

CANACOL ENERGY LTD.

**INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
THREE AND NINE MONTHS ENDED MARCH 31, 2014**



INTERIM CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION (UNAUDITED)

(in thousands of United States dollars)

As at	Note	March 31, 2014	June 30, 2013 (restated) (note 17)	July 1, 2012 (restated) (note 17)
ASSETS				
Current assets				
Cash and cash equivalents		\$ 35,699	\$ 52,290	\$ 30,789
Restricted cash	6	6,028	7,127	6,072
Trade and other receivables		53,664	38,141	31,810
Prepaid expenses and deposits		11,834	11,331	4,630
Embedded derivatives asset		-	1,875	3,156
Crude oil inventory		1,537	3,261	8,136
		108,762	114,025	84,593
Non-current assets				
Restricted cash	6	46,097	19,267	483
Embedded derivatives asset		-	839	3,942
Exploration and evaluation assets	4	121,743	92,753	126,295
Property, plant and equipment	5	261,886	238,278	183,838
Investment in joint venture	16	7,306	1,963	4,361
Investments		2,707	2,467	2,690
Deferred tax assets		-	-	626
		439,739	355,567	322,235
Total assets		\$ 548,501	\$ 469,592	\$ 406,828
LIABILITIES AND EQUITY				
Current liabilities				
Bank debt		\$ 18,667	\$ -	\$ 12,000
Trade and other payables		52,124	37,219	47,602
Commodity contracts	14	33	280	303
Warrants	8	3,522	37	-
Restricted share units	14	6,044	3,914	-
Equity tax payable		1,106	1,294	1,236
Taxes payable		16,160	575	3,893
		97,656	43,319	65,034
Non-current liabilities				
Bank debt		117,008	134,316	15,986
Deferred income		3,731	3,731	-
Commodity contracts	14	-	-	124
Decommissioning obligations		9,434	7,995	6,642
Convertible debentures	7	24,241	22,091	25,381
Restricted share units	14	133	-	-
Warrants	8	4,217	1,834	896
Phantom warrants	14	7,930	1,866	-
Equity tax payable		-	512	1,671
Other long term obligations	15	219	10,764	-
Deferred tax liabilities		7,169	3,861	-
Total liabilities		271,738	230,289	115,734
Equity				
Share capital	9	430,512	408,770	340,775
Other reserves		43,785	40,074	32,053
Accumulated other comprehensive loss		347	347	347
Deficit		(197,881)	(209,888)	(82,081)
Total equity		276,763	239,303	291,094
Total liabilities and equity		\$ 548,501	\$ 469,592	\$ 406,828

Commitments and contingencies (note 15)

Subsequent events (note 18)

See accompanying notes to interim condensed consolidated financial statements.

INTERIM CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

(UNAUDITED)

(in thousands of United States dollars, except per share amounts)

	Note	Three months ended March 31,		Nine months ended March 31,	
		2014	2013 (restated) (note 17)	2014	2013 (restated) (note 17)
Revenues					
Petroleum and natural gas revenues, net of royalties	12	\$ 55,653	\$ 34,602	\$ 146,043	\$ 102,394
Share of joint venture profit (loss)	16	1,599	(1,056)	2,792	(2,190)
Expenses					
Production and transportation expenses		16,786	13,970	49,337	58,066
Pre-license and exploration costs		3,405	95	3,645	14,449
General and administrative		5,674	6,045	20,065	16,678
Stock-based compensation	9	2,454	1,435	3,204	3,475
Depletion and depreciation	5	9,015	11,446	23,843	34,585
Foreign exchange (gain) loss and other		(2,962)	(316)	(1,732)	257
(Gain) loss on derivatives and financial instruments	12	(1,311)	1,330	25,345	4,520
Change in provision	15	(10,545)	-	(10,545)	-
Gain on sale of assets		-	(1,359)	-	(1,359)
Loss (gain) on business acquisition		-	1,240	-	(26,907)
		22,516	33,886	113,162	103,764
Net finance expense	10	2,416	2,607	6,565	5,227
Income (loss) before income taxes		32,320	(2,947)	29,108	(8,787)
Income taxes (recovery)					
Current		6,623	2,470	13,793	827
Deferred		6,259	(1,992)	3,308	(853)
		12,882	478	17,101	(26)
Net income (loss) and comprehensive income (loss)		19,438	(3,425)	12,007	(8,761)
Earnings (loss) per share					
Basic	11	\$ 0.22	\$ (0.04)	\$ 0.14	\$ (0.12)
Diluted	11	\$ 0.21	\$ (0.04)	\$ 0.14	\$ (0.12)

See accompanying notes to interim condensed consolidated financial statements.

INTERIM CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY (UNAUDITED)

(in thousands of United States dollars, number of shares in thousands)

	Number of Common Shares	Share Capital	Other Reserves	Accumulated Other Comprehensive Income	Deficit	Total Equity
Balance as at June 30, 2012	61,898	\$ 340,775	\$ 32,053	\$ 347	\$ (82,081)	\$ 291,094
Issue of common shares, net of costs	24,601	67,985	-	-	-	67,985
Stock-based compensation	-	-	6,125	-	-	6,125
Net loss for the period	-	-	-	-	(8,761)	(8,761)
Balance at March 31, 2013	86,499	\$ 408,760	\$ 38,178	\$ 347	\$ (90,842)	\$ 356,443
Balance as at June 30, 2013	86,506	\$ 408,770	\$ 40,074	\$ 347	\$ (209,888)	\$ 239,303
Issue of common shares, net of costs	2,454	15,000	-	-	-	15,000
Stock options and warrants exercised	1,260	6,742	(930)	-	-	5,812
Stock-based compensation	-	-	4,641	-	-	4,641
Net loss for the period	-	-	-	-	12,007	12,007
Balance at March 31, 2014	90,220	\$ 430,512	\$ 43,785	\$ 347	\$ (197,881)	\$ 276,763

See accompanying notes to interim condensed consolidated financial statements.

