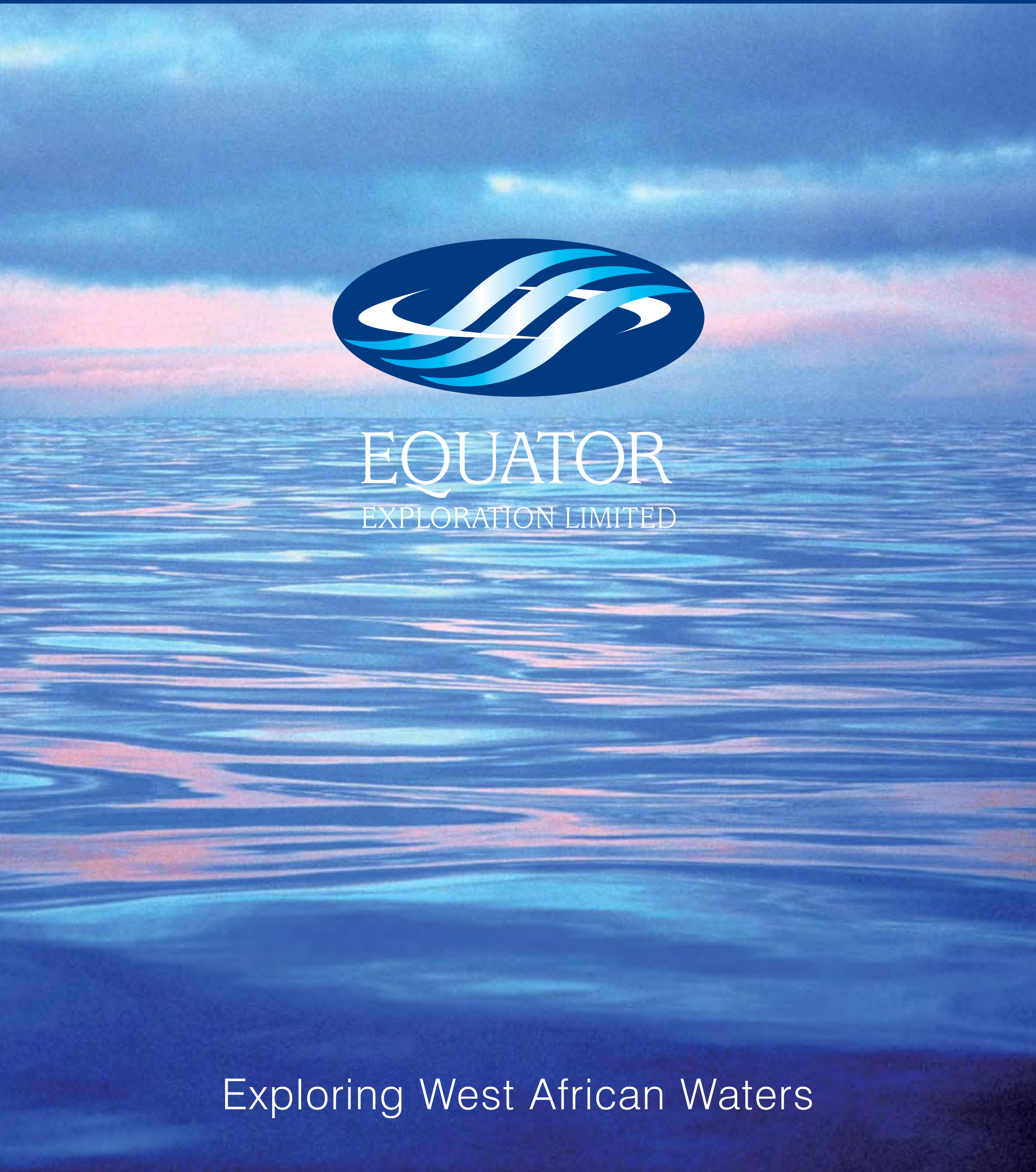
ANNUAL REPORT AND
FINANCIAL STATEMENTS 2005



EQUATOR
EXPLORATION LIMITED

Exploring West African Waters

Equator Exploration is an independent oil and gas exploration and production company founded in December 2000 and was listed on the Alternative Investment Market of the London Stock Exchange in December 2004. Equator's objective is to build a diversified portfolio of exploration, appraisal and production assets in the highly prospective Gulf of Guinea region. The Company also generates revenue from the acquisition, marketing and sale of seismic data.

Contents

BUSINESS HIGHLIGHTS

"EQUATOR HAS BUILT A PORTFOLIO OF DIVERSE OIL & GAS ASSETS IN ONE OF THE MOST PROLIFIC HYDROCARBON REGIONS OF THE WORLD. WE SHALL CONTINUE TO BUILD SHAREHOLDER VALUE THROUGH AN AGGRESSIVE 2006 DRILLING PROGRAM AND PRODUCTION PLANNED IN Q3 2007."

Wade Cherwayko, Chief Executive

Highlights during 2005

- Appointments of Sir Sam Jonah as Executive Chairman, Philip Dimmock as Chief Operating Officer, Baroness Chalker of Wallasey as Non-executive Director and Jean-Luc Vermeulen as an advisor to the Board
- Signing of an agreement with Peak Petroleum Nigeria Limited "Peak" for rights to certain areas of OML 122 license offshore Nigeria "OML 122"
- Successful drilling of B-D1X well in OML 122 with Peak confirming commercial oil and gas discovery
- Purchased significant 3D seismic database offshore Nigeria

Highlights post 2005

- Commercial Discovery of 130 million barrels of oil in place and 900 bscf of gas in place (tested at flow rate of over 7,000 bopd and 26 mm scfpd)
- US$250 million institutional placing
- 30% interest in blocks OPL 323 and OPL 321, offshore Nigeria, awarded to consortium of Equator (30%), the Korean National Oil Corporation (60% and operator) and Nigerian companies (10%)
- 15% interest in Block 2 of the Joint Development Zone ("JDZ") awarded to a consortium comprising Equator and ONGC Videsh awarded by Nigeria-São Tomé and Príncipe Joint Development Authority ("JDA"). Equator net 6% interest subsequently increased to 9%
- Gas discovery on Owanare AX1 well, Equator and Peak Petroleum's second well in the OML 122 license area, offshore Nigeria.

CHAIRMAN AND CHIEF EXECUTIVE'S STATEMENT

PRINCIPAL ACTIVITY AND REVIEW OF THE BUSINESS

Equator Exploration Limited is a company incorporated in the British Virgin Islands.

Equator Exploration Limited engages in the exploration and development of oil and gas projects in the prospective waters of West Africa. The company's objective is to build a diversified portfolio of exploration, appraisal and production assets in this region.

2005 was a year of rapid growth for Equator. We undertook several initiatives to increase our interests in our geographical area of focus, namely the Gulf of Guinea.

In November 2005, Equator commenced drilling its first well on OML 122 offshore Nigeria with Peak Petroleum Industries Nigeria Ltd. In February 2006 the companies confirmed the discovery of a major gas reservoir and approximately 130 million barrels of oil in place as a result of its first appraisal well. Together with our partner we are now aggressively pursuing an oil development project using floating production, storage and offtake technology with production planned to begin in Q3 2007. Equator and its partner are planning a further two to three wells during 2006 in this block in order both to prove additional reserves and for further field development.

Equator also continues to pursue exploration opportunities in the region.

During 2005, Sir Sam Jonah became Executive Chairman and Equator made two new appointments to the Board of Directors. Baroness Chalker of Wallasey was appointed as a non-executive director on 9th June 2005 and Philip Dimmock was appointed Director and Chief Operating Officer on 11th August 2005. In addition Jean-Luc Vermeulen was appointed as an advisor to the Board in a non-executive capacity on 18th September 2005 and Philip Rand was appointed Vice President Finance on 27th October 2005. These appointments considerably strengthen the Board of Directors and the company's management thereby providing Equator with the necessary skills to guide the company forward.

As at 31 December 2005 there were 131,417,190 Ordinary Shares issued and at 31st March 2006 there were 174,951,926 Ordinary Shares in issue.

As at 31 December 2005 there were 11,269,000 outstanding share options and 11,395,000 outstanding warrants all of which are exchangeable into Ordinary Shares at prices ranging from US$1.00 per share to £2.068 per share.

RESULTS AND DIVIDEND

The Group made a loss of US$3.85 million in the year, an increase of US$2.07 million over the 2004 loss of US$1.78million. However the operational activities of the group increased significantly during the year with the founding of offices in Lagos and Port Harcourt together with a large amount of groundwork to set up the opportunities realized in 2005 and early 2006.

Samuel E. Jonah KBE
Executive Chairman

Wade Cherwayko
Chief Executive Officer

2005 WAS A YEAR OF CONSOLIDATION FOR EQUATOR. WE UNDERTOOK SEVERAL INITIATIVES TO INCREASE OUR INTERESTS IN OUR GEOGRAPHICAL AREA OF FOCUS, NAMELY THE GULF OF GUINEA. AS IS THE CASE IN THIS AREA THE NEGOTIATION OF INTEREST TAKES TIME AND IT WAS ONLY TOWARDS THE END OF 2005 THAT THE WORK PUT IN BY THE COMPANY BEGAN TO COME TO FRUITION.

The Group's Balance Sheet was further strengthened, following the listing on London's Alternative Investment Market in 2004. In December 2005, the company raised US$60million at a share price of £2.068 per share and in February 2006 completed an additional US$250million at £3.50 per share. Both of these capital raising exercises were completed by private placement subscribed by institutional investors.

The company has not paid a dividend during the year (2004: $Nil).

FUTURE PROSPECTS

West Africa is one of the most prolific offshore deepwater exploration and production regions. Discoveries in the region include the Akpo field (Nigeria) with estimated reserves of 800 million barrels, the Agbami field (Nigeria) with estimated reserves of 1 billion barrels, and the Zafiro field (Equatorial Guinea) with estimated reserves of 1 billion barrels. Despite the exploration successes to date, the bulk of the deepwater acreage is still virgin territory.

POST CLOSURE EVENTS

In March 2006 the Production Sharing Agreements for two exploration blocks in Nigerian waters and one block in the joint São Tomé/Nigerian waters were signed.

1. Blocks 321 and 323, where Equator has a 30% working interest in each, are in Nigerian waters and are operated by The Korean National Oil Company.
2. Block 2 in the Joint Development Zone, where Equator has a 9% working interest is operated by Sinopec.

The award of these licenses was the culmination of a significant amount of hard work and places Equator as a mainstream oil and gas explorer in the region. All three blocks are prospective with large hydrocarbon-bearing source rock identified. Drilling will take place over the next 24 months to confirm the presence of hydrocarbons.

The directors wish to acknowledge the commitment and determination of our staff in building shareholder value.

Also, the directors wish to recognize the support of stakeholders, suppliers and business partners, without whose support the satisfactory progress made in the year to 31 December 2005 may not have been possible.

