

CALVALLEY PETROLEUM INC.

2009 2nd Quarter Interim Report to Shareholders

**For the three and six months
ended June 30, 2009**

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CORPORATE PROFILE

Calvalley Petroleum Inc. is an international oil and gas company based in Calgary, Alberta which is focused on exploration and development of Block 9 in the Republic of Yemen and exploration of the Gimbi and Metema Blocks in Ethiopia. Calvalley is well-financed and debt-free and expects to maintain a healthy balance sheet by funding its 2009 capital program from cash generated by operating activities. Calvalley's common shares are listed on the Toronto Stock Exchange under the symbol "CVI.A."

Calvalley's principal assets and operations are related to its 50% working interest in the Production Sharing Agreement for Block 9, which consists of 2,234 km² (552,000 acres) of land within the prolific Sayun-Masila basin. Calvalley has made several significant hydrocarbon discoveries on Block 9. Calvalley declared commerciality during 2005 and started commercial production in December of that year.

Calvalley also owns a 100% working interest in a Production Sharing Contract in Ethiopia for the Metema and Gimbi blocks which cover a total area of 46,470 km² (11.5 million acres). The two blocks lie adjacent to the Sudan border, offsetting the Melut/Muglad and Blue Nile Basins, both of which are proven oil basins which form part of the Central African rift system. The Central African rift system is a series of Cretaceous to Tertiary-aged failed rifts that trend across Central Africa from the Benue Trough in Nigeria, through Chad, into Sudan. This early stage project provides Calvalley with additional opportunities to diversify its asset base.

FORWARD LOOKING STATEMENTS

Some of the statements contained herein including, without limitation, financial and business prospects and financial outlooks of the Company may be forward-looking statements which reflect management's expectations regarding future plans and intentions, growth, results of operations, performance and business prospects and opportunities. Words such as "may", "will", "should", "could", "anticipate", "believe", "expect", "intend", "plan", "potential", "continue", and similar expressions have been used to identify these forward-looking statements. These statements reflect management's current beliefs and are based on information currently available to management. Forward-looking statements involve significant risk and uncertainties. A number of factors could cause actual results to differ materially from the results discussed in the forward-looking statements including, but not limited to, changes in general economic, political and market conditions and other risk factors. Although the forward-looking statements contained herein are based upon what management believes to be reasonable assumptions, management cannot assure that actual results will be consistent with these forward-looking statements. Investors should not place undue reliance on forward-looking statements. These forward-looking statements are made as of the date hereof.

Forward-looking statements and other information contained herein concerning the oil and gas industry and Calvalley's general expectations concerning this industry are based on estimates prepared by management using data from publicly available industry sources as well as from reserve reports, market research and industry analysis and on assumptions based on data and knowledge of this industry which Calvalley believes to be reasonable. However, this data is inherently imprecise, although generally indicative of relative market positions, market shares and performance characteristics. While Calvalley is not aware of any misstatements regarding any industry data presented herein, the industry involves risks and uncertainties and is subject to change based on various factors. See "Risk Factors."

Calvalley does not undertake any obligation to update publically or revise any forward-looking statements contained in this or in any other document filed with Canadian securities regulatory authorities, whether as a result of new information, future events or otherwise, except as required by applicable securities laws.

ABBREVIATIONS

bbls barrels
 mbbls thousands of barrels
 bopd barrels of oil per day
 mmcfcd million cubic feet per day
 km² square kilometre

HIGHLIGHTS

Financial

These key financial indicators are discussed in more detail in the following sections.

(in thousands of US dollars)	Three months ended June 30		Six months ended June 30	
	2009	2008	2009	2008
Revenue (Gross)	17,252	25,434	24,112	45,544
Revenue from crude oil sales (net of royalties)	10,686	15,791	14,846	28,247
EBITDA ⁽¹⁾	5,548	11,504	5,504	80,813
Operating income ⁽¹⁾	1,904	8,727	110	15,259
Net income (loss)	765	4,432	(1,280)	10,031
Capital expenditures	2,812	9,493	5,211	16,852
Funds flow from operations ⁽¹⁾	4,644	10,266	4,495	18,667
Cash flow from operating activities	3,325	34,061	2,363	34,370

⁽¹⁾ See "Non-GAAP Measures"

- Calvalley's revenue from crude oil sales was \$17.2 million (gross) and \$10.7 million (net of royalties) for the quarter ended June 30, 2009 (2008 - \$25.4 (gross) and \$15.8 million (net of royalties)). The sales decline was due to soft commodity prices partially offset by the timing of lifts.
- Net income was \$0.8 million for the three months ended June 30, 2009, as compared to \$4.4 million for the same period of 2008. The decrease in net income was largely attributable to the factors noted above which reduced revenue.
- Funds flow from operations was \$4.6 million (\$0.05/share) for the three months ended June 30, 2009, as compared to \$10.3 million (\$0.10/share) for the same period of 2008.
- Operating costs during the second quarter of 2009 were \$3.7 million (\$11.12/bbl) as compared to \$2.8 million (\$13.81/bbl) for the three months ended June 30, 2008.

- Calvalley continues to be well financed and capitalized with no outstanding debt and working capital of \$72.1 million.
- Significant progress was made in negotiations relating to marketing all of Block 9 crude oil during the quarter. Successful conclusion of these negotiations is expected to allow Calvalley to commence production from the Al Roidhat field in the fourth quarter of 2009 or first quarter of 2010.
- Necessary materials were mobilized to the Qarn Qaymah 2 location to commence testing. A rig is currently being mobilized to the location for the commencement of testing of the fractured basement followed by completion and testing of the Kohlan sand.
- The 2009 drilling program begins in the third quarter with the drilling of two exploration wells and up to six development wells during the balance of 2009. The two exploration wells will be drilled into Ras Nowman and Salmin prospects with an estimated combined mean oil-in-place of approximately 200 million barrels.

Operating

(barrels of oil per day)	Three months ended June 30		Six months ended June 30,	
	2009	2008	2009	2008
Total Block 9 production	4,164	4,759	4,347	4,681
Calvalley working interest (50.0%)	2,082	2,380	2,174	2,341

- Average daily production from the Block 9 for the three months ended June 30, 2009 was 4,164 gross barrels per day (Calvalley working interest 2,082 bopd), a decrease from the previous quarter's average of 4,532 bopd (2,266 bopd working interest share) and also a decrease from 2008 second quarter average production of 4,759 bopd (2,380 bopd working interest share).
- Construction of water and gas injection facilities at Hiswah continues with completion targeted for late-2009.
- Calvalley is constructing a heavy crude blending facility at the CPF, which will enable the Company to produce from the currently shut-in Al Roidhat field. Wells at Al Roidhat are being worked over to prepare them for production.

CHAIRMAN AND CHIEF EXECUTIVE OFFICER'S REPORT

Calvalley remains in an excellent position for future growth with a strong balance sheet and opportunities for organic growth through the drill bit. The Company has working capital of US\$72.1 million with no debt. Despite limited access to the export market for all types of crude which have been discovered on Block 9, our production capability continues to grow. Our inventory of development and exploration drilling locations continues to increase and be high-graded to support a multi-year drilling program. We have made significant progress toward finalizing a marketing agreement which will enable Calvalley to export all of its crude at world prices including heavier crude at Al Roidhat. We anticipate the first oil delivery of blended crude to a new export market in the first quarter of 2010.

Production remains restricted to 2,000 – 2,500 bopd (gross field 4,000 - 5,000 bopd) due to limited access to the export market. Calvalley's production is hindered by limited access to Safer (Block 18) facilities due to crude quality differentials. As a result, certain wells in the Hiswah field have been shut in and the field is producing suboptimally from an average of 16 producing wells of the existing 23 wells which are capable of production. The drilling of development wells at Hiswah was postponed during the first half of the year while we negotiated the marketing agreement. The long-term solution for crude marketing will resolve the crude quality issue and as a result, Calvalley has commenced the development drilling campaign at Hiswah. We continue working diligently to resolve the marketing issue to increase production as our reserves base and shut-in wells support significant production growth opportunities.

Calvalley continued to make progress toward the completion of key infrastructure projects including the blending, water and gas injection facilities. These facilities are key to our production growth from existing and future discoveries. We expect to complete these capital projects in the second half of the year. The Qarn Qaymah 2 testing program will resume in the third quarter. The test was halted during the first quarter due to delays in the delivery of specialized downhole equipment. The complex nature of the reservoirs encountered necessitates an extensive testing program for the well. The necessary equipment is now on-site and we have mobilized the required services to re-test the fractured granitic basement. The service rig is scheduled to arrive at QQ-2 before the end of August. Upon completion of the test of the fractured basement, we will move uphole to perforate and test the Kohlan gas/condensate discovery.

Commodity prices improved during the second quarter. Calvalley realized an average sale price of \$51.31 per barrel. The net earnings for the quarter totaled \$0.8 million or \$0.01 per share. Capital expenditures for the quarter were \$2.8 million, primarily for the injection and blending facility projects and preparation of the Al Roidhat wells for production. With working capital of \$72.1 million, Calvalley remains debt-free and well positioned to fund its capital program without further dilution to its shareholders. The Company continued its share buyback programs spending \$1.5 million to buy back 656,074 shares during the quarter

Our exploration team has increased the number of exploration plays and prospects to over 50, with numerous high impact exploration targets, two of which are planned to be drilled in the second half of the year: Ras Nowmah and Salmin. The two prospects are shallower multi-horizon targets with total depth not exceeding 1,500 meters and have a combined unrisksed mean oil-in-place potential of approximately 200 million barrels.

“Edmund Shimon”

Edmund M. Shimon
Chairman and Chief Executive Officer
August 12, 2009

OPERATIONS REPORT

Production Overview

During the second quarter of 2009, daily production from Block 9 averaged 4,164 barrels of oil per day (“bopd”) (2008 - 4,759 bopd), with the Company’s working interest share being 2,082 bopd (2008 – 2,380 bopd). All of our production came from the partially developed Hiswah oil field, which produces high-quality, lighter sweet crude oil that is sold at a price comparable to Dated Brent Crude.

Despite expected performance from the existing producing wells at the Hiswah field, production has been constrained due to the limitation of sales volume that is accepted by the Safer Facilities at Block 18 (“Safer”). Production from the Hiswah field continues to be limited to an average of sixteen of twenty-three existing horizontal wells due to this limitation. The Facility Usage Agreement at Block 18 dictates that blended crude at the facility shall not exceed 0.12% in sulfur content by weight. The sulfur content of Safer production is 0.09%. After blending Safer production with the production from Block 9, the sulfur content averages 0.12%. Increases or decreases in Safer’s production impact the sales volume that can be accepted for blending from Block 9. Safer’s production at Block 18 has been continuously declining and consequently, Block 9 has been forced to reduce its crude oil volume to keep overall sulfur content at Safer under 0.12%. Calvalley’s crude is sweet and has an average of 0.43% sulfur which is comparable to 0.42% which is the standard for Dated Brent Crude.

