

CABO DRILLING CORP.
Consolidated Financial Statements
2nd Quarter ended December 31, 2009

CABO DRILLING CORP.

Management's Statement of Responsibility for Financial Reporting

February 26, 2010

The accompanying consolidated financial statements of Cabo Drilling Corp. have been prepared by management within the framework of Canadian generally accepted accounting principles. The financial information contained elsewhere in this report, including the Management's Discussion and Analysis ("MD&A"), has been reviewed to ensure consistency with the financial statements.

Management has established a system of internal controls to meet its responsibility for reliability and accuracy of financial reporting based on the accounting principles summarized in the notes to the consolidated financial statements. The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and is ultimately responsible for reviewing and approving the consolidated financial statements. The Board carries out this responsibility primarily through the Audit Committee and by meeting quarterly to review management's decisions, estimates and uncertainties.

The Audit Committee of the Board of Directors, composed of four independent directors, has reviewed the consolidated financial statements with management and the external auditors. The Audit Committee meets quarterly to review the consolidated financial statements and the MD&A prior to their recommendation for approval to the Board of Directors.

"John Versfelt"

John A. Versfelt
President and Chief Executive Officer

"Cal Lucyshyn"

Cal Lucyshyn
Controller and Chief Financial Officer

CABO DRILLING CORP.

Consolidated Balance Sheets

As at	December 31, 2009	June 30, 2009
ASSETS		
Current		
Cash and cash equivalents	\$	\$ 455,006
Marketable securities	683,300	40,728
Accounts receivable	70,075	6,169,784
Prepaid expenses	6,031,311	593,899
Inventories	514,046	8,729,315
Convertible debenture receivable (Note 6)	9,214,632	174,450
Future income tax assets	157,500	465,000
	<u>465,000</u>	
	17,135,684	16,628,182
Property, plant and equipment (Note 7)	14,159,201	15,329,055
Convertible debenture receivable (Note 6)	380,181	413,877
Long-term investment (Note 8)	406,071	342,857
Future income tax assets	473,000	473,000
	<u>32,554,317</u>	<u>\$ 33,186,971</u>
	\$	\$
LIABILITIES		
Current		
Demand loans (Note 9)	\$5,304,142	\$ 5,305,963
Accounts payable and accrued liabilities	3,403,499	3,856,002
Unearned revenue	948,318	1,048,367
Income tax payable	587,507	1,048,249
Current portion of long-term debt (Note 10)	816,453	791,787
	<u>11,059,919</u>	<u>12,050,368</u>
Long-term debt (Note 10)	1,378,306	1,387,567
Future income tax liabilities	701,591	660,000
	<u>13,139,816</u>	<u>14,097,935</u>
SHAREHOLDERS' EQUITY		
Share capital (Note 11)	30,116,078	29,287,865
Contributed surplus	2,019,900	2,012,150
Accumulated other comprehensive loss	(671,939)	(775,029)
Deficit	(12,049,538)	(11,435,950)
	<u>19,414,501</u>	<u>19,089,036</u>
	\$ 32,554,317	\$ 33,186,971

Approved on behalf of the Board of Directors

"John Versfelt", Director

"Tom Oliver", Director

The accompanying notes are an integral part of these consolidated financial statements.

CABO DRILLING CORP.

Consolidated Statements of Operations and Comprehensive (Loss) Income

<i>Unaudited – prepared by management</i>	For the quarter-ended December 31		For six months ended December 31	
	2009	2008	2009	2008
Revenue	\$ 7,983,295	\$ 11,824,526	\$ 14,323,878	\$ 28,441,943
Direct costs	5,709,345	8,740,968	10,205,406	21,032,856
Gross profit	2,273,950	3,083,558	4,118,472	7,409,087
Expenses				
General and administrative	1,434,567	1,697,920	2,800,239	3,490,910
Stock-based compensation	7,750	-	7,750	-
Amortization	829,409	741,518	1,681,143	1,419,092
Interest expense	145,804	184,859	239,717	321,275
(Gain) loss on foreign exchange	3,806	(57,663)	504	(28,621)
Other (income) expense	-	-	-	-
	2,421,336	2,566,634	4,729,353	5,202,656
Income before other items and income taxes	(147,386)	516,924	(610,881)	2,206,431
Other items				
Gain/(loss) on disposition of assets	-	(2,208)	-	(5,864)
	-	-	-	-
(Loss)/Income before income taxes	(147,386)	514,716	(610,881)	2,200,567
Income tax expense (recovery)				
Current	(38,884)	325,663	(38,884)	880,663
Future	41,591	(150,000)	41,591	(100,000)
Net income for the period	(150,093)	339,053	(613,588)	1,419,905
Deficit, beginning of period	(11,899,445)	(9,499,424)	(11,435,950)	(10,589,041)
Deficit, end of period	\$ (12,049,538)	\$ (9,160,371)	\$ (12,049,538)	\$ (9,169,136)
Earnings per share (Note 2)				
Fully diluted and Basic earnings per share	(0.00)	\$0.01	(0.01)	\$0.03
Weighted average number of common shares outstanding	55,240,679	47,767,013	55,240,679	47,767,013

The accompanying notes are an integral part of these consolidated financial statements.