Dr S E Jonah, KBE
Director – Executive Chairman

Mr Wade G Cherwayko,
Director – President – CEO

REVIEW
OF OPERATIONS

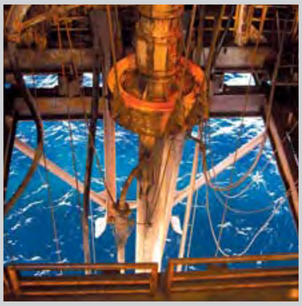
OVERVIEW

Equator Exploration Limited engages in oil and gas exploration and development projects in the highly prospective waters of the Gulf of Guinea, West Africa. The Company's objective is to build a diversified portfolio of exploration, appraisal and production assets in the region.

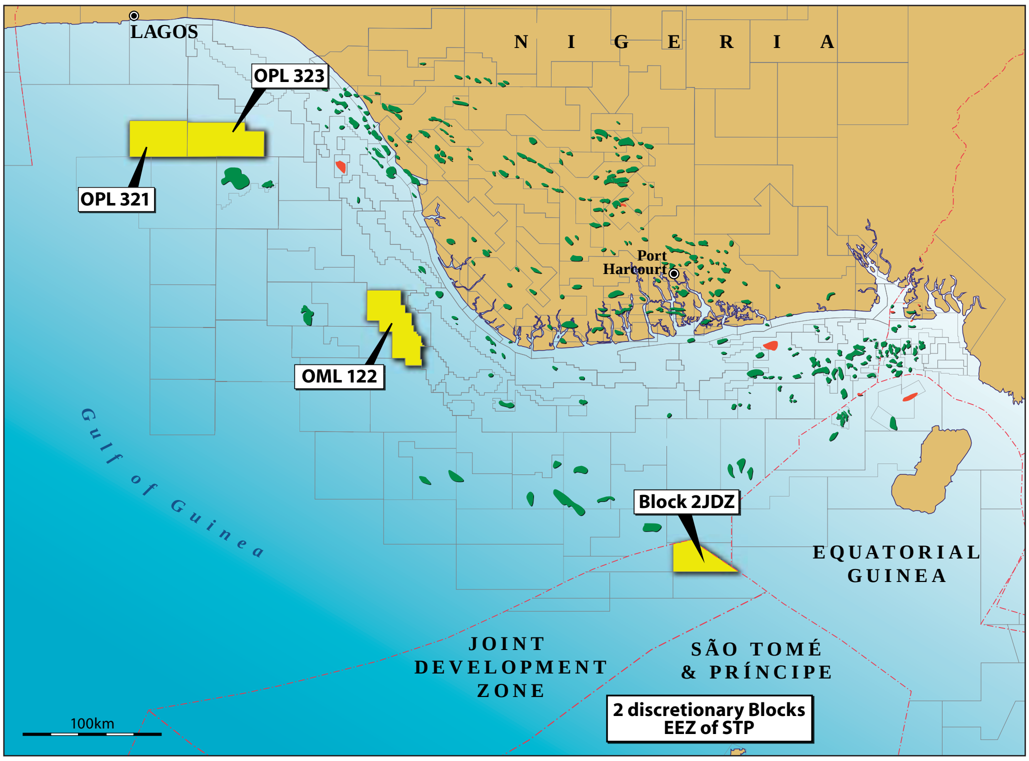
Offshore Nigeria, the Company has acquired interests in blocks OML 122, OPL 323 and OPL 321. In the Joint Development Zone between Nigeria and São Tomé & Príncipe, it has acquired an interest in Block 2. Equator also owns rights to two blocks of its choice in the Exclusive Economic Zone of São Tomé and Príncipe, along with the rights to seismic data it acquired in the region and Equator continues to evaluate other exploration opportunities. In OML 122, Equator recently drilled two wells resulting in commercial discoveries of hydrocarbons.

BULFORD DOLPHIN SEMI-SUBMERSIBLE DRILLING RIG LEASED TO PEAK AND EQUATOR, CURRENTLY DRILLING ON OML 122 OFFSHORE SHALLOW WATER, NIGERIA.

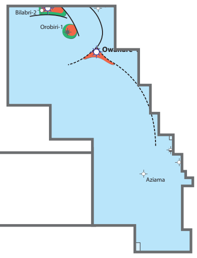
SEISMIC VESSEL



EQUATOR EXPLORATION LIMITED ENGAGES IN THE EXPLORATION AND DEVELOPMENT OF OIL AND GAS PROJECTS IN THE HIGHLY PROSPECTIVE GULF OF GUINEA WATERS IN WEST AFRICA. THE COMPANY'S OBJECTIVE IS TO BUILD A DIVERSIFIED PORTFOLIO OF EXPLORATION, APPRAISAL AND PRODUCTION ASSETS IN THE REGION.



MAP OF EQUATOR'S INTERESTS IN THE GULF OF GUINEA



NIGERIA – OML 122

OML 122 is located 25 to 60 km offshore in water depths of 40 to 300 metres. It covers an area of 1,295 square km on the Western Niger Delta, east of Shell's giant Bonga Field (estimated 1.4 billion barrels) on OML 118 and southwest of Shell's EA Field on OML 79.

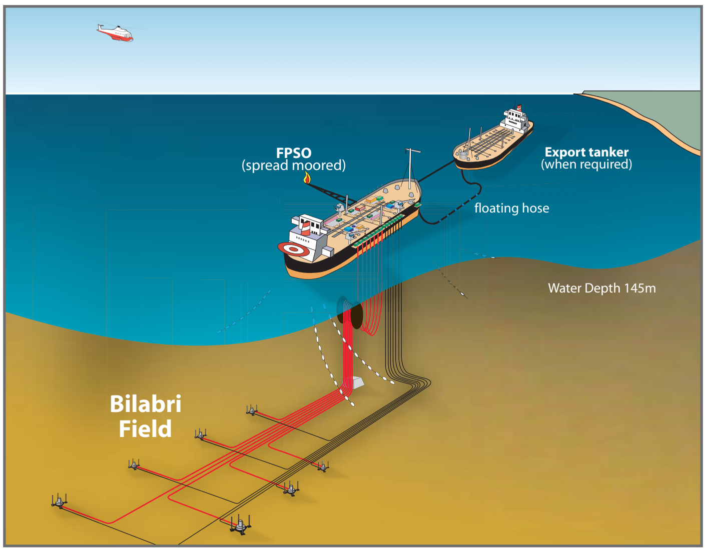
In April 2005, Equator signed a Finance and Service Agreement with Peak Petroleum Industries Nigeria Limited (Peak), the operator of OML 122. In return for funding and supplying technical services for an appraisal well on each of two discoveries and for an exploration well on a selected prospect, Equator is entitled to a share of the revenues from the oil and gas production from subsequent developments.

The Company's objective in the OML 122 area is to prove significant volumes of gas to supply the numerous gas utilisation projects currently being developed or planned in close proximity to the licence area. In addition, the near term objective is the development of the oil reservoir discovered in the Bilabri field.

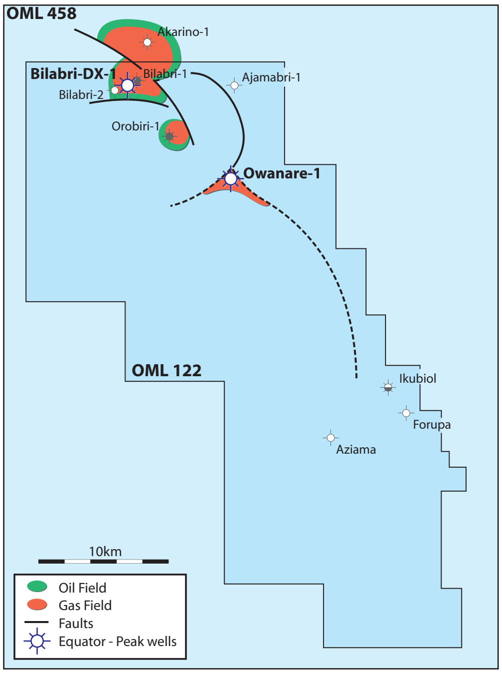
In September 2005, Equator and Peak signed a contract for the "Bulford Dolphin" semi-submersible drilling rig and, in November 2005, commenced drilling their first well, Bilabri DX1, on a discovery made in the 1970's. The extent of the existing hydrocarbon reservoirs exceeded expectations and, furthermore, the well discovered additional reservoirs. On test, the oil reservoir flowed crude oil with a specific gravity of 40 degrees API at a rate of 7188 barrels per day and the main gas sand flowed at a rate of 26 million standard cubic feet per day. The flow testing combined with well logs confirmed that reservoir properties and crude oil quality are excellent. The independent technical advisers to Equator, Horizon Energy Partners BV (Horizon), quote the Proven and Probable reserves of the oil reservoir as 45 million barrels and the aggregate Proven and Probable reserves of the gas reservoirs as 734 billion standard cubic feet, both at the Best Estimate level.

Equator and Peak are pursuing the immediate development of the oil reservoir with a scheme based on 6-7 sub-sea horizontal wells and a floating production, storage and offloading system (FPSO). Orders for long-lead time equipment have been placed and a letter of intent has been signed with Bergesen Worldwide Offshore AS for the FPSO, "BW Endeavour". Subject to further engineering, reservoir evaluation and drilling, it is anticipated that oil production could commence in the third quarter of 2007. The development of the gas reserves in Bilabri is under evaluation and markets are being aggressively sought.

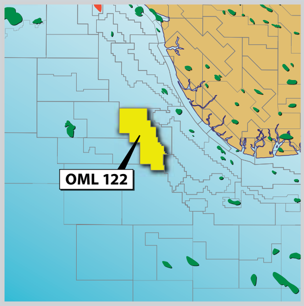
In March 2005, a second well, Owanare 1, commenced the exploration of the Owanare prospect and discovered gas in two zones with a total thickness of 61 metres (200ft). Horizon estimates the gas-in-place to be 185 bcf, an amount considered to be capable of commercial production as a satellite to a gas development on the Bilabri field.