Calvalley initiated a number of alternative solutions to sell blended crude oil from all discoveries at Block 9 including production from wells that are currently shut-in. Based on the evaluation of the various alternatives; Calvalley has narrowed the focus to deliver Block 9 crude to either Block 14 or Block 51. Negotiations with the operator of these blocks have advanced significantly and we are optimistic that delivery of the first oil to one of these blocks could commence by the end of 2009. The Government of Yemen has formed a “tie-committee” to oversee the progress of these negotiations. Once an agreement to evacuate all types of crude from Block 9 is finalized, Calvalley will commence the construction process of the main sales pipeline which has been approved by the government.

In anticipation of finalizing an alternative marketing solution for all kinds of crude discovered at Block 9, Calvalley has substantially completed a heavy crude blending facility at the CPF. The blending facility will enable the Company to process production from the currently shut-in Al Roidhat field. Three additional wells were equipped during the quarter at Al Roidhat, increasing to seven the number of wells which are fully equipped and ready to produce at Al Roidhat. An additional well is undergoing completion. Once fully developed, Al Roidhat is expected to reach peak production of 10,000 bopd based on the existing reserves. However, the Al Roidhat field will remain shut-in until a marketing solution is finalized. We expect to commence production from this field as early as the yearend.

Hiswah Field Development

During the second quarter, no development wells were drilled at the Hiswah field. However, a number of workover programs were carried out to enhance well performance. The 2009 budget includes the drilling of six horizontal development wells. Drilling is expected to commence by the end of August, 2009.

Facilities

The CPF, with a 60,000 barrel per day processing capability, is now fully functional. Construction of key components of water injection and gas re-injection facilities for the Hiswah field has advanced significantly. Water injection facilities have been constructed and delivered to Block 9. On-site construction is expected to be completed during the third quarter with the first water injection expected to commence late in the year. The gas injection facilities are currently being constructed in Dubai with expected completion in October. The Hiswah field currently produces approximately 5.5 mmcf/d of solution gas which is being flared and will be utilized for pressure maintenance once these facilities are completed.

Exploration Drilling Program

No exploration wells were drilled during the second quarter. Testing of the Qarn Qaymah 2 ("QQ-2") well was halted early in the year due to the lack of specialized downhole equipment including smaller diameter (2 7/8 inch) production tubing. All required equipment has now been received and Calvalley will re-test the fractured granitic basement at QQ-2 commencing in late August. Upon full evaluation of the fractured basement, we will move up-hole to perforate and test the Kohlan sand gas condensate discovery. Completion of QQ-2 will enable us to high-grade and then proceed with drilling a number of attractive deep well targets in the greater Qarn Qaymah area.

Calvalley plans to drill two exploration wells at shallower depths (less than 1500 meters) during 2009. These wells are to be drilled in Ras Nowmah and Salmin prospects, both of which are on a proven oil fairway. Salmin is situated approximately five (5) kilometers northwest of the Auqban discovery targeting a light oil carbonate structure with an estimated mean oil-in-place volume of 45 million barrels. The Ras Nowmah structure is situated between Hiswah and Al Roidhat with a potential of 149 million barrel of mean oil-in-place. Site preparation for Ras Nowmah has commenced and we expect to start drilling this well in October followed by the Salmin prospect.

Future Plans

For the balance of the 2009, Calvalley plans to drill up to six horizontal development wells at Hiswah, and the two exploration wells at Ras Nowmah and Salmin prospects. Once Calvalley resolves the marketing issue of all its crude from Block 9, we expect to accelerate development and exploration activities substantially to unlock the potential of the block.

MANAGEMENT'S DISCUSSION AND ANALYSIS

References to "Calvalley" or the "Company" refer to Calvalley Petroleum Inc. and its share of consolidated subsidiaries and joint ventures unless the context indicates otherwise. All currency references are to United States dollars unless otherwise specifically indicated. References to "C\$" are to Canadian dollars.

The purpose of this Management's Discussion and Analysis is to provide readers the ability to view Calvalley in much the same way as Management. The following combination of historic and prospective information and financial and business analyses, together with the consolidated financial statements, are intended to impart useful knowledge to investors and other readers. This Management's Discussion and Analysis should be read in conjunction with the unaudited interim consolidated financial statements and related notes of Calvalley for the six and three month periods ended June 30, 2009. Additional information relating to the Company, including the Company's Annual Information Form, is available on SEDAR at www.sedar.com or on the Company's web site at www.calvalleypetroleum.com.

This Management's Discussion and Analysis is as of August 12, 2009.

Forward-Looking Statements

This Management's Discussion and Analysis contains certain forward-looking statements. Some of the statements contained herein including, without limitation, financial and business prospects and financial outlooks of the Company may be forward-looking statements which reflect management's expectations regarding future plans and intentions, growth, results of operations, performance and business prospects and opportunities. Words such as "may", "will", "should", "could", "anticipate", "believe", "expect", "intend", "plan", "potential", "continue", and similar expressions have been used to identify these forward-looking statements. These statements reflect management's current beliefs and are based on information currently available to management. Forward-looking statements involve significant risk and uncertainties. A number of factors could cause actual results to differ materially from the results discussed in the forward-looking statements including, but not limited to, changes in general economic, political and market conditions and other risk factors. Although the forward-looking statements contained herein are based upon what management believes to be reasonable assumptions, management cannot assure that actual results will be consistent with these forward-looking statements. Investors should not place undue reliance on forward-looking statements. These forward-looking statements are made as of the date hereof.

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Calvalley does not undertake any obligation to update publicly or revise any forward-looking statements contained in this or in any other document filed with Canadian securities regulatory authorities, whether as a result of new information, future events or otherwise, except as required by applicable securities laws.

Non-GAAP Measures

Funds flow from operations is a non-GAAP measure that represents funds generated from operating activities before changes in non-cash working capital. Funds flow from operations should not be considered an alternative to, or more meaningful than, cash flow from operating activities. Management believes that funds flow from operations is a useful supplemental measure to analyze the Company's ability to generate cash flow to fund capital investment and working capital requirements. Funds flow from operations may not be comparable to similar measures used by other companies.

Earnings before interest, taxes, depreciation and amortization ("EBITDA") and operating income are non-GAAP measures. The Company calculates EBITDA as revenue net of royalties, operating expenses and general and administrative expenses. The Company calculates operating income by deducting depletion, depreciation and accretion expense from EBITDA. Management believes that EBITDA and operating income are useful supplemental measures to analyze operating performance and to provide an indication of the results generated by the Company's principal business activities prior to the consideration of other income and expenses. EBITDA and operating income may not be comparable to similar measures used by other companies.

Netback is a non-GAAP measure that represents revenue net of royalties, operating expenses and current taxes. Management believes that netback is a useful supplemental measure to analyze operating performance and provide an indication of the results generated by the Company's principal business activities prior to the consideration of other income and expenses. Netback may not be comparable to similar measures used by other companies.

Overall Performance

Net income for the three month period ended June 30, 2009 was \$0.8 million versus \$4.4 million for 2008. Funds flow from (used in) operations decreased to \$4.6 from \$10.3 million in 2008. Working capital at June 30, 2009 was \$72.1 million versus \$75.8 million at December 31, 2008. Funds flow from operations is anticipated to finance the Company's capital program during 2009 without the requirement for external financing.

Business Environment

The Company's financial results are significantly influenced by fluctuations in commodity prices. The following table shows select market benchmark prices for 2008 and 2009:

	Q2 2009	Q1 2009	Q4 2008	Q3 2008	Q2 2008
Dated Brent average oil price (\$/bbl)	59.13	44.46	54.91	114.78	121.38

The price of Dated Brent oil averaged \$59.13/bbl in Q2 2009, a decrease of 51.3% from the Q2 2008 price of \$121.38/bbl. The price of Dated Brent oil reached a record high of \$144.23/bbl in July 2008. However, financial market instability and a worldwide recession resulted in a steep decline in the price of Dated Brent oil from August to December 2008. The closing price of Dated Brent oil at June 30, 2009 was \$68.06/bbl.

The current global financial crisis has reduced liquidity in financial markets, restricted access to financing and caused significant volatility in commodity prices. These factors will continue to impact the performance of the global economy going forward. Companies such as Calvalley, with no debt, strong cash generation from operations, and the availability of cash and cash equivalents, will be well positioned to manage through the crisis. Furthermore, Calvalley's approach is to operate within a balanced budget and the Company does not expect to incur long-term debt in the near future.

Canadian Oil and Gas Properties

The Company disposed of most of its Canadian oil and gas properties in 2004 and existing properties are comprised of a working interest in one property in Saskatchewan and some overriding royalties. The remaining Canadian properties are not material to the overall financial position and results of operations of the Company.

Comparability with Prior Periods

Revenue may fluctuate from year to year due to the timing of shipments of oil from the Ras Isa Oil Terminal. Revenue is recognized only when oil is loaded onto a tanker. In situations where the take-or-pay provisions of the crude marketing agreement take effect, the Company records a receivable and defers the related revenue until ownership transfers to the purchaser. Oil in storage at period-end is recorded as inventory at the average cost of production and depletion. At June 30, 2009, the Company's share of take-or-pay revenue was \$Nil. The Company's share of oil inventory at period end was \$0.4 million.

In April 2009, the Government of Yemen charged Calvalley \$1.1 million for facilities usage. All producers of crude oil in Yemen are subject to the Facility Usage Fee ("FUF"). The charge was applied retroactively from the commencement of production at Block 9 and was accrued in the first quarter 2009 financial statements. The portion of the charge related to deliveries that occurred prior to January 1, 2009 amounted to \$1.0 million. The balance of the charge in the amount of \$81,000 (\$0.40/bbl) related to oil that was delivered to the government facility during Q1 2009. The Company will continue to incur the \$0.40/bbl FUF in future periods. The FUF is recoverable from the Company's share of cost oil in accordance with the terms of the Production Sharing Agreement.

Block 9 Republic of Yemen – Exploration and Development Program

Joint Operating Agreement

Substantially all of Calvalley's operations and assets are related to its 50% working interest in the Block 9 Production Sharing Agreement ("PSA") with the Government of Yemen. Calvalley is the operator of Block 9 pursuant to the Joint Operating Agreement ("JOA") between Calvalley, HoodOil Ltd. ("HoodOil"), Reliance Industries Limited ("Reliance") and a subsidiary of the Yemen Oil and Gas General Corporation ("Yemen Co."), an entity owned by the Government of Yemen. Yemen Co.'s interest under the JOA consists of a 15% overriding royalty on the joint venture's allocation of profit oil under the PSA.

