

**PETAQUILLA MINERALS LTD.**  
**(An Exploration Stage Company)**

**INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

**Three Months Ended August 31, 2008, and Three Months Ended July 31, 2007**

**(Unaudited – Prepared by Management)**

**PETAQUILLA MINERALS LTD.**  
(An Exploration Stage Company)

(the “Company”)

**CONSOLIDATED INTERIM FINANCIAL STATEMENTS**  
**Three months ended August 31, 2008, and Three months ended July 31, 2007**

**NOTICE OF NO AUDITOR REVIEW OF INTERIM FINANCIAL STATEMENTS**

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

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

**PETAQUILLA MINERALS LTD.**

(An Exploration Stage Company)

**CONSOLIDATED BALANCE SHEETS**

(Unaudited, expressed in Canadian Dollars) (See Note 1 Nature of Operations and Going Concern Uncertainty)

|  | August 31,<br>2008    | May 31,<br>2008       |
|--|-----------------------|-----------------------|
| <b>ASSETS (Note 11)</b>  |                       |                       |
| <b>Current</b>   |                       |                       |
| Cash and cash equivalents (Note 3)                                       | \$ 17,193,885         | \$ 12,775,606         |
| Receivables  | 48,068                | 448,270               |
| Prepaid expenses   | <u>460,273</u>        | <u>308,456</u>        |
| <b>Total current assets</b>  | 17,702,226            | 13,532,332            |
| <b>Restricted cash</b> (Note 6)  | 712,729               | 666,288               |
| <b>Investment in Petaquilla Copper Ltd.</b> (Note 5)                     | 9,238,745             | 9,452,421             |
| <b>Deposit on equipment</b>  | 295,694               | -                     |
| <b>Property and equipment</b>  | 17,346,969            | 16,681,830            |
| <b>Mineral properties</b> (Note 4)                                       | <u>76,797,968</u>     | <u>67,149,615</u>     |
| <b>Total assets</b>  | <u>\$ 122,094,331</u> | <u>\$ 107,482,486</u> |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>                              |                       |                       |
| <b>Current</b>   |                       |                       |
| Bank overdraft   | \$ -                  | \$ 2,087,820          |
| Operating credit line facility (Note 7)                                  | 5,858,087             | 3,849,974             |
| Accounts payable and accrued liabilities                                 | 3,841,817             | 7,286,410             |
| Amount payable to a related party (Note 15)                              | 999,514               | 1,157,788             |
| Current portion of deferred services and materials (Note 9)              | 242,332               | 247,343               |
| Current portion of obligation under capital leases (Note 10)             | 2,283,811             | 2,162,289             |
| Current portion of long-term debt (Note 8)                               | <u>432,827</u>        | <u>433,621</u>        |
| <b>Total current liabilities</b>   | 13,658,388            | 17,225,245            |
| <b>Deferred services and materials</b> (Note 9)                          | 3,922,767             | 3,980,203             |
| <b>Asset retirement obligations</b> (Note 19)                            | 4,701,093             | 4,308,083             |
| <b>Senior secured notes</b> (Note 11)                                    | 55,992,194            | 26,630,004            |
| <b>Long-term debt</b> (Note 8)   | 88,945                | 161,625               |
| <b>Obligations under capital leases</b> (Note 10)                        | 3,446,946             | 3,968,591             |
| <b>Total liabilities</b>   | <u>81,810,333</u>     | <u>56,273,751</u>     |
| <b>Commitments and contingencies</b> (Notes 17 and 21)                   |                       |                       |
| <b>Shareholders' equity</b>  |                       |                       |
| Share capital (Note 12)  |                       |                       |
| Authorized   |                       |                       |
| Unlimited common shares and preferred shares without par value (Note 12) |                       |                       |
| Issued and outstanding   |                       |                       |
| 96,018,641 (May 31, 2008 – 95,958,641) common shares                     | 105,937,271           | 105,858,083           |
| Warrants (Notes 12 and 14)   | 13,795,840            | 12,976,997            |
| Treasury shares, at cost   |                       |                       |
| 44,200 (May 31, 2008 – 44,200) common shares                             | (166,981)             | (166,981)             |
| Contributed surplus (Note 12)  | 16,549,748            | 16,406,018            |
| Deficit  | <u>(95,831,880)</u>   | <u>(83,865,382)</u>   |
| <b>Total shareholders' equity</b>  | <u>40,283,998</u>     | <u>51,208,735</u>     |
| <b>Total liabilities and shareholders' equity</b>                        | <u>\$ 122,094,331</u> | <u>\$ 107,482,486</u> |

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

**PETAQUILLA MINERALS LTD.**

(An Exploration Stage Company)

**CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS AND DEFICIT**

(Unaudited, expressed in Canadian Dollars)

|   | Three months<br>ended August 31,<br>2008 | Three months<br>ended July 31,<br>2007 |
|---|--|--|
| <b>EXPENSES</b>   |  |  |
| Accounting and legal  | \$ 408,275                               | \$ 191,100                             |
| Accretion of asset retirement obligation                    | 85,112                                   | 84,250                                 |
| Consulting fees   | 33,300                                   | 296,919                                |
| Amortization  | 84,818                                   | 437,133                                |
| Filing fees   | 102,521                                  | 22,695                                 |
| Investor relations and shareholder information              | 107,314                                  | 204,541                                |
| Office administration                                       | 327,615                                  | 628,687                                |
| Rent  | 36,824                                   | 44,696                                 |
| Stock-based compensation                                    | 270,865                                  | 2,109,004                              |
| Travel  | 122,324                                  | 261,563                                |
| Debt issuance costs   | 3,157,133                                | -                                      |
| Wages and benefits  | 761,614                                  | 492,969                                |
| Total expenses  | <u>(5,497,715)</u>                       | <u>(4,773,557)</u>                     |
| <b>OTHER INCOME (EXPENSE)</b>                               |  |  |
| Foreign exchange gain (loss)                                | (3,367,758)                              | (475,200)                              |
| Gain on sale of marketable securities                       | -  | 28,067                                 |
| Interest income   | 82,002                                   | -                                      |
| Interest on long-term debt                                  | (13,799)                                 | -                                      |
| Asset usage fees  | (2,067)                                  | 195,997                                |
| Power and drilling services                                 | 60,583                                   | -                                      |
| Loss from equity investment                                 | (1,253,146)                              | (1,261,757)                            |
| Loss on senior secured notes                                | (3,014,068)                              | -                                      |
| Gain on dilution of equity investment                       | 1,039,470                                | 362,322                                |
| Total other income (expenses)                               | <u>(6,468,783)</u>                       | <u>(1,150,571)</u>                     |
| <b>Net Loss and comprehensive loss for the period</b>       | (11,966,498)                             | (5,924,128)                            |
| <b>Deficit, beginning of period</b>                         | <u>(83,865,382)</u>                      | <u>(79,521,082)</u>                    |
| <b>Deficit, end of period</b>                               | <u>\$ (95,831,880)</u>                   | <u>\$ (85,445,210)</u>                 |
| <b>Basic and diluted loss per share</b>                     | <u>(0.13)</u>                            | <u>(0.06)</u>                          |
| <b>Weighted average number of common shares outstanding</b> | <u>95,959,132</u>                        | <u>91,146,116</u>                      |