CABO DRILLING CORP.
Consolidated Statements of Cash Flows

<i>Unaudited – prepared by management</i>	For the quarter ended December 31		For the six months ended December 31	
	2009	2008	2009	2008
Cash flows (used in) from Operating Activities				
Net income for the period	\$ (150,093)	\$328,802	\$ (613,588)	\$ 1,418,419
Items not involving cash:				
Amortization	829,409	741,518	1,681,143	1,419,092
Gain on disposition of assets	-	3,694	-	7,350
Stock based compensation	7,750	-	7,750	-
Future income tax	41,591	(150,000)	41,591	(100,000)
	<u>728,657</u>	<u>924,014</u>	<u>1,116,896</u>	<u>2,744,861</u>
Changes in non-cash working capital items (Note 14)	(1,041,050)	1,734,291	(1,143,115)	374,130
	<u>(312,393)</u>	<u>2,658,305</u>	<u>(26,219)</u>	<u>3,118,990</u>
Cash flows used in Investing Activities				
Property, plant and equipment purchases	57,188	(1,425,690)	(519,051)	(3,658,845)
Proceeds from sale of assets	-	335,737	7,762	702,339
Purchase of long term investment	(51,952)	-	(51,952)	-
	<u>5,236</u>	<u>(1,089,953)</u>	<u>(563,241)</u>	<u>(2,956,506)</u>
Cash flows used in Financing Activities				
Shares issued for cash - net	804,173	-	804,173	-
Demand loan	(179,212)	-	(1,824)	-
Repayment of long term liabilities	(221,630)	(466,856)	15,405	510,669
Repayment of obligation under capital lease	-	(114,029)	-	(1,009,255)
Additional long term debt	-	66,555	-	1,352,555
	<u>403,331</u>	<u>(514,330)</u>	<u>817,754</u>	<u>853,969</u>
Increase in cash and cash equivalents during the period	96,174	1,054,021	228,294	1,016,453
Cash and cash equivalents, beginning of period	587,126	747,693	455,006	785,261
Cash and cash equivalents, end of period	\$ 683,300	1,801,714	\$ 683,300	\$ 1,801,714

Supplementary cash flow information (Note 14)

CABO DRILLING CORP.

Consolidated Statements of Shareholders' Equity
 Period ended December 31, 2009 and June 30, 2009

	SHARE CAPITAL		CONTRIBUTED SURPLUS	ACCUMULATED OTHER COMPREHENSIVE LOSS	DEFICIT	TOTAL
	NUMBER	AMOUNT				
Balance, June 30, 2008	47,767,013	\$ 29,287,865	\$ 1,892,032	\$(494,497)	\$(10,589,041)	\$20,096,359
Stock based compensation	-	-	120,118	-	-	120,118
Unrealized losses on available-for-sale financial assets	-	-	-	(280,532)	-	(280,532)
Net loss for the year	-	-	-	-	(846,909)	(846,909)
Balance, June 30, 2009	47,767,013	\$ 29,287,865	\$ 2,012,150	\$ (775,029)	\$ (11,435,950)	\$ 19,089,036
Unrealized losses on available-for-sale financial assets	-	-	-	103,092	-	103,092
Shares issued for debt	200,333	24,040	-	-	-	24,040
Share subscription - net	7,273,333	804,173	-	-	-	804,173
Stock based compensation	-	-	7,750	-	-	7,750
Net loss for the period	-	-	-	-	(613,588)	(613,588)
Balance, December 31, 2009	55,240,679	\$ 30,116,078	\$ 2,019,900	\$ (671,937)	\$ (12,049,538)	\$ (19,336,503)

The accompanying notes are an integral part of these consolidated financial statements.

CABO DRILLING CORP.

Notes to Consolidated Financial Statements

Periods ended December 31, 2009 and June 30, 2009

1. NATURE OF OPERATIONS

Cabo Drilling Corp. ("Cabo", the "Company"), a Canadian company incorporated in British Columbia, Canada, and continued under the Yukon Business Corporations Act, provides contract diamond drilling services to companies involved in mining and mineral exploration.