INTERIM CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

(in thousands of United States dollars)

	Note	Three months ended		Nine months ended	
		2014	March 31, 2013 (restated) (note 17)	2014	March 31, 2013 (restated) (note 17)
Operating activities					
Net income (loss) for the period		\$ 19,438	\$ (3,425)	\$ 12,007	\$ (8,761)
Adjustments:					
Net financing expense		2,416	2,607	6,565	5,227
Share of joint venture (profit) loss		(1,599)	1,056	(2,792)	2,190
Stock-based compensation	9	2,454	1,435	3,204	3,475
Depletion and depreciation	5	9,015	11,446	23,843	34,585
Unrealized loss (gain) on derivatives and financial instruments	12	(1,311)	607	24,295	2,886
Unrealized foreign exchange (gain) loss and other		(2,657)	(320)	(2,436)	222
Deferred income		-	-	-	2,500
Settlement of restricted share units liability	14	-	-	(1,321)	-
Deferred income tax		6,259	(1,992)	3,308	(853)
Exploration costs		2,907	-	2,907	14,011
Change in provision	15	(10,545)	-	(10,545)	-
Loss (gain) on business acquisition		-	1,240	-	(26,907)
Changes in non-cash working capital	12	(13,278)	(21,174)	10,194	(24,259)
		13,099	(8,520)	69,229	4,316
Investing activities					
Expenditures on exploration and evaluation assets		(3,263)	(1,423)	(14,376)	(19,058)
Expenditures on property, plant and equipment		(16,396)	(4,342)	(44,074)	(18,752)
Disposition of exploration and evaluation assets		-	5,391	-	5,391
Investments		(262)	-	(3,102)	-
Change in restricted cash		(9,795)	3,423	(25,731)	(11,825)
Cash paid for business acquisition		-	-	-	(40,224)
Cash acquired in business acquisition		-	-	-	8,300
Changes in non-cash working capital	12	(6,121)	(5,076)	1,917	(6,727)
		(35,837)	(2,027)	(85,366)	(82,895)
Financing activities					
Net financing expense paid		(1,804)	(1,670)	(4,709)	(1,848)
Issue of common shares		3,773	-	4,255	-
Share issuance costs		-	-	-	(361)
Draw on bank debt		-	-	-	77,035
Repayment of bank debt		-	(9,912)	-	(15,912)
		1,969	(11,582)	(454)	58,914
Change in cash and cash equivalents		(20,769)	(22,129)	(16,591)	(19,665)
Cash and cash equivalents, beginning of period		56,468	33,253	52,290	30,789
Cash and cash equivalents, end of period		\$ 35,699	\$ 11,124	\$ 35,699	\$ 11,124
Cash and cash equivalents consists of:					
Cash				\$ 35,679	\$ 10,964
Cash equivalents				20	160
Cash and cash equivalents, end of period				\$ 35,699	\$ 11,124

See accompanying notes to interim condensed consolidated financial statements.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the three and nine months ended March 31, 2014 and 2013

(in United States dollars (tabular amounts in thousands) except as otherwise noted)

NOTE 1 - GENERAL INFORMATION

Canacol Energy Ltd. (“Canacol” or the “Corporation”) and its subsidiaries are primarily engaged in petroleum and natural gas exploration and development activities in Colombia and Ecuador, with non-core activities in Brazil and Peru. The Corporation’s head office is located at 4500, 525 - 8th Avenue SW, Calgary, Alberta, T2P 1G1, Canada. The Corporation’s shares are traded on the Toronto Stock Exchange under the symbol CNE and the Bolsa de Valores de Colombia under the symbol CNEC.

The Board of Directors approved these interim condensed consolidated financial statements (the “financial statements”) for issuance on May 12, 2014.

NOTE 2 - BASIS OF PREPARATION

The financial statements have been prepared by management in accordance with International Accounting Standard 34, “Interim Financial Reporting”. These financial statements do not include all of the information required for full annual consolidated financial statements and should be read in conjunction with the Corporation’s annual consolidated financial statements for the year ended June 30, 2013.

Basis of Measurement

These financial statements have been prepared on a historical cost basis, except for commodity contracts, convertible debentures, embedded derivatives, investments, warrants, phantom warrants, restricted share units and overlifted volumes payable, which are measured at fair value with changes in fair value recorded in profit or loss (“fair value through profit or loss”).

These financial statements have been prepared on a going concern basis.

Functional and Presentation Currency

These financial statements are presented in United States dollars, which is both the functional and presentation currency.

NOTE 3 - SIGNIFICANT ACCOUNTING POLICIES

These financial statements are prepared using the same accounting policies and methods of computation as disclosed in note 3 of the annual consolidated financial statements as of and for the year ended June 30, 2013 except as follows.

Application of New and Revised International Financial Reporting Standards (“IFRS”)

The International Accounting Standards Board released the following new standards: IFRS 10 “Consolidated Financial Statements”, IFRS 11 “Joint Arrangements”, IFRS 12 “Disclosures of Interests in Other Entities” and IFRS 13 “Fair Value Measurement”. These standards have been adopted in the financial statements for the fiscal period beginning July 1, 2013. The following describes the impact as a result of the application of the new and revised standards.

(i) Consolidated Financial Statements

IFRS 10 “Consolidated Financial Statements” supersedes IAS 27 “Consolidation and Separate Financial Statements” and SIC-12 “Consolidation – Special Purpose Entities”. This standard provides a single model to be applied in control analysis for all investees, including special purpose entities.

The adoption of this standard had no impact on the financial statements.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

For the three and nine months ended March 31, 2014 and 2013

(in United States dollars (tabular amounts in thousands) except as otherwise noted)

(ii) Joint Arrangements

IFRS 11 “Joint Arrangements” divides joint arrangements into two types, joint operations and joint ventures, each with their own accounting model. All joint arrangements are required to be reassessed on transition to IFRS 11 to determine their type to apply the appropriate accounting.