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

**PETAQUILLA MINERALS LTD.**  
(An Exploration Stage Company)  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Unaudited, expressed in Canadian Dollars)

|   | Three months<br>ended August<br>31, 2008 | Three months<br>ended July 31,<br>2007 |
|---|--|--|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                             |  |  |
| Loss for the period   | (11,966,498)                             | (5,924,128)                            |
| Items not affecting cash:   |  |  |
| Accretion of asset retirement obligation                                | 85,112                                   | 84,250                                 |
| Amortization  | 84,818                                   | 437,133                                |
| Gain on dilution of equity investment                                   | (1,039,470)                              | (362,322)                              |
| Loss from equity investment   | 1,253,146                                | 1,261,757                              |
| Stock-based compensation  | 270,865                                  | 2,109,004                              |
| Loss on senior secured notes  | 3,014,068                                | -                                      |
| Debt issuance costs   | 3,157,133                                | -                                      |
| Foreign exchange (gain) loss on restricted cash                         | (46,441)                                 | 60,355                                 |
| Unrealized foreign exchange loss  | 3,450,980                                | -                                      |
| Changes in non-cash working capital items:                              |  |  |
| (Increase) decrease in receivables                                      | 400,202                                  | (49,145)                               |
| (Increase) decrease in prepaid expenses                                 | (151,817)                                | (600,490)                              |
| Prepaid services and materials  | (60,583)                                 | -                                      |
| Decrease in accounts payable to a related party                         | (158,274)                                | -                                      |
| (Decrease) increase in accounts payable and accrued liabilities         | (3,444,593)                              | (529,941)                              |
| Net cash used in operating activities                                   | <u>(5,151,352)</u>                       | <u>(3,513,527)</u>                     |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>                             |  |  |
| Net proceeds from exercise of warrants and options                      | 31,500                                   | 62,851                                 |
| Proceeds from shares subscribed   | -  | (150,000)                              |
| Share issuance costs  | -  | (30,568)                               |
| Repayment of bank overdraft   | (2,087,820)                              | -                                      |
| Proceeds from senior secured notes                                      | 28,211,000                               | -                                      |
| Proceeds from private placement   | -  | 2,824,305                              |
| Proceeds from capital leases  | -  | 6,697,259                              |
| Prepaid interest on senior secured notes                                | (4,231,650)                              | -                                      |
| Repayment of capital leases   | (400,123)                                | -                                      |
| Debt issuance costs   | (3,157,133)                              | -                                      |
| Repayment of long-term debt   | (73,474)                                 | (182,623)                              |
| Net cash provided by financing activities                               | <u>18,292,300</u>                        | <u>9,221,224</u>                       |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>                             |  |  |
| Acquisition of property and equipment                                   | (1,022,528)                              | (6,276,407)                            |
| Investment in mineral properties  | (8,387,625)                              | (5,063,545)                            |
| Deposits for equipment  | (295,694)                                | (649,292)                              |
| Payments from Petaquilla Copper Ltd                                     | -  | 8,310,183                              |
| Net cash used in investing activities                                   | <u>(9,705,847)</u>                       | <u>(3,679,061)</u>                     |
| <b>Impact of exchange rate changes on cash and cash<br/>Equivalents</b> | <u>983,178</u>                           | <u>-</u>                               |
| <b>Change in cash and cash equivalents</b>                              | <u>4,418,279</u>                         | <u>2,028,636</u>                       |
| <b>Cash and cash equivalents, beginning of period</b>                   | <u>12,775,606</u>                        | <u>665,291</u>                         |
| <b>Cash and cash equivalents, end of period</b>                         | <u><u>17,193,885</u></u>                 | <u><u>2,693,927</u></u>                |

**Supplemental disclosure with respect to cash flows**  
(Note 20)

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

**PETAQUILLA MINERALS LTD.**

(An Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited, expressed in Canadian Dollars)

August 31, 2008 and July 31, 2007

---

**1. NATURE OF OPERATIONS AND GOING CONCERN UNCERTAINTY**

Petaquilla Minerals Ltd. ("the Company") was incorporated in the Province of British Columbia. The Company's main focus is the Molejon Property located in the District of Donoso, Province of Colon, Panama.

The Company is in the process of exploring its mineral properties and has not yet determined whether these properties contain ore reserves. The recoverability of the amounts shown for mineral properties is dependent upon the ability of the Company to obtain the necessary financing to complete the exploration and development and upon future profitable production or proceeds from the disposition of properties. The Company will have to raise additional funds to complete the development phase of its programs and, while it has been successful in doing so in the past, there can be no assurance that it will be able to do so in the future.

The amounts shown as mineral properties represent costs to date and do not necessarily represent present or future values. Changes in future conditions could require material write-downs of the carrying amounts of the mineral properties.

The interim consolidated financial statements of the Company have been prepared by management in accordance with Canadian generally accepted accounting principles, except that they do not contain all disclosures as required for annual financial statements. The interim consolidated financial statements have been prepared following the same accounting policies as for the consolidated financial statements for the year ended May 31, 2008 except as noted. Accordingly, they should be read in conjunction with the 2008 consolidated financial statements and the notes thereto.

**2. SIGNIFICANT ACCOUNTING POLICIES**

**Basis of consolidation**

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Petaquilla Minerals, S.A. (a Panama corporation), Adrian Resources (BVI) Ltd. (a British Virgin Island corporation), Petaquilla Gold, S.A. (a Panama corporation), Aqua Azure S.A (a Panama corporation) and its 51% interest in Petaquilla Infraestructura Ltd. ("PQI") formerly Petaquilla Power and Water, S.A. ("PPW") (a Panama corporation). The Company proportionately consolidates its 69% interest in a joint venture investment, Compania Minera Belencillo, S.A. ("Belencillo") (a Panama corporation).

All inter-company transactions and balances have been eliminated upon consolidation.

**Adoption of new accounting policies**

On June 1, 2008, the Company adopted new accounting standards related to general standards of financial statement presentation, capital disclosure and financial instruments that were issued by the Canadian Institute of Chartered Accountants ("CICA"). The new CICA standards are as follows:

Section 1400, General Standards of Financial Statement Presentation

This Section specifies the requirements for assessing an entity's ability to continue as a going concern and disclosing any material uncertainties that cast doubt on its ability to continue as a going concern. The Company's disclosure reflects such assessment.

**PETAQUILLA MINERALS LTD.**  
 (An Exploration Stage Company)  
 NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS  
 (Unaudited, expressed in Canadian Dollars)  
 August 31, 2008 and July 31, 2007

---

**2. SIGNIFICANT ACCOUNTING POLICIES** (continued)

Section 1535, Capital Disclosures

This Section specifies the disclosure of information that enables users of an entity's financial statements to evaluate its objectives, policies and processes for managing capital such as qualitative information about these objectives, policies and processes for managing capital, summary quantitative data about what the entity manages as capital, whether it has complied with any capital requirements and, if it has not complied, the consequences of non-compliance. Disclosure requirements pertaining to this Section are contained in note 18.