Cabo provides contract drilling services which include surface and underground coring, directional, reverse circulation and geotechnical drilling. These operations are performed by the following wholly-owned subsidiaries: Cabo Drilling (Ontario) Corp., the Cabo Drilling (Atlantic) group, Cabo Drilling (International) Inc. (formerly the Stratacan group), the Cabo Drilling (Pacific) group, Forages Cabo Inc., Cabo Drilling de Mexico, SA de CV, Cabo Drilling Spain, SL, Cabo Drilling (Panama) Corp., Balkan States Drilling SH.P.K (Albania), and Cabo Drilling (Ghana) Limited.

2. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") in Canadian dollars and include the following significant accounting policies:

a) Consolidation

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All material inter-company transactions and balances have been eliminated.

b) Cash and cash equivalents

Cash includes cash on hand and demand deposits. Cash equivalents comprise short-term, highly liquid investments that are readily convertible to known amounts of cash which are subject to insignificant risk of change and have maturities of three months or less from the date of acquisition, held for the purpose of meeting short-term cash commitments rather than for investing or other purposes.

c) Marketable securities and long-term investment

In accordance with the recommendations of Section 3855 "Financial Instruments – Recognition and Measurement" of the Canadian Institute of Chartered Accountants ("CICA") Handbook, the Company has designated its marketable securities and long-term investment, comprising of shares listed on a recognized stock exchange, as available-for-sale securities and reports them at fair value. The amounts by which fair values for these securities differ from written down cost represent unrealized gains and losses and are recognized in other comprehensive income (loss). All realized gains and losses are recognized in net income (loss) in the period of disposition. The fair value of these securities is market value. The market value of publicly traded securities is based on quoted market prices.

d) Inventories

Inventories are comprised of spare parts and operating supplies for drilling, and field equipment.

Inventories are recorded at the lower of cost and net realizable value. Net realizable value on inventories is measured by replacement cost at the financial reporting date. The cost of inventories is determined using the weighted average cost formula.

CABO DRILLING CORP.

Notes to Consolidated Financial Statements
Periods ended December 31, 2009 and June 30, 2009

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

e) Property, plant and equipment

Property, plant and equipment is recorded at cost less accumulated amortization. Amortization is provided using the straight-line method at the following rates:

	<u>Amortization Rate</u>
Parking lot	8%
Buildings	5%
Computer & office equipment	30%
Software	20%
Vehicle & equipment	20%
Drilling & field equipment	15%

Costs incurred to repair or maintain property, plant and equipment are expensed as incurred. Assets under capital lease are amortized according to the classification of the specific assets using the above rates.

f) Leases

Leases are classified as either capital or operating. Assets that are held by the Company under leases, which transfer to the Company substantially all the benefits and risks of ownership, are accounted for as assets acquired under capital leases. The capitalized lease obligations are included in long-term debt and reflect the present value of future lease payments, discounted at an appropriate interest rate. Leases that are not classified as capital leases are accounted for as operating leases with payments included in operating expenses in the year incurred.

g) Financial instruments – Recognition and measurement

The Company's financial instruments consist of cash and cash equivalents, marketable securities, receivables, investments, advances to and from related parties, demand loans, accounts payable and accrued liabilities, and long-term debt.

Cash and cash equivalents are designated as "held-for-trading" and measured at fair value. Receivables are designated as "loans and receivables" and measured at amortized cost. Marketable securities and investments are designated as "available-for-sale" and measured at fair value. Demand loans, accounts payable and accrued liabilities, and long-term debt are designated as "other financial liabilities" and measured at amortized cost.

h) Revenue recognition

Revenues from drilling contracts are recognized on the basis of actual metres/footage drilled for each contract. Revenues from ancillary services are recorded when the services are rendered. Provision for estimated losses on uncompleted contracts is made in the period in which such losses are determined. Contract prepayments and amounts pre-billed for mobilization and demobilization equipment and personnel moves are deferred to unearned revenue until performance is accomplished.

CABO DRILLING CORP.

Notes to Consolidated Financial Statements
Periods ended December 31, 2009 and June 30, 2009

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

i) Use of estimates

The preparation of consolidated financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from management estimates as additional information becomes available in the future.

Significant areas requiring the use of management estimates relate to the useful lives of property, plant and equipment for amortization purposes, inventory valuation, determination of income and other taxes, assumptions used in compilation of stock-based compensation and amounts recorded as accrued liabilities.

j) Non-monetary transactions

Shares of the Company issued for non-monetary consideration are valued at the quoted market price per share at the close of trading on the date of the agreement or completion of the transaction except for those circumstances where, in the opinion of the Company and due to the nature of the transaction, the trading price does not fairly represent the value of the transactions. In those circumstances, the value of the shares is determined based on the estimated fair value of the consideration received.

k) Foreign currency translation

Transactions in foreign currencies and financial statements of integrated subsidiaries are translated using the temporal method as follows:

- Monetary assets and liabilities at the rate prevailing at the balance sheet date.
- Non-monetary assets and liabilities at historical rates.
- Revenue and expenses at the average rate in effect during the year.
- Exchange gains or losses are recorded in the consolidated statements of operations and comprehensive income.

l) Income taxes

Income taxes are calculated using the asset and liability method of accounting. Under this method, current income taxes are recognized for the estimated income taxes payable for the current period. Future income tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities, and are measured using the substantially enacted tax rates and laws that will be in effect when the differences are expected to reverse. A valuation allowance is provided to the extent that future income tax benefits are not likely to be realized.