Production Sharing Agreement

The Company has a 50% working interest in Block 9. Oil and gas production from Block 9 is allocated between the Joint Venture (the "JV") and agencies of the Government of Yemen pursuant to the terms of the PSA. The Government of Yemen receives a 10% royalty in kind from all Block 9 production, after which the remaining oil production is shared between the JV and the Government of Yemen. The JV is first allocated up to 45% of gross production to recover capital and operating costs incurred in order to operate Block 9. To the extent that recoverable costs exceed 45% of the fair value of gross production, any excess costs are carried forward for recovery against future production. After deducting cost oil, the remaining profit oil is allocated between the Government of Yemen and the JV as follows:

- 39.23% of total profit oil to the JV (before deducting 35% income tax on JV's share of profit oil and after deducting 15% override to Yemen Co.); and
- 60.77% to the Government of Yemen (including Yemen Co.'s override and before including income tax on JV's share of profit oil).

Provided that total recoverable costs do not exceed 45% of gross production, the JV may recover operating costs during the year in which they are incurred and may deduct 50% of capital costs incurred during the year of expenditure and 50% during the following year.

As at March 31, 2009, the Company's share of capital costs to be carried forward for recovery against future production was approximately \$52 million. Until these costs have been recovered, together with future operating and capital costs that become eligible for recovery during that time period, the Company's net oil production will equal 31.33% of gross oil production (22.5% from cost oil and 8.83% from profit oil). Following full recovery of past operating costs, the Company's net oil production will range between 17.65% and 31.33% of gross oil production, which will vary depending upon prevailing crude oil selling prices and the capital and operating costs incurred by the JV. The Company's share of profit oil is subject to 35% income tax to the Government of Yemen.

Outlook

The Company's 2009 program is designed to debottleneck production by executing a marketing solution for all kinds of crudes discovered on Block 9 and continue to add reserves at attractive costs. While Calvalley has increased its production capability since the beginning of 2009, significant production was shut-in due to the lack of a marketing solution for all types of crude discovered in the block including the heavier oil at Al Roidhat. Calvalley expects to bring new production on stream in the late 2009/early 2010 by concluding the ongoing marketing efforts for all crudes from Block 9. With ongoing cooperation from the Government, Calvalley has made significant progress to gain access to an alternative export market which will take all of the Company's production. We are optimistic that our effort will result in the finalization of a marketing agreement by the end of 2009.

The budget was developed to maintain the strength of the Company's balance sheet by funding the entire capital expenditure program of approximately \$18 million with internally generated cash flow. The capital program calls for six horizontal development wells at Hiswah and two exploration wells: one at Ras Nowmah and one at Salmin prospects. However, the resolution of the marketing issue will enable the commencement of our contingent capital program which includes additional development wells at Hiswah and Roidhat and additional exploration wells.

Uncertainty surrounding crude oil marketing and low commodity prices eliminated drilling activities for the first half of 2009. However, we are now in the process of commencing both development and exploration drilling activities for the balance of 2009. The first well will be a development well at Hiswah (Hiswah 29) followed by the first exploration well at Ras Nowmah.

Encouraged by the progress of the marketing efforts, we have initiated the completion, testing, and equipping of four Al Roidhat wells, which were drilled in 2007 but not completed, to prepare the field for production upon the finalization of a marketing agreement.

In addition, the 2009 capital program focuses on unlocking the potential of deeper horizons (fractured basement and Kohlan sands) in the Qarn Qaymah area. Calvalley has moved all necessary production and testing equipment to the Qarn Qaymah 2 ("QQ-2") well site to re-test the fractured basement. After re-testing the fractured basement, we will move up-hole to perforate and test the Kohlan sands. We expect to start testing of QQ-2 before the end of August.

Major milestones are subject to factors noted in the Risk Factors section of this Management Discussion and Analysis. Milestones planned for the balance of 2009 include the following:

- Increase total production by concluding a marketing agreement for heavy crude from the Al Roidhat field;
- Complete the initial phase of the pressure maintenance program (water and gas injection) to commence full field development at Hiswah;
- Continue to add new reserves and production through new exploration and development;
- Fully evaluate the Qarn Qaymah discovery through additional testing of the fractured basement and completion of the Kohlan sands gas/condensate discovery;
- Commence drilling of six budgeted horizontal producers at the Hiswah Field;
- Develop an appraisal program in the Qarn Qaymah area, based on test results from QQ-2, which will include a 3D seismic program and future well locations;
- Commence the drilling of two exploration wells (Ras Nowmah and Salmin) on Block 9;
- High-grade the existing exploration portfolio of 42 prospects and leads;
- Undertake a gravity/magnetic survey at Metema and Gimbi blocks in Ethiopia; and
- Continue to take advantage of Calvalley's strong balance sheet and its international operating experience by continuing to evaluate the potential acquisition of additional assets in the Middle East and Africa.

Key Financial Indicators

Calvalley uses key financial indicators to help assess its business performance and manage its operations. These financial indicators measure business growth (revenue and capital expenditures), cash generation (EBITDA and funds flow from operations) and profitability (operating income and net income). These key financial indicators are discussed in more detail in the following sections.

Production

Substantially all of Calvalley's crude oil production in 2009 and 2008 came from the Hiswah oil field, which produces high-quality, lighter crude oil that is sold at prices comparable to the Dated

Brent crude oil reference price. All of the Company's crude oil production was trucked more than 250 kilometers to the Safer Exploration and Production Operations Co. processing facility on Block 18, where the crude oil was processed and shipped via pipeline to the Ras Isa marine terminal facility for export. During the second quarter of 2009, the Company's working interest oil production averaged 2,082 barrels of oil per day ("bopd") (2008 – 2,393 bopd), from which the Company was allocated 1,305 bopd net (2008 – 1,499 bopd) pursuant to the PSA. Production during the first quarter of 2009 recovered from the levels of the fourth quarter of 2008 as shut in production came on-stream as pumps became available. Fourth quarter 2008 production also suffered due to flooding during the month of October which essentially shut in the Hiswah field for four days. During the second quarter of 2009, production decreased. The decrease is attributable to the fact that the facility through which the Company sells its oil restricted the volumes of oil delivered by the Company. The restriction results from the facility seeking to achieve target sulfur content in the oil blend exiting the facility. Sulfur content had been increasing due to decreased production from other fields feeding the facility. The Company shut-in certain higher sulfur producing wells to meet the requirements of this externally imposed restriction. The Company is currently in negotiations to remove these restrictions to its production capacity. Notwithstanding the above, the Company's working interest oil production has improved in July 2009 and has averaged 2,179 bopd from which the Company was allocated 1,366 bopd.

The following table sets forth the Company's production and sales information for the periods indicated.

Production and sales information	2009			2008			
	2009 Total	Q2	Q1	2008 Total	Q4	Q3	Q2
Block 9 Oil Production (bopd)	4,347	4,164	4,532	4,522	3,989	4,743	4,759
Company working interest share (bopd)	2,174	2,082	2,266	2,261	1,994	2,372	2,380
Company net share (bopd) ⁽¹⁾	1,362	1,305	1,420	1,417	1,250	1,484	1,489
Company net production (mdbl)	247	119	128	518	115	137	135
Company net sales (mdbl) ⁽²⁾	322	211	111	431	36	141	130

(1) Company net share is equal to the working interest share less government share of production under the terms of the PSA before income taxes.

(2) Company net sales before income taxes varies from Company net production due to changes in inventory and shrinkage.

The following table sets forth the key financial indicators for 2009 and 2008.

Selected operating information (thousands of dollars)	2009			2008			
	2009 Total	Q2	Q1	2008 Total	Q4	Q3	Q2
Oil sales	24,112	17,252	6,860	74,686	4,060	25,082	25,434
Royalties	(9,266)	(6,566)	(2,700)	(28,440)	(1,609)	(9,534)	(9,643)
Operating expenses	(5,851) ⁽¹⁾	(3,738)	2,113 ⁽¹⁾	(7,741)	(837)	(2,045)	(2,841)
Current taxes	(1,484)	(1,066)	(418)	(4,622)	(257)	(1,550)	(1,572)
Netback ⁽²⁾	7,511	5,882	1,629	33,883	1,357	11,953	11,378

General and administration	(2,661)	(1,496)	(1,165)	(4,376)	(1,094)	(509)	(1,540)
EBITDA ⁽²⁾	5,504	5,548	(44)	34,682	691	13,178	11,504
Operating income (loss) ⁽²⁾	110	1,904	(1,794)	25,318	(13)	10,072	8,727
Net income (loss)	(1,280)	765	(2,045)	19,161	25	9,105	4,432
Capital expenditures	5,211	2,812	2,399	27,504	4,687	5,965	9,493
Funds flow from operations ⁽²⁾	4,495	4,644	(149)	31,131	414	12,050	10,266
Cash flow from operating activities	2,363	3,325	(962)	37,220	(1,661)	4,511	34,061

(1) For the purpose of calculating Netback, operating expenses in the first quarter of 2009 have been adjusted to exclude the portion of the Facility Usage Fee which relates to deliveries of crude oil prior to January 1, 2009 in the amount of \$1,025. See discussion on Operating Expenses for further details.

(2) See "Non-GAAP Measures".

Netbacks are calculated on barrels sold as government royalties, sales taxes and operating expenses are recognized when the underlying oil is sold. Government royalties and taxes taken in kind are attributed value at the price received by Calvalley for its production as follows:

(dollars per bbl)	2009			2008			
	2009 Total	Q2	Q1	2008 Total	Q4	Q3	Q2
Oil sales	46.97	51.30	38.75	108.23	70.50	111.12	123.60
Royalties	(18.07)	(19.53)	(15.28)	(41.67)	(27.58)	(42.75)	(47.41)
Operating expenses	(11.40)	(11.12)	(11.93) ⁽¹⁾	(11.22)	(14.53)	(9.06)	(13.81)
Current taxes	(2.90)	(3.17)	(2.39)	(6.69)	(4.36)	(6.87)	(7.64)
Netback ⁽²⁾	14.60	17.48	9.14	48.65	24.03	52.44	54.75

(1) For the purpose of calculating Netback, operating expenses in the first quarter of 2009 have been adjusted to exclude the portion of the Facility Usage Fee which relates to deliveries of crude oil prior to January 1, 2009 in the amount of \$5.79/bbl. See discussion on Operating Expenses for further details.

(2) See "Non-GAAP Measures".