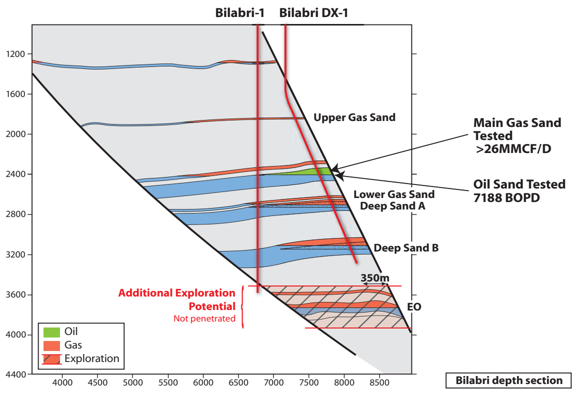


PLANNED OIL DEVELOPMENT

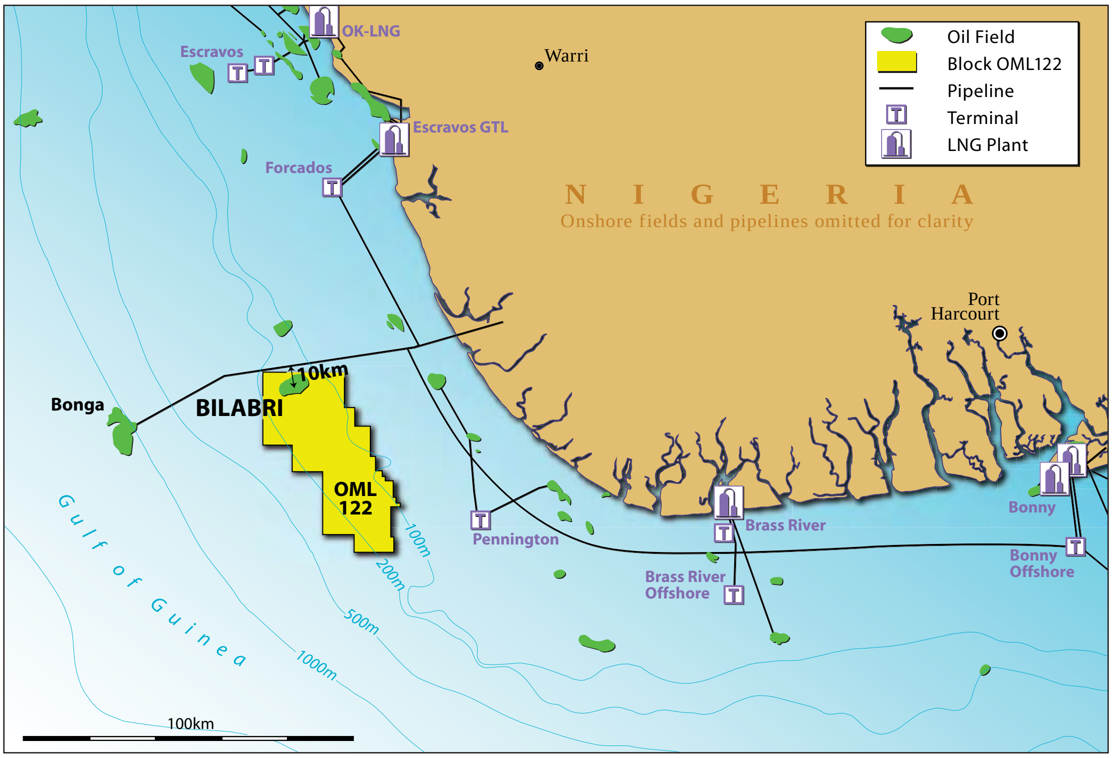


OML 122

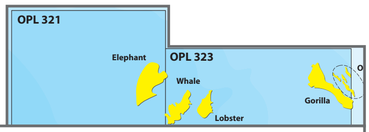




OML 122 IS LOCATED 25 TO 60 KM OFFSHORE IN WATER DEPTHS OF 40 TO 300 M AND COVERS AN AREA OF 1,295 SQUARE KM ON THE WESTERN NIGER DELTA, EAST OF SHELL'S GIANT BONGA FIELD (ESTIMATED 1.4 BILLION BARRELS) ON OML 118 AND SOUTHWEST OF SHELL'S EA FIELD ON OML 79.



LOCATION OF OML 122



NIGERIA – OPL 323 AND OPL 321

The deepwater offshore northwest Nigeria contains one of the most prolific hydrocarbon exploration plays in the world, estimated to contain more than five billion barrels oil equivalent of proven plus probable reserves. During 2005 and 2006, exploration and development activity in this area has been increasing significantly.

In March 2006, Equator was awarded a 30% interest in the Production Sharing Contracts for two of the most prospective and exciting deepwater blocks in West Africa today – OPL 323 and OPL 321. The Korean National Oil Corporation was awarded a 60% interest in both blocks and is operator of both joint ventures. The remaining 10% interests are held by local Nigerian companies.

OPL 323

OPL 323 is located 80 km offshore in water depths of 1300 to 2000 metres. Technical work is advanced on the four key prospects in OPL 323: Whale, Lobster, Gorilla and Octopus, each of which have an exploration potential equal to or exceeding that of the adjacent fields. They have aggregate Prospective Resources, estimated by Horizon, of 4.8 billion barrels at the Best Estimate Level. Equator and the Operator are actively working on the selection of our first well and securing an appropriate drilling rig.

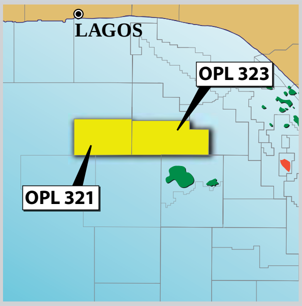
Immediately south of OPL 323, Exxon-Mobil have started production from the Erha field at a rate of 150,000 bopd. The Erha North Extension will add another 50,000 bopd. One of the prospects on OPL 323, Gorilla, is less than 10 kilometres from these fields and exhibits many of the same geologic and geophysical characteristics. In the block adjacent to the eastern boundary of OPL 323, Agip have increased the production of Abo field to more than 35,000 bopd and are extending their exploration activities to both the northeast and south of OPL 323.

OPL 321

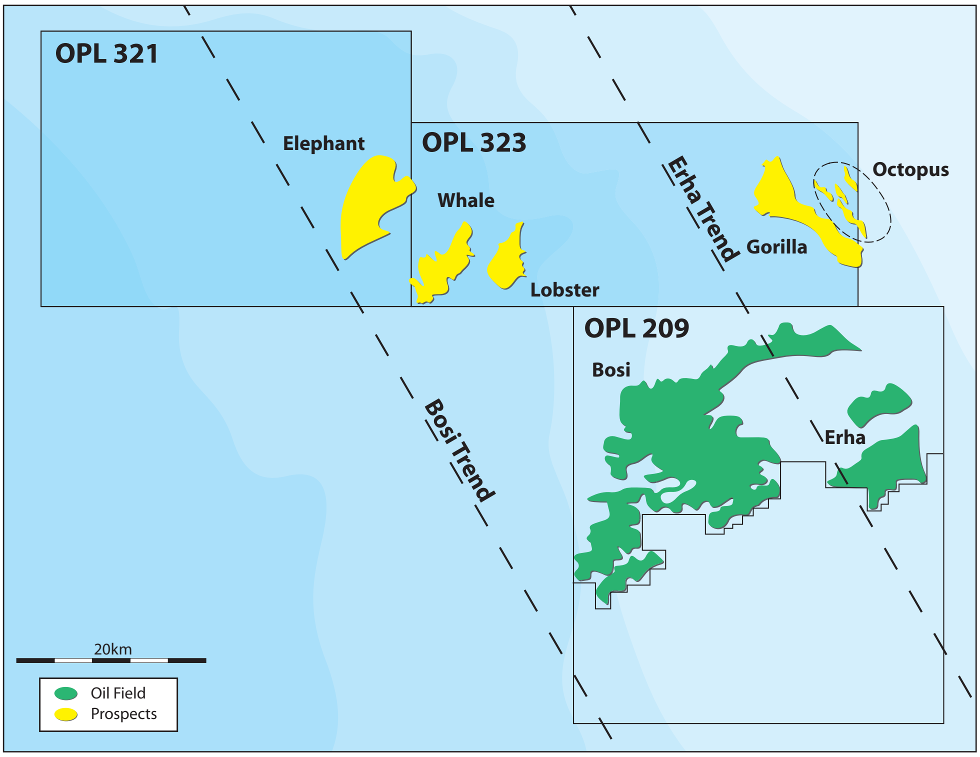
OPL 321 is next to and west of OPL 323 in deeper water. It is surrounded by exploration activity and discoveries. Initial assessment of the prospectivity of the block has identified the very large Elephant prospect with Prospective Resources estimated by Horizon to be 2.8 billion barrels at the Best Estimate Level. Additional exploration potential exists in other leads, including Cobra, and more prospects are anticipated.

Adjacent to OPL 321, the continued growth in reserves of the Giant Bosi Field may make it one of the largest fields in deepwater Nigeria. Exxon-Mobil have requested tenders for an FPSO capable of handling more than 120,000 bopd. Qualitative calibrations from 2D seismic of the geophysical response of interpreted hydrocarbon zones on the Bosi Field are identical to the objectives of Elephant Prospect.

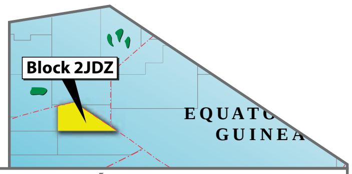
To the south along the geologic trend that crosses Elephant prospect, there have been two major discoveries, Shell's Bobo oil discovery, with reported 200 metre net oil sand, and Petrobras's Erinmi gas condensate discovery. On the northern side of OPL 321, Petrobras is starting exploration activity while BG is acquiring a 3D seismic survey.



OPL 323 IS LOCATED 80 KM OFFSHORE IN WATER DEPTHS OF 1,300 TO 2,000 M. THE LARGE ABO FIELD IN OML 125 OPERATED BY AGIP IS LOCATED TO THE EAST AND EXXONMOBIL'S BOSI AND EHRA DISCOVERIES IN OPL 209 ARE LOCATED TO THE IMMEDIATE SOUTH OF THE BLOCK.



PROSPECTS ON OPL 323 AND OPL 321



JDZ AND EEZ OF SÃO TOMÉ & PRÍNCIPE

JOINT DEVELOPMENT ZONE

In 2001, the governments of Nigeria and São Tomé and Príncipe signed a treaty that established the Joint Development Zone (JDZ) to govern previously disputed territorial waters. The rest of the territorial waters of São Tomé and Príncipe are known as the Exclusive Economic Zone (EEZ).

JDZ BLOCK 2

In March 2006, a consortium of Equator and ONGC Videsh Limited (OVL), the international arm of the Oil and Natural Gas Corporation of India, secured a 15% interest in the highly sought after Block 2. Subsequently, the consortium acquired 7.5% of the 10% held by Nigerian firm, A & Hatman Ltd. Under the terms of the joint bidding agreement between OVL and Equator, allocations in the JDZ are shared on a 60:40 basis; thereby, giving Equator a 9% interest in the block.

Of the remaining interest, 65% is held by a consortium of Sinopec (operator), ERHC Energy and Addax Petroleum. The Nigerian firms, Amber Petroleum and Foby Engineering hold 5% each. Some 15 prospects and leads have been identified in the block, four of which are very significant. Equator and its partners are enhancing the technical assessment integrating the recently licensed 3D seismic with the extensive 2D coverage. This work will enable the partnership to select which of the four top prospects to drill first. The partners are actively searching for a deepwater drilling rig.

Block 2 is adjacent to Nigerian Block OML 130 which hosts Akpo field, with reserves of 800 million barrels and 4 tcf, and a series of further discoveries with reserves totalling additional 500 million barrels and several tcf of gas. In 2006, CNOOC purchased a 45% working interest in OML 130 for US$ 2.68 billion.

The Obo 1 discovery in the adjacent JDZ Block 1 has proven the existence of a working hydrocarbon kitchen and excellent reservoir sands in the region of Block 2, confirming its good prospectivity.