Section 3862, Financial Instruments – Disclosures

Section 3863, Financial Instruments – Presentation

These Sections replace Section 3861, Financial Instruments – Disclosure and Presentation, revising and enhancing disclosure requirements while carrying forward its presentation requirements. These new sections place increased emphasis on disclosure about the nature and extent of risk arising from financial instruments and how the entity manages those risks. Disclosure requirements pertaining to this section are contained in note 18.

**Convergence with International Financial Reporting Standards (IFRS)**

In February 2008, Canada's Accounting Standards Board ratified a strategic plan that will result in Canadian GAAP, as used by public companies, being evolved and converged with International Financial Reporting Standards (IFRS) over a transitional period to be complete by 2011. The Company will be required to report using the converged standards effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011.

Canadian GAAP will be converged with IFRS through a combination of two methods: as current joint-convergence projects of the United States' Financial Accounting Standards Board and the International Accounting Standards Board are agreed upon, they will be adopted by Canada's Accounting Standards Board and may be introduced in Canada before the complete changeover to IFRS; and standards not subject to a joint-convergence project will be exposed in an omnibus manner for introduction at the time of the complete changeover to IFRS. Also the United States' Financial Accounting Standards Board and the International Accounting Standards Board have completed a joint-project on business combinations and non-controlling interests. As the International Accounting Standards Board currently, and expectedly, has projects underway that should result in new pronouncements that continue to evolve IFRS, and as this Canadian convergence initiative is in an early stage as of the date of these consolidated financial statements, it is premature to currently assess the impact of the Canadian initiative on the Company.

**3. CASH AND CASH EQUIVELANTS**

|                                       | August 31, 2008 | May 31, 2008  |
|---------------------------------------|-----------------|---------------|
| Cash and cash equivalents consist of: |                 |               |
| Cash                                  | \$ 1,706,008    | \$ 6,357,871  |
| Term deposits                         | 15,487,877      | 6,417,735     |
|                                       | \$ 17,193,885   | \$ 12,775,606 |

**PETAQUILLA MINERALS LTD.**

(An Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited, expressed in Canadian Dollars)

August 31, 2008 and July 31, 2007

**4. MINERAL PROPERTIES**

|                           | August 31, 2008 | May 31, 2008  |
|---------------------------|-----------------|---------------|
| Molejon property          | \$ 76,749,096   | \$ 67,100,743 |
| Rio Belencillo concession | 48,872          | 48,872        |
|                           | \$ 76,797,968   | \$ 67,149,615 |

***Molejon Property – Panama***

The Molejon Property is located in the District of Donoso, Province of Colon, Panama. The project is located in the Ley Petaquilla Property. In June 2005, the shareholders of Minera Petaquilla S.A. (“Minera Petaquilla”) (formerly a joint venture investment) agreed to separate the gold deposit and other precious metal mineral deposits that might be developed within the Ley Petaquilla mineral concession from the copper mineral deposits within the Ley Petaquilla mineral concession. The agreement provides for the Company, through Petaquilla Gold, S.A., to own a 100% interest in the Molejon gold deposit, as well as all other gold and precious metal mineral deposits that might be developed within the Ley Petaquilla mineral concession, subject to a graduated 1% - 5% Net Smelter Return, based on the future gold price at the time of production, payable to the former joint venture partners as to 35.135% and 64.865% respectively.

Approval of the phased Mine Development Plan was obtained in September 2005. The Company proceeded with the development of the property and construction of the processing mill commenced in July of 2007.

***Rio Bellencillo Concession - Panama***

The Company holds various interests in other land concession areas adjacent to the Ley Petaquilla Property in Panama, including the Rio Belencillo and Rio Petaquilla concessions.

By an Agreement dated May 7, 2005 and amended on June 10, 2005, Gold Dragon Capital Management Ltd. (“Gold Dragon”), a company having a common director, had an option to purchase all of the Company’s interest in the Rio Belencillo and Rio Petaquilla concessions by the expenditure of \$100,000 in approved exploration costs by May 7, 2007, an additional \$400,000 in approved exploration costs by February 7, 2008 and by then paying the Company \$1,152,400. This sum is payable in shares of Gold Dragon.

The payment of \$100,000 on account of exploration expenditures has not been made in accordance with the terms and conditions of the May 7, 2005 agreement. The Company is in the process of amending the agreement with Gold Dragon.

The Company’s proportionate share of exploration costs totalling \$48,872 has been capitalized on the Company’s balance sheet.

***San Juan Concessions - Panama***

During the period ended April 30, 2007, the Company entered into an agreement with Geneva Gold, formerly Eurogold Mining Inc. (“Eurogold”), for the exploration and development of the San Juan Concessions. The San Juan Property is adjacent to the Company’s Molejon gold project and the Petaquilla porphyry copper project in west central Panama. Under the agreement, Geneva Gold may earn a 60% interest in the San Juan Property by incurring exploration expenditures of at least US\$6,000,000, by paying Petaquilla Minerals Ltd. US\$600,000 in cash and by causing to be issued to Petaquilla Minerals Ltd. 9,000,000 shares of Geneva Gold, over a period of three years. If Geneva Gold acquired a 60% interest in the property, it may increase its interest to 70% by incurring US\$3,000,000 in additional exploration expenditures in the fourth year. The Company was to be the operator of the project. The Company received the initial cash option payment of \$111,120 (US\$100,000). All capitalized costs relating to this concession have been previously written off.

During the period ended April 30, 2007, the Company rescinded the above agreement and returned the initial cash option

## **PETAQUILLA MINERALS LTD.**

(An Exploration Stage Company)

### **NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited, expressed in Canadian Dollars)

August 31, 2008 and July 31, 2007

---

#### **4. MINERAL PROPERTIES (continued)**

payment of \$111,120 (US\$100,000) to Geneva Gold.

Geneva Gold has claimed a loss in the share value said to be caused by the Company's news release announcing that the agreement with the Company has been rescinded. The legal claim was settled in the period ended May 31, 2008 by issuing 100,000 shares in Petaquilla Minerals Ltd., valued at the market value \$2.61 per share.

#### **5. INVESTMENT IN PETAQUILLA COPPER LTD.**

During the period ended April 30, 2007, the shareholders of the Company voted in favour of the April 21, 2006 proposed Plan of Arrangement. During the same period, Supreme Court approval in the Province of British Columbia was obtained for the Plan of Arrangement.

The result of the Plan of Arrangement was that each shareholder of the Company received one share of Petaquilla Copper Ltd. ("Copper"), a private company. Each shareholder continued to hold one share of the Company and one share of Copper, for each one share of the Company held on the effective date of the Plan of Arrangement.

The Effective Date of the Plan of Arrangement was October 18, 2006 whereby each holder of the common shares of the Company on October 17, 2006 was entitled to receive one common share of Copper for each common share of the Company held.

