.

Asset Retirement Obligations

The Company recognizes the fair value of an Asset Retirement Obligation ("ARO") in the period in which it is incurred when a reasonable estimate of the fair value can be made. The fair value is determined through a review of engineering studies, industry guidelines and management's estimate on a site-by-site basis. The fair value of the estimated ARO is recorded as a liability, with a corresponding increase in the carrying amount of the related asset. The capitalized amount is depleted on the unit-of-production method based on gross proved reserves. The liability amount is increased each reporting period to reflect the passage of time with the corresponding amount charged to earnings as accretion expense. Actual costs incurred upon the settlement of the asset retirement obligation are charged against the asset retirement obligation to the extent of the liability recorded.

Joint Operations

Substantially all of the exploration and production activities of the Company will be conducted jointly with others and these financial statements reflect only the Company's proportionate interest in such activities.

Income Taxes

The Company follows the asset and liability method of accounting for income taxes. Under this method, future tax assets and liabilities are recognized for the future tax consequences attributable to differences between financial statement carrying amounts of assets and liabilities and their respective tax basis. Future tax assets and liabilities are measured using substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. A valuation allowance is recorded against any future income tax assets if it is more likely than not that the asset will not be realized. The effect on future tax assets and liabilities of a change in tax rates is recognized in earnings in the period that includes the date of substantive enactment.

Flow-Through Shares

Periodically, the Company may finance a portion of its exploration and development activities through the issuance of flow-through shares. Under the terms of the flow-through share issues, the tax attributes of the related expenditures are renounced to subscribers. Share capital is reduced and future tax liability is increased by the tax effected amount of the renounced tax deductions at the time of renouncement, which is when the related documentation is filed with the appropriate governmental agency and there is reasonable certainty that the expenditures will be incurred.

Revenue Recognition

Revenue from the sale of crude oil, natural gas and natural gas liquids are recognized based on volume delivered at contractual delivery points and rates. The cost associated with the delivery, including operating, transportation and production-based royalty expenses are recognized in the same period in which the related revenue is earned and recorded.

Per Share Amounts

Basic income (loss) per share is computed by dividing net income (loss) by the weighted average number of Class A and Class B common shares outstanding during the period. The treasury stock method is used to calculate diluted per share amounts whereby proceeds from the exercise of in-the-money stock options or warrants and unrecognized future stock-based compensation expense are assumed to be used to purchase common shares of the Company at the average market price during the period. Diluted per share amounts reflect the potential dilution that could occur if stock options or warrants to purchase common shares were exercised and converted to common shares. In addition, Class B shares are converted into Class A shares at \$10 divided by the last 30 day weighted average price of the Class A shares.

Cash and Cash Equivalents

The Company considers all highly liquid investments with maturity of three months or less at the time of purchase to be cash equivalents. These cash equivalents primarily consist of funds on deposit under various terms.

Measurement Uncertainty

The amount recorded for depletion and depreciation of petroleum and natural gas properties and the ceiling test calculation are based on estimates of gross proved reserves, production rates, commodity prices, future costs and other relevant assumptions. By their nature, these estimates are subject to measurement uncertainty and the effects on the financial statements of changes in such estimates in future years could be significant.

Change in Accounting Policies

As of January 1, 2007, the Company adopted new accounting standards for "Accounting Changes", "Comprehensive Income", "Equity", "Financial Instruments – Recognition and Measurement", "Financial Instruments - Disclosure and Presentation" and "Hedges".

Accounting Changes provides expanded disclosures for changes in accounting policies, accounting estimates and corrections of errors. Under the new standard, accounting changes should be applied retrospectively unless otherwise permitted or where impracticable to determine. As well, voluntary changes in accounting policy are made only when required by a primary source of GAAP or the change results in more relevant and reliable information.

Comprehensive Income introduces a new requirement to temporarily present certain gains and losses from changes in fair value outside net income. It includes unrealized gains and losses, such as changes in currency translation adjustment relating to self-sustaining foreign operations, unrealized gains or losses on available-for-sale investments and the effective portion of gains or losses on derivatives designated as cash flow hedges. The application of this revised standard did not result in comprehensive income (loss) being different from the net income for the periods presented.