Revenue

Calvalley recorded oil revenue of \$17.3 million during the three month period ended June 30, 2009 as compared to \$25.4 million for the three month period ended June 30, 2008. The significant decrease in revenue is primarily attributable to a 51.3% decrease in the average selling price realized in the second quarter of 2009 compared with the second quarter of 2008. Conversely, the Company recognized revenue on the sale of 336,244 barrels during the three months ended June 30, 2009 compared with 205,772 barrels in three months ended June 30, 2008 representing a 63.4% increase in volume. The increase in sales volume is attributable to the timing of lifts and is not correlated with production which was 189,478 in 2009 versus 217,790 in 2008.

For the six months ended June 30, 2009 oil revenues totaled \$24.1 million compared to \$45.5 million for the six months ended June 30, 2008.

Other Revenue

Other revenue, comprised primarily of interest revenue, amounted to \$0.3 million for the three months ended June 30, 2009 (2008 - \$0.4 million) and \$0.7 million for the six month period ended June 30, 2009 (2008 - \$1.0 million). Interest revenue resulted from maintaining significant cash reserves and GIC's throughout the period. Interest income has declined from 2008 due to reductions in interest rates. Interest rates on US denominated deposits declined as the Federal Reserve attempted to stimulate the US economy by reducing its borrowing rates.

Operating Expenses

Operating expenses during the second quarter of 2009 were \$3.7 million (\$11.12/bbl) as compared to \$2.8 million (\$13.81/bbl) for the three months ended June 30, 2008. Operating expenses for the six months ended June 30, 2009 were \$6.9 million (\$11.40/bbl) compared to \$4.9 million (\$11.95/bbl) for the six month period ended June 30, 2008.

During the first quarter of 2009, the Government of Yemen charged Calvalley \$1.1 million for facilities usage. All producers of crude oil in Yemen are subject to the Facility Usage Fee ("FUF"). The charge was applied retroactively from the commencement of production at Block 9. The portion of the charge related to deliveries that occurred prior to January 1, 2009 amounts to \$1.0 million and has been excluded from operating expenses for the purpose of this MD&A to maintain comparability of operating expenses by including the portion which represents a current charge and will be continued in future quarters. The balance of the charge in the amount of \$81,000 (\$0.40/bbl) relates to oil that was delivered to the government facility during the first quarter of 2009. The FUF is recoverable from the Company's share of cost oil in accordance with the terms of the Production Sharing Agreement.

As a result of the current global financial crisis and falling oil prices, the oil industry has cut back or delayed certain capital intensive projects, which may in turn lead to less demand and lower costs. Calvalley attempts to manage operating costs through competitive bidding, long term contracts and, recently, renegotiation of current contract terms, where possible.

Operating expenses for the second quarter include \$5.35 (2008 - \$4.68) per gross barrel for trucking costs, third party processing costs, and tariffs for use of pipeline and marine terminal facilities.

Netback

Netbacks for the quarter were \$17.48 per barrel compared to \$54.75 for 2008. Commodity price declines of \$62.25 per barrel are the main contributor to this decline. This is partially offset by the decline in royalties. The Company is implementing strict cost control measures in all of its operations to preserve the highest netbacks possible.

General and Administration

General and administration expenses, net of \$0.2 million that was capitalized into resource development costs, totaled \$1.5 million for the three month period ended June 30, 2009 which was consistent with \$1.5 million for the quarter ended June 30, 2008. For the six months ended June 30, 2009 general and administration costs were \$2.7 million compared to \$2.8 million during the six month period ended June 30, 2008. General and administrative costs directly associated with Block 9 become recoverable costs and will be recovered from revenue associated with cost oil under the terms of the PSA.

EBITDA

During the second quarter of 2009, the Company generated EBITDA of \$5.5 million compared with \$11.6 million during the second quarter of 2008. For the six month period ended June 30, 2009, EBITDA was \$5.5 million compared with 20.9 million in the corresponding period of 2008. The decrease is primarily related to the significant decrease in commodity prices during the first and second quarters of 2009 in comparison with the first and second quarters of 2008. The facility usage charge referred to above in the discussion on operating expenses was a major contributor to the negative EBITDA recognized in the first quarter. EBITDA is also impacted by the timing of lifts by the purchaser of the Company's crude oil.

Depletion and Depreciation

Calvalley recorded depletion, depreciation and accretion expenses of \$3.6 million for the three months ended June 30, 2009 as compared to \$2.8 million for the second quarter of 2008. The increase was caused by the sale of crude which was held in inventory at March 31, 2009. The provision was lower in the 2008 comparable period due to a buildup of inventory during the second quarter of 2008. Depletion relating to crude held in inventory is recognized as an expense in the period the inventory is sold. During the six month period ended June 30, 2009 depletion, depreciation and accretion expenses amounted to \$5.4 million (2008 - \$5.6 million). The decrease is primarily related to upward technical revisions to the Company's reserves as estimated by independent reserve engineers at December 31, 2008.

Operating Income

During the quarter, the Company generated operating income of \$1.9 million compared with operating income of \$8.7 million during the second quarter of 2008. During the six month period ended June 30, 2009 the Company generated operating income of \$0.1 million compared with operating income of \$15.3 million for the six months ended June 30, 2008. Operating income was impacted by the same factors as those affecting netbacks and EBITDA.

Foreign Exchange Loss

The Company recognized a small exchange loss of \$42,000 during the second quarter of 2009 compared with a loss of \$22,000 during the second quarter of 2008.

Income Taxes

Current income tax expense in the second quarter of 2009 amounted to \$1.1 million (2008 - \$1.6 million) and income tax for the six months ended June 30, 2008 was \$1.5 million (2008 - \$2.8 million). Current income tax represents taxes incurred and paid under the laws of Yemen pursuant to the PSA. The income tax is calculated as 35% of the Company's profit oil revenue in Yemen, and is paid by the Government of Yemen out of its portion of profit oil. As a result, income taxes are more closely correlated with revenue than with income before taxes.

Consolidated Cash Flow

Operating Activities

(thousands of dollars)	2009			2008			
	2009 Total	Q2	Q1	2008 Total	Q4	Q3	Q2
Funds flow from operations	4,495	4,644	(149)	31,131	414	12,050	10,266
Change in non-cash working capital	(2,132)	(1,315)	(817)	6,136	(2,081)	(7,445)	23,675
Unrealized foreign exchange gain(loss) relating to non-cash working capital	-	(4)	4	(48)	6	(94)	120
Cash provided by (used in) operations	2,363	3,325	(962)	37,219	(1,661)	4,511	34,061

As at June 30, 2009, the Company held cash and cash equivalents of \$12.4 million compared with \$21.0 million at the end of the preceding year. Additionally, the Company held Guaranteed Investment Certificates with an initial term of greater than 90 days in the amount of \$43.9 million (December 31, 2008 - \$42.7 million). The Company invests its cash reserves in Guaranteed Investment Certificates issued by an Alberta credit union guaranteed by the Province of Alberta.

Investing Activities

(thousands of dollars)	2009			2008			
	2009 Total	Q2	Q1	2008 Total	Q4	Q3	Q2
Additions to property, plant and equipment	(5,211)	(2,812)	(2,399)	(27,504)	(4,687)	(5,965)	(9,493)
Change in non-cash working capital	(2,728)	3,675	(6,403)	1,629	2,721	583	(1,163)
Net investment in GIC's	(1,127)	3,314	(4,441)	(37,719)	279	12,269	(23,513)
Cash provided by (used in) investing activities	(9,066)	4,177	(13,243)	(63,594)	(1,687)	6,887	(34,169)

During the second quarter of 2009, the Company made capital expenditures of \$2.8 million compared with \$9.5 million during the second quarter of 2008. During the quarter, the Company invested in the construction of additional facilities for water and gas injection and the blending of crude oil. Expenditures were also incurred to prepare the Al-Roidhat wells for production on the completion of marketing arrangements for the blended crude. Payments received from the Company's partners exceeded the Company's funding of expenditures on behalf of its partners in the amount of \$3.7 million during the quarter. The Company also converted GICs to cash in the three months ended June 30, 2009.

Financing Activities

(thousands of dollars)	2009			2008			
	2009 Total	Q2	Q1	2008 Total	Q4	Q3	Q2
Issuance of common shares	692	692	-	514	-	-	400
Common share repurchase	(2,556)	(1,462)	(1,094)	(4,822)	(371)	(2,098)	(2,353)
	(1,864)	(770)	(1,094)	(4,308)	(371)	(2,098)	(1,953)

During the six months ended June 30, 2009, the company repurchased 2,260,970 Class A Common Voting Shares on the open market pursuant to its normal course issuer bid at a total cost of \$2.6 million. Proceeds from the issuance of Class A Common Voting Shares was related solely to the exercise of stock options and totaled \$0.7 million.

Consolidated Financial Position

(thousands of dollars)	2009		2008		
	Q2	Q1	Q4	Q3	Q2
Cash and cash equivalents	12,420	5,697	20,989	24,414	15,151
Guaranteed Investment Certificate	43,873	47,187	42,746	43,025	55,294
Accounts receivable	2,570	2,302	3,296	4,144	5,544
Prepaid expenses	259	280	281	262	351
Due from joint venture partners	20,058	22,719	18,419	19,565	14,144
Oil inventory	379	3,621	2,995	240	684
Property and equipment	84,634	83,887	83,863	80,876	77,929
Total Assets	164,193	165,683	172,406	172,526	169,097

As at June 30, 2009, the Company's total assets were \$164.2 million, a decrease of \$8.2 million from December 31, 2008. Cash and cash equivalents amounted to \$12.4 million compared with \$21.0 million at the beginning of the year.

During the three months ended June 30, 2009, accounts receivable increased by \$0.3 million to \$2.6 million. The balance at June 30, 2009 primarily relates to revenue receivable and due in July 2009 from oil sold during June 2009. Amounts due from joint venture partners increased from \$18.4 million at the beginning of the year to \$20.1 million as at June 30, 2009. Management is working with the JV partners to decrease this receivable.

Oil inventory decreased from \$3.0 million at the beginning of the year to \$0.4 million because most of 2009's production was lifted by June 30, 2009. The oil inventory relates to oil production in storage at the end of the quarter, valued at the average cost of production.

Property, plant and equipment increased to \$84.6 million as at June 30, 2009 compared with \$83.7 million at the end of December 2008. The increase in property, plant and equipment resulted from capital expenditures of \$5.2 million, which was partially offset by depletion, depreciation and amortization expense of \$5.4 million less the \$1.1 million in net adjustments to depletion related to oil in inventory.

(thousands of dollars)	2009		2008		
	Q2	Q1	Q4	Q3	Q2
Accounts payable and accrued liabilities	7,500	7,554	9,693	12,703	15,992
Deferred revenue	-	1,653	3,255	-	-
Share Capital	116,671	116,888	118,243	118,697	119,400

Accounts payable and accrued liabilities decreased to \$7.5 million as at June 30, 2009, compared with \$9.7 million as at December 31, 2008. The primary reason for this decrease is related to the reduction in capital spending due to the completion of the Central Processing Facility and reduced capital spending on drilling operations during the first and second quarters.