Upon the adoption of IFRS 11, the Corporation reviewed and assessed the legal form and terms of the contractual arrangements in relation to the Corporation’s investments in joint arrangements. The adoption of IFRS 11 resulted in a change in the method of accounting for the Corporation’s interest in the incremental production contract for the Libertador and Atacapi fields in Ecuador (the “Ecuador IPC”) from a jointly-controlled entity, using the proportionate consolidation method, to being accounted for using the equity method. This change in accounting for the Corporation’s investment in the Ecuador IPC has been applied in accordance with the relevant IFRS transitional provisions. The initial investment in the Ecuador IPC as at July 1, 2012 for the purposes of applying the equity method was measured as the aggregate of the carrying amounts of the assets and liabilities that the Corporation had previously proportionately consolidated. The change in accounting method has affected the amounts previously reported in the Corporation’s financial statements (see note 17).

(iii) Disclosure of Interests in Other Entities

IFRS 12 “Disclosure of Interests in Other Entities” combines in a single standard the disclosure requirements for subsidiaries, associates and joint arrangements as well as unconsolidated structured entities.

The adoption of this standard had no impact on the financial statements for interim disclosures.

(iv) Fair Value Measurement

IFRS 13 “Fair Value Measurement” defines fair value, establishes a framework for measuring fair value and sets out disclosure requirements for fair value measurements. This standard defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The adoption of this standard had no impact on the financial statements.

NOTE 4 – EXPLORATION AND EVALUATION ASSETS

Balance at July 1, 2012	\$	126,295
Acquisition of Shona Energy Company, Inc. (“Shona”)		6,523
Additions		24,813
Dispositions		(6,249)
Transferred to Property, Plant and Equipment (note 5)		(8,377)
Transferred to exploration expense		(50,252)
Balance at June 30, 2013		92,753
Additions		29,376
Transferred to exploration expense		(386)
Balance at March 31, 2014	\$	121,743

On January 31, 2014, the Corporation acquired a right to an 80% interest in each of the COR 4 and COR 12 Exploration and Production contracts located in the Upper Magdalena Basin of Colombia for a total payment of \$15 million (\$7.5 million for each block) payable entirely in newly issued common shares of the Corporation. The Corporation issued 2,454,590 common shares in satisfaction of the share consideration.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

For the three and nine months ended March 31, 2014 and 2013

(in United States dollars (tabular amounts in thousands) except as otherwise noted)

NOTE 5 – PROPERTY, PLANT AND EQUIPMENT

	Crude Oil Assets	Gas Processing Facilities	Corporate and Other Assets	Total
Cost or deemed cost				
Balance at July 1, 2012	\$ 238,212	\$ 31,745	\$ 5,456	\$ 275,413
Acquisition of Shona	162,063	-	-	162,063
Net additions	30,726	(22)	1,272	31,976
Transferred from Exploration and Evaluation assets (note 4)	8,377	-	-	8,377
Reclassifications	3,860	(1,964)	-	1,896
Balance at June 30, 2013	443,238	29,759	6,728	479,725
Additions	45,923	44	729	46,696
Balance at March 31, 2014	\$ 489,161	\$ 29,803	\$ 7,457	\$ 526,421
Accumulated depletion and depreciation				
Balance at July 1, 2012	\$ (88,085)	\$ (847)	\$ (2,643)	\$ (91,575)
Depletion and depreciation	(38,852)	(6,547)	(1,511)	(46,910)
Impairment	(106,755)	-	-	(106,755)
Reclassifications	(1,893)	-	-	(1,893)
Derecognition, inventory adjustments and other	5,663	-	23	5,686
Balance at June 30, 2013	(229,922)	(7,394)	(4,131)	(241,447)
Depletion and depreciation	(20,605)	(2,628)	(610)	(23,843)
Inventory adjustments and other	755	-	-	755
Balance at March 31, 2014	\$ (249,772)	\$ (10,022)	\$ (4,741)	\$ (264,535)
Carrying amounts				
At July 1, 2012 (restated – note 17)	\$ 150,127	\$ 30,898	\$ 2,813	\$ 183,838
At June 30, 2013 (restated – note 17)	\$ 213,316	\$ 22,365	\$ 2,597	\$ 238,278
At March 31, 2014	\$ 239,389	\$ 19,781	\$ 2,716	\$ 261,886

During the three and nine months ended March 31, 2014, \$1.9 million and \$4.1 million (2013 - \$1.5 million and \$4.1 million) of compensation and other costs were capitalized, respectively, which reduced general and administrative expense and stock-based compensation expense for the periods.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the three and nine months ended March 31, 2014 and 2013

(in United States dollars (tabular amounts in thousands) except as otherwise noted)

NOTE 6 – RESTRICTED CASH

	March 31, 2014	June 30, 2013 (restated) (note 17)	July 1, 2012
Restricted cash – current	\$ 6,028	\$ 7,127	\$ 6,072
Restricted cash – long term	46,097	19,267	483
	\$ 52,125	\$ 26,394	\$ 6,555

At March 31, 2014, restricted cash consisted of \$36.8 million of term deposits used as collateral to secure the Ecuador IPC's borrowings, \$8.6 million for work commitments and other capital commitments, and \$6.7 million held in a debt reserve account as required under its senior secured term loan.

NOTE 7 – CONVERTIBLE DEBENTURES

Convertible debentures are recorded at fair value through profit or loss. Subsequent to initial recognition, these financial instruments are measured at fair value and changes therein are recognized in profit or loss. A reconciliation of convertible debentures is provided below.