EXCLUSIVE ECONOMIC ZONE

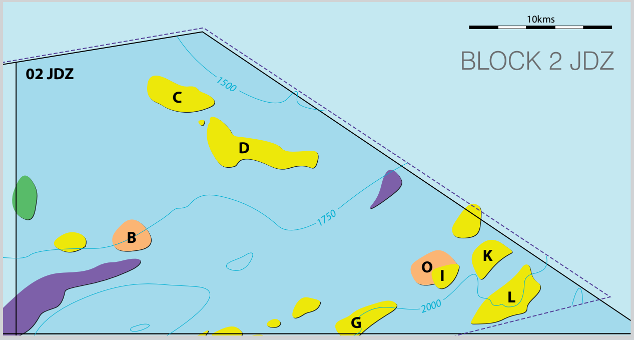
São Tomé and Príncipe's offshore territorial boundaries encompass an area of approximately 160,000 square kilometres. The close proximity of São Tomé and Príncipe's offshore waters to the proven hydrocarbon systems in the adjacent waters of Nigeria, Cameroon, Equatorial Guinea and Gabon suggests the potential for hydrocarbons. In addition, seismic data for the region also indicates widespread prospectivity in the waters of São Tomé and Príncipe.

It is anticipated that the government will publish block outlines by the end of 2006. Equator has the right to acquire a 100% interest in two blocks of its choice in the EEZ. In addition, the Company has an option to take up to a 15% share in any eventual participation by the government in any other block.

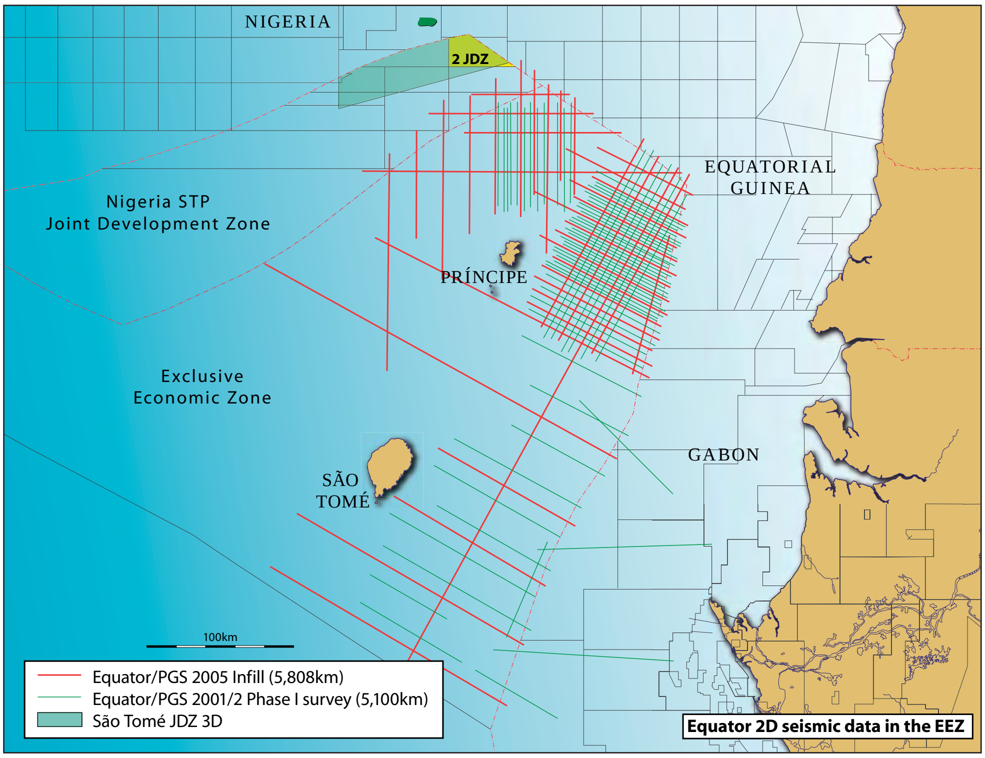
Equator has funded the acquisition of ten thousand kilometres of 2D seismic data and interpreted more than twenty thousand across this frontier acreage. The Company's regional and prospect work was initially carried out through PGS Reservoir and is nearing completion. The recent industry successes in Nigeria, Cameroon and Equatorial Guinea have increased the prospectivity of this frontier acreage.

The growing evidence of an Upper Cretaceous source charging both Upper Cretaceous as well as Tertiary reservoirs through the major fracture zones has significantly elevated the prospectivity of this acreage. The seismic evidence of well defined basin floor sandstones, together with these fractures has set up a potential world class play. Four play types have been identified with the presence of a number of leads and prospects.

Equator plans to select its two option blocks and commence negotiations on production sharing contracts with the Government for each block in the near-term.



SÃO TOMÉ AND PRÍNCIPE'S OFFSHORE TERRITORIAL BOUNDARIES ENCOMPASS AN AREA OF APPROXIMATELY 160,000 KM2. THE CLOSE PROXIMITY OF SÃO TOMÉ AND PRÍNCIPE'S OFFSHORE WATERS TO THE PROVEN HYDROCARBON SYSTEMS IN THE ADJACENT WATERS OF NIGERIA, CAMEROON, EQUATORIAL GUINEA AND GABON SUGGESTS THE POTENTIAL FOR HYDROCARBONS.



SEISMIC ACQUIRED BY EQUATOR AND PGS OFFSHORE SÃO TOMÉ AND PRÍNCIPE

Samuel E. Jonah KBE
Executive Chairman

Wade Cherwayko
Chief Executive Officer

Philip Dimmock
Chief Operating Officer

James Ladner
Non-executive Director

Alexander L. Dembitz
Non-executive Director

The Rt. Hon. The Baroness Chalker of Wallasey
Non-executive Director

BOARD OF DIRECTORS

Samuel E. Jonah KBE, Executive Chairman

Samuel Jonah is non-executive president of AngloGold Ashanti Limited, a NYSE-listed company which is one of the world's largest gold companies and the largest African-based gold producer. He is also a director on a number of public and private company boards including Anglo American Corporation of South Africa, Anglo American Platinum Corporation Ltd. (Amplats), Transnet Ltd., Titanium Resources Group Ltd. and Standard Bank Group. He is also an advisor to three African Presidents – President Kufuor of Ghana, President Obasanjo of Nigeria and President Mbeki of South Africa.

Wade Cherwayko, Chief Executive Officer

Over the last fourteen years, Mr. Cherwayko has been active in negotiating, developing and financing a number of projects in West and North Africa. Such projects have included the acquisition, financing, exploration and development of several onshore and offshore oil and gas assets for Mart Resources Inc., Abacan Resource Corporation, Centurion Energy International Inc. and Yinka Folawiyo Petroleum Company Ltd. He is also a director of Mart Resources Inc.

Philip Dimmock, Chief Operating Officer

Prior to joining Equator, Mr. Dimmock served as general manager of operations of Houston-based Vanco where he oversaw the company's exploration activities in Africa, including the drilling of deepwater wells in Equatorial Guinea, Morocco and Cote d'Ivoire. Prior thereto, he was Vice President International for Ranger Oil, directing business development and operations in the United Kingdom and a number of West African countries. Mr. Dimmock began his career at British Petroleum where he spent 26 years and held a number of senior positions. He also serves as a non-executive director of Nautical Petroleum PLC.

James Ladner, Non-executive Director

Mr. Ladner is a financial consultant and investment banker in Zurich. He also serves as director of a number of banks and companies, including F. van Lanschot Bankiers (Switzerland) Ltd., Alpine Atlantic Asset Management AG, Colombia Gold AG, Pan Pacific Aggregates plc and StrataGold Corporation. Previously he acted as an executive vice president of Coutts Bank (Switzerland), Chairman of Bank Austria (Switzerland) and as a founding executive director of RP&C International.

Alexander L. Dembitz, Non-executive Director

Mr. Dembitz has over thirty years of experience in international banking, investment management and consulting. He is Chairman, Everest Capital S.A., Geneva, an advisory firm that provides consulting services to Everest Capital Limited, a global investment advisory firm managing over $2 billion in a family of funds. Formerly, Mr. Dembitz was Chairman, Deloitte & Touche Central Europe and founder /Chairman, IDOM Group, the largest management consulting firm in information technology/banking in East and Central Europe.

The Rt. Hon. The Baroness Chalker of Wallasey, Non-executive Director

Baroness Chalker is an independent advisor on Africa and business development to companies and institutions in Britain and sub-Saharan Africa through her own commercial company, Africa Matters Ltd. She is also coordinator of the President of Nigeria's International Investment Council and a member of the Presidential Economic/ Investment Advisory bodies for Kenya, Uganda and Tanzania. She is a non-executive director of Unilever plc & NV, Group 5 (Pty) Ltd. and Freeplay Energy Holdings, and a member of the International Advisory Boards of Lafarge et Cie and of MerchantBridge Investments.

John Munson
Country Manager – Nigeria

Philip Rand
Vice President, Finance

Miss Stacey Kivel
Vice President,
Business Development,
Legal Affairs & Company Secretary

Dr Ken Seymour
Country Asset Manager – Nigeria

SENIOR MANAGEMENT

John Munson, Country Manager – Nigeria

Mr. Munson has been involved in West African drilling operations and executive management for more than twenty years, with the most recent ten years primarily in Nigeria. With degrees in petroleum engineering and law, he has served as drilling supervisor, operations manager, consultant or executive for several independent Nigerian and foreign oil companies, as well as for larger companies including Amoco, Conoco and Global Marine. He has overseen more than twenty exploration, drilling or development projects for seven different oil companies during his tenure in Nigeria.

Philip Rand, Vice President, Finance

Mr. Rand has over thirty years of financial experience of which seventeen have been in the upstream energy sector. Prior to joining Equator, he was chief financial officer of Burren Energy, group treasurer of Monument Oil & Gas and held senior financial roles at Deminex and Louisiana Land & Exploration. Mr. Rand was also finance director of Utilyx and group treasurer of both Sema Group and CMG. Mr. Rand is a Fellow of the Association of Corporate Treasurers.

Miss Stacey Kivel, Vice President, Business Development, Legal Affairs & Company Secretary

Prior to joining Equator, Miss. Kivel represented major US and European corporations regarding legal and business development in more than thirty African countries; working at presidential or ministerial levels. Her experience included heading the Africa / Middle East Government Relations and Business Development Division of Institutional Investor Inc. Prior to her involvement in Africa, Miss. Kivel was in-house legal council and head of acquisitions consecutively for Cinequanon International and Image Organization in Los Angeles, specializing in negotiating international licensing and finance agreements. She is a California qualified attorney at law.

Dr Ken Seymour, Country Asset Manager – Nigeria

Ken Seymour commenced his career with BP in the late 1970's as a Drilling Engineer and worked in the North Sea and China. In 1982 he joined Danbury Drilling, a consulting engineering company, and worked on the slant rig design for Morecambe Bay. In 1984 he joined Ranger Oil as a Senior Drilling Engineer and worked with them as Drilling Engineer, Drilling Superintendent, Drilling Manager, General Manager and Director. He was the Director of Business Development when Ranger was sold to Canadian Natural Resources and was an executive board member of the six man management committee that transformed CNR International's management system and portfolio. He left CNR in 2003 to work as an independent consultant and has just completed an assignment for Roc Oil as their General Manager in Angola. He joined Equator in June 2006 as Country Asset Manager in Nigeria.