Share capital decreased to \$116.7 million as at June 30, 2009 from \$118.2 million as at the end of 2008 as a result of the repurchase of Common Shares through the Company's normal course issuer bid partially offset by the issuance of Common Shares pursuant the exercise of stock options.

Liquidity and Capital Resources

Calvalley's principal source of liquidity has been funds flow from operations. Calvalley manages its liquidity risk by regularly monitoring its cash flows from operating activities and holding adequate amounts of cash and cash equivalents. The Company does not invest its funds in speculative securities. The 2009 budget is expected to be funded from cash flow from operations and existing cash resources. Should the prevailing Brent Crude price continue to be depressed for the balance of 2009, Calvalley has sufficient flexibility in its capital budget to adjust capital expenditures to ensure they continue to be funded by internally generated cash flow. Fluctuations in commodity prices, product demand, foreign exchange rates, interest rates and various other risks relating to factors beyond the control of Calvalley may impact capital resources.

Calvalley has no outstanding bank debt or other interest bearing indebtedness as at June 30, 2009. The Company has not arranged any undrawn operating lines of credit with any financial institution as the Company intends to fund its near-term capital expenditure programs from available cash on hand, funds flow from operations and, if required, from the issuance of additional share capital.

As at June 30, 2009, the Company's total assets were \$164.2 million, a decrease of \$8.2 million from December 31, 2008. Cash and cash equivalents amounted to \$12.4 million compared with \$21.0 million at the beginning of the year. Cash equivalents are invested with high quality financial institutions with terms to maturity of less than three months. Additionally, the Company held GIC's with an initial term of greater than 90 days. Total cash and cash equivalents plus GIC's decreased from \$63.7 million at December 31, 2008 to \$56.3 million at June 30, 2009.

Interest rates on US denominated funds have decreased substantially over the past year as the Federal Reserve attempts to stimulate the US economy by reducing its borrowing rates. Most of Calvalley's funds are deposited at a credit union where deposits are guaranteed by the Government of Alberta.

As at June 30, 2009 the Company's working capital was \$72.1 million as compared to \$75.8 million as at December 31, 2008.

At December 31, 2008 the Company had Canadian tax pools of approximately \$28.2 million of which \$10.8 million were non-capital losses, \$5.6 million were Canadian resource tax pools, \$8.4 million were undepreciated capital cost allowance and \$3.4 million were deferred financing costs. No provision has been made to record these pools as an asset because the Company is not likely to take advantage of them due to the insignificance of its Canadian operations and assets.

The Company has no long-term contractual obligations in Canada other than an operating lease for office space of approximately \$0.3 million in 2009 and \$0.2 million in 2010. Its long-term commitments regarding its Yemen property include its 50% proportionate share of government allowances and bonuses payable under the terms of the PSA of \$0.45 million per year, plus its 50% proportionate share of certain other bonus payments of \$2 million, \$3 million and \$4 million when and if sustainable production exceeds 25,000, 75,000 and 100,000 barrels of oil per day, respectively.

Calvalley entered into its first Production Sharing Contract ("PSC") with the Ethiopian Government for the exploration, development and production of petroleum resources in the Gimbi and Metema blocks under a single contract covering a total area of over 46,470 square kilometers (11.5 million acres). Both blocks are located in the western part of the country, adjacent to the Sudan border. As part of the PSC, the Company has entered into certain commitments to spend approximately \$8.5 million during the first four years of its work program.

Calvalley had no off balance sheet arrangements as at June 30, 2009 or at December 31, 2008.

Economic Sensitivities

The following table shows the estimated after-tax effect that changes to crude oil prices, gross crude oil production, operating costs and interest rates would have had on Calvalley's net income for the three month period ended June 30, 2009, had these changes occurred on January 1, 2009. These calculations are based on business conditions, production and sales volumes existing for the current period. The 1,000 bopd increase assumes the increase is to gross field production and that all incremental production was sold at the price received during the quarter, and Calvalley's entitlement is calculated according to the provisions of the PSA and JOA.

Economic Sensitivities	Change (+)	Net Income impact (US\$ millions)	Net Income impact (\$ per basic share)
Average realized price	\$10.00/bbl	1.6	0.02
Crude oil production (gross at field level)	1,000 bbls/d	2.3	0.02
Operating expenses	\$1.00/bbl	(0.5)	(0.01)
Interest rate	1%	0.1	0.00

The impact of the above changes may be compounded or offset by changes to other business conditions. In addition, the table does not reflect any inter-relationships between the above factors. Changes in the foreign exchange rates have not been considered in this analysis.

Related Party Transactions

On June 10, 2009 the Company advanced \$113,000 to a director for the exercise of options. The advance, which is included in accounts receivable is non-interest bearing, repayable within 90 days, and is secured by shares of the Company.

Risk Factors

Calvalley is exposed to a number of risks inherent in exploring for, developing and producing oil and gas. This section describes the risks and other matters that would be most likely to influence an investor's decision to purchase securities of Calvalley.

Calvalley manages a number of risks in its business in order to achieve an acceptable level of risk without hindering the ability to maximize returns. Management has adopted procedures to identify and manage significant operational and financial risks.

Commodity Risk

Calvalley's principal business is the production and sale of crude oil. Revenues, earnings and cash flows from the sale of crude oil are sensitive to change in market prices, over which the Company has little or no control. The Company has the ability to address its price related exposures through the limited use of options, future and forward contracts, but generally does not enter into such arrangements.

Currency Fluctuations

Calvalley undertakes transactions in currencies other than the United States dollar. The Company's primary foreign exchange risk is to changes in the value of the Canadian dollar relative to the United States dollar. Fluctuations in exchange rates between the United States dollar and other currencies will give rise to foreign currency exposure, either favourable or unfavourable, which may have material affects on the Company's operations and financial condition. The Company has the ability to address its currency related exposures through the use of foreign exchange contracts. It generally does not enter into such hedging arrangements but maintains a portion of its currency in Canadian dollars to meet its Canadian dollar requirements.

Interest Rates

The Company has no interest bearing debt. The Company invests surplus cash balances in short-term investments with recognized Canadian financial institutions. Fluctuations in interest rates, either favourable or unfavourable, may have material affects on the Company's interest income on short-term cash investments.

Credit risk and concentration of sales risk

In January 2007, the Company entered into a long-term crude oil marketing agreement under which the Company sells all of its crude oil production to a single purchaser for a period of eighteen months. The purchaser is a subsidiary of Reliance Industries Limited, India's largest business enterprise, which is a party to the JOA for Yemen Block 9. The purchaser's obligations under the crude oil marketing agreement are guaranteed by Reliance Industries Limited, which has been assigned credit ratings of Baa2 Stable Outlook by Moody's and BBB Stable Outlook by S&P (above Sovereign Rating). The contract was extended in April 2009 for an additional period which expires in June, 2010 and can be extended for additional twelve month periods if agreed by the Company and the purchaser.

Credit risk also relates to the risk that joint venture partners may not fulfill their contractual obligations for financial contributions towards exploration, development, appraisal and production operations.

During the initial agreement negotiations and ratification, these risks are considered and incorporated into the terms of the applicable contracts. Furthermore, cash calls can be made in advance of incurring costs to help ensure costs are recovered. However, it is possible that the interest of Calvalley and its joint venture partners are not aligned resulting in project delays, additional costs or disagreements, which could adversely affect business results.

Insurable Risk

Calvalley employs risk management practices to reduce and mitigate operational risks and other hazard risks and exposures, although it is impossible to completely protect its operations from all such risks. The Company places types and an amount of insurance that it considers consistent with industry practice to the extent coverage is available and cost effective. Such coverage includes third-party liability insurance and property and business interruption insurance.

The Company may become liable for damages arising from unforeseen events which it cannot insure against or chooses to self-insure. Costs incurred to repair such uninsured damage or to pay associated liabilities may have a material effect on the financial condition of the Company.

Legal Contingencies

The Company has been named in a claim filed in the Commercial Court of Yemen by a Saudi Arabian company. The claimant alleges that, pursuant to an agency agreement entered into in 1996, it is entitled to a percentage of the net profit attributable to the Company. The matter was heard and a ruling was made which awarded the claimant 10% of the Company's profit oil, calculated as being the oil produced in excess of the production that the Company is entitled to for cost recoveries as defined in the PSA, from the production of Block 9 from the date of commercial production to February 13, 2008.

The decision of the Commercial Court of Yemen is now under appeal by both parties. The Company's legal advisors in Sana'a and Calgary are pursuing the appeal jointly. The outcome of the action in the Yemen Commercial Court of Appeal is undeterminable at this time. No amounts have been accrued in the financial statements for the year ended December 31, 2008 as the ultimate resolution is uncertain. The Company will record any amounts due once the outcome of the contingency is likely and estimable.

As the ruling now stands, management does not anticipate a material impact on the Company. Both parties have appealed the ruling and the final decision of the Yemen Commercial Court of Appeal could vary significantly from the ruling of the lower court.

Concentration of Producing Assets

Substantially all of Calvalley's production is generated from highly productive individual wells in Yemen. The production and sale of crude oil in Yemen involves the use of central production facilities, oil pipelines, and export terminals, either operated by the Company or by third parties. As significant production is generated from each of these assets, any single event causing an interruption to any one of these operations could result in the loss of production and reserves as a result.

Exploration, Development and Production Risks

Acquiring, developing and exploring for oil and natural gas involves many risks which include but are not limited to encountering unexpected formations or pressures, premature declines of reservoirs, blow-outs, well bore collapse, equipment failures and other accidents, craterings and sour gas releases, uncontrollable flows of oil, natural gas or well fluids, and environmental risks.

In many oil and natural gas producing countries, oil and gas properties, together with related production and transportation infrastructure, are often situated in remote areas. In addition to the operational risks described above, oil and gas properties in some of these countries may be vulnerable to premeditated acts of violence which have the potential to cause significant damage to oil and gas operations and injury to personnel. The Company relies on the Government of Yemen's support in providing appropriate security for crude oil operations in Block 9.

Calvalley may not be fully insured against all of these risks. Losses resulting from the occurrence of these risks could have a material impact on the Company's financial results.

Reserve Additions

Calvalley's future crude oil reserves and production, and therefore its operating cash flows and results of operations, are highly dependent upon the Company's success in exploiting its current

reserve base and acquiring or discovering additional reserves. Without reserve additions through exploration, development or acquisitions, the Company's reserves and production will decline over time as reserves are produced. The business of exploring for, developing or acquiring reserves is capital intensive. To the extent cash flows from operations are insufficient and external sources of capital become limited or unavailable, Calvalley's ability to make the necessary capital investments to maintain and expand its oil and reserves will be impaired.