According to the terms of the Plan of Arrangement, the Company transferred title to Copper of its wholly-owned subsidiary, Georecursos International S.A., the holder of the 52% interest in the Ley Petaquilla concession lands. The Company would retain 100% ownership of the gold and precious metal deposits within the Ley Petaquilla concession as well as all the other concession lands adjacent to the Ley Petaquilla concession.

The Company initially owned 22,233,634 of the issued shares of Copper at a cost of \$500,000. This initial 20% equity stake has been and may be further diluted upon future share capital financings that are anticipated to be necessary for the ongoing funding of the Copper deposit project. Subsequent to the Plan of Arrangement, the Company has accounted for Copper on an equity basis. Under the equity method, the Company records the percentage of net income (loss) that would be attributed to the investment by adjusting the carrying value of the investment. If the percentage of loss from the investee is greater than carrying cost, the amount is not reduced beyond the full carrying value. Dilution gains arise whenever Copper issues equity at a price greater than the carrying value of the equity investment.

As at August the 31, 2008 the Company held 20,418,565 Copper shares with a Market value of \$44,920,843.

#### **6. RESTRICTED CASH**

The Company deposited \$30,000 with HSBC Bank to be used as collateral for the credit card used by the Company to pay ongoing travel and related costs. The Company has pledged as security for financings (Note 8) a term deposit in the amount of \$425,792 (US\$ 400,000). The Company is required to post a performance bond to comply with Environmental law, article 112 in Panama, the Company has posted a term deposit for \$212,896 (US\$ 200,000) as a guarantee. Also, the Company posted a term deposit for \$42,579 (US\$ 40,000) for a performance bond with the Ministry of Commerce and Trade in Panama. Interest rates on these deposits ranges from 2.60% to 4.875%.

#### **7. OPERATING CREDIT LINE FACILITY**

The Company has an operating credit line facility with BBVA up to a maximum of \$14,242,268 (US\$ 13,379,554) (May 31 2008 – \$13,301,952 (US\$ 13,379,554) ). The facility is drawdown, reduced and converted to a capital lease on the 25<sup>th</sup> of each month. The facility has a fixed rate of 9% on \$11,728,926 (US\$ 11,018,456) (May 31, 2008 – 10,954,549 (US\$ 11,018,456)) and fixed rate of 6% on \$2,513,342 (US\$ 2,361,098) (May 31, 2008 – \$2,347,403 (US\$ 2,361,098)). The facility is secured by the assets purchased under the facility and is registered with the Public Registry of the Republic of Panama.

**PETAQUILLA MINERALS LTD.**

(An Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited, expressed in Canadian Dollars)

August 31, 2008 and July 31, 2007

**8. LONG-TERM DEBT**

During the period ended April 30, 2007, the Company arranged a bank loan of \$407,057 (US\$ 382,400) to acquire road and mine site equipment. The loan is repayable in 36 equal monthly instalments of \$12,499 (US\$ 11,742) commencing in May 2006 and bears interest at an annual rate of 5.625%. Collateral for this loan is comprised of a pledge of a Fixed First charge on the purchased equipment and \$266,120 (US\$ 250,000) renewable term deposit.

During the period ended April 30, 2007, the Company arranged a bank loan of \$83,892 (US\$ 78,810) to acquire vehicles to be used for the mine site. The loan is repayable in 36 equal monthly instalments of \$2,668 (US\$ 2,506) commencing in May 2006 and bears interest at an annual rate of 9.25%. Collateral for this loan is comprised of a fixed first charge on the purchased equipment.

During the period ended April 30, 2007, the Company arranged a bank loan of \$245,597 (US\$ 230,720) to acquire additional road and mine site equipment. The loan is repayable in 36 monthly instalments of \$7,925 (US \$7,445) commencing in October 2006 and bears interest at an annual rate of 9.00%. Collateral for this loan is comprised of a first charge on the purchased equipment.

During the period ended April 30, 2007, the Company arranged a bank loan of \$596,960 (US \$560,800) to acquire additional road and mine site equipment. The loan is repayable in 36 monthly instalments of \$19,262 (US \$18,095) commencing in January 2007 and bears interest at an annual rate of 9.25%. Collateral for this loan is comprised of a pledge of a first charge on the purchased equipment and \$159,672 (US \$150,000) renewable term deposit.

During the period ended April 30, 2007, the Company arranged a bank loan of \$26,080 (US \$24,500) to acquire a vehicle to be used for the mine site. The loan is repayable in 36 monthly instalments of \$844 (US \$793) commencing in January 2007 and bears interest at an annual rate of 9.25%. Collateral for this loan is comprised of a first charge on the purchased vehicle.

The following table summarizes the loans outstanding as at August 31, 2008 and May 31, 2008:

|                       | August 31, 2008  | May 31, 2008      |
|-----------------------|------------------|-------------------|
| Long-term debt        |                  |                   |
| Equipment loan #1     | \$ 98,523        | \$ 125,053        |
| Vehicle loan #1       | 22,559           | 27,978            |
| Equipment loan #2     | 97,847           | 110,984           |
| Equipment loan #3     | 290,119          | 317,324           |
| Vehicle loan #2       | <u>12,724</u>    | <u>13,907</u>     |
|                       | 521,772          | 595,246           |
| Less: current portion | <u>(432,827)</u> | <u>(433,621)</u>  |
|                       | <u>\$ 88,945</u> | <u>\$ 161,625</u> |

Anticipated long-term debt principal repayments are as follows:

|      |                  |
|------|------------------|
| 2009 | \$432,827        |
| 2010 | 88,945           |
|      | <u>\$521,772</u> |

**PETAQUILLA MINERALS LTD.**

(An Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited, expressed in Canadian Dollars)

August 31, 2008 and July 31, 2007

**9. DEFERRED SERVICES AND MATERIALS TO BE PROVIDED TO PETAQUILLA COPPER LTD.**

On September 30, 2007, Petaquilla Gold S.A. ("Gold"), a subsidiary of the Company entered into a Service Agreement with Petaquilla Copper, S.A. ("Copper") to provide electric generation, aggregate for construction and the rental of a drill machine (collectively, the "services") for a 3-year period. In return for receiving certain benefits and assurances, payment for services has been assumed and prepaid by Petaquilla Copper Ltd. in the amount of \$4,387,705 (US \$4,404,000) as per the following table, which details Copper's minimum needs:

| <b>Service/Supply</b>  | <b>Minimum Requirement</b> | <b>Estimated Cost per Unit</b> | <b>Estimated Cost per Month</b> | <b>Estimated cost for 3-year contract</b> |
|--|----------------------------|--------------------------------|---------------------------------|---|
| Electric Generation  | 350,000<br>kw.hr/month     | 0.19 USD/kw.hr                 | \$ 66,254                       | \$ 2,385,142                              |
| Aggregate for construction,<br>including transportation to<br>site | 100,000 yd <sup>3</sup>    | 16.5 USD/yd <sup>3</sup>       | -                               | 1,643,895                                 |
| Rental of LF 70 Drill<br>Machine                                   | -                          | -                              | 9,963                           | 358,668                                   |
| <b>Total prepaid services</b>                                      |                            |                                |                                 | <b>\$ 4,387,705</b>                       |
| <b>Balance at August 31, 2008</b>                                  |                            |                                |                                 | <b>4,165,099</b>                          |
| <b>Current portion</b>   |                            |                                |                                 | <b>\$ 242,332</b>                         |
| <b>Non-current portion</b>   |                            |                                |                                 | <b>\$ 3,922,767</b>                       |

During the first two years of the Service Agreement, Copper shall have the option to purchase the equipment from Gold at the market price of the equipment less the unamortized amount of rental costs prepaid (See Note 15).