CABO DRILLING CORP.

Notes to Consolidated Financial Statements
Periods ended December 31, 2009 and June 30, 2009

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

m) Earnings (loss) per share

Basic earnings (loss) per share are computed by dividing net income (loss) by the weighted average number of common shares outstanding during the year. Shares issued during the year are weighted for the portion of the year that they were outstanding. Diluted earnings per share are computed similar to basic earnings per share except that the weighted average number of shares outstanding is increased to include additional shares from the assumed exercise of stock options and warrants, if dilutive. The number of additional shares is calculated by assuming that outstanding stock options and warrants were exercised and that the proceeds from such exercises were used to acquire shares of common stock at the average market price during the year.

n) Share capital

i) Non-monetary consideration

Shares, agent's warrants, stock options and other equity instruments issued as purchase consideration in non-monetary transactions are recorded at fair value determined by management using the Black-Scholes option pricing model. The fair value of the shares issued is based on the trading price of those shares on the TSX Venture Exchange ("TSX.V") on the date of the agreement to issue shares as determined by the Board of Directors.

ii) Stock based compensation

The Company measures the cost of the service received for all stock options made to consultants, employees and directors based on an estimate of fair value at the date of grant. The Company uses the Black-Scholes option pricing model to estimate the fair value of each stock option at the date of grant. Stock options that vest immediately are recorded at the date of grant. Stock options that vest over time are recorded over the vesting period using the straight line method. Stock options issued to outside consultants that vest over time are valued at the grant date and subsequently re-valued on each vesting date as services are rendered. Stock based compensation is recognized as expense with a corresponding increase in contributed surplus. On exercise of the stock option, consideration received and the estimated fair value previously recorded in contributed surplus is recorded as share capital.

iii) Share issue costs

Costs directly identifiable with the raising of share capital financing are charged against share capital. Share issue costs incurred in advance of share subscriptions are recorded as non-current deferred assets. Share issue costs related to uncompleted share subscriptions are charged to operations.

iv) Fair value of warrants

Proceeds from unit placements are allocated between shares and warrants issued according to their relative fair value using the residual method to determine the fair value of warrants issued. The value of warrants issued to brokers is determined by using the Black-Scholes model.

CABO DRILLING CORP.

Notes to Consolidated Financial Statements
Periods ended December 31, 2009 and June 30, 2009

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

o) Variable interest entities

The CICA issued Accounting Guidelines 15, "Consolidation of Variable Interest Entities", to provide accounting guidance related to variable interest entities ("VIE"). A VIE exists when the entity's equity investment is at risk. When a VIE is determined to exist, the guidance requires the VIE to be consolidated by the primary beneficiary. The Company has determined that it does not have a primary beneficiary interest in VIE.

p) Comprehensive income

The Company adopts CICA Handbook Section 1530, which establishes standards for reporting and presenting comprehensive income, defined as the change in equity from transactions and other events from non-owner sources. Accordingly, a consolidated statement of operations and comprehensive income (loss) forms part of the Company's consolidated financial statements and displays current period net income (loss) and other comprehensive loss. Other comprehensive loss consists of unrealized losses on available-for-sale financial assets. The cumulative changes in other comprehensive loss are included in accumulated other comprehensive loss, which is a separate category within shareholders' equity in the consolidated balance sheet.

q) Comparative figures

Certain prior year's comparative numbers have been reclassified to conform to current year's financial statement presentation.

3. CHANGES IN ACCOUNTING POLICIES

a) Inventory

In June 2007, the CICA issued Section 3031, "Inventories", which requires inventory to be measured at the lower of cost and net realizable value and which includes guidance on the determination of cost, including allocation of overheads and other costs to inventory. Further, it requires the reversal of previous write-downs to net realizable value when the economic circumstances have changed to support an increased inventory value. This standard was effective for fiscal years beginning on or after January 1, 2008. This section had no material impact on the Company's financial position or results of operations.

b) Financial instruments – Disclosures and presentation

In March 2007, the CICA issued Section 3862, "Financial Instruments – Disclosures", and Section 3863, "Financial instruments – Presentation", which together comprise a complete set of disclosure and presentation requirements that revise and enhance current disclosure requirements for financial instruments. These sections apply to interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007. Section 3862 requires disclosure of additional detail by financial asset and liability categories. Section 3863 establishes standards for presentation of financial instruments and non-financial derivatives. It deals with the classification of financial instruments, from the perspective of the issuer, between liabilities and equity, the classification of related interest, dividends, losses and gains, and the circumstances in which financial assets and financial liabilities are offset. Effective June 30, 2008, the Company implemented these disclosures, although the adoption of these sections did not impact the Company.