Financial Instruments – Recognition and Measurement prescribes when a financial instrument is to be recognized on the balance sheet and at what amount. It also specifies how financial instrument gains and losses are to be presented. All financial instruments are classified into one of the following five categories: held-for-trading, held-to-maturity, loans and receivables, available-for-sale financial assets, and other financial liabilities. Initial and subsequent measurement and recognition of changes in the value of financial instruments depends on their initial classification.

- Held-to-maturity investments, loans and receivables, and other financial liabilities are initially measured at fair value and subsequently measured at amortized cost. Amortization of premiums or discounts and losses due to impairment are included in current period net earnings.
- Available-for-sale financial assets are measured at fair value. Revaluation gains and losses are included in other comprehensive income until the asset is removed from the balance sheet.
- Held for trading financial instruments are measured at fair value. All gains and losses are included in the net earnings in the period in which they arise.
- All derivative financial instruments are classified as held-for-trading financial instruments and are measured at fair value, even when they are part of a hedging relationship. All gains and losses are included in net earnings in the period which they arise.

The application of these new standards did not have an impact on the Company's financial statements.

Hedges provide alternative treatments for entities that choose to designate qualifying transactions as hedges for accounting purposes. The Company currently uses mark-to-market accounting for its derivative instrument, which does not qualify or have not been designated as a hedge.

4. Financial Reorganization

Effective March 20, 2007, the Company's debt and equity holders approved a financial reorganization, as part of an overall restructuring of the Company.

The Company's assets and liabilities have been adjusted to reflect the values established during the financial reorganization. The contributed surplus and the original share capital have been reclassified to deficit, and the Company commenced operations as of the date after the financial reorganization. The effect of the financial reorganization on the balance sheet accounts is as follows:

	March 20, 2007 prior to financial reorganization	Reorganization adjustments	March 20, 2007 after financial reorganization
ASSETS	\$ -	\$ -	\$ -
LIABILITIES AND SHAREHOLDERS' EQUITY			
Due to StoneBridge Merchant			
Capital Corp.	\$ 550,909	\$ 68,091 ^(a)	\$ 619,000
Convertible debentures	347,500	-	347,500
Common shares	42,500	(5,000) ^(b)	37,500
Contributed surplus	15,690,266	(15,690,266) ^(c)	-
Deficit	(16,631,175)	15,627,175 ^(c)	(1,004,000)
	\$ -	\$ -	\$ -

(a) To reflect the agreed upon fair value of the debt.

(b) To eliminate share capital attributable to previously issued common shares.

(c) Reclassification of contributed surplus to deficit to reflect fresh start accounting as of the date of the financial reorganization.

On April 3, 2007, the Company:

- changed its name from 1300873 Alberta Ltd. to Painted Pony Petroleum Ltd.;
- authorized an unlimited number of Class A shares;
- authorized an unlimited number of Class B shares convertible at the option of the Company at anytime after June 30, 2010 and before June 30, 2012, and convertible at the option of the holder after July 1, 2012 and before August 1, 2012, into Class A shares. Any outstanding Class B shares at August 1, 2012 shall be automatically converted into Class A shares;
- authorized an unlimited number of common voting shares;
- authorized an unlimited number of common non-voting shares, redeemable at the option of the holder;
- authorized an unlimited number of preferred shares issuable in series from time to time to be determined by the directors; and
- changed the 196 issued and outstanding common voting shares into:

- (i) 29,400 issued and outstanding Class A shares on the basis of 150 Class A shares for each existing common voting shares, and
- (ii) 6,615 issued and outstanding Class B shares on the basis of 33.75 Class B shares for each existing common voting share.

5. Property and Equipment

June 30, 2007	Cost	Accumulated depreciation	Net book value
Petroleum properties, including exploration and development thereon	\$ 450,629	\$ -	\$ 450,629
Production equipment and facilities	-	-	-
Other	52,067	868	51,199
	\$ 502,696	\$ 868	\$ 501,828

For the three month period ending June 30, 2007, the Company capitalized general and administrative expenses in the amount of \$112,096 relating to exploration and development activities.

All the costs of petroleum properties have been excluded from the cost pool for the purpose of calculating depletion, pending assignment of reserves or determination that the costs are impaired.