OFFICERS AND PROFESSIONAL ADVISERS

Directors
Mr S E Jonah, KBE – Executive Chairman
Baroness Chalker of Wallasey (appointed 9 June 2005)
Mr W G Cherwayko
Mr A L Dembitz
Mr P Dimmock (appointed 11 August 2005)
Mr J Ladner

Correspondence Office, London
Equator Exploration Limited
Third Floor
192 Sloane Street
London SW1X 9QX
United Kingdom
Phone: +44 (0) 20 7235 2555
Fax: +44 (0) 20 7235 2224

Nigeria Office
Equator Exploration Nigeria Limited
7, Anifowoshe Street
Victoria Island
Lagos, Nigeria
Phone: +234 (1) 271 1751
Fax: +234 (1) 271 1752

Nominated Adviser & Broker
Nabarro Wells & Co. Limited
Saddlers House
Gutter Lane
London EC2V 6HS
United Kingdom

Accountants
Chantrey Vellacott DFK
Russell Square House
London WC1B 5LF
United Kingdom

UK Solicitors
Pinsent Masons
Dashwood House
69 Old Broad Street
London EC2M 1NR
United Kingdom

Nigeria Solicitors
Adepetun, Caxton–Martins, Agbor & Segun
9th Floor, St. Nicholas House
Catholic Mission Street
Lagos
Nigeria

Registered Office
Equator Exploration Limited
Craigmuir Chambers
PO Box 71
Road Town
Tortola
British Virgin Islands

Registered Agent
HWR Services Limited
Craigmuir Chambers
PO Box 71
Road Town
Tortola
British Virgin Islands

Registrars
Computershare Investor Services
(Channel Islands) Limited
PO Box 83
Ordnance House
31 Pier Road
St Helier
Jersey JE4 8PW
Channel Islands

Financial Public Relations Consultants
Buchanan Communications Ltd
107 Cheapside
London EC2V 6DN
United Kingdom

Share Listing
London Stock Exchange (AIM)
Symbol: EEL

DIRECTORS' REPORT

The directors submit their report and the audited financial statements of the Group for the year ended 31December 2005. The directors' report has been prepared using the provisions in the UK Companies Act 1985 for a limited company.

Principal activity and review of the business

Equator Exploration Limited is a company incorporated in the British Virgin Islands. The address of the registered office is given on page 14.

Equator Exploration Limited engages in the exploration and development of oil and gas projects in the prospective waters in West Africa. The company's objective is to build a diversified portfolio of exploration, appraisal and production assets in this region.

2005 was a year of consolidation for Equator. We undertook several initiatives to increase our interests in our geographical area of focus, namely the Gulf of Guinea.

In November 2005, Equator commenced drilling its first well on OML 122 offshore Nigeria with Peak Petroleum Industries Nigeria Ltd. Equator is paying 100% of the costs in return for a 40% economic interest. In February 2006 the company confirmed the discovery of a major gas reservoir and approximately 130 million barrels of oil in place as a result of its first appraisal well. Together with our partner we are now planning a fast track development project using floating production, storage and off take technology to begin production in 2007. Equator and its partner are planning a further 4 wells during 2006 in this block in order both to prove additional reserves and for further field development.

As at 31st December 2005 there were 131,417,190 Ordinary Shares issued and at 31st March 2006 there were 174,951,926 Ordinary Shares in issue.

As at 31st December 2005 there were 11,269,000 outstanding share options and 11,395,000 outstanding warrants all of which are exchangeable into Ordinary Shares at prices ranging from US$1.00 per share to £2.068 per share.

Equator also continues to pursue exploration opportunities in the region.

Results and dividend

The group made a loss of US$3.71 million in the year, an increase of US$1.93 million over the 2004 loss of US$1.78million. However the operational activities of the group increased significantly during the year with the founding of offices in Lagos and Port Harcourt together with a large amount of groundwork to set up the opportunities realized in 2005 and early 2006.

The Group's Balance Sheet was further strengthened, following the listing on London's Alternative Investment Market in 2004. In December 2005, the company raised US$60 million at a share price of £2.068 per share and in February 2006 completed an additional US$250 million at £3.50 per share. Both of these capital raising exercises were completed in very short time by private placement subscribed by institutional investors.

The company has not paid a dividend during the year (2004: $Nil).

Future prospects

West Africa is one of the most prolific offshore deepwater exploration and production regions. Discoveries in the region include the Akpo field (Nigeria) with estimated reserves of 800 million barrels, the Agbami field (Nigeria) with estimated reserves of 710 million barrels, and the Zafiro field (Equatorial Guinea) with estimated reserves of 1 billion barrels. Despite the exploration successes to date, the bulk of the deepwater acreage is still virgin territory.

DIRECTORS' REPORT CONTINUED

Post closure events

In March 2006 the Production Sharing Agreements for two exploration blocks in Nigerian waters and one block in the joint São Tomé/Nigerian waters were signed.

1. Blocks 321 and 323, where Equator has a 30% working interest in each, are in Nigerian waters and are operated by The Korean National Oil Company.

2. Block 2 in the Joint Development Zone, where Equator has a 9% working interest is operated by Sinopec.

The award of these licenses was the culmination of a significant amount of hard work and places Equator as a mainstream oil and gas explorer in the region. All three blocks are prospective with large hydrocarbon-bearing source rock identified. Drilling will take place over the next 24 months to confirm the presence of hydrocarbons.

The directors wish to acknowledge the commitment and determination of staff to build shareholder value. Also, the directors wish to recognize the support of stakeholders, suppliers and business partners, without whose resolve the satisfactory progress made in the year to 31 December 2005 may not have been possible.

Directors and their interests

The names of the directors who held office during the year and after the year end are disclosed on page 1.

The following directors held the following interest in common shares for the year ended 31 December 2005:

Number of common shares	At 31 December 2005	At 31 December 2004
Mr W G Cherwayko	3,300,000	3,300,000
Dr S E Jonah, KBE*	426,472	426,472
Mr J Ladner	468,000	548,000

* 176,472 common shares are held in the name of Pictet and Cie.

Directors hold the following options to subscribe for common shares:

	Exercise price	Date of grant	Date of expiry	Number of shares
Baroness Chalker	£1.56	22 July 2005	21 July 2010	150,000
Mr W G Cherwayko	£1	23 November 2004	23 November 2014	1,600,000
Mr W G Cherwayko	£2.068	9 November 2005	8 November 2010	400,000
Mr A L Dembitz	£1	23 November 2004	23 November 2014	80,000
Mr A L Dembitz	£1.56	22 July 2005	21 July 2010	20,000
Mr P Dimmock	£1.56	22 July 2005	21 July 2010	325,000
Mr P Dimmock	£2.068	9 November 2005	8 November 2005	200,000
Dr S E Jonah, KBE	£1	23 November 2004	23 November 2014	400,000
Dr S E Jonah, KBE	£1.56	22 July 2005	21 July 2010	1,800,000
Mr J Ladner	$1.25	22 August 2003	21 August 2008	200,000
Mr J Ladner	£1 23	November 2004	23 November 2014	80,000
Mr J Ladner	£1.56	22July 2005	21 July 2010	20,000

Going concern

The Board, after making suitable enquiries, is satisfied that the Group has adequate resources to continue in operational existence for the foreseeable future. Accordingly, the Board continues to adopt the going concern basis in preparing the financial statements.

Substantial shareholders

The following had interest in 3% or more of the voting capital of the Company at 31 December 2005:

Holder	No. of shares	%
Morstan Nominees Ltd	48,006,148	36.30
Bear Stearns Securities Corp	9,281,326	7.02
Goldman Sachs Securities (Nominees) Ltd	7,756,696	5.87
Barclays Capital Nominees Ltd	7,401,081	5.60
The Bank of New York (Nominees) Ltd	4,766,303	3.60
HSBC Global Custody Nominee (UK) Ltd	4,493,444	3.40
Lehman Brothers International (Europe)	4,075,000	3.08

Auditors

A resolution for the re-appointment of Chantrey Vellacott DFK LLP as auditors of the Company is to be proposed at the forthcoming Annual General Meeting.

Dr S E Jonah, KBE
Director – Executive Chairman

Mr W G Cherwayko
Director – Chief Executive

CORPORATE GOVERNANCE STATEMENT

The Directors are committed to applying the requirements of the Combined Code applicable to listed Companies. As an AIM quoted company, the Company is fully complying with all the recommendations applicable to a company of its current size. The Company has a published Governance Handbook, which covers Board and general Corporate Governance and which can be viewed at any time at the Company's representative offices.

Board Structure

The Board is accountable to shareholders for the effective management of the Group. The Board consists of three Executive Directors and three Non–Executive Directors. The Board meets at least quarterly and as issues arise which need Board attention. The Board has a schedule of matters specifically referred to it for decision. These include issues around strategy and policy, risk management, structure and capital, financial reporting and controls and major capital projects, investments, acquisitions, divestments and contracts.

Operational decisions and the execution of business strategies are delegated to senior management through the vehicle of a recently formed Executive Committee (EXCOM) that is chaired by the Executive Chairman.

Biographies of the Board Directors will be found on page 12 of this annual report.

Board sub–committees

The Board has established the following sub–committees.

Audit Committee

This committee is intended to provide a link between the auditors and the Equator Exploration Board, independent of the Company's executives. It assists the Board in fulfilling its responsibilities in relation to financial reporting and control. This committee is chaired by non-executive director Alexander Dembitz and the other members are also non-executive directors, Baroness Chalker of Wallasey and James Ladner. The Committee meets at least twice a year.

Nomination and Governance Committee

This committee makes recommendations on good corporate governance matters to the Board. It is then accountable for evaluating the performance of the Company against these recommendations and for determining the independence of non-executive directors. It also leads the process for succession planning and appointments to the Board. This committee is chaired by Baroness Chalker of Wallasey. The other members are non-executive director Alexander Dembitz and Executive Chairman, Sir Sam Jonah. The Committee meets at least twice a year.

Compensation Committee

This committee makes recommendations on executive remuneration, benefits and bonuses to the Board. This committee is chaired by non-executive director James Ladner. The other members are non-executive director Baroness Chalker of Wallasey, non-executive director Alexander Dembitz and Executive Chairman, Sir Sam Jonah. The Committee meets at least quarterly.

Internal Controls

The Board has responsibility for establishing and maintaining the Group's system of internal controls and reviewing its effectiveness. The procedures which include inter alia financial, operational and compliance matters and risk management are reviewed on an on-going basis by the relevant Board sub-committee and as part of the Schedule of Matters Reserved for the meetings of the full board.

The internal control system can only provide reasonable and not absolute assurance against material misstatement or loss. The Board has considered the need for an internal audit function but does not consider it necessary at the current time.