During the period, the Company provided \$60,583 (US\$ 60,808) in services under this agreement.

**10. CAPITAL LEASE OBLIGATIONS**

The Company entered into two capital lease arrangements with Banco Bilbao Vizcaya Argentaria (Panama) S.A. ("BBVA") for the purchase of equipment to advance the Molejon project into production.

The equipment includes but is not restricted to: ball mills, a Metso crushing plant, cranes and an aggregate crushing plant.

As a condition of the lease, the equipment will serve as collateral throughout the amortization period and will be registered with the Public Registry of the Republic of Panama. Further, a related company subject to significant influence, has pledged a term deposit in the amount of \$2,513,342 (US\$ 2,361,098) (May 31, 2008 - \$2,347,403 (US\$ 2,361,098)) as additional security.

**PETAQUILLA MINERALS LTD.**

(An Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited, expressed in Canadian Dollars)

August 31, 2008 and July 31, 2007

**10. CAPITAL LEASE OBLIGATIONS (continued)**

Future minimum lease payments on the capital lease obligation are as follows:

|                             | August 31, 2008  | May 31, 2008     |
|-----------------------------|------------------|------------------|
| 2009                        | \$ 2,709,885     | \$ 2,648,121     |
| 2010                        | 2,520,408        | 2,648,121        |
| 2011                        | 1,179,708        | 1,674,278        |
|                             | <u>6,410,001</u> | <u>6,970,520</u> |
| Less imputed interest of 9% | (679,244)        | (839,640)        |
| Total                       | 5,730,757        | 6,130,880        |
| Current obligation          | 2,283,811        | 2,162,289        |
| Long-obligation             | \$ 3,446,946     | \$ ,968,591      |

**11. SENIOR SECURED NOTES**

|                                      | August 31, 2008 | May 31, 2008  |
|--------------------------------------|-----------------|---------------|
| US\$ 60 Million Senior Secured Notes | \$ 55,992,194   | \$ 26,630,004 |

As at August 31, 2008, the Company issued \$ 63,868,800 (US\$ 60,000,000) (May 31, 2008 - \$31,746,900 (US\$ 32,250,000)) of its US\$60 Million senior secured notes ("Notes"). The Notes bear interest at an annual rate of 15%. The Notes will mature five years from date of issuance at 120% of the principal. The Company has the right to redeem the Notes at any time at 120% of the principal amount plus any accrued or unpaid interest on the Notes. If the Notes are redeemed within one year of issuance, all prepaid interest is forfeited. After 24 months from the date of issuance of the Notes, holders of the Notes shall have the right to cause the Company to purchase all of its Notes then outstanding at a price equal to the sum of (a) 120% of the principal amount of such Notes to be purchased and (b) accrued and unpaid interest on the principal amount of the Notes. On an annual basis, the Note holders can cause the Company to redeem Notes equal to 35% of free cash flow. Free cash flow is to be defined mutually between the Company and the Note holders. As of August 31, 2008, no definition of free cash flow has been defined

Each Note was issued with 382 share purchase warrants. Each warrant entitles the holder to purchase one common share at CDN \$2.30 for a period of five years from the date of purchase. The warrants are subject to a weighted average anti-dilution price protection with a floor equivalent to CDN \$ 2.15.

The Notes have been accounted for in accordance with HB 3855 "Financial Instruments – Recognition and Measurement", HB 3862 "Financial Instruments – Disclosure" and HB 3863 "Financial Instruments – Presentation". Under this guidance, the Company valued the liability component of the Notes and assigned the difference to the warrants. On the valuation date, the value of the Notes was calculated to be \$58,487,339 (US\$ 58,474,937) and the amount allocated to the warrants \$ 1,525,386 (US\$ 1,525,063). Prepaid interest of \$8,993,685 (US\$ 9,000,000) was applied as a reduction of the Notes. The liability component was calculated using a discount rate of 26.65% and a maturity date of two years from issue. The senior secured notes contain embedded derivatives as a result of the call and put options. The Company is unable to fair value the embedded derivatives component separately and thus has classified the combined contract as a financial liability that is held for trading.

During the three months ended August 31, 2008 The Company incurred \$3,157,133 (US\$ 3,011,246) (Three months period ended July 31, 2007 – Nil) in financing costs. These costs have been expensed in the period they are incurred in accordance with the Company's accounting policy.

The Notes are guaranteed, on a joint and several basis, by all the assets of the Company and of the Company's subsidiaries.

**PETAQUILLA MINERALS LTD.**

(An Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited, expressed in Canadian Dollars)

August 31, 2008 and July 31, 2007

**12. SHARE CAPITAL, WARRANTS AND CONTRIBUTED SURPLUS**

## Authorized Capital

Unlimited common shares without par value

Unlimited preference shares without par value – rights and privileges conferred on issuance

|  | Number<br>of Common<br>Shares | Amount        | Contributed<br>Surplus | Warrants      |
|--|-------------------------------|---------------|------------------------|---------------|
| Issued   |                               |               |                        |               |
| Balance as at April 30, 2007                             | 89,876,951                    | \$ 91,596,035 | \$ 12,073,149          | \$ 10,706,498 |
| Non-brokered private placement, net of finders' fees (a) | 4,552,412                     | 10,918,342    | -                      | 1,327,463     |
| Exercise of stock options                                | 1,055,883                     | 3,110,114     | (2,026,487)            | -             |
| Exercise of warrants                                     | 373,395                       | 1,153,659     | -                      | (578,617)     |
| Share issue relating to legal settlement                 | 100,000                       | 261,000       | -                      | -             |
| Stock-based compensation                                 | -                             | -             | 6,359,356              | -             |
| Senior secured notes warrants                            | -                             | -             | -                      | 808,327       |
| Share issuance costs                                     | -                             | (1,181,067)   | -                      | 713,326       |
| Balance as at May 31, 2008                               | 95,958,641                    | \$105,858,083 | \$16,406,018           | \$12,976,997  |
| Exercise of stock options                                | 60,000                        | 180,972       | (149,472)              | -             |
| Stock-based compensation                                 | -                             | -             | 293,202                | -             |
| Senior secured notes warrants                            | -                             | -             | -                      | 717,059       |
| Senior secured notes finders warrants cost               | -                             | (101,784)     | -                      | 101,784       |
| Balance as at August 31, 2008                            | 96,018,641                    | \$105,937,271 | \$ 16,549,748          | \$ 13,795,840 |

- (a) In May 2007, the Company closed a non-brokered private placement comprising of 1,387,879 units at \$2.00 per unit, and 24,033 units at \$2.02 per unit for gross proceeds of \$2,824,305. Each unit consists of one common share and one-half of one common share purchase warrant, with each whole warrant exercisable into a common share at a price of \$3.50 per share for a period of two years following closing of the private placement. The share purchase warrants are subject to an accelerated expiry provision that, if the volume weighted average trading price of the common shares of the Company as traded on the Toronto Stock Exchange exceeds \$7.00 per share for at least 30 consecutive trading days, the Company shall have the right, exercisable within 30 days thereafter, to give notice to each warrant holder requiring the exercising of the warrants within a 30 day period. If the Company exercises such right, the warrant will, if not exercised by the warrant holder in accordance with their terms and conditions, expire at the end of such 30 day period. The securities issued under this private placement were subject to a four-month and a day resale restriction that expired on September 10, 2007. The fair value of the warrants issued on this private placement is \$291,274.