Balance at July 1, 2012	\$ 25,381
Unrealized gain	(2,614)
Foreign exchange gain	(676)
Balance at June 30, 2013	22,091
Unrealized loss	3,403
Foreign exchange gain	(1,253)
Balance at March 31, 2014	\$ 24,241

NOTE 8 – WARRANTS

	Number (000s)	Amount
Balance at July 1, 2012	329	\$ 896
Issued on Shona acquisition	5,053	2,231
Unrealized gain	-	(1,085)
Foreign exchange gain	-	(171)
Balance at June 30, 2013	5,382	1,871
Exercised	(607)	(1,579)
Expired	(1,114)	(650)
Unrealized loss	-	8,591
Foreign exchange gain	-	(494)
Balance at March 31, 2014	3,661	\$ 7,739

1,145,818 warrants were exercised subsequent to March 31, 2014 up to and including May 12, 2014.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the three and nine months ended March 31, 2014 and 2013

(in United States dollars (tabular amounts in thousands) except as otherwise noted)

NOTE 9 – SHARE CAPITAL

Authorized

The Corporation is authorized to issue an unlimited number of common shares.

Issued and Outstanding

	Number (000s)		Amount
Balance at July 1, 2012	61,898	\$	340,775
Issued on Shona acquisition	24,601		68,346
Issued on exercise of stock options	7		7
Transfer from other reserves for stock options exercised	-		3
Share issuance costs	-		(361)
Balance at June 30, 2013	86,506		408,770
Issued on property acquisition	2,454		15,000
Issued on exercise of stock options and warrants	1,260		4,255
Transfer from other reserves and warrants for stock options and warrants exercised	-		2,487
Balance at March 31, 2014	90,220	\$	430,512

On May 6, 2014, the Corporation announced that it has entered into an agreement with a syndicate of underwriters to purchase, on a bought deal basis, 15,823,000 common shares of Canacol at a price of C\$7.90 per Common Share for gross proceeds of C\$125,001,700 (the "Offering"). The Corporation has granted the Underwriters an option to purchase up to 15% additional common shares, exercisable for a period of 30 days following the date of closing to cover over-allotments, if any. The Offering is expected to close on or about May 27, 2014.

Stock Options

The number and weighted-average exercise prices of stock options were as follows:

	Number (000s)	Weighted-Average Exercise Price (C\$)
Balance at June 30, 2013	7,451	6.61
Granted	1,771	6.52
Exercised	(653)	2.84
Forfeited and cancelled	(555)	9.13
Balance at March 31, 2014	8,014	6.72

Information with respect to stock options outstanding at December 31, 2013 is presented below.

Stock Options Outstanding				Stock Options Exercisable	
Range of Exercise Prices (C\$)	Number of Stock Options (000s)	Weighted-Average Remaining Contractual Life (years)	Weighted-Average Exercise Price (C\$)	Number of Stock Options (000s)	Weighted-Average Exercise Price (C\$)
\$1.00 to \$3.50	2,067	2.73	3.20	1,642	3.16
\$3.60 to \$7.00	3,148	3.61	6.00	2,094	5.90
\$7.10 to \$10.50	2,137	2.12	8.83	2,053	8.84
\$10.60 to \$14.00	133	1.93	12.10	120	12.11
\$14.10 and higher	529	1.82	14.90	526	14.90
	8,014	2.84	6.72	6,435	6.99

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

For the three and nine months ended March 31, 2014 and 2013

(in United States dollars (tabular amounts in thousands) except as otherwise noted)

Stock-based compensation of \$2.5 million and \$3.2 million (2013 – \$1.4 million and \$3.5 million) were expensed and \$1.0 million and \$1.6 million (2013 – \$1.0 million and \$2.6 million) were capitalized during the three and nine months ended March 31, 2014, respectively.

NOTE 10 – FINANCE INCOME AND EXPENSE

	Three months ended March 31,		Nine months ended March 31,	
	2014	2013	2014	2013
Finance income				
Interest and other income	\$ (386)	\$ (800)	\$ (1,243)	\$ (1,499)
Finance expense				
Fair value adjustment on equity tax payable	13	30	46	92
Accretion on decommissioning obligations	125	105	395	245
Amortization of upfront fees	474	802	1,415	1,136
Phantom warrants issued on closing of term loan	-	-	-	1,906
Interest and other expense	2,190	2,470	5,952	3,347
	2,802	3,407	7,808	6,726
Net finance expense	\$ 2,416	\$ 2,607	\$ 6,565	\$ 5,227

NOTE 11 – EARNINGS (LOSS) PER SHARE

Basic and diluted earnings per share were calculated as follows:

	Three months ended March 31,		Nine months ended March 31,	
	2014	2013	2014	2013
		(restated) (note 17)		(restated) (note 17)
Net income (loss), basic and diluted	\$ 19,438	\$ (3,425)	\$ 12,007	\$ (8,761)
Weighted-average common share adjustments				
Weighted-average common shares outstanding, basic	88,767	86,499	87,323	70,966
Effect of warrants	1,038	-	394	-
Effect of stock options	1,502	-	906	-
Weighted-average common shares outstanding, diluted	91,307	86,499	88,623	70,966

For the three and nine months ended March 31, 2014 and 2013, the effect of the convertible debentures was anti-dilutive. For the three and nine months ended March 31, 2013, all other items were anti-dilutive due to the net loss.