Environment, Health, Safety and Regulatory Approvals

Environmental, health and safety laws and regulations are continually evolving. Compliance with such laws and regulations can require significant expenditures which may materially affect the Company's financial condition or results of operations.

Expansion of existing operations and the development of new operating sites generally require approval of regulatory authorities. If such approvals are delayed or not achieved, the Company's ability to meet project schedule or cost objectives or to operate at expanded or existing levels could be materially impacted.

Workplace health and safety risks for workers arise from the inherent nature of the Company's operations and the jurisdictions within which it operates.

Competition

There is strong competition relating to all aspects of the oil and gas industry. Calvalley actively competes for skilled industry personnel which are in high demand, particularly at its Canadian headquarters, with a substantial number of other oil and gas companies, many of which have significantly greater financial and other resources.

Changes in Legislation

There can be no assurance that laws and regulations relating to the oil and gas industry will not be changed in a manner which would adversely affect the operations of the Company. Under the PSA, the Company is not obligated to comply with regulatory changes that are inconsistent with the provisions of the PSA. Further, the PSA stipulates that the interests, rights and obligations of the Government of Yemen and the Company shall be solely governed by the provisions of the PSA unless altered or amended by mutual agreement. In particular, the PSA requires that the Government of Yemen pay profit taxes on the Company's behalf, out of the Government of Yemen's share of profit oil.

Selected Quarterly Information

(\$000)	Revenue	Expenses	Net Income (Loss) for the Period	Earnings (Loss) per Basic Share	Earnings (Loss) per Diluted Share	Total Assets	Long Term Debt
2009							
Second quarter	10,973	9,100	765	\$0.01	\$0.01	164,193	-
First quarter	4,543	6,210	(2,045)	(\$0.02)	(\$0.02)	165,683	-
2008							
Fourth Quarter	2,901	2,617	25	\$0.00	\$0.00	172,406	-
Third Quarter	16,066	5,370	9,105	\$0.10	\$0.10	172,526	-
Second Quarter	16,242	10,134	4,432	\$0.03	\$0.03	169,097	-
First Quarter	13,150	6,149	5,599	\$0.06	\$0.06	158,833	-
2007							
Fourth Quarter	21,858	10,614	10,322	\$0.10	\$0.10	162,730	-
Third Quarter	15,194	6,858	7,907	\$0.08	\$0.08	151,325	-

The past eight quarters have witnessed the stabilization of Calvalley's business. The Company continues to develop the field and build related infrastructure. The Company has invested in significant studies of the existing pools and exploration areas of Block 9 and expects to increase production during 2009 as a result of this groundwork. Volatility of revenue amounts can be caused by the timing of loading crude oil onto tankers (See "Comparability with Prior Periods").

Measurement Uncertainty

The preparation of consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and revenue and expenses during the reporting period. Actual results, including petroleum and natural gas sales, royalties and operating expenses can differ from these estimates.

In particular, amounts recorded for depreciation and depletion and amounts used for ceiling test calculations are based on estimates of petroleum and natural gas reserves and future costs required to develop those reserves. The Company's reserve estimates are evaluated annually by an independent engineering firm. By their nature, these estimates of reserves and the related future cash flows are subject to measurement uncertainty and the impact on the

consolidated financial statements of future periods could be material.

Computations of provisions and estimates for income taxes involve management making judgments with respect to interpretation of tax regulations and related legislation which is continually changing. In addition, there are tax matters that have not yet been confirmed by taxation authorities. While management believes the provision for income taxes is adequate, these amounts are subject to measurement uncertainty. Adjustments required, if any, to these provisions will be reflected in the period where it is determined that adjustments are warranted.

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options which were fully tradable with no vesting restrictions. This option valuation model requires the input of highly subjective assumptions including the expected stock price volatility. Because the Company's stock options and warrants have characteristics significantly different from those of traded options and because changes in the subjective input assumptions can materially affect the calculated fair value, such value is subject to measurement uncertainty.

Amounts recorded as due from joint venture partners are based on the Company's interpretation of underlying agreements and may be subject to joint approval. The Company has recorded balances due based on costs incurred and its interpretation of allowable expenditures. Any adjustments required as a result of joint venture audits are recorded in the period of settlement with joint venture partners.

Additional Information

As at June 30, 2009, the Company had 98.5 common shares outstanding. Additionally, there were 4.2 million options outstanding which were issued pursuant to the Company's stock option plan.

Disclosure Controls and Procedures

Disclosure Controls and Procedures ("DC&P") are designed to provide reasonable assurance that information required to be disclosed is recorded, processed, summarized and reported within the time periods specified in applicable securities legislation, and include controls and procedures designed to ensure that information required to be disclosed is accumulated and communicated to management, including the CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

As at June 30, 2009, an evaluation of the design of the Company's DC&P was carried out under the supervision of, and with the participation of management including its certifying officers. Based on that evaluation, the Company's certifying officers concluded that the design of the Company's DC&P was effective as at June 30, 2009 and would provide reasonable assurance that material information relating to the Company and its consolidated subsidiaries would be made known to them by others within those entities during the period in which the interim filings were prepared, and that information required to be disclosed by the Company would be recorded, processed, summarized and reported within the time periods specified under applicable securities legislation.

Internal Controls over Financial Reporting

Internal Controls over Financial Reporting ("ICFR") are designed to provide reasonable

assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with Canadian GAAP. ICFR can only provide reasonable assurance and may not prevent or detect misstatements. Projections of an evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate due to changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate. As at June 30, 2009, an evaluation of the design of the Company's ICFR was carried out under the supervision of, and with the participation of management including its certifying officers. Based on that evaluation, the Company's certifying officers concluded that the design of the Company's ICFR was effective as at June 30, 2009 and would provide reasonable assurance that material weaknesses in ICFR would be made known to them, and reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP.

EFFECT OF FUTURE CHANGES IN ACCOUNTING POLICIES

International Financial Reporting Standards ("IFRS")

In February 2008, the Accounting Standards Board confirmed that all Canadian publicly accountable enterprises will be required to adopt IFRS for interim and annual reporting purposes for fiscal years beginning on or after January 1, 2011. Calvalley is continually assessing the impact of the convergence of Canadian GAAP with IFRS on the Company's results of operations, financial position and disclosures. Under the direction and oversight of the Board of Directors and Audit Committee, the Company has assembled a project team to manage the transition and to ensure successful implementation within the required time frame.

The Company recognizes that the changeover to IFRS has complex implications on a combination of accounting, financial reporting, IT and business systems. Consequently, senior management has engaged external consultants to conduct a Business Impact Study, to assist in the development a Project Plan, and to provide assistance in considering various accounting policy decisions which will be required throughout the transition period. Company personnel involved with the transition project have also received appropriate training and education.

The overall IFRS transition project consists of 5 phases: (i) Scope; (ii) Plan; (iii) Design and Build; (iv) Implement; (v) Review. The Scope phase, which consisted primarily of identifying the significant differences between Canadian GAAP and IFRS has been completed. The Company has concluded that the following key issues are expected to have the most significant impact on Calvalley's results of operations, financial position and disclosures:

- IFRS 1 – First-time adoption of International Financial Reporting Standards;
- IFRS 6 – Exploration and evaluation of mineral resources;
- IFRS 16 – Property, Plant and Equipment;
- IAS 36 – Impairment of assets;

The Company is currently in the Planning phase. During this phase, the Company is gathering information and financial data to assess the potential impacts of the differences identified during the Scoping phase. The IFRS project team is also developing recommendations for IFRS policy decisions which are based on appropriately documented consideration of the following factors:

- Impact on financial and key performance indicators;
- Impact on information technology and systems;
- Impact on the internal control and disclosure control frameworks;

- Transition and maintenance costs;
- Impact on communications with key stakeholders;
- Other general business impacts.

The Company anticipates completion of the Planning phase by the end of 2009 and will provide additional disclosures of the key elements of its plan and progress of the project as the information becomes available.

NORMAL COURSE ISSUER BID

On April 21, 2009, the Company made the necessary filings, and received the necessary approvals, to make a normal course issuer bid through the facilities of the Toronto Stock Exchange commencing April 23, 2009 and ending April 22, 2010, or on such earlier date as Calvalley may complete its purchases under the bid. A copy of the notice filed with the Toronto Stock Exchange can be obtained by any shareholder of the Company, without charge, by contacting the Company.

A total of 4,948,029 Class A Common Shares (the "Common Shares") may be acquired under the bid, representing 5% of the 98,960,580 Common Shares outstanding as of April 15, 2008. Calvalley will acquire Common Shares under the bid at the market price at the time of purchase, and all Common Shares acquired will be canceled. Unless Calvalley is utilizing a Block Purchase Exemption as permitted by the TSX, purchases are subject to a daily purchase restriction equal to 25% of the average daily trading volume of the Common Shares over the past six calendar months, or a maximum of 28,824 Common Shares per trading day.

In the opinion of Calvalley's Board of Directors, Calvalley's Common Shares are, from time to time, undervalued by the market, and the cost of acquiring the shares is an expense prudently incurred by Calvalley to increase shareholder value.

A total of 983,448 shares have been acquired to August 11, 2009 under the bid.