Relations with shareholders

The Board is fully committed to maintaining regular and effective communications with shareholders. In addition to the Annual General Meeting there is regular dialogue and meetings with the larger shareholders and enquiries are received and are welcomed from all shareholders. Also, industry and geography reports which directly impact investment decisions are regularly sent to shareholders including the monthly West Africa E & P Update which the Company compiles and publishes. The Company's website www.equatorexploration.com is also regularly updated with Press Releases and statements and shareholders are invited to visit and comment on this website.

Directors Service Agreements

No Directors have any service or consultancy agreements with a notice period in excess of one year.

CORPORATE AND SOCIAL RESPONSIBILITY STATEMENT

The Group is an ethical company, working in compliance with laws and regulations wherever we operate. This statement summarises the policies and standards that are in place to guide the appropriate ethical and professional behaviour for all employees, Directors and contractors to the Group.

Ethics
The Company requires that all employees and Directors should always act with the highest standards of honesty, integrity and fairness in all their business dealings with others, wherever they may be operating. We are committed to transparency in all our dealings.

Conflicts of Interest
The Nomination and Governance Committee of the Board monitors to ensure that all employees and Directors avoid conflicts of interest between their private financial and personal activities and their role in the conduct of Company business.

Health, Safety and the Environment
The Group places a high degree of importance on health, safety and the environment and the wellbeing of all those connected to it and its activities. Specific policies are supported by the HSE Management System Framework that documents the responsibilities and activities of every employee in the Company with respect to HSE.

Communities
The Group places a high value on the support and endorsement of its activities by the communities in which it operates. We add additional value to those communities where we can for example in providing training and medical supplies to local communities in Nigeria and São Tomé.

Employees
The Group is committed to creating a work environment of mutual trust where every employee is treated with dignity and respect. Our policy is to recruit, select, develop and promote employees on merit, irrespective of race, colour, gender, religion, age, national origin, sexual orientation, marital status or disability.

Public and Political Activities
The Group neither supports political parties nor contributes to the funds of groups whose activities are calculated to promote partisan party interests. Therefore no political donations for the financial year 2005 were paid.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

Under the Company's Articles of Association the directors are required to prepare financial statements that give a true and fair view of the state of affairs of the Group at the end of its financial year and of the profit or loss of the Group for the year. In preparing these financial statements, the directors are required to:

- elect suitable accounting policies and apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and

The directors are also responsible for keeping proper accounting records, which disclose with reasonable accuracy at any time the financial position of the Group and to enable them to ensure that the financial statements comply with the provisions in the International Financial Reporting Standards. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF EQUATOR EXPLORATION LIMITED

We have audited the financial statements of Equator Exploration Limited for the year ended 31 December 2005 which comprise the consolidated income statement, consolidated balance sheet, company balance sheet, consolidated statement of changes in equity, company statement of changes in equity, consolidated cash flow statement, company cash flow statement and related notes. These financial statements have been prepared under the historical cost convention and the accounting policies set out therein.

This report is made solely to the Company's members, as a body, in accordance with the terms of our engagement letter. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As described in the statement of directors' responsibilities the Company's directors are responsible for the preparation of financial statements in accordance with applicable law and International Financial Reporting and Accounting Standards.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view in accordance with International Financial Reporting and Accounting Standards. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions with the Company is not disclosed.

We read the directors' report and consider the implications for our report if we become aware of any apparent misstatement within it.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Group and Company as at 31 December 2005 and of the results of the Group for the year then ended and have been properly prepared in accordance with International Financial Reporting Standards.

CHANTREY VELLACOTT DFK LLP
Chartered Accountants
Registered Auditors
London

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2005

	Note	2005 $'000	2004 $'000
Continuing operations			
Revenue	2	**102**	431
Cost of sales		**(51)**	(36)
Gross profit		**51**	395
Administrative expenses		**(6,997)**	(2,220)
Loss from operations	3	**(6,946)**	(1,825)
Income from investments	6	**3,233**	46
Loss for the period from continuing operations		**(3,713)**	(1,779)
Loss per share	7		
Basic		**($0.03)**	($0.54)
Diluted		**($0.03)**	($0.54)

The notes on pages 29 to 40 form part of these financial statements.

CONSOLIDATED BALANCE SHEET

as at 31 December 2005

	Notes	2005 $'000	2004 $'000
Assets			
Non–current assets			
Goodwill	8	**1,373**	1,373
Exploration and evaluation assets	9	**50,334**	2,249
Multi–client library	10	**2,598**	2,152
Fixtures and equipment	11	**739**	41
		55,044	5,815
Current assets			
Trade and other receivables	14	**3,945**	268
Cash and cash equivalents	15	**135,972**	131,037
		139,917	131,305
Total assets		**194,961**	137,120
Equity and liabilities			
Equity attributable to equity holders of the Company			
Share capital	16	**–**	–
Capital reserves		**203,342**	142,159
Accumulated losses		**(8,797)**	(5,084)
		194,545	137,075
Current liabilities			
Trade and other liabilities	18	**416**	45
Total equity and liabilities		**194,961**	137,120

The notes on pages 29 to 40 form part of these financial statements.

COMPANY BALANCE SHEET
as at 31 December 2005

	Notes	2005 $'000	2004 $'000
Assets			
Non–current assets			
Exploration and evaluation assets	9	**13,898**	249
Multi–client library	10	**2,598**	2,152
Fixtures and equipment	11	**109**	41
Amount owed by subsidiary undertakings	12	**37,710**	–
Investments	13	**3,198**	3,198
		57,514	5,640
Current assets			
Trade and other receivables	14	**1,824**	268
Cash and cash equivalents	15	**135,613**	131,037
		137,437	131,305
Total assets		**194,951**	136,945
Equity and liabilities			
Equity attributable to equity holders of the Company			
Share capital	16	**–**	–
Capital reserves		**203,342**	142,159
Accumulated losses		**(8,693)**	(5,259)
		194,649	136,900
Current liabilities			
Trade and other liabilities	18	**302**	45
Total equity and liabilities		**194,951**	136,945

The notes on pages 29 to 40 form part of these financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2005

	Share capital $'000	Capital reserves $'000	Accumulated losses $'000	Total $'000
Balance at 31 December 2003	–	6,319	(3,305)	3,014
Changes in equity for 2004				
Loss for the year	–	–	(1,779)	(1,779)
Total recognised expense for the year	–	–	(1,779)	(1,779)
Issue of share capital	–	144,030	–	144,030
Share based transactions	–	2,879	–	2,879
Cost associated with issue of share capital				
Cost of options issued	–	(2,755)	–	(2,755)
Cash costs	–	(8,314)	–	(8,314)
Balance at 31 December 2004	**–**	**142,159**	**(5,084)**	**137,075**
Changes in equity for 2005				
Loss for the year	–	–	(3,713)	(3,713)
Total recognised expense for the year	–		(3,713)	(3,713)
Shares issued	–	61,070	–	61,070
Cost of shares issued	–	(1,777)	–	(1,777)
Share based transactions	–	1,890	–	1,890
Balance at 31 December 2005	**–**	**203,342**	**(8,797)**	**194,545**

Included in capital reserves as at 31 December 2005 are amounts attributable to share based transactions of $4,784,000 (2004: $2,894,000).

The notes on pages 29 to 40 form part of these financial statements.

COMPANY STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2005

	Share capital $'000	Capital reserves $'000	Accumulated losses $'000	Total $'000
Balance at 31 December 2003	–	6,319	(2,953)	3,366
Changes in equity for 2004				
Loss for the year	–	–	(2,306)	(2,306)
Total recognised expense for the year	–	–	(2,306)	(2,306)
Issue of share capital	–	144,030	–	144,030
Share based transactions	–	2,879	–	2,879
Cost associated with issue of share capital				
Cost of options issued	–	(2,755)	–	(2,755)
Cash costs	–	(8,314)	–	(8,314)
Balance at 31 December 2004	**–**	**142,159**	**(5,259)**	**136,900**
Changes in equity for 2005				
Loss for the year	–	–	(3,434)	(3,434)
Total recognised expense for the year	–	–	(3,434)	(3,434)
Shares issued	–	61,070	–	61,070
Cost of shares issued	–	(1,777)	–	(1,777)
Share based transactions	–	1,890	–	1,890
Balance at 31 December 2005	**–**	**203,342**	**(8,693)**	**194,649**

Included in capital reserves as at 31 December 2005 are amounts attributable to share based transactions of $4,784,000 (2004: $2,894,000).

The notes on pages 29 to 40 form part of these financial statements.

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2005

	2005		2004	
	$'000	$'000	$'000	$'000
Cash flows from operating activities				
Loss from operations	**(6,946)**		(1,825)	
Adjustments for:				
Amortisation of multi–client library	**606**		324	
Share based transactions	**1,890**		124	
Depreciation on fixtures and equipment	**135**		2	
Operating cash flows before movement in working capital	**(4,315)**		(1,375)	
(Increase)/decrease in receivables	**(3,668)**		128	
Increase/(decrease) in payables	**371**		(698)	
Net cash used in operating activities		**(7,621)**		(1,945)
Cash flows from investing activities				
Interest received	**3,233**		46	
Acquisition of subsidiary	**–**		(1,198)	
Acquisition of multi–client library	**(1,052)**		(1,357)	
Acquisition of exploration and evaluation assets	**(48,085)**		(249)	
Acquisition of fixtures and equipment	**(833)**		(43)	
Net cash used in investment activities		**(46,737)**		(2,801)
Cash flows from financing activities				
Share capital issued (net of costs)	**59,293**		135,716	
Net cash from financing activities		**59,293**		135,716
Net increase in cash and cash equivalents		**4,935**		130,970
Cash and cash equivalents at beginning of period		**131,037**		67
Cash and cash equivalents at end of period		**135,972**		131,037

COMPANY CASH FLOW STATEMENT

For the year ended 31 December 2005

	2005		2004	
	$'000	**$'000**	$'000	$'000
Cash flows from operating activities				
Loss from operations	**(6,668)**		(2,352)	
Adjustments for:				
Amortisation of multi–client library	**606**		324	
Share based transactions	**1,890**		124	
Depreciation on fixtures and equipment	**41**		2	
Operating cash flows before movement in working capital	**(4,131)**		(1,902)	
(Increase)/decrease in receivables	**(1,555)**		93	
Increase/(decrease) in payables	**257**		(136)	
Net cash used in operating activities		**(5,429)**		(1,945)
Cash flows from investing activities				
Interest received	**3,232**		46	
Acquisition of subsidiary	**–**		(1,198)	
Acquisition of multi–client library	**(1,052)**		(1,357)	
Acquisition of exploration and evaluation assets	**(13,649)**		(249)	
Acquisition of fixtures and equipment	**(109)**		(43)	
Loans to subsidiary undertakings	**(37,710)**		–	
Net cash used in investment activities		**(49,288)**		(2,801)
Cash flows from financing activities				
Share capital issued (net of costs)	**59,293**		135,716	
Net cash from financing activities		**59,293**		135,716
Net increase in cash and cash equivalents		**4,576**		130,970
Cash and cash equivalents at beginning of period		**131,037**		67
Cash and cash equivalents at end of period	**135,613**		131,037	

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

1. PRESENTATION OF FINANCIAL STATEMENTS

The Group and Company financial statements have been prepared in accordance with International Financial Reporting Standards. The Group and Company has adopted IFRS 6 "Exploration for and Evaluation of Mineral Resources" for the year ended 31 December 2005. The Group and Company has adjusted its accounting policies from the previous policy disclosed for the year ended 31 December 2004. The adoption has had no material impact on the financial statements of the Group and Company.