CABO DRILLING CORP.

Notes to Consolidated Financial Statements

Periods ended December 31, 2009 and June 30, 2009

3. CHANGES IN ACCOUNTING POLICIES (Continued)

c) Accounting changes

Effective July 1, 2007, the Company adopted Section 1506, "Accounting Changes", which establishes criteria for changing accounting policies, together with the accounting treatment and disclosure of changes in accounting policies, changes in accounting estimates and the correction of errors. The disclosure is to include, on an interim and annual basis, a description and the impact on the Company of any new primary source of GAAP that has been issued but is not yet effective. The impact that the adoption of Section 1506 will have on the Company's results of operations and financial condition will depend on the nature of future accounting changes.

d) Capital disclosures

The CICA issued Section 1535, "Capital Disclosures", which requires the disclosure of both qualitative and quantitative information that provides users of financial statements with information to evaluate the entity's objectives, policies and processes for managing capital. This section was effective for the Company beginning July 1, 2008.

e) General standards of financial statement presentation

The CICA approved amendments to CICA Handbook Section 1400, "General Standards of Financial Statement Presentation". These amendments require management to assess an entity's ability to continue as a going concern. When management is aware of material uncertainties related to events or conditions that may cast doubt on an entity's ability to continue as a going concern, those uncertainties must be disclosed. In assessing the appropriateness of the going concern assumption, the standard requires management to consider all available information about the future, which is at least, but not limited to, twelve months from the balance sheet date. The new requirements of the standard are applicable for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2008.

f) Goodwill and intangible assets

On January 8, 2008, the CICA issued Section 3064, "Goodwill and Intangible Assets". Section 3064 establishes standards for the recognition, measurement and disclosure of goodwill and intangible assets. Section 3064 is effective for annual and interim financial statements relating to fiscal years beginning on or after October 1, 2008. The Company is currently evaluating the effects of adopting this standard.

g) Business combinations

Section 1582, "Business Combinations", applies prospectively to the Company's business combinations on or after January 1, 2011. Early adoption of this recommendation is permitted. This section replaces Section 1581, "Business Combinations", and harmonizes the Canadian accounting standards with International Financial Reporting Standards ("IFRS"). Under the new guidance, the purchase price used in a business combination will be the new fair value of the shares exchanged at their market price on the date of the exchange.

CABO DRILLING CORP.

Notes to Consolidated Financial Statements

Periods ended December 31, 2009 and June 30, 2009

3. CHANGES IN ACCOUNTING POLICIES (Continued)

g) Business combinations (Continued)

Currently, when shares are issued, they are valued based on the market price for a reasonable period before and after the date the acquisition is agreed upon and announced. Under the new guidelines, all acquisition costs are expensed where currently they are capitalized as part of the acquisition costs. There are also a number of other differences between the new guidelines and current GAAP. The Company does not expect the adoption of this pronouncement to impact the financial statements.

h) Consolidated financial statements and non-controlling interests

Section 1601, "Consolidated Financial Statements", and 1602, "Non-Controlling Interests", change the accounting and reporting of ownership in interests in subsidiaries held by parties other than the parent. Non-controlling interests are to be presented in the consolidated statement of financial position (balance sheet) within equity, but separately from the parent's equity. The amount of consolidated net income attributable to the parent and to the non-controlling interest is to be clearly identified and presented on the face of the consolidated statement of operations. In addition, these pronouncements establish standards for a change in a parent's ownership interest in a subsidiary and the valuation of retained non-controlling equity investments when a subsidiary is deconsolidated. They also establish reporting requirements for providing sufficient disclosures that clearly identify and distinguish between the interests of the parent and the interest of the non-controlling owners. The Company does not expect the adoption of these pronouncements to impact its financial statements in fiscal 2011.

i) International Financial Reporting Standards ("IFRS")

In 2006, the Canadian Accounting Standards Board ("AcSB") published a new strategic plan that will significantly affect financial reporting requirements for Canadian companies. The AcSB strategic plan outlines the convergence of Canadian GAAP with IFRS over an expected five year transitional period. In February 2008, the AcSB announced that 2011 is the changeover date for publicly-listed companies to use IFRS, replacing Canada's own GAAP. The date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011, requiring the restatement for comparative purposes of amounts reported by the Company for the year ended December 31, 2010. While the Company has begun assessing the adoption of IFRS for 2011, the financial reporting impact of the transition to IFRS cannot be reasonably estimated at this time.