NOTE 12 – SUPPLEMENTAL INFORMATION

The Corporation records petroleum and natural gas sales net of royalties. Royalties incurred were as follows:

	Three months ended March 31,		Nine months ended March 31,	
	2014	2013	2014	2013
Petroleum and natural gas royalties	\$ 5,746	\$ 3,103	\$ 14,591	\$ 8,751

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

For the three and nine months ended March 31, 2014 and 2013

(in United States dollars (tabular amounts in thousands) except as otherwise noted)

Income taxes and interest paid were as follows:

	Three months ended March 31,		Nine months ended March 31,	
	2014	2013	2014	2013
Income taxes paid	\$ 17	\$ 3,952	\$ 17	\$ 3,952
Interest paid	\$ 1,779	\$ 2,056	\$ 6,645	\$ 3,716

(Gain) loss on derivatives and financial instruments:

	Three months ended March 31,		Nine months ended March 31,	
	2014	2013	2014	2013
Embedded derivatives	\$ -	\$ 978	\$ 2,714	\$ 1,886
Convertible debentures – unrealized	808	(251)	3,403	(1,885)
Warrants – unrealized	(1,494)	360	8,591	594
Warrants – realized	-	-	(611)	-
Phantom warrants – unrealized	(532)	678	6,481	1,301
Restricted share units – unrealized	(88)	-	3,653	-
Restricted share units - realized	-	-	618	-
Share investments – unrealized	47	-	311	-
Commodity contracts – unrealized	(52)	(1,158)	(247)	990
Commodity contracts – realized	-	723	432	1,634
	\$ (1,311)	\$ 1,330	\$ 25,345	\$ 4,520

Changes in non-cash working capital are comprised of:

	Three months ended March 31,		Nine months ended March 31,	
	2014	2013	2014	2013
Change in:				
Trade and other receivables	\$ (19,129)	\$ (14,835)	\$ (14,004)	\$ (1,999)
Prepaid expenses and deposits	(27)	20	(503)	(344)
Crude oil inventory	2,330	(2,369)	1,011	1,584
Trade and other payables	(13,883)	(11,449)	10,768	(29,988)
Equity tax payable	(21)	(78)	(746)	(638)
Taxes payable	11,331	2,461	15,585	399
	(19,399)	(26,250)	12,111	(30,986)
Attributable to:				
Operating activities	(13,278)	(21,174)	10,194	(24,259)
Investing activities	(6,121)	(5,076)	1,917	(6,727)
	\$ (19,399)	\$ (26,250)	\$ 12,111	\$ (30,986)

NOTE 13 – SEGMENTED INFORMATION

The Corporation's only reportable segment is "Colombia" (previously "Colombia" and "Ecuador"). As a result of the adoption of IFRS 11, "Ecuador" no longer meets the definition of a reportable segment under IFRS 8. Consequently, "Ecuador" has been removed from the composition of the Corporation's reportable segments during the three and nine months ended March 31, 2014.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

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The Corporation's investment and its share of profit in the Ecuador IPC (the unconsolidated joint venture that was previously proportionately consolidated as "Ecuador") have been added to "Other Segments". The main purpose of "Other Segments" is to reconcile the reportable segment to the Corporation's combined results. "Other Segments" is not a reportable segment. The Corporation's chief operating decision maker is its executive officers.

The following tables show information regarding the Corporation's segments.

	Colombia		Other Segments		Total
	(reportable)		(non-reportable)		
Three months ended March 31, 2014					
Revenues	\$	55,653	\$	-	\$ 55,653
Share of joint venture profits		-		1,599	1,599
Expenses, excluding income taxes		(22,582)		(2,350)	(24,932)
Net income (loss) before taxes		33,071		(751)	32,320
Income taxes		12,882		-	12,882
Net income (loss)	\$	20,189	\$	(751)	\$ 19,438
Capital expenditures, net	\$	35,866	\$	49	\$ 35,915
Three months ended March 31, 2013					
Revenues	\$	34,602	\$	-	\$ 34,602
Share of joint venture loss		-		(1,056)	(1,056)
Expenses, excluding income taxes		(29,549)		(6,944)	(36,493)
Net income (loss) before taxes		5,053		(8,000)	(2,947)
Income taxes		281		197	478
Net income (loss)	\$	4,772	\$	(8,197)	\$ (3,425)
Capital expenditures, net	\$	2,947	\$	74	\$ 3,021
Nine months ended March 31, 2014					
Revenues	\$	146,043	\$	-	\$ 146,043
Share of joint venture profits		-		2,792	2,792
Expenses, excluding income taxes		(88,928)		(30,799)	(119,727)
Net income (loss) before taxes		57,115		(28,007)	29,108
Income taxes		17,101		-	17,101
Net income (loss)	\$	40,014	\$	(28,007)	\$ 12,007
Capital expenditures, net	\$	75,343	\$	729	\$ 76,072
Nine months ended March 31, 2013					
Revenues	\$	102,394	\$	-	\$ 102,394
Share of joint venture loss		-		(2,190)	(2,190)
Expenses, excluding income taxes		(96,028)		(12,963)	(108,991)
Net income (loss) before taxes		6,366		(15,153)	(8,787)
Income taxes (recovery)		(753)		727	(26)
Net income (loss)	\$	7,119	\$	(15,880)	\$ (8,761)
Capital expenditures, net	\$	217,356	\$	1,019	\$ 218,375

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	Colombia (reportable)		Other Segments (non-reportable)		Total
As at March 31, 2014					
Total assets	\$	446,770	\$	101,731	\$ 548,501
Total liabilities	\$	155,196	\$	116,542	\$ 271,738
As at June 30, 2013 (restated) (note 17)					
Total assets	\$	383,651	\$	85,941	\$ 469,592
Total liabilities	\$	123,625	\$	106,664	\$ 230,289
As at July 1, 2012					
Total assets	\$	314,394	\$	92,434	\$ 406,828
Total liabilities	\$	64,658	\$	51,076	\$ 115,734

NOTE 14 – FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Fair Value of Financial Instruments

The carrying values and respective fair values of financial assets and liabilities at March 31, 2014 are summarized as follows:

	Carrying Value		Fair Value	
Fair value through profit or loss				
Cash and cash equivalents	\$	35,699	\$	35,699
Restricted cash		52,125		52,125
Convertible debentures		24,241		24,241
Commodity contracts liabilities		33		33
Phantom warrants		7,930		7,930
Warrants		7,739		7,739
Restricted share units		6,177		6,177
Investments		2,707		2,707
Loans and receivables				
Bank debt		135,675		140,000
Trade and other receivables		53,664		53,664
Other liabilities				
Trade and other payables		52,124		52,124
Equity tax payable		1,106		1,106
Other long term obligations		219		219
Deferred income		3,731		3,731

The Corporation classifies the fair value of financial instruments measured at fair value according to the following hierarchy based on the amount of observable inputs used to value the instrument.