**Calvalley Petroleum Inc.
Consolidated Financial Statements
For the Three and Six Months Ended
June 30, 2009 and 2008
(Expressed in United States Dollars)**

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Calvalley Petroleum Inc.
CONSOLIDATED BALANCE SHEETS
(Unaudited - Expressed in United States Dollars)

(\$000)	June 30, 2009 \$	December 31, 2008 \$
ASSETS		
Current		
Cash and cash equivalents [note 3]	12,420	20,989
Guaranteed Investment Certificate [note 4]	43,873	42,746
Accounts receivable	2,570	3,293
Prepaid expenses	259	281
Due from joint venture partners [note 5]	20,058	18,419
Oil inventory [note 6]	379	2,995
	79,559	88,723
Property, plant and equipment [note 7]	84,634	83,683
	164,193	172,406
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Accounts payable and accrued liabilities	7,500	9,693
Deferred revenue	-	3,255
	7,500	12,948
Commitments and contingency [note 15]		
Shareholders' equity		
Share capital [note 8]	116,671	118,243
Contributed surplus [note 9]	6,859	6,772
Accumulated other comprehensive income	3,963	3,963
Retained earnings	29,200	30,480
	156,693	159,458
	164,193	172,406

See accompanying notes

On behalf of the Board:

"Signed"

Edmund Shimoon

"Signed"

Gary Robertson

Calvalley Petroleum Inc.
CONSOLIDATED STATEMENTS OF OPERATIONS
AND RETAINED EARNINGS
(Unaudited - Expressed in thousands of US Dollars)

(\$000)	Three months ended June 30		Six months ended June 30	
	2009 \$	2008 \$	2009 \$	2008 \$
REVENUE				
Oil sales	17,252	25,434	24,112	45,544
Royalties	(6,566)	(9,643)	(9,266)	(17,297)
	10,686	15,791	14,846	28,247
Management fees	96	94	195	198
Interest and other	191	274	475	818
	10,973	16,159	15,516	29,263
EXPENSES				
Operating	3,738	2,841	6,876	4,859
General and administration, net of recoveries	1,496	1,540	2,661	2,773
Stock-based compensation	222	2,976	379	3,097
Depletion, depreciation and accretion	3,644	2,777	5,394	5,554
	9,100	10,134	15,310	16,283
Income before other items	1,873	6,025	206	12,980
Foreign exchange loss	(42)	(22)	(2)	(135)
Income before income tax	1,831	6,003	204	12,845
Income tax	1,066	1,571	1,484	2,814
Net income (loss) and comprehensive income (loss)	765	4,432	(1,280)	10,031
Retained earnings, beginning of period	28,435	19,949	30,480	14,350
Common share repurchases	-	(1,618)	-	(1,618)
Retained earnings, end of period	29,200	22,763	29,200	22,763
Earnings (loss) per share [note 13]				
Basic	\$0.01	\$0.03	(\$0.01)	\$0.09
Diluted	\$0.01	\$0.03	(\$0.01)	\$0.09

See accompanying notes

Calvalley Petroleum Inc.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited - Expressed in United States Dollars)

	Three months ended		Six months ended	
	June 30		June 30	
	2009	2008	2009	2008
<i>(\$000)</i>	\$	\$	\$	\$
OPERATING ACTIVITIES				
Net income (loss) for the period	765	4,432	(1,280)	10,031
Add (deduct) items not affecting cash:				
Stock based compensation	222	2,976	379	3,097
Depletion, depreciation and accretion	3,644	2,777	5,394	5,554
Unrealised foreign exchange gain (loss)	13	81	2	(15)
	4,644	10,266	4,495	18,667
Change in non-cash working capital [note 11]	(1,315)	23,675	(2,132)	15,663
Unrealized foreign exchange loss (gain) relating to non- cash working capital	(4)	120	-	40
	3,325	34,061	2,363	34,370
INVESTING ACTIVITIES				
Additions to property, plant and equipment	(2,812)	(9,493)	(5,211)	(16,852)
Change in non-cash working capital [note 11]	3,675	(1,163)	(2,728)	(1,675)
Investment in GIC	(9,024)	(28,540)	(62,804)	(55,294)
Redemption of GIC	12,338	5,027	61,677	5,027
	4,177	(34,169)	(9,066)	(68,794)
FINANCING ACTIVITIES				
Issuance of share capital [note 8]	692	399	692	514
Common share repurchase [note 8]	(1,462)	(2,353)	(2,556)	(2,353)
	(770)	(1,954)	(1,864)	(1,839)
Foreign exchange gain on cash and cash equivalents held in foreign currencies	(9)	(199)	(2)	(27)
Increase (decrease) in cash and cash equivalents	6,723	(2,264)	(8,569)	(36,290)
Cash and cash equivalents, beginning of period	5,697	17,412	20,989	51,441
Cash and cash equivalents, end of period	12,420	15,151	12,420	15,151

See accompanying notes

1. BASIS OF PRESENTATION

The interim consolidated financial statements include the accounts of Calvalley Petroleum Inc. and its subsidiaries ("Calvalley" or the "Company") for the three and six month periods ended June 30, 2009 and 2008 are presented in accordance with Canadian generally accepted accounting principles on the same basis as the audited consolidated financial statements as at and for the year ended December 31, 2008, except as outlined in Note 2. These interim consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto in Calvalley's annual report for the year ended December 31, 2008 as the disclosures in these interim financial statements do not conform in all respects to the requirements of generally accepted accounting principles for annual financial statements. In these interim consolidated financial statements, unless otherwise indicated, all dollars are expressed in thousands of United States (US) dollars. All references to US\$ or to \$ are US dollars and references to C\$ are to Canadian dollars.

2. CHANGES IN ACCOUNTING POLICIES

On January 1, 2009 the company adopted CICA Handbook Section 3064, "Goodwill and Intangible Assets" which replaced Section 3062, "Goodwill and Other Intangible Assets" and Section 3450, "Research and Development Costs". Section 3064 incorporates guidance addressing when an internally developed intangible asset meets the criteria for recognition as an asset. The adoption of this standard did not impact the Company's consolidated financial statements.

Effective January 1, 2009 the Company adopted EIC 173, "Credit Risk and the Fair Value of Financial Assets and Financial Liabilities". This abstract concludes that for all financial assets and liabilities measured at fair value an entity's own credit risk and the credit risk of the counterparty should be taken into account when determining the fair values of financial assets and financial liabilities, including derivative instruments. The adoption of this abstract did not impact the Company's consolidated financial statements.

In June 2009, the CICA issued amendments to CICA Handbook Section 3862, Financial Instruments — Disclosures. The amendments include enhanced disclosures related to the fair value of financial instruments and the liquidity risk associated with financial instruments. The amendments will be effective for annual financial statements for fiscal years ending after September 30, 2009. The amendments are consistent with recent amendments to financial instrument disclosure standards in IFRS. The Company will include these additional disclosures in its annual consolidated financial statements for the year ending December 31, 2009.

3. CASH AND CASH EQUIVALENTS

Cash and cash equivalents at June 30, 2009 include various short-term deposits of \$6,943 (2008 - \$4,882), bearing interest at 0.35% to 0.5% (2008 - 1.85% to 1.90%) and maturing from July 18, 2009 to July 29, 2009 and \$5,477 (2008 - \$10,269) of cash.

Calvalley Petroleum Inc.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited - Expressed in thousands of United States Dollars)

4. GUARANTEED INVESTMENT CERTIFICATE

Guaranteed investment certificates ("GIC") with original maturity dates in excess of 90 days at June 30, 2009 have been excluded from cash and cash equivalents.

Maturity	Face Value \$	Interest Rate %
December 10, 2009	10,111	2.25
January 16, 2010	6,127	1.50
September 21, 2009	27,344	1.50

The GIC's are carried at cost plus interest, which approximates fair value and can be redeemed at any time without penalty.

5. DUE FROM JOINT VENTURE PARTNERS

Amounts due from joint venture partners are comprised primarily of amounts due for operating costs and capital expenditures. The balances are due under normal trade terms.

6. OIL INVENTORY

Inventory sold is expensed through production and depletion expenses in the period when it is sold. During the six months ended June 30, 2009, \$2,995 (2008 - \$71) was expensed with respect to oil which was sold.

7. PROPERTY, PLANT AND EQUIPMENT

	June 30, 2009		
	Cost \$	Accumulated Depletion and Depreciation \$	Net Book Value \$
(\$000)			
Canada			
Oil and gas properties and equipment	128	74	54
Other capital assets	293	135	158
	421	209	212
Yemen			
Oil and gas properties	116,250	32,296	83,954
Ethiopia			
Oil and gas properties	468	-	468
	117,139	32,505	84,634

Calvalley Petroleum Inc.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited - Expressed in thousands of United States Dollars)

7. PROPERTY, PLANT AND EQUIPMENT (Continued)

(\$000)	December 31, 2008		
	Cost \$	Accumulated Depletion and Depreciation \$	Net Book Value \$
Canada			
Oil and gas properties	128	67	61
Other capital assets	269	120	149
	397	187	210
Yemen			
Oil and gas properties	111,190	28,059	83,131
Ethiopia			
Oil and gas properties	342	-	342
	111,929	28,246	83,683

Yemen

The Company has a 50% working interest in the Malik Block 9 Joint Venture in Yemen. The Company's right to produce crude oil under the Production Sharing agreement ("PSA") continues to 2025, with a provision for a 5 year extension. The ownership of all assets, tangible and intangible, remains with the Yemen authority.

During the six months ended June 30, 2009, the Company capitalized overhead costs relating to oil and gas exploration and development activities of \$626 (2008 - \$1,886). The Company excluded from capital costs subject to the depletion expense calculation an amount of \$Nil (2008 - \$14,692) in respect of the capital costs incurred for processing facilities under construction. Costs related to processing facilities have been included in costs subject to depletion in December 2008 which is the date when the facilities were available for use.

Ethiopia

During 2008, the Company signed a Production Sharing Contract ("PSC") with the Ethiopian Government on the Metema and Gimbi Blocks covering a total area of 11.5 million acres.

Properties in Ethiopia are unproven and the costs incurred of \$368 (2008 - \$Nil) have been excluded from costs subject to depletion and depreciation.

Canada

Existing properties are comprised of a working interest in one property in Saskatchewan and overriding royalties.

Calvalley Petroleum Inc.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited - Expressed in thousands of United States Dollars)

8. SHARE CAPITAL

a. Common shares

Authorized:

Unlimited number of Class A Common Voting Shares.

Issued:

Six month period ended June 30, 2009	Number	Amount (\$000s)
Class A Common Voting Shares		
Shares outstanding, beginning of period	100,265,602	118,243
Issued on the exercise of options (i)	500,000	692
Contributed surplus reclassified on exercise of options (i)	-	406
Repurchased and cancelled (ii)	(2,260,970)	(2,670)
Balance, end of period	98,504,632	116,671

- (i) The Company issued 500,000 Class A Common Voting Shares upon the exercise of options for proceeds of \$692. An amount of \$406 related to stock based compensation expensed in prior years was reclassified from contributed surplus to share capital in connection with options exercised in 2009.
- (ii) The Company repurchased 2,260,970 Class A Common Voting Shares pursuant to a Normal Course Issuer Bid at a net cost of \$2,556. The cost to repurchase shares at prices below their average book value has been credited to contributed surplus.

Year ended December 31, 2008	Number	Amount (\$000)
Class A Common Voting Shares		
Shares outstanding, beginning of year	101,430,498	119,485
Issued on the exercise of options (i)	440,000	514
Contributed surplus reclassified on exercise of options (i)	-	137
Repurchased and cancelled (ii)	(1,604,896)	(1,893)
Balance, end of year	100,265,602	118,243

- (i) The Company issued 440,000 Class A Common Voting Shares upon the exercise of options for proceeds of \$514. An amount of \$137 related to stock based compensation expensed in prior years was reclassified from contributed surplus to share capital in connection with options exercised in 2008.
- (ii) The Company repurchased 1,604,896 Class A Common Voting Shares pursuant to a Normal Course Issuer Bid at a cost of \$4,822. The cost to repurchase common shares at prices in excess of their average book value has been charged to retained earnings. The cost to repurchase shares at prices below their average book value has been credited to contributed surplus.