The financial statements are presented in US dollars since this is the currency in which the majority of the Group's transactions are denominated.

At the date of authorisation of these financial statements, there were Standards and Interpretations which have not been applied in these financial statements, that were in issue but not yet effective. The Directors anticipate that the adoption of these Standards and Interpretations in future periods will have no material impact on the financial statement of the Group and Company except for additional disclosures when the relevant standards come into effect.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements have been prepared on the historical cost basis. The principal accounting policies adopted are set out below.

Basis of consolidation
The consolidated financial statements incorporate the financial statements of the Company and enterprises controlled by the Company (its subsidiaries) made up to 31 December each year. Control is achieved where the Company has the power to govern the financial and operating policies of an investee entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the period are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

All intra–group transactions, balances, income and expenses are eliminated on consolidation.

Business combinations
The acquisition of subsidiaries is accounted for using the purchase method. The cost of the acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 are recognised at their fair value at the acquisition date, except for non-current assets (or disposal groups) that are classified as held for resale in accordance with IFRS 5 "Non Current Assets Held for Sale and Discontinued Operations", which are recognised and measured at fair value less costs to sell.

Goodwill arising on acquisition is recognised as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognised. If, after reassessment, the Group's interest in the fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in profit or loss.

Interest in joint ventures
A joint venture is a contractual arrangement whereby the Company and other parties undertake an economic activity, which is subject to joint control.

Joint venture arrangements which involve the establishment of a separate entity in which each venturer has an interest are referred to as jointly-controlled entities. The Company reports its interest in jointly-controlled entities using proportionate consolidation – the Company's share of the assets, liabilities, income and expenses of jointly-controlled entities are combined with the equivalent items in the consolidated financial statements on a line-by-line basis.

Where the Company transacts with its jointly-controlled entities, unrealised profits and losses are eliminated to the extent of the Company's interest in the joint venture, except where unrealised losses provide evidence of an impairment of the asset.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2005

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

Revenue recognition

Revenue is measured at fair value of the consideration received or receivable and represents amounts receivable for goods and services provided in the normal course of business, net of discounts and sales related taxes.

Revenue from sales of multi-client library data is recognised when the majority owner of the seismic surveys has received the revenue from the customer as agreed under the joint agreement.

Interest income is accrued on a time basis, by reference to the principal outstanding and the interest rate applicable.

Employee services settled in equity instruments

The Group issues equity-settled share–based payments to certain employees. These are measured at fair value (excluding the effect of non market-based vesting conditions) at the date of grant. The fair value determined at the grant date is expensed on a straight line basis over the vesting period, based on the Group's estimate of shares that will eventually vest and adjusted for the effect of non market-based vesting conditions.

Fair value is measured by use of a binomial model. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations.

Other goods or services settled in equity instruments

Goods or services (other than employee services) received in exchange for equity-settled share-based payments are measured directly at their current fair value at each balance sheet date. The proceeds received on exercise of the options, net of any directly attributable transaction costs, are credited to share capital (nominal value) and share premium when the options are exercised.

Foreign currencies

Transactions in currencies other than US dollars are recorded at the rates of exchange prevailing on the dates of the transactions. Monetary assets and liabilities denominated in such currencies are retranslated at the rates prevailing on the balance sheet date. Profits and losses arising on exchange are included in the income statement for the period.

Goodwill

Goodwill arising on consolidation represents the excess of the cost of acquisition over the Company's interest in the fair value of the identifiable assets, liabilities and contingent liabilities of a subsidiary, associate or jointly controlled entity at the date of acquisition. Goodwill is recognised as an asset and is tested for impairment annually, or on such occasions that events or changes in circumstances indicate that its value might be impaired in accordance with IAS 36.

Goodwill arising on the acquisition of associates is included within the carrying value of the associates. Goodwill arising on the acquisition of subsidiaries and jointly controlled entities is presented separately in the balance sheet.

Negative goodwill arising on acquisition of a subsidiary and jointly controlled entities is set against a reassessment of the identifiable assets, liabilities and contingent liabilities and the measurement of the cost of the consideration if applicable and then recognised in the income statement.

On disposal of a subsidiary, associate or jointly controlled entity, the attributable amount of unamortised goodwill, which has not been subject to impairment, is included in the determination of the profit or loss on disposal.

Exploration and evaluation assets

The Group has capitalised at cost expenditure which is directly associated with the acquisition, exploration and appraisal of their oil and gas interests.

The exploration and evaluation assets are reviewed for impairment at least at each balance sheet date and when fact and circumstances suggest that the carrying amount exceeds the recoverable amount. Any impairment loss is calculated and recognised as an expense in accordance with IAS 36.

Fixtures and equipment
Fixtures and equipment are stated at cost less accumulated depreciation and any impairment losses. Depreciation is charged so as to write off the costs over their estimated useful lives, using the straight-line method commencing in the month following the purchase, on the following basis:

Fixtures and equipment	3 years
Motor Vehicles	3 years

The gain or loss arising on the disposal of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in income.

Investment in multi–client library
This investment represents the Group's participating interest in seismic surveys that are licensed to customers on a non-exclusive basis. All costs directly or indirectly incurred in acquiring, processing and otherwise completing seismic surveys are capitalised in the multi-client library.

Group policy is to amortise the survey costs over five years from the point that the survey has been completed.

Impairment
At each balance sheet date, the Group reviews the carrying amount of its tangible and intangible assets with finite lives to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash–generating unit to which the asset belongs.

Goodwill arising on acquisitions is allocated to cash-generating units. The recoverable amount of the cash-generating unit to which goodwill is allocated is tested for impairment annually, or on such other occasions that events or changes in circumstances indicate that it might be impaired.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. Impairment losses are recognised as an expense immediately, unless the relevant asset is land or buildings at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (or cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (or cash-generating unit) in prior periods. A reversal of an impairment loss is recognised as income immediately, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase. However, impairment losses relating to goodwill may not be reversed.

Financial instruments
Financial assets and financial liabilities are recognised in the Group's and Company's balance sheets when the Group or Company has become a party to the contractual provisions of the instrument.

Trade receivables
Trade receivables are stated at their nominal value as reduced by appropriate provisions for estimated irrecoverable amounts. Appropriate provisions for estimated irrecoverable amounts are recognised on profit or loss when there is objective evidence that the assets is impaired.
Cash and cash equivalents
Cash and cash equivalents comprise cash on hand and demand deposits, and other short-term highly liquid investments that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2005

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

Financial liabilities and equity

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidence a residual interest in the asset of the Group after deducting all of its liabilities.

Trade payables

Trade payables are stated at their nominal value less any discount or rebate received.

Provisions

Provisions are recognised when the Group has a present obligation as a result of a past event, which it is likely that an outflow of economic benefits will occur and can be reasonably quantified.

Equity instruments

Equity issued by the Company is recorded at the proceeds received, net of direct issue costs.

3. LOSS FROM OPERATIONS

	2005 $'000	2004 $'000
Loss from operations has been arrived at after charging/(crediting):		
Net foreign exchange loss/(gain)	**67**	(135)
Share based transactions	**1,890**	124
Amortisation of multi–client library	**606**	324
Depreciation on fixtures and equipment	**135**	2
Auditors' fees	**30**	18
Directors' remuneration	**722**	249
Staff costs	**324**	249

The audit fee for the parent company was $25,000 (2004: $14,000).

4. STAFF COSTS

	2005 No.	2004 No.
The average monthly number of employees (including executive directors) was:	**6**	3

Their aggregate remuneration comprised (excluding executive directors):

	2005 $'000	2004 $'000
Wages and salaries	**290**	–
Social security costs	**22**	–
Other pension costs	**12**	–
	324	–

The Group contributes to individual personal pension plans.

5. DIRECTORS' REMUNERATION

Remuneration paid to directors during the period was as follows:

	2005 $'000	2004 $'000
Salaries	**210**	17
Fees	**422**	232
Pensions	**90**	–
	722	249

The remuneration of directors and key executives is decided by the remuneration committee having regard to comparable market statistics.

6. INCOME FROM INVESTMENTS

	2005 $'000	2004 $'000
Interest on bank deposits	**3,233**	46

7. LOSS PER SHARE

The calculations of the basic and diluted loss per share is based on the following data:

	2005 $'000	2004 $'000
Loss		
Loss for the purpose of basic loss per share (net loss for the year)	**(3,713)**	(1,779)
Effect of dilutive options and warrants	**–**	–
Loss for the purposes of diluted loss per share	**(3,713)**	(1,779)
Number of shares		
Weighted average number of common shares in issue during the year	**113,710,957**	32,757,808
Effect of dilutive options and warrants	**9,111,563**	–
Weighted average number of common shares in issue during the year for the purpose of diluted loss per share	**122,822,520**	32,757,808

The options and warrants in existence at the end of the year ended 31 December 2004 did not have a dilutive effect as the exercise price exceeded the average market price of the common shares

8. GOODWILL

	$'000
Cost	
At 1 January 2004 and 31 December 2005	1,762
Impairment provision	
At 1 January 2004 and 31 December 2005	389
Carrying amount	
At 31 December 2005	**1,373**
At 31 December 2004	1,373

NOTES TO THE FINANCIAL STATEMENTS CONTINUED
For the year ended 31 December 2005

9. EXPLORATION AND EVALUATION ASSETS

	West Africa $'000
Group	
Cost	
At 1 January 2004	–
Additions	2,249
At 1 January 2005	2,249
Additions	48,085
At 31 December 2005	**50,334**

	West Africa $'000
Company	
Cost	
At 1 January 2004	–
Additions	249
At 1 January 2005	249
Addition	13,649
At 31 December 2005	**13,898**

10. INVESTMENT IN MULTI-CLIENT LIBRARY

	$'000
Group and Company	
Cost	
At 1 January 2004	1,626
Additions	1,357
At 1 January 2005	2,983
Additions	1,052
At 31 December 2005	**4,035**
Accumulated amortisation	
At 1 January 2004	507
Charge for year	324
At 1 January 2005	831
Charge for year	606
At 31 December 2005	**1,437**
Carrying amount	
At 31 December 2005	**2,598**
At 31 December 2004	2,152

11. FIXTURES AND EQUIPMENT

	Fixtures and fittings $'000	Equipment $'000	Motor vehicles $'000	Total $'000
Group				
Cost				
At 1 January 2004	–	–	–	–
Additions	–	43	–	43
At 1 January 2005	–	43	–	43
Additions	251	219	363	833
At 31 December 2005	**251**	**262**	**363**	**876**
Accumulated depreciation				
At 1 January 2004	–	–	–	–
Charge for year	–	2	–	2
At 1 January 2005	–	2	–	2
Charge for the year	36	57	42	135
At 31 December 2005	**36**	**59**	**42**	**137**
Carrying amount				
At 31 December 2005	**215**	**203**	**321**	**739**
At 31 December 2004	–	41	–	41

	Equipment $'000
Company	
Cost	
At 1 January 2004	–
Additions	43
At 1 January 2005	43
Additions	109
At 31 December 2005	**152**
Accumulated depreciation	
At 1 January 2004	–
Charge for year	2
At 1 January 2005	2
Charge for the year	41
At 31 December 2005	**43**
Carrying amount	
At 31 December 2005	**109**
At 31 December 2004	41

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2005

12. AMOUNT OWED BY SUBSIDIARY UNDERTAKINGS

	Equator Exploration (OML 122) Limited $'000	Equator Exploration Nigeria Limited $'000	Total $'000
At 1 January 2004 and 1 January 2005	–	–	–
Funds provided	34,183	3,527	37,710
At 31 December 2005	**34,183**	**3,527**	**37,710**

The loans have been provided to both subsidiaries to provide funds for investment in the Group's principal activity. There are no set repayment dates and no interest is charged on the outstanding amounts.