- Level 1 – Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.
- Level 2 – Pricing inputs are other than quoted prices in active markets included in Level 1. Prices in Level 2 are either directly or indirectly observable as of the reporting date. Level 2 valuations are based on inputs, including quoted forward prices for commodities, time value and volatility factors, which can be substantially observed or corroborated in the marketplace.

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- Level 3 – Valuations in this level are those with inputs for the asset or liability that are not based on observable market data.

The Corporation's financial instruments have been assessed on the fair value hierarchy described above. Cash and cash equivalents, restricted share units and convertible debentures are classified as Level 1. Commodity contracts liabilities and investments are classified as Level 2. Warrants and phantom warrants are classified as Level 3. Assessment of the significance of a particular input to the fair value measurement requires judgement and may affect the placement within the fair value hierarchy level.

During the three months ended December 31, 2013, the Corporation amended its trucking contract whereby i) the Corporation no longer has the option to purchase up to 50 trucks at the end of the contract and ii) any excess or shortage of the fees charged over the actual operating costs will no longer be shared between the Corporation and the trucking company. Consequently, the embedded derivatives asset was de-recognized as at December 31, 2013, resulting in a loss on embedded derivatives of \$2.7 million for the nine months ended March 31, 2014. The amended trucking contract will expire in June 2016.

Restricted Share Units

	Number (000s)	Amount
Balance at July 1, 2012	-	\$ -
Granted	1,404	3,592
Unrealized loss	-	468
Foreign exchange gain	-	(146)
Balance at June 30, 2013	1,404	3,914
Granted	42	233
Settled	(468)	(1,321)
Unrealized loss	-	3,653
Foreign exchange gain	-	(302)
Balance at March 31, 2014	978	\$ 6,177

Subsequent to March 31, 2014, 936,095 restricted share units vested and were settled in cash.

Phantom Warrants

In connection with the closing of the Shona business acquisition on December 21, 2012, the Corporation entered into a credit agreement for \$45.0 million, which has since been replaced. In consideration for entering into the credit agreement, the Corporation agreed to a "phantom warrant payment" arrangement such that the Corporation would pay an amount (in cash or Canacol Shares, at the election of the Corporation) equal to the in-the-money amount of 2,697,292 common share purchase warrants of the Corporation at an exercise price of C\$4.50 per Canacol Share. The phantom warrant payment may be demanded partially or in full at any time for a period of three years.

	Number (000s)	Amount
Balance at July 1, 2012	-	\$ -
Issued	2,697	1,906
Unrealized loss	-	120
Foreign exchange gain	-	(160)
Balance at June 30, 2013	2,697	1,866
Unrealized loss	-	6,481
Foreign exchange gain	-	(417)
Balance at March 31, 2014	2,697	\$ 7,930

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The fair value of the phantom warrants was estimated using the Black-Scholes option pricing model with the following inputs:

	March 31, 2014	June 30, 2013
Fair value at grant date (C\$)	0.70	0.70
Share price (C\$)	6.98	2.93
Exercise price (C\$)	4.50	4.50
Volatility	58.07%	60.76%
Remaining warrant life	1.7 years	2.5 years
Dividends	Nil	Nil
Risk-free interest rate	1.07%	1.22%

Market Risk

Market risk is the risk that changes in market factors, such as commodity prices, foreign exchange rates, and interest rates will affect the Corporation's cash flows, profit or loss, liquidity or the value of financial instruments. The objective of market risk management is to mitigate market risk exposures where considered appropriate and maximize returns.

(i) Commodity Price Risk

Commodity price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate as a result of changes in commodity prices. Lower commodity prices can also impact the Corporation's ability to raise capital. Commodity prices for crude oil are impacted by world economic events that dictate the levels of supply and demand. From time to time the Corporation may attempt to mitigate commodity price risk through the use of financial derivatives. The Corporation's policy is to only enter into commodity contracts considered appropriate to a maximum of 50% of forecasted production volumes.

At March 31, 2014, the Corporation had one financial oil collar outstanding under the following terms:

Period	Volume	Type	Price Range
Jan 2014 – Dec 2014	500 bbls/day	Financial Brent Oil Collar	\$75.00 – \$123.50

(ii) Foreign Currency Risk

Foreign currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate as a result of changes in foreign currency exchange rates. The Corporation is exposed to foreign currency fluctuations as certain expenditures are denominated in Colombian pesos and Canadian dollars, and to a lesser extent, Brazilian reais and Peruvian sol.

The Corporation had no forward exchange rate contracts in place as at or during the three and nine months ended March 31, 2014.

(iii) Interest Rate Risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate as a result of changes in market interest rates. The Corporation is exposed to interest rate risk on certain variable interest rate debt instruments, to the extent they are drawn. The remainder of the Corporation's financial assets and liabilities are not exposed to interest rate risk. The Corporation had no interest rate swap or financial contracts in place as at or during the three and nine months ended March 31, 2014.

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Liquidity Risk

Liquidity risk is the risk that the Corporation will not be able to meet its financial obligations as they become due. The Corporation's approach to managing liquidity is to ensure, within reasonable means, sufficient liquidity to meet its liabilities when due, under both normal and unusual conditions, without incurring unacceptable losses or jeopardizing the Corporation's business objectives. The Corporation prepares annual capital expenditure budgets which are monitored regularly and updated as considered necessary. Petroleum and natural gas production is monitored daily to provide current cash flow estimates and the Corporation utilizes authorizations for expenditures on projects to manage capital expenditures.