6. Promissory Notes

During 2006 and 2007, certain officers and other individuals advanced funds in return for promissory notes totalling \$120,000. The promissory notes are unsecured, have no fixed terms of repayment and bear interest at a rate of 5% per annum beginning on the first anniversary of the date they were issued.

7. Asset Retirement Obligations

The total future asset retirement obligations were estimated by management based on the Company's net ownership in wells and facilities, estimated costs to reclaim and abandon the wells and facilities, and the estimated timing of the costs to be incurred in future periods. The Company has estimated the total undiscounted asset retirement obligation to be \$23,682 as at June 30, 2007. These payments are expected to be made over the next 20 years. The Company used a credit adjusted risk free rate of 8.0% and an inflation rate of 2% to calculate the present value of the asset retirement obligation.

The following table reconciles the Company's asset retirement obligations:

	Three months ended June 30, 2007
Obligation, beginning of period	\$ -
Liabilities incurred	5,081
Obligation, end of period	\$ 5,081

8. Capital Stock

a) Authorized

Unlimited	Common voting shares, of which none are outstanding as at June 30, 2007
Unlimited	Common non-voting shares, of which none are outstanding as at June 30, 2007
Unlimited	Class A shares
Unlimited	Class B shares
Unlimited	Preferred shares, of which none are outstanding as at June 30, 2007

The Class A Shares and the Class B Shares are voting on the basis of one vote per share. There are no fixed dividends payable on either the Class A Shares or the Class B Shares. In the event of the liquidation or dissolution of the Corporation, the Class B Shares will be converted into Class A Shares and the Class A Shares are entitled to receive, on a pro rata basis with the Common Voting and Common Non-Voting Shares, all assets of the Corporation as are distributable to the holders of shares.

Class B Shares

The Class B Shares will be convertible, at the option of the Corporation, at any time after June 30, 2010 and on or before June 30, 2012 into Class A Shares. The number of Class A Shares obtained upon conversion of each Class B Shares will be equal to \$10.00 divided by the greater of \$1.00 and the current market price of the Class A Shares.

If the conversion has not occurred by the close of business on June 30, 2012, the Class B Shares become convertible, at the option of the shareholder, into Class A Shares on the same basis. Any Class B Shares outstanding at the close of business on August 1, 2012 shall be automatically converted into Class A Shares on the same basis.

b) Issued

Common Voting Shares

	June 30, 2007		December 31, 2006	
	Number of Shares	Amount	Number of Shares	Amount
Balance, beginning of period	100	\$ 5,000	100	\$ 5,000
Shares issued	96	37,500	-	-
Financial reorganization	-	(5,000)	-	-
April 3, 2007 prior to financial reorganization	196	37,500	100	\$ 5,000
Exchange into Class A and Class B Shares	(196)	(37,500)		
Balance, after financial reorganization	-	\$ -		

Class A and Class B Shares

	Class A Shares		Class B Shares	
	Number of Shares	Amount	Number of Shares	Amount
Common Voting Shares exchanged into Class A and Class B shares pursuant to the financial reorganization	29,400	\$ 3,750	6,615	\$ 33,750
Flow through shares issued	4,800,000	1,200,000	1,080,000	10,800,000
Shares issued in satisfaction of debt	386,600	96,650	86,985	869,850
Private placement to founders	5,900,000	1,475,000	-	-
	11,116,000	2,775,400	1,173,600	11,703,600
Share issuance costs, allocated	-	(91,916)	-	(827,247)
Balance, June 30, 2007	11,116,000	\$ 2,683,484	1,173,600	\$10,876,353

On January 31, 2007, 96 post-consolidation common shares were issued for cash consideration of \$37,500 pursuant to a private placement.

On February 2, 2007, by Articles of Amendment, the Company created an unlimited number of non-voting common shares and consolidated the issued common shares on the basis that up to 2,500 of such shares shall become one common share. All share and per share amounts have been retroactively adjusted to reflect this share consolidation.

Effective April 3, 2007 pursuant to the financial reorganization, the 196 issued and outstanding common voting shares were exchanged for:

- (i) 29,400 issued and outstanding Class A shares on the basis of 150 Class A shares for each existing common voting shares, and
- (ii) 6,615 issued and outstanding Class B shares on the basis of 33.75 Class B shares for each existing common voting share.