In October 2007, the Company closed the first tranche of the non-brokered private placement announced in October 2007 comprising 2,093,500 units at \$3.00 per unit for gross proceeds of \$6,280,500. Each unit consists of one common share and one-half of one common share purchase warrant, with each whole warrant exercisable into a common share at a price of \$3.50 per share for a period of two years following closing of the private placement. The Company paid \$222,375 and agreed to issue 74,125 share purchase warrants as finders' fees in connection with part of the private placement. The fair value of the finders' warrants is \$52,584.

In December 2007, the Company closed the second tranche of the non-brokered private placement announced in October 2007 comprising of 339,000 units at \$3.00 per unit for gross proceeds of \$1,017,000. Each unit consists of one common share and one-half of one common share purchase warrant, with each whole warrant exercisable into a common share at a price of \$3.50 per share for a period of two years following closing of the private placement. The Company paid \$43,500 and agreed to issue 12,500 share purchase warrants as finders' fees in connection with part of the private placement. The fair value of the finders' warrants is \$8,304.

**PETAQUILLA MINERALS LTD.**

(An Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited, expressed in Canadian Dollars)

August 31, 2008 and July 31, 2007

---

**12. SHARE CAPITAL, WARRANTS AND CONTRIBUTED SURPLUS (continued)**

In January 2008, the Company closed the third tranche of the non-brokered private placement announced in October 2007 comprising of 708,000 units at \$3.00 per unit for gross proceeds of \$2,124,000. Each unit consists of one common share and one-half of one common share purchase warrant, with each whole warrant exercisable into a common share at a price of \$3.50 per share for a period of two years following closing of the private placement. The Company paid \$105,000 and agreed to issue 35,000 share purchase warrants as finders' fees in connection with part of the private placement. The fair value of the finders' warrants is \$22,957.

- (b) In May 2008, the Company closed the first tranche of its Senior Secured Notes issuing 32,250 units with gross proceeds of US\$ 32,250,000. Each unit of US\$ 1,000 consists of one Secured Senior Note and a warrant to purchase 382 Common shares. Each warrant entitles the holder to purchase one common share at CDN \$2.30 for a period of five years from the date of purchase. The warrant is subject to a weighted average anti-dilution price protection with a floor equivalent to \$2.15. The Notes will mature at 120% of the principal amount. The Notes also carry a 15% interest of which the first year's interest is prepaid at the date the funds were received. The Company agreed to issue 492,780 share purchase warrants as finders' fees in connection with this tranche of the private placement. The fair value of the finders' warrants is \$629,481.
- (c) In June 2008, the Company closed the second tranche of its Senior Secured Notes issuing 10,000 units with gross proceeds of US\$ 10,000,000. Each unit of US\$ 1,000 consists of one Secured Senior Note and a warrant to purchase 382 Common shares. Each warrant entitles the holder to purchase one common share at CDN \$2.30 for a period of five years from the date of purchase. The warrant is subject to a weighted average anti-dilution price protection with a floor equivalent to \$2.15. The Notes will mature at 120% of the principal amount. The Notes also carry a 15% interest of which the first year's interest is prepaid at the date the funds were received. The Company to issue 152,800 share purchase warrants as finders' fees in connection with this tranche of the private placement. The fair value of the finders' warrants is \$ 55,890
- (d) In July 2008, the Company closed the first tranche of its Senior Secured Notes issuing 27,750 units with gross proceeds of US\$ 27,750,000. Each unit of US\$ 1,000 consists of one Secured Senior Note and a warrant to purchase 382 Common shares. Each warrant entitles the holder to purchase one common share at CDN \$2.30 for a period of five years from the date of purchase. The warrant is subject to a weighted average anti-dilution price protection with a floor equivalent to \$2.15. The Notes will mature at 120% of the principal amount. The Notes also carry a 15% interest of which the first year's interest is prepaid at the date the funds were received. The Company agreed to issue 271,220 share purchase warrants as finders' fees in connection with this tranche of the private placement. The fair value of the finders' warrants is \$ 45,883

**13. STOCK OPTIONS**

During the period ended April 30, 2007, the Company received approval for its stock option plan (the "New Plan") which authorizes the board of directors to grant incentive stock options to directors, officers and employees. The maximum number of shares reserved for issuance under the Company's Plan is 10,000,000.

Prior to the Plan of Arrangement taking effect, and in order to create unallocated options to be granted in the future to new employees, officers and directors, the existing optionees were asked to voluntarily reduce the number of shares under option to each of them to 60% of the number of shares held under the option on the day before the Effective Date ("October 18, 2006") of the Plan of Arrangement. All of the optionees agreed to this arrangement except for an option holder holding 675,000 options who elected to retain the number of options held under the existing grants. Each revised option outstanding would enable the option holder to receive one share of the Company and one share of Copper upon exercising. For example, when an optionee prior to the Effective Date held an option to purchase 100,000 shares of the Company, that optionee after the Effective Date would hold an option to purchase 60,000 shares of the Company and 60,000 shares of Copper. Both options must be exercised together. The modification of stock options as a result of the Plan of Arrangement resulted in no incremental stock-based compensation expense to recognize.

**PETAQUILLA MINERALS LTD.**

(An Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited, expressed in Canadian Dollars)

August 31, 2008 and July 31, 2007

**13. STOCK OPTIONS (continued)**

The aggregate number of common shares reserved for issuance to any person may not exceed 5% of the number of outstanding common shares. The exercise price of the options will be determined by the five day volume weighted average price of the Company's shares prior to the date of the grant. Options granted must be exercised no later than 10 years after the date of grant or such lesser period as may be determined by the Board. The Board may at its discretion in any granting of an option set a vesting period whereby the option may only be exercisable in pre-determined instalments. Stock option transactions are summarized as follows:

|                                     | Number<br>of Shares | Weighted<br>Average<br>Exercise<br>Price |
|-------------------------------------|---------------------|--|
| Balance at April 30, 2007           | 8,115,767           | 1.76 <sup>(1)</sup>                      |
| Granted                             | 1,375,000           | 0.00                                     |
| Exercised                           | (1,055,883)         | 0.53                                     |
| Cancelled                           | (319,750)           | 2.49                                     |
| Balance at May 31, 2008             | 8,115,134           | 1.83                                     |
| Granted                             |                     |  |
| Exercised                           | (60,000)            | 0.53                                     |
| Cancelled                           | (25,000)            | 2.49                                     |
| Balance at August 31, 2008          | <b>8,030,134</b>    | 1.83                                     |
| Number of stock options exercisable | 6,829,540           | \$ 1.75                                  |

- <sup>(1)</sup> Exercise price is the aggregate exercise price required to exercise one option of Petaquilla Copper Ltd. and one option of the Company with half of the proceeds to be allocated to the Company and half to Petaquilla Copper Ltd. Both options must be exercised together.