The following table outlines the contractual maturities of the Corporation's financial liabilities at March 31, 2014:

	Less than 1 year	1-2 years	Thereafter	Total
Bank debt – principal	18,667	37,333	84,000	140,000
Trade and other payables	52,124	-	-	52,124
Deferred income	-	3,731	-	3,731
Equity tax payable – undiscounted	1,119	-	-	1,119
Other long term obligations	-	-	219	219
Convertible debentures – principal	-	23,087	-	23,087
Commodity contracts	33	-	-	33
Phantom warrants	-	7,930	-	7,930
Warrants	3,522	4,217	-	7,739
Restricted share units	6,044	133	-	6,177
	81,509	76,431	84,219	242,159

In addition to the above, the Corporation has issued letters of credit totalling \$33.2 million to guarantee certain obligations under its exploration contracts and to guarantee other contractual commitments. Such amounts only become payable should the Corporation not meet those obligations.

Credit Risk

Credit risk reflects the risk of loss if counterparties do not fulfill their contractual obligations. The majority of the Corporation's trade receivable balances relate to petroleum and natural gas sales. The Corporation's policy is to enter into agreements with customers that are well established and well financed entities in the oil and gas industry such that the level of risk is mitigated. To date, the Corporation has not experienced any material credit losses in the collection of its trade receivables. In Colombia, a significant portion of crude oil sales are with customers that are directly or indirectly controlled by the government. The Corporation has also entered into sales agreements with certain Colombian private sector companies.

The Corporation's trade receivables primarily relate to sales of petroleum and natural gas, which are normally collected within 45 days of the month of production. The Corporation has historically not experienced any collection issues with its customers.

Capital Management

The Corporation's policy is to maintain a strong capital base in order to provide flexibility in the future development of the business and maintain investor, creditor and market confidence. The Corporation manages its capital structure and makes adjustments in response to changes in economic conditions and the risk characteristics of the underlying assets. The Corporation considers its capital structure to include common share capital, convertible debentures, bank debt and working capital, defined as current assets less current liabilities, excluding non-cash items such as the current portion of commodity contracts, warrants and any embedded derivatives asset/liability. In order to maintain or adjust the capital structure, from time to time the Corporation may issue common shares or other securities, sell assets or adjust its capital spending to manage current and projected debt levels.

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The Corporation monitors leverage and adjusts its capital structure based on the ratio of net debt to funds from operations. This ratio is calculated as net debt, defined as the principal amount of its outstanding bank debt plus the principal amount of its convertible debentures, unless the debentures are in-the-money or may otherwise be settled in common shares at the option of the Corporation, less working capital, as defined above and less the current portion of bank debt and convertible debentures included above, divided by annualized adjusted funds from operations, defined as cash flows from operating activities, excluding changes in non-cash working capital, and adjusted for the Corporation's share of operating funds flows under the Ecuador IPC, which was previously proportionately consolidated and is now accounted for under the equity method (see note 16). The Corporation uses the ratio of net debt to adjusted funds from operations as a key indicator of the Corporation's leverage and to monitor the strength of its financial position.

In order to facilitate the management of this ratio, the Corporation prepares annual budgets, which are updated as necessary depending on varying factors including current and forecast crude oil prices, changes in capital structure, execution of the Corporation's business plan and general industry conditions. The annual budget is approved by the Board of Directors and updates are prepared and reviewed as required.

	March 31, 2014	
Bank debt (current and long-term) – principal	\$	140,000
Working capital surplus, excluding the current portion of bank debt, warrants, and derivatives		(33,328)
Net debt	\$	106,672
Annualized adjusted funds from operations ⁽¹⁾	\$	96,201
Net debt to adjusted funds from operations		1.1

(1) Adjusted funds from operations for the nine months ended March 31, 2014, annualized, and inclusive of amounts related to the Ecuador IPC.

NOTE 15 – COMMITMENTS AND CONTINGENCIES

Presented below are the Corporation's contractual commitments at March 31, 2014:

	Less than 1 year		1-3 years		Thereafter		Total
Exploration and production contracts	\$	21,065	\$	25,608	\$	-	\$ 46,673
Office lease		1,007		1,679		4,136	6,822

Ecuador Incremental Production Contract

In addition to the commitments described above, the Corporation has a non-operated 25% equity participation interest (27.9% capital participation interest) in a joint-venture consortium which in 2012 was awarded an incremental production contract for the Libertador and Atacapi mature oil fields in Ecuador. The consortium is committed to incur project expenditures for a total of \$334 million (\$93.3 million net to the Corporation) over the 15 year term of the contract. As at March 31, 2014, the Corporation had incurred \$45.1 million of expenditures in connection with its Ecuador IPC commitment.

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Contingencies

In the normal course of operations, the Corporation has disputes with industry participants for which it currently cannot determine the ultimate results. The Corporation has a policy to record contingent liabilities as they become determinable and the probability of loss is more likely than not.

Provisions

There is an ongoing disagreement between the Corporation and another Colombian entity (the “Counterparty”) over the payment of certain operating costs relating to crude oil production. The Counterparty has asserted that Canacol is liable for certain operating costs incurred by the Counterparty. Canacol disagrees with this assertion because it believes the Counterparty has not met the terms of the contract governing these operating costs. The ultimate result of this disagreement cannot be determined at March 31, 2014.

At June 30, 2013, the Corporation believed that the disagreement may result in a cash settlement and had recorded a provision of \$10.5 million based on management’s estimate. At March 31, 2014, the Corporation believes that the possibility of an outflow of resources embodying economic benefits to settle this disagreement is remote and has consequently reversed such provision during the three months ended March 31, 2014 in accordance with IAS 37.

Detailed information of the estimated provision and the reversal thereof was not disclosed as it may prejudice seriously the position of the Corporation in the disagreement with the Counterparty.