4. CAPITAL MANAGEMENT

The Company's objectives when managing capital are to safeguard its ability to continue as a going concern, to provide an adequate return to shareholders, to meet external capital requirements on credit facilities and to support any growth plans.

In the management of its capital, the Company includes its cash and cash equivalent balances. The Company monitors capital based on the debt to debt-plus-equity ratio. Debt is total debt shown on the balance sheet, less cash and cash equivalents. Debt-plus-equity is calculated as debt shown on the balance sheet, plus total shareholders' equity which includes accumulated other comprehensive loss, share capital, contributed surplus and deficit.

CABO DRILLING CORP.

Notes to Consolidated Financial Statements
Periods ended December 31, 2009 and June 30, 2009

4. CAPITAL MANAGEMENT (Continued)

The Company's policy is to keep its debt to debt-plus-equity ratio at a manageable level consistent with the current business cycle and the business opportunities outlook foreseen by the Company. As a general guideline, the Company's policy will be to keep its debt to debt-plus-equity ratio to a minimal level, except in unusual circumstances such as major acquisition. Currently, the Company is in full compliance with its capital risk management policies. The Company's Board of Director's approves management's annual capital expenditures plans and reviews and approves any material debt borrowing plans proposed by the Company's management.

To effectively manage the entity's capital requirements, the Company has in place a planning and budgeting process to help determine the funds required to ensure the Company has the appropriate liquidity to meet its operating and growth objectives. The Company ensures that there are sufficient cash and cash equivalents to meet its short-term business requirements, taking into account its anticipated cash flows from operations and its holdings of cash and cash equivalents.

5. FINANCIAL INSTRUMENTS

Financial instruments are exposed to credit, liquidity and market risks. Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. Liquidity risk is the risk that the Company will not be able to meet its obligations as they fall due. Market risk is that the fair value of the Company's financial instruments will fluctuate because of changes in market prices, principal currency and interest rates.

There have been no substantive changes in the Company's exposure to financial instrument risks, its objectives, policies and processes for managing those risks, or the methods used to measure them, from previous periods, unless otherwise stated in this note.

a) Credit risk

The Company is exposed to credit risk from accounts receivable. The Company has adopted a policy of dealing only with creditworthy counterparties and obtaining sufficient collateral where appropriate, as a means of mitigating the risk of financial loss from defaults. The Company carries out, on a continuing basis, credit checks on its customers, initiates collection activity immediately on past due accounts, negotiates settlements and maintains adequate provisions for contingent credit losses. The Company diversifies its credit risk by dealing with a large number of customers in various domestic and foreign locations. As at December 31, 2009, the Company's largest customer accounted for 13% of total accounts receivable, and the next largest customer represented less than 12%. The maximum exposure to credit risk is the net carrying value of receivables and unearned revenue.

Credit risk also arises from cash and cash equivalents with banks and financial institutions. This risk is limited because the counterparties are mainly Canadian banks with high credit rating.

b) Liquidity risk

Liquidity risk arises from the Company's management of working capital, finance charges and principal repayments on long-term debt. The Company manages liquidity risk by maintaining adequate reserves, banking facilities and reserve borrowing facilities (Note 10), by maintaining accounts payable current and preserving a good credit rating, and by continuously monitoring forecast and actual cash flows.

CABO DRILLING CORP.

Notes to Consolidated Financial Statements

Periods ended December 31, 2009 and June 30, 2009

5. FINANCIAL INSTRUMENTS (Continued)

c) Market risk

The Company operates on an international basis on four continents and therefore, currency risk exposures arise from transactions denominated in foreign currencies. The majority of its international sales contracts are denominated in US dollars, Euros and Mexican pesos. The Company does not actively manage its currency risk at this time. As at December 31, 2009, the Company had cash in US dollars, Euros and Mexican pesos totalling US\$363,424, €31,946 and 11,401 pesos, respectively.

The Company's demand credit facilities and certain long-term debt bear a floating rate of interest based on the financial institution's prime rate of interest, which exposes the Company to interest rate fluctuations. The Company has estimated that a one percent increase or decrease in the prime interest rate would have caused a corresponding annual increase or decrease in net earnings of approximately \$75,000.

6. CONVERTIBLE DEBENTURE RECEIVABLE

As part of a settlement of an account receivable, the Company received a \$537,681 (US\$511,589) convertible debenture ("Debenture") from a customer. The Debenture has a three-year term, and an interest rate of 12% per annum compounded annually. The Debenture is fully secured by a lien on a mine of the customer. The amounts owing under this Debenture will be payable as follows: payment of \$157,500 (US\$150,000) on the first and second anniversary of the date of issuance, and the balance, including interest, on the maturity date. The Company has the right, at any time prior to the maturity date or such time when the Debenture is fully repaid, to convert any portion of the amounts owing into the publicly listed common shares of the customer at US\$0.20 per share.