**PETAQUILLA MINERALS LTD.**

(An Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited, expressed in Canadian Dollars)

August 31, 2008 and July 31, 2007

**13. STOCK OPTIONS (continued)**

As at August 31, 2008, the following stock options were outstanding as follows:

| Number of Shares<br>Outstanding | Exercise Price       | Expiry Date        |
|---------------------------------|----------------------|--------------------|
| 150,000                         | 2.25                 | October 19, 2008   |
| 36,480                          | 0.25 <sup>(1)</sup>  | April 21, 2010     |
| 193,800                         | 0.25 <sup>(1)</sup>  | July 11, 2010      |
| 934,200                         | 0.525 <sup>(1)</sup> | February 1, 2011   |
| 96,000                          | 0.865 <sup>(1)</sup> | April 27, 2011     |
| 5,409,654                       | 2.01                 | January 15, 2012   |
| 200,000                         | 2.22                 | June 12, 2012      |
| 500,000                         | 2.25                 | June 20, 2012      |
| 50,000                          | 2.48                 | July 11, 2012      |
| 50,000                          | 2.49                 | July 12, 2012      |
| 50,000                          | 2.54                 | July 23, 2012      |
| 50,000                          | 2.76                 | September 10, 2012 |
| 5,000                           | 3.04                 | November 15, 2012  |
| 75,000                          | 2.70                 | February 14, 2013  |
| 100,000                         | 2.80                 | February 11, 2013  |
| 30,000                          | 1.96                 | May 5, 2013        |
| 100,000                         | 1.96                 | May 5, 2013        |
| <hr/>                           |                      |                    |
| 8,030,134                       |                      |                    |

(1) Exercise price is the aggregate exercise price required to exercise one option of Petaquilla Copper Ltd. and one option of the Company with half of the proceeds to be allocated to the Company and half to Petaquilla Copper Ltd. Both options must be exercised together.

Total stock-based compensation recognized for the fair value of stock options granted, vested and approved by the directors during the three months period ended August 31, 2008 was \$293,202 (Three months period ended July 31, 2007 - \$2,109,004).

Stock-based compensation charged to mineral property costs amounted to \$22,337 for the three months ended August 31, 2008 (three months ended July 31, 2007 - Nil).

These financial statements include the stock-based compensation costs associated with the exchange of options and warrants in connection with the Plan of Arrangement, and the options and warrants issued to Copper in respect thereof.

The Company did not issue any stock options during the three months period ended August 31, 2008. The weighted average fair value of stock options granted is estimated to be approximately \$1.75 for the three months ended July 31, 2007 by using the Black-Scholes options pricing model with the following weighted average assumptions:

|                                 | Three months ended<br>August 31, 2008 | Three months ended<br>July 31, 2007 |
|---------------------------------|---------------------------------------|-------------------------------------|
| Risk-free interest              | -                                     | 4.67%                               |
| Expected dividend yield         | -                                     | -                                   |
| Expected stock price volatility | -                                     | 92%                                 |
| Expected option life in years   | -                                     | 5.00 years                          |

**PETAQUILLA MINERALS LTD.**

(An Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited, expressed in Canadian Dollars)

August 31, 2008 and July 31, 2007

**14. SHARE PURCHASE WARRANTS**

Share purchase warrant transactions are summarized as follows:

|                            | Number<br>of Shares | Weighted<br>Average<br>Exercise<br>Price |
|----------------------------|---------------------|--|
| Balance at April 30, 2007  | 9,798,000           | 1.54                                     |
| Issued                     | 15,210,110          | 2.30                                     |
| Exercised                  | (373,395)           | -  |
| Balance at May 31, 2008    | 24,634,715          | 2.18                                     |
| Issued                     | 11,024,520          | 2.30                                     |
| Exercised                  |                     |  |
| Balance at August 31, 2008 | 35,659,235          | \$ 2.18                                  |

On October 17, 2006, the Company issued share purchase warrants in connection with the non-brokered private placement which closed during the period. Each warrant entitles the holder to purchase an additional common share of the Company for a period of five years at a price of \$3.00 per share. In addition, the Company agreed to issue 398,000 finders' warrants, each finder's warrant entitling the holder to purchase one additional common share of the Company at an exercise price of \$3.00 per share for a period of five years.

On the Effective Date of the Plan of Arrangement, the warrant holders received:

- one share purchase warrant (a "PTQ Warrant"), where each PTQ Warrant entitles the holder to purchase one common share of the Company for a period of five years; and
- one share purchase warrant (a "Copper Warrant"), where each Copper Warrant entitles the holder to purchase one common share of Copper for a period of five years.

Until such time as Copper has been listed on a recognized Canadian stock exchange (the "Copper Listing Date"), the Copper Warrant and the PTQ Warrant must be exercised together. From and after the first five trading days after the Copper Listing Date, the Warrants can be exercised separately, and in that event, the respective exercise prices of the PTQ Warrants and the Copper Warrants will be based on \$3.00 multiplied by the ratio of the five day volume weighted average price of each of the PTQ and Copper shares during the first five trading days for Copper.

The PTQ Warrants were subject to a hold period that expired on February 18, 2007. The Copper shares and Copper Warrants are subject to resale restrictions until such time that Copper becomes a reporting issuer or another exemption from resale restrictions is available. The PTQ common shares will be freely tradable following the Effective Date.

On December 31, 2007, Copper commenced trading on the Toronto Stock Exchange. The respective exercise prices of the PTQ Warrants and the Copper Warrants have been determined to be \$1.54 and \$1.46 based on \$3.00 multiplied by the ratio of the five day weighted average price of each of the PTQ and Copper shares during the first five trading days of Copper.

On May 10, 2007, the Company closed a non-brokered private placement comprising of 1,387,879 units at \$2.00 per unit, and 24,033 units at \$2.02 per unit for gross proceeds of \$2,824,305. Each unit consists of one common share and one-half of one common share purchase warrant, with each whole warrant exercisable into a common share at a price of \$3.50 per share for a period of two years following closing of the private placement (See Note 14). The fair value of the warrants issued on this private placement is \$291,274.

**PETAQUILLA MINERALS LTD.**

(An Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited, expressed in Canadian Dollars)

August 31, 2008 and July 31, 2007

---

**14. SHARE PURCHASE WARRANTS (continued)**

In October 2007, the Company closed a non-brokered private placement comprising of 2,093,500 units at \$3.00 per unit for gross proceeds of \$6,280,500. Each unit consists of one common share and one-half of one common share purchase warrants, with each whole warrant exercisable into a common share at a price of \$3.50 per share for a period of two years following closing of the private placement. The Company paid \$222,375 and agreed to issue 74,125 share purchase warrants as finders' fees in connection with part of the private placement. The fair value of the warrants issued on this tranche of the private placement is \$720,134. The fair value of the finders' warrants is \$52,584.