On May 17, 2007, the Company issued 12,000 units at a price of \$1,000 per unit for gross proceeds of \$12,000,000 (the "Offering"). Each unit is comprised of 400 Class A shares and 90 Class B shares issued on a "flow-through" basis.

On May 2007, the Company issued 12,000 units at \$1,000 per unit for total proceeds of \$12,000,000, committing to spend these funds on qualified exploration and development expenditures by December 31, 2008. The Company intends to renounce the full \$12,000,000 effective December 31, 2007. The tax effect of the tax benefits renounced to subscribers will be recognized in the financial statements when the renouncement documents are filed in February, 2008. As at June 30, 2007, the Company had expended approximately \$433,922 of funds on qualified expenditures related to this financing.

Subsequent to the closing of the Offering, Painted Pony issued on a non-flow through basis, 386,600 Class A shares and 86,985 Class B shares in satisfaction of the convertible debenture in the amount of \$347,500 and other debt in the amount of \$619,000 (the "Debt Satisfaction").

Immediately after the closing of both the Offering and the Debt Satisfaction, a non-brokered private placement (the "Private Placement") was completed of 5,900,000 Class A Shares at a price of \$0.25 per share to the new Directors, Officers, employees and certain of their associates and affiliates.

c) Stock Option Plan

The Company has a Stock Option Plan (the "Plan") pursuant to which options to purchase Class A Shares may be granted by the board of directors to directors, officers, employees of, and consultants to the Corporation. The Plan has reserved for issuance a number of Class A shares equal to 10% of the aggregate number of Class A Shares and Class B Shares issued and outstanding from time to time.

As at the date hereof, no options are issued and outstanding.

9. Per Share Amounts

The weighted average number of Class A shares outstanding during the three month period ended June 30, 2007 was 5,511,785. The weighted average number of Class A shares outstanding after deemed conversion of the Class B shares was 9,093,837 for the three months ending June 30, 2007. Basic and diluted net loss per share is computed using the weighted average number of outstanding common shares outstanding at for each period.

10. Related Party Transactions

The Company utilizes the services of a law firm in which the Corporate Secretary is an Associate. During the three months ended June 30, 2007, the Company incurred \$111,815, excluding reimbursement of costs, on services obtained from the firm.

For the three months ended June 30, 2007, a family member of the President provided computer consulting services entered into on normal commercial terms for \$2,302.

11. Commitments

The Company is committed to spending \$12,000,000 on qualifying exploration and development expenditures prior to December 31, 2008 relating to a flowthrough agreement, of which \$433,922 has been expended as at June 30, 2007.

The Company is committed to payment for office space, exclusive of occupancy costs, as follows:

	Amount
2007	\$ 24,800
2008	\$ 24,800

12. Financial Instruments

The fair values of the Company's term deposits, accounts receivables, accounts payables and accrued liabilities approximate their carrying amounts due to the short-tem nature of these financial instruments. The carrying amount of the promissory notes payable approximate their fair value due to the capacity of prompt liquidation.

The Company's accounts receivables are primarily with industry competitors and are subject to normal industry credit risks. As the Company extends unsecured credit to these entities, the collection of any receivables may be affected by changes in the economic environment or other conditions. Management believes the risk is mitigated by the financial position of the entities, and the Company's practice of requesting cash call advances for funds estimated to be incurred.

**PAINTED PONY PETROLEUM LTD.
CORPORATE INFORMATION**

DIRECTORS

Ronald R. Talbot
Glenn R. Carley
Kevin Angus
Allan K. Ashton
Craig Reed
Patrick R. Ward

OFFICERS

Patrick R. Ward	President & Chief Executive Officer
Joan E. Dunne	Vice President, Finance & Chief Financial Officer
James S. Thomson	Vice President, Land
James H. French	Vice President, Engineering
Donald J. Slater	Vice President, Geophysics
Doug McCartney	Corporate Secretary

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STOCK EXCHANGE

TSX Venture Exchange
Trading Symbols:
A Shares: PPY.A
B Shares: PPY.B