CABO DRILLING CORP.

Notes to Consolidated Financial Statements
Periods ended December 31, 2009 and June 30, 2009

7. PROPERTY, PLANT AND EQUIPMENT

	December 31, 2009			June 30, 2009		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Land	\$ 144,246	\$ -	\$ 144,246	\$ 144,246	\$ -	\$ 144,246
Parking lot	41,788	13,322	28,466	41,788	11,452	30,336
Buildings	1,072,044	230,510	841,534	1,052,095	202,016	850,079
Computer & office equipment	559,907	470,844	89,063	548,117	431,353	116,764
Software	412,464	143,541	268,923	276,348	119,657	156,691
Vehicle & equipment	1,827,522	1,002,073	825,449	1,830,582	821,211	1,009,371
Drilling & field equipment	16,804,293	6,923,038	9,881,255	16,345,654	5,767,974	10,577,680
Assets under capital lease	3,127,353	1,047,088	2,080,265	3,127,353	799,819	2,327,534
	<u>\$23,989,617</u>	<u>\$ 9,830,416</u>	<u>\$14,159,201</u>	<u>\$23,366,183</u>	<u>\$ 8,153,482</u>	<u>\$15,212,701</u>

Included in software are consulting fees and related expenses paid for implementation of accounting software in the amount of \$135,404 (2009 - \$116,354). The Company will commence amortization of these costs once the implementation is fully completed.

8. LONG-TERM INVESTMENT

	December 31, 2009	June 30, 2009
Investment in IMMC, beginning of year	342,857	685,714
Participate in share subscription	65,000	-
Other comprehensive income/(loss)	(1,786)	(342,857)
Investment in IMMC, end of year	<u>406,071</u>	<u>342,857</u>

As of December 31, 2009, the Company owned 4,511,904 (June 30, 2009 - 3,377,235) common shares of International Millennium Mining Corp. ("IMMC"), a TSX.V public company with common directors and officers. The shares had a market value of \$0.09 (June 30, 2009 - \$0.10) per share. As a result, the Company recorded an unrealized loss of \$1,786 (2009 - \$342,857) on the consolidated statements of operations and comprehensive income.

CABO DRILLING CORP.

Notes to Consolidated Financial Statements

Periods ended December 31, 2009 and June 30, 2009

9. DEMAND LOAN FACILITIES

	<u>December 31, 2009</u>	<u>June 30, 2009</u>
The Company's credit facilities are as follows:		
Demand loan facility of \$600,000, bearing interest at prime plus 1.75%, secured by promissory notes and general security agreement over drilling equipment of the Company. The loan is payable in monthly instalments of \$10,000, plus interest, maturing 2012.	\$ 170,000	\$ 230,000
Demand loan facility of \$500,000, bearing interest at prime plus 1.75%, secured by promissory notes and general security agreement over drilling equipment of the Company. The loan is payable in monthly instalments of \$8,333, plus interest, maturing 2013.	233,316	283,316
Demand loan facility of \$400,000, bearing interest at prime plus 1.75%, secured by promissory notes and general security agreement over drilling equipment of the Company. The loan is payable in monthly instalments of \$6,667, plus interest, maturing 2013.	266,660	306,662
Operating line of credit facility of up to \$5,000,000, bearing interest at prime plus 2.75%. This facility is secured by promissory notes and general assignment over accounts receivable, inventory and drilling equipment of the Company. Under the terms of the operating line of credit agreement, the Company must satisfy certain restrictive covenants as to minimum financial ratios.	4,634,163	4,485,985
	<u>5,304,139</u>	<u>5,305,963</u>

CABO DRILLING CORP.

Notes to Consolidated Financial Statements

Periods ended December 31, 2009 and June 30, 2009

10. LONG-TERM DEBT

	<u>December 31, 2009</u>	<u>June 30, 2009</u>
Term loan, bearing interest at prime plus 1.25%, payable in monthly instalments of \$8,335 plus interest, secured by a general security agreement over land, building and drilling equipment of the Company, maturing in 2016.	\$ 591,785	\$ 641,634
Term loans and capital leases, bearing interest at rates ranging from 0% to 9.98%, payable in monthly instalments ranging from \$560 to \$15,000, secured by automobiles and drilling equipment, maturing from 2009 to 2013.	752,107	284,464
Capital lease, bearing interest at rates ranging from 5.93% to 7.80%, payable in monthly instalments ranging from \$2,443 to \$15,572 secured by drilling equipment, maturing from 2010 to 2014.	850,866	1,253,256
	<u>2,194,758</u>	<u>2,179,354</u>
Less: Current portion	(816,453)	(791,787)
	<u>\$ 1,378,305</u>	<u>\$ 1,387,567</u>

The required annual principal and interest repayments on long-term debt are as follows:

1 – 12 months	979,954
13 – 24 months	759,259
25 – 36 months	431,295
37 – 48 months	199,121
49 – 60 months	125,170
Thereafter	117,367
	<u>2,612,166</u>
Less: Imputed interest	417,411
Principal payments	<u>2,194,755</u>

CABO DRILLING CORP.