Calvalley Petroleum Inc.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited - Expressed in thousands of United States Dollars)

8. SHARE CAPITAL (Continued)

b. Stock options

The Company's restated stock option plan, as approved effective May 21, 2006 provides for the issue of stock options to directors, officers, employees and consultants. Vesting terms are determined by the Board as they are granted and currently include periods ranging from immediately to evenly over 3 or 5 years. The options' maximum term is 5 years (10 years for options granted prior to October 1, 2001).

A total of 9,850,463 (2008 – 10,026,560) shares have been reserved for issue under this plan. Options which are forfeited are available for reissue.

The following is a continuity of stock options outstanding:

	Six months ended June 30, 2009		Six months ended June 30, 2008	
	Options (000s)	Weighted Average Exercise Price – C\$	Options (000s)	Weighted Average Exercise Price – C\$
Opening Balance	4,358	3.29	2,970	3.92
Granted	745	1.64	1,730	4.32
Forfeited	(370)	4.19	(185)	6.06
Exercised	(500)	1.60	(440)	1.16
Ending balance	4,233	3.17	4,075	3.74

Stock options outstanding at June 30, 2009 were as follows:

Number of Options (000)		Exercise Price C\$	Weighted Average Exercise Price C\$	Expiry Date
Granted	Exercisable			
50	50	1.40	1.40	2009
75	75	1.60	1.60	2010
855	855	3.80-4.20	4.07	2010
50	50	0.90	0.90	2011
75	75	6.86	6.86	2011
260	193	6.05-7.61	7.01	2012
1,525	1,117	3.45-4.50	4.29	2013
598	100	1.50-2.45	1.64	2013
745	-	1.50-1.80	1.64	2014
4,233	2,515	3.17		

Calvalley Petroleum Inc.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited - Expressed in thousands of United States Dollars)

8. SHARE CAPITAL (continued)

During the six months ended June 30, 2009, stock based compensation expense of \$379 was expensed and credited to contributed surplus. The fair value of the options granted during the six months ended June 30, 2009 was \$581 (2008 - \$3,836) or \$0.77 (2008 - \$2.35) per option using the Black-Scholes Option Pricing model with the following assumptions:

	2009	2008
Risk-free interest rate	1.63 to 2.11%	3.4%
Expected hold period to exercise	5 years	5 years
Volatility in the price of the Company's shares	70.04 to 70.61%	71.3 to 73.6%
Dividend yield	Nil	Nil

9. CONTRIBUTED SURPLUS

	Six months ended June 30, 2009 \$	Year ended December 31, 2008 \$
Opening balance	6,772	4,019
Stock based compensation	379	2,789
Stock based compensation associated with exercised options	(406)	(137)
Shares repurchased and cancelled	114	101
Closing balance	6,859	6,772

10. CAPITAL DISCLOSURE

The Company defines and computes its capital as follows:

(000s)	June 30, 2009 \$	December 31, 2008 \$
Shareholders' equity	156,693	159,458
Long-term debt	-	-
Cash	(12,420)	(20,989)
Guaranteed Investment Certificates	(43,873)	(42,746)
Total capital	100,400	95,723

The Company's objectives when managing capital are to safeguard the company's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders. The Company sets the amount of capital in proportion to risk. The Company manages the capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the Company may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue or repurchase shares, incur debt or sell assets to reduce debt.

The Company currently has no requirement for debt financing and has not required debt financing over the last two completed fiscal years. The objectives and strategy for utilizing capital are monitored to provide the appropriate capital structure for the risk profile of corporate objectives.

The Company has no financial covenants.

Calvalley Petroleum Inc.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited - Expressed in thousands of United States Dollars)

11. SUPPLEMENTAL CASH FLOW INFORMATION

	Three months ended June 30,		Six months ended June 30,	
	2009 \$	2008 \$	2009 \$	2008 \$
(000s)				
Changes in non-cash working capital				
Accounts receivable	(268)	8,374	723	11,431
Due from joint venture partners	2,661	9,578	(1,639)	8,075
Oil inventory	1,653	(144)	1,482	(426)
Prepaid expenses	21	(104)	22	(172)
Deferred revenue	(1,653)	-	(3,255)	-
Accounts payable and accrued liabilities	(54)	4,808	(2,193)	(4,920)
	2,360	22,512	(4,860)	13,988
Changes in non-cash working capital				
Operating activities	(1,315)	23,675	(2,132)	15,663
Investing activities	3,675	(1,163)	(2,728)	(1,675)
	2,360	22,512	(4,860)	13,988

During the period ended June 30, 2009, the Company paid \$Nil in interest (2008 – \$Nil) and \$Nil in taxes (2008 - \$Nil). Yemen income taxes are paid to the government through their allocation of oil under the PSA.

12. GEOGRAPHICAL INFORMATION

The Company has defined its continuing operations as oil and gas operations. The majority of the Company's oil and gas operations are located in Yemen with lesser operations in Ethiopia and Canada.

Segmented information is as follows:

Six months ended June 30, 2009

	Ethiopia \$	Yemen \$	Canada \$	Total \$
(000s)				
Revenue	-	24,235	547	24,782
Property, plant and equipment	468	83,954	212	84,634

Six months ended June 30, 2008

	Yemen \$	Canada \$	Total \$
Revenue	45,829	731	45,560
Property, plant and equipment	77,747	182	77,929

Calvalley Petroleum Inc.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited - Expressed in thousands of United States Dollars)

13. PER SHARE AMOUNTS

In calculating basic and diluted earnings (loss) per share, the following weighted average shares were used:

(000s)	Three months ended June 30,		Six months ended June 30,	
	2009	2008	2009	2008
Weighted average number of shares outstanding	98,911	101,424	99,386	101,275
Dilutive effect of stock options	80	312	-	312
Weighted average number of diluted shares outstanding	98,991	101,736	99,386	101,587

The calculation of diluted loss per share for the six month period ended June 30, 2009 excludes all options warrants as the effect is anti-dilutive. For the six months ended June 30, 2008, a total of 2,045,000 options were not in the money and were excluded from the dilutive calculation. For the three months ended June 30, 2009, a total of 4,133,000 (2008 – 2,045,000) options were not in the money and were excluded from the dilutive calculation.

14. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Carrying Values and Estimated Fair Values of Financial Assets and Liabilities

The Company has classified its cash and cash equivalents and GIC's as assets held for trading which are measured at fair value with changes being recognized in net income. Accounts receivable and amounts due from joint venture partners are classified as loans and receivables, which are measured at amortized cost.

The carrying value and fair value of financial assets and liabilities are summarized as follows:

Classification	June 30, 2009	
	Carrying Value	Fair Value
Financial assets held for trading	\$56,293	\$56,293
Loans and receivables	\$22,628	\$22,628

Credit Risk

The majority of the accounts receivable are in respect of oil and gas operations and are due from the Company's joint venture partners or its customer for oil sales. Management believes the risk is mitigated by the size and reputation of the companies to which the Company extends credit. The Company has not experienced any material credit loss in the collection of accounts receivable to date.

The Company is currently under contract to sell all of its production to one purchaser until July 1, 2010. The selling price is based on the quoted Brent price on the date of shipment adjusted for the official selling price differential posted by the Government of Yemen. At June 30, 2009, \$2,423 (December 31, 2008 - \$3,255) was receivable under the contract and was received in July 2009. Payment is secured by a guarantee issued by the purchaser's parent company. The Company has an option to extend the contract on the same terms for a further 12 months.

14. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)

The Company funds capital and operating costs and bills joint venture partners their share of those costs. In the event that a joint venture partner was incapable of fulfilling its obligation to pay its share of the costs, the Company could, under the terms of the joint operating agreement, recover the costs from the joint venture partners' share of proceeds from crude oil sales.

Trade and other receivables from continuing operations are analyzed in the table below. With respect to the trade and other receivables that are neither impaired nor past due, there are no indications as of the reporting date that the debtors will not meet their payment obligations.

Trade and other receivables at June 30, 2009	(\$000)
Neither impaired nor past due	9,768
Not impaired and past due in the following period:	
Within 30 days	1,568
31-60 days	2,220
61-90 days	2,132
Over 90 days	6,940

Interest rate risk

The Company has exposure to interest rate risk as it relates to investments in GICs. Interest rate risk relates to the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company incurs interest rate risk on its cash and cash equivalents and GICs. All cash balances are current and available immediately. The Company does not hedge its exposure to interest rate risk.

Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. Liquidity describes a company's ability to access cash. Companies operating in the upstream oil and gas industry require sufficient cash in order to fund capital programs necessary to maintain and increase production and proved reserves, to acquire strategic oil and gas assets, and to repay debt. The Company actively monitors its cash requirements to ensure it has sufficient available funds to meet current and foreseeable financial requirements at a reasonable cost. The Company prepares annual capital expenditure budgets, which are regularly monitored and updated as considered necessary. The Company also utilizes authorizations for expenditures to further manage capital expenditures.

The Company's obligations coming due in the next twelve months are accounts payable and accrued liabilities of \$7,500. In addition, the Company has commitments under existing agreements as described in note 15. Given the Company's working capital position, management assesses liquidity risk as being low.

Commodity Price Risk Management

While the Company is exposed to business risk associated with fluctuations in the price of crude oil, the Company does not hold financial instruments whose fair values are susceptible to variability resulting from changes in the price of crude oil.

Foreign Exchange Risk

The Company holds substantially all of its cash, cash and equivalents and GICs at one financial institution. The Company invests its cash reserves in GICs issued by an Alberta Credit Union guaranteed by the Province of Alberta. Approximately \$1,056 of the \$12,420 cash and cash equivalents is held in Canadian dollar denominated accounts. As such, the Company is exposed to foreign currency

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risk. The impact to net income of a 10% change in the foreign exchange rates between the Canadian and United States dollars at June 30, 2009 would have been approximately \$42 (\$0.00/share).

15. COMMITMENTS AND CONTINGENCY

There have been no material changes or developments with respect to the Company's commitments and contingency as disclosed in the Company's audited financial statements for the year ended December 31, 2008.

16. RELATED PARTY TRANSACTION

On June 10, 2009 the Company advanced \$113 to a director for the exercise of options. The advance which is included in accounts receivable is non-interest bearing, repayable within 90 days, and is secured by shares of the Company.

17. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform to current period presentation.

The presentation of oil sales revenue has been restated to report oil sales before royalties paid in kind to government agencies in Yemen. Royalties taken in kind are then shown as a reduction to revenue. The change in presentation does not result in a change to prior period earnings.



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