NOTE 16 – INVESTMENT IN JOINT VENTURE

The Corporation conducts its operations in Ecuador through a 25% equity interest (27.9% capital participation interest) in the Ecuador IPC, which is reported in these financial statements using the equity method of accounting. Prior to the adoption of IFRS 11, the Ecuador IPC was accounted for using the proportionate consolidation method of accounting. Details of the Ecuador IPC’s net assets, revenues and net income (loss) are shown below with comparative information due to the adoption of IFRS 11.

As at	March 31, 2014		June 30, 2013		July 1, 2012
Total assets	\$	200,690	\$	94,878	\$ 21,154
Total liabilities		185,001		105,334	21,926
Equity		15,689		(10,456)	(772)
Investment in joint venture		7,306		1,963	4,361

	Three months ended		Nine months ended	
	2014	March 31, 2013	2014	March 31, 2013
Joint venture net income (loss)	\$ 6,396	\$ (4,224)	\$ 11,168	\$ (8,760)
Corporation’s share of joint venture profit (loss)	\$ 1,599	\$ (1,056)	\$ 2,792	\$ (2,190)

NOTE 17 – EFFECT OF IFRS 11 ADOPTION AND CHANGE OF COMPARATIVE STATEMENT OF CASH FLOWS

The adoption of IFRS 11 affected the Corporation’s previously reported Consolidated Statement of Financial Position as at June 30, 2013 and the Consolidated Statement of Operations and Comprehensive Income (Loss), and Consolidated Statement of Cash Flows for the three and nine months ended March 31, 2013. Prior to the adoption of IFRS 11, the Ecuador IPC was accounted for using the proportionate consolidation method and is now being accounted for using the equity method of accounting.

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Impact on Consolidated Statements of Financial Position

As at July 1, 2012	As Previously Reported	Effect of IFRS 11 Adoption	Restated
Trade and other receivables	\$ 32,801	\$ (991)	\$ 31,810
Property, plant and equipment	187,208	(3,370)	183,838
Investment in joint venture	-	4,361	4,361

As at June 30, 2013	As Previously Reported	Effect of IFRS 11 Adoption	Restated
Trade and other receivables	\$ 41,957	\$ (3,816)	\$ 38,141
Restricted cash – non-current	4,849	14,418	19,267
Property, plant and equipment	257,586	(19,308)	238,278
Investment in joint venture	-	1,963	1,963
Deferred tax liabilities	3,409	452	3,861
Deficit	(202,693)	(7,195)	(209,888)

Impact on Consolidated Statements of Operations and Comprehensive Income (Loss)

For the three months ended March 31, 2013	As Previously Reported	Effect of IFRS 11 Adoption	Restated
Petroleum and natural gas revenue, net of royalties	\$ 36,725	\$ (2,123)	\$ 34,602
Share of joint venture loss	-	(1,056)	(1,056)
Depreciation and depreciation	12,026	(580)	11,446
Deferred tax recovery	(2,189)	198	(1,991)
Net income and comprehensive income	(628)	(2,797)	(3,425)

For the nine months ended March 31, 2013	As Previously Reported	Effect of IFRS 11 Adoption	Restated
Petroleum and natural gas revenue, net of royalties	\$ 105,870	\$ (3,476)	\$ 102,394
Share of joint venture loss	-	(2,190)	(2,190)
Depreciation and depreciation	35,520	(935)	34,585
Deferred tax recovery	(1,170)	318	(852)
Net loss and comprehensive loss	(3,711)	(5,050)	(8,761)

Further, at June 30, 2013, the Corporation changed the presentation of its statements of cash flows whereby interest expense paid was reclassified from operating activities to financing activities. The Corporation believes that this approach provides more reliable and relevant information on its operating activities. For the three and nine months ended March 31, 2013, the effect of such reclassification was an increase in cash flows from operating activities, offset by a decrease of the same amount in cash flows from financing activities.

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Impact on Consolidated Statements of Cash Flows

For the three months ended March 31, 2013	As Previously Reported	Effect of IFRS 11 Adoption	Effect of Reclassification	Restated
Cash flows from operating activities	\$ (1,154)	\$ (9,036)	\$ 1,670	\$ (8,520)
Cash flows from investing activities	(11,063)	9,036	-	(2,027)
Cash flows from financing activities	(9,912)	-	(1,670)	(11,582)
Change in cash and cash equivalents	\$ (22,129)	\$ -	\$ -	\$ (22,129)

For the nine months ended March 31, 2013	As Previously Reported	Effect of IFRS 11 Adoption	Effect of Reclassification	Restated
Cash flows from operating activities	\$ 13,868	\$ (11,400)	\$ 1,848	\$ 4,316
Cash flows from investing activities	(94,295)	11,400	-	(82,895)
Cash flows from financing activities	60,762	-	(1,848)	58,914
Change in cash and cash equivalents	\$ (19,665)	\$ -	\$ -	\$ (19,665)

NOTE 18 – SUBSEQUENT EVENTS

On April 24, 2014, the Corporation completed the upsizing of its existing Senior Secured Term Loan, from \$140 million to \$220 million, with no changes to the terms of the Senior Secured Term Loan or the repayment schedule. Interest is payable quarterly and principal repayable in 15 equal quarterly instalments starting in October 2014. The revised term loan carries interest at LIBOR plus 4.50-5.00% and is secured by all of the material assets of the Corporation.

On May 6, 2014, the Corporation announced that it has entered into an agreement with a syndicate of underwriters to purchase, on a bought deal basis, 15,823,000 common shares of Canacol at a price of C\$7.90 per Common Share for gross proceeds of C\$125,001,700 (the "Offering"). The Corporation has granted the Underwriters an option to purchase up to 15% additional common shares, exercisable for a period of 30 days following the date of closing to cover over-allotments, if any. The Offering is expected to close on or about May 27, 2014.

Subsequent to March 31, 2014, 936,095 restricted share units vested and were settled in cash.

1,145,818 warrants were exercised subsequent to March 31, 2014 up to and including May 12, 2014.