Notes to Consolidated Financial Statements
Periods ended December 31, 2009 and June 30, 2009

11. SHARE CAPITAL

a) Authorized

100,000,000 common shares without par value

b) Stock options

At December 31, 2009, the following stock options were outstanding:

Number	Exercise Price	Expiry Date
1,450,000	0.225	June 30, 2012
1,450,000	0.25	June 30, 2012
<u>2,900,000</u>		

All options are currently exercisable.

A summary of the changes in stock options for the period ended December 31, 2009 is presented below:

	Number of Options	Price	Expiry
Balance, June 30, 2008	2,477,500		
Options granted	1,350,000	\$0.225	June 30, 2012
Options granted	1,350,000	\$0.25	June 30, 2012
Options expired or forfeited	(2,477,500)		
Balance, June 30 and			
Options granted	100,000	\$0.225	June 30, 2012
Options granted	100,000	\$0.25	June 30, 2012
December 31, 2009	2,900,000		

12. RELATED PARTY TRANSACTIONS

	Period ended December 31, 2009	Year ended June 30, 2009
Management and accounting services charged by a company controlled by a director.	\$89,685	\$195,359
Amount due to company at June 30	-	5,200

Included in marketable securities is an investment of \$14,400 (June 30, 2009 – \$4,800) in a company with a common officer.

The Company shares office services and personnel with IMMC. At December 31, 2009, \$8,878 (June 30, 200 - \$54,417) was due from IMMC for shared services.

The amounts due to directors or companies controlled by directors are unsecured, non-interest bearing and have no specific terms of repayment. These transactions were in the normal course of operations and were measured at the exchange amount, which is the amount established and agreed to by the related parties.

CABO DRILLING CORP.

Notes to Consolidated Financial Statements

Periods ended December 31, 2009 and June 30, 2009

13. SEGMENTED INFORMATION

The Company has one reportable business segment: providing contract diamond drilling services to companies involved in mining and mineral exploration.

The Company's operations are divided into two geographic segments, Canada and International. The services provided in each of the reportable drilling segments are essentially the same. The accounting policies of the segments are the same as those described in Notes 2 and 3. Data relating to each of the Company's reportable segments is presented as follows:

	Period ended December 31, 2009	Year ended June 30, 2009
Revenue		
Canada	\$ 11,493,872	22,870,220
International	2,830,006	18,291,412
	\$ 14,323,878	41,161,632
Net (loss) income		
Canada	\$ (473,220)	(3,355,201)
International	(140,368)	2,508,292
	\$ (613,588)	(846,909)
Property, plant and equipment		
Canada	\$ 11,800,017	12,140,256
International	2,359,184	3,188,799
	\$ 14,159,201	15,329,055
Amortization		
Canada	\$ 1,478,531	2,553,034
International	202,612	444,111
	\$ 1,681,143	2,997,145

CABO DRILLING CORP.

Notes to Consolidated Financial Statements
Periods ended December 31, 2009 and June 30, 2009

14. SUPPLEMENTARY CASH FLOW INFORMATION

	Period ended December 31, 2009	Year ended June 30, 2009
Interest received	-	
Interest paid	\$ 239,717	\$ 453,912
Income taxes paid	\$ 421,858	\$ 1,048,258

Non-cash investing and financing activities:

	Period ended December 31, 2009	Year ended June 30, 2009
Acquisition of assets under capital lease	-	2,439,949

Changes in non-cash working capital items:

	Period ended December 31, 2009	Year ended June 30, 2009
Accounts receivable	\$153,117	\$ 5,873,768
Convertible debenture receivable	50,646	(588,327)
Prepaid expenses	79,853	(192,905)
Inventories	(485,317)	879,599
Accounts payable and accrued liabilities	(404,661)	(3,759,101)
Unearned revenue	(100,050)	(1,524,156)
Income tax payable	(460,742)	883,121
Shares issued for debt	24,040	-
	\$(1,143,115)	\$ 1,571,999

15. CONTINGENCIES

The Company is involved in various legal claims and legal notices arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Company's financial position, results of operations, or cash flows. Any amounts awarded as a result of these actions will be reflected when known.

16. SUBSEQUENT EVENTS