13. INVESTMENTS

	Investment in subsidiary undertakings $'000
At 1 January 2004	2,000
Additions	1,198
At 1 January 2005	3,198
Additions	–
At 31 December 2005	**3,198**

The subsidiary undertakings of the company are as follows:

Name	**Percentage owned**	**Country of registration**
Aqua Exploration Limited	100%	Bahamas
Equator Exploration Nigeria Limited	100%	Nigeria
Equator Exploration (OML 122) Limited (note 1)	100%	BVI
Equator Exploration (Congo) Limited (note 2)	100%	BVI
Equator JDZ Nigeria Block 2 Limited (note 3)	100%	Nigeria

Note 1: The company was formed on 31 March 2005
Note 2: The company was formed on 19 July 2005
Note 3: The company was formed on 14 December 2005

The principal activity of the above companies is the exploration and development of oil and gas projects

14. TRADE AND OTHER RECEIVABLES

	2005 $'000	2004 $'000
Group		
Trade receivables	**157**	55
Other receivables	**1,594**	12
Short term loans	**900**	–
Prepayments and accrued income	**1,294**	201
	3,945	268

	2005 $'000	2004 $'000
Company		
Trade receivables	**157**	55
Other receivables	**765**	12
Short term loans	**900**	–
Prepayments and accrued income	**2**	201
	1,824	268

The short term loan was repayable by 31 January 2006 but has since been extended until 31 March 2006 and is secured on personal assets. Interest is charged at 5% payable on repayment of the capital amount.

The directors consider that the carrying amount of trade and other receivables approximates to their fair value. There have been no allowances for doubtful receivables due to the Group's managements' prior experience.

Credit risk

The Group's principal financial assets are bank balances and cash, trade receivables, other receivable and short term loans.

The Group's credit risk is primarily attributable to its trade receivables, other receivable and short term loans. An allowance is provided for doubtful receivables where there is an identified loss event, which, based on previous experience, is evidence of a reduction in the recoverability of the cash flows.

The credit risk on liquid funds is limited because the counterparties are banks with high credit ratings assigned by international credit–rating agencies.

15. CASH AND CASH EQUIVALENTS

Cash and cash equivalents comprise cash held by the Group and Company and short–term deposits with an original maturity of three months or less. The carrying amount of these assets approximate their fair value.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED
For the year ended 31 December 2005

16. SHARE CAPITAL

	2005 No.	2004 No.
Issued and fully paid		
Common shares with no par value	**131,417,190**	113,400,124

On 8 July 2005, the Company issued 305,500 common shares for $1.31 per share on exercise of warrants.

On 11 July 2005, the Company issued 15,000 common shares for $1.31 per share on exercise of warrants.

On 12 July 2005, the Company issued 205,500 common shares for $1.31 per share on exercise of warrants.

On 14 July 2005, the Company issued 200,000 common shares for $1.25 per share on exercise of share options.

On 3 October 2005, the Company issued 100,000 common shares for $1.31 per share on exercise of warrants.

On 8 December 2005, the Company issued 17,291,066 for $3.47 per share.

Warrant & option issues
As at 31 December 2005, there were 11,395,000 (2004: 12,021,000) warrants outstanding exercisable up to three years from date of issuance at an exercise price of $1.3125 per share, with each warrant being convertible into one common share.

17. SHARE BASED PAYMENTS

During the year ended 31 December 2005, the Company had the following share options in issue:

	Number of options
Option 1	
Outstanding at 1 January 2005	600,000
Exercised during year	(200,000)
Outstanding at 31 December 2005	**400,000**

The 400,000 options outstanding as at 31 December 2005 were granted on 21 August 2003 with an exercise price of $5.00 per share. Due to the split of shares on a four to one basis on 26 October 2004, the exercise price was reduced to $1.25 per share. The options are exercisable until 21 August 2008 with each option convertible into one common share.

	Number of options
Option 2	
Outstanding at 1 January 2005 and 31 December 2005	**3,360,000**

The Company granted 3,360,000 options to officers, directors, employees and consultants on 23 November 2004. The options had an exercise price of £1 and expire on 23 November 2014. The options vest on a pro-rata basis over 24 months. Management has estimated the fair value of these options, once vested, to be $0.89 per option. The value of these options was determined using the Black-Scholes option-pricing model with assumptions of the risk free rate of 4.5%, the average term of 9 years, stock value at time of granting of £1 and volatility of 30%. The total value of $1,500,000 was recorded in the consolidated income statement for the year ended 31 December 2005.

Option 3	Number of options
Outstanding at 1 January 2005	–
Granted	2,315,000
Outstanding at 31 December 2005	**2,315,000**

The Company granted 2,315,000 options to directors on 22 July 2005. The options had an exercise price of £1.56 and expire on 21 July 2010. The options vest semi-annually over 24 months. Management has estimated the fair value of these options, once vested, to be $0.88 per option. The value of these options was determined using the Black-Scholes option-pricing model with assumptions of the risk free rate of 4.3%, the average term of 4.5 years, stock value at time of granting of £1.56 and volatility of 30%. The total value of $203,000 was recorded in the consolidated income statement for the year ended 31 December 2005.

Option 4	Number of options
Outstanding at 1 January 2005	–
Granted	1,525,000
Outstanding at 31 December 2005	**1,525,000**

The Company granted 1,525,000 options to directors on 9 November 2005. The options had an exercise price of £2.068 and expire on 8 November 2010. The options vest semi-annually over 24 months. Management has estimated the fair value of these options, once vested, to be $1.23 per option. The value of these options was determined using the Black-Scholes option-pricing model with assumptions of the risk free rate of 4.3%, the average term of 9 years, stock value at time of granting of £2.06 and volatility of 30%. The total value of $187,000 was recorded in the consolidated income statement for the year ended 31 December 2005.

Option 5	Number of options
Outstanding at 1 January 2005	–
Granted	60,000
Outstanding at 31 December 2005	**60,000**

The Company granted 1,525,000 options to directors on 8 December 2005. The options had an exercise price of £2.068 and expire on 7 December 2010. The options vest semi-annually over 24 months. The value of these options was determined using the Black-Scholes option-pricing model with assumptions of the risk free rate of 4.3%, the average term of 9 years, stock value at time of granting of £2.07 and volatility of 30%. The total value of $7,000 was recorded in the consolidated income statement for the year ended 31 December 2005.

Other options

On 3 December 2004, the Company granted 1,134,000 assignable options to NWCF LLP as partial consideration for their advisory services in connection with the admission of the Company to AIM. These options have an exercise price of £1 and expire on 9 December 2009. Management has estimated the fair value of these options to be $0.65 per option, totalling $752,000. The value of these options was determined using the Black-Scholes option-pricing model with assumptions of the risk free rate of 4.25%, the term of 5 years, stock value at time of granting of £1 and volatility of 30%. The total value of $752,000 was recorded in other reserves. This did not affect the consolidated income statement as the cost was taken to the capital reserve as an expense of the issue of common shares on AIM.

On 3 December 2004, the Company granted 2,400,000 assignable options to ODL Securities Limited as partial consideration for their advisory services in connection with the admission of the Company to AIM. These options have an exercise price of £1 and expire on 9 December 2007. Management has estimated the fair value of these options to be $0.48 per option, totaling $1,163,000. The value of these options was determined using the Black-Scholes option-pricing model with assumptions of the risk free rate of 3.75%, the term of 3 years, stock value at time of granting of £1 and volatility of 30%. The total value of $1,163,000 was recorded in other reserves. This did not affect the consolidated income statement as the cost was taken to the capital reserve as an expense of the issue of common shares on AIM.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

For the year ended 31 December 2005

18. TRADE AND OTHER PAYABLES

	2005 $'000	2004 $'000
Group		
Other taxes and social security	**14**	–
Accruals and deferred income	**401**	45
	415	45

	2005 $'000	2004 $'000
Company		
Other taxes and social security	**14**	–
Accruals and deferred income	**288**	45
	302	45

Accruals principally comprise amounts outstanding for trade purchases and ongoing costs.

19. RELATED PARTY TRANSACTIONS

a) Transactions between group companies are disclosed in note 13.

b) Payments were made in respect of administrative services through other companies that are related to the shareholders of the Company, for which fees of $231,000 (2004: $132,000) were charged, being an appropriate allocation of costs incurred by relevant administrative departments.

20. CONTINGENT LIABILITIES

Seisco Investments Limited

Seisco Investments Limited ('Seisco') is a special purpose vehicle that has a common director and shareholder. During 2002 Seisco provided Equator with $500,000 to fund Equator's share of the acquisition costs of certain seismic data. The amount borrowed was repaid during 2002 and 2003 from the revenue generated from licensing the seismic data.

In the event that no future seismic revenues can be expected from the majority owner (the 'Majority Owner') of this designated batch of seismic data acquired in 2002, the acquisition cost of which was funded by Seisco, as a result of the Majority Owner of such data entering into liquidation proceedings Equator will issue Seisco with a maximum of 100,000 common shares. The number of common shares to be issued to Seisco in the event of the cessation of seismic revenues due to the liquidation of the Majority Owner will be dependant upon the extent to which the funds provided by Seisco have been repaid prior to the cessation of seismic revenues as shown below:

	Number of shares to be issued
Amount of initial investment repaid	
Greater than initial funds provided but less than 1.5 times initial funds provided	100,000
Greater than 1.5 times initial funds provided	50,000

21. SUBSEQUENT EVENTS

On 19 January 2006, the Company issued 380,000 new common shares on exercise of warrants at $1.31 per share.

On 2 February 2006, the Company issued 2,030,000 new common shares on exercise of warrants at $1.31 per share.

On 20 February 2006, the Company issued 41,050,900 new common shares with institutional investors at $6.09 per share.

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Equator Exploration Limited
Third Floor
192 Sloane Street
London SW1X 9QX
United Kingdom

www.equatorexploration.com