In December 2007, the Company closed the second tranche of the non-brokered private placement announced in October 2007 comprising of 339,000 units at \$3.00 per unit for gross proceeds of \$1,017,000. Each unit consists of one common share and one-half of one common share purchase warrants, with each whole warrant exercisable into a common share at a price of \$3.50 per share for a period of two years following closing of the private placement. The Company paid \$43,500 and agreed to issue 12,500 share purchase warrants as finders' fees in connection with part of the private placement. The fair value of the warrants issued on this tranche of the private placement is \$103,549. The fair value of the finders' warrants is \$8,304.

In January 2008, the Company closed the third tranche of the non-brokered private placement announced in October 2007 comprising of 708,000 units at \$3.00 per unit for gross proceeds of \$2,124,000. Each unit consists of one common share and one-half of one common share purchase warrants, with each whole warrant exercisable into a common share at a price of \$3.50 per share for a period of two years following closing of the private placement. The Company paid \$105,000 and agreed to issue 35,000 share purchase warrants as finders' fees in connection with part of the private placement. The fair value of the warrants issued on this tranche of the private placement is \$212,504. The fair value of the finders' warrants is \$22,957.

In May 2008, the Company closed the first tranche of its Senior Secured Notes issuing 32,250 units with gross proceeds of US\$ 32,250,000. Each unit of US\$ 1,000 consists of one Secured Senior Note and a warrant to purchase 382 Common shares. Each warrant entitles the holder to purchase one common share at CDN \$2.30 for a period of five years from the date of purchase. The warrant is subject to a weighted average anti-dilution price protection with a floor equivalent to \$2.15. The Notes will mature at 120% of the principal amount. The Notes also carry a 15% interest of which the first year's interest is prepaid at the date the funds were received. The Company paid \$1,612,500 and agreed to issue 492,780 share purchase warrants as finders' fees in connection with part of the private placement. The fair value of the finders' warrants is \$629,481.

In June 2008, the Company closed the second tranche of its Senior Secured Notes issuing 10,000 units with gross proceeds of US\$ 10,000,000. Each unit of US\$ 1,000 consists of one Secured Senior Note and a warrant to purchase 382 Common shares. Each warrant entitles the holder to purchase one common share at CDN \$2.30 for a period of five years from the date of purchase. The warrant is subject to a weighted average anti-dilution price protection with a floor equivalent to \$2.15. The Notes will mature at 120% of the principal amount. The Notes also carry a 15% interest of which the first year's interest is prepaid at the date the funds were received. The Company to issue 152,800 share purchase warrants as finders' fees in connection with this tranche of the private placement. The fair value of the finders' warrants is \$ 55,890.

In July 2008, the Company closed the first tranche of its Senior Secured Notes issuing 27,750 units with gross proceeds of US\$ 27,750,000. Each unit of US\$ 1,000 consists of one Secured Senior Note and a warrant to purchase 382 Common shares. Each warrant entitles the holder to purchase one common share at CDN \$2.30 for a period of five years from the date of purchase. The warrant is subject to a weighted average anti-dilution price protection with a floor equivalent to \$2.15. The Notes will mature at 120% of the principal amount. The Notes also carry a 15% interest of which the first year's interest is prepaid at the date the funds were received. The Company agreed to issue 271,220 share purchase warrants as finders' fees in connection with this tranche of the private placement. The fair value of the finders' warrants is \$ 45,883.

**PETAQUILLA MINERALS LTD.**

(An Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited, expressed in Canadian Dollars)

August 31, 2008 and July 31, 2007

**14. SHARE PURCHASE WARRANTS (continued)**

The weighted average fair value of the finders' warrants issued is estimated to be approximately \$0.24 and Nil for the three months ended August 31, 2008 and the three months ended July 31, 2007, respectively, by using the Black-Scholes options pricing model with the following assumptions:

|                                 | Three months ended<br>August 31, 2008 | Three months ended<br>July 31, 2007 |
|---------------------------------|---------------------------------------|-------------------------------------|
| Risk-free interest              | 3.29%                                 | -                                   |
| Expected dividend yield         | -                                     | -                                   |
| Expected stock price volatility | 43%                                   | -                                   |
| Expected option life in years   | 5.00 years                            | -                                   |

**15. RELATED PARTY TRANSACTIONS**

During the three months ended August 31, 2008, PTQ had the following transactions with related parties:

- a) The Company paid consulting fees of \$2,850 (Three months period ended July 31, 2007 - \$4,985) to companies controlled by a director, a former director and a former officer.
- b) The Company paid wages and benefits of \$152,260 (Three months period ended July 31, 2007 - \$107,001) to companies controlled by directors and officers.
- c) The Company paid legal fees of \$28,375 (Three months period ended July 31, 2007 - \$22,639) and share issue costs of \$10,334 (Three months period ended July 31, 2007 - \$30,568) to a law firm controlled by an officer.
- d) During the period, the Company accrued \$ 2,067 (Three months period ended July 31, 2007 - received \$195,997) in asset usage fees from Copper for the use of certain equipment.
- e) During the period, the Company recorded \$60,583 (Three months period ended July 31, 2007 - Nil) in power and drilling services related to the deferred services and materials contract with Copper

As at August 31, 2008, the Company has an amount payable to Copper of \$999,514 (May 31, 2008 - \$1,157,788).

These transactions are measured at the exchange amount, which is the amount of consideration established and agreed to by the transacting parties.

**16. SEGMENT INFORMATION**

The Company has one operating segment being the exploration of resource properties. The Company has not earned revenues from any projects.

**17. COMMITMENTS**

- (a) During the period ended April 30, 2007, the Company entered into a five-year lease for office premises at an estimated annual cost of \$66,240 commencing September 1, 2006. Cancellation of two previous lease obligations was obtained effective May 15, 2006. From October 18, 2006, the office leasing costs have been split equally between the Company and Petaquilla Copper Ltd., consequent to the Plan of Arrangement. Therefore the estimated annual cost is \$33,120 to the Company.
- (b) As of August 31, 2008, the Company had a commitment to purchase plant equipment of \$3,334,074 (US\$3,132,115) and other support equipment of \$177,110 (US\$166,381).

**PETAQUILLA MINERALS LTD.**

(An Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited, expressed in Canadian Dollars)

August 31, 2008 and July 31, 2007

---

**18. FINANCIAL INSTRUMENTS AND CAPITAL MANAGEMENT**

The Company thoroughly examines the various financial instrument risks to which it is exposed and assesses the impact and likelihood of those risks. These risks may include credit risk, liquidity risk, currency risk, and interest rate. Where material, these risks are reviewed and monitored by the Board of Directors.

**(a) Fair Values**

The Company's financial instruments consist of cash and cash equivalents, receivables, restricted cash, operating credit line facility, accounts payable, long-term debt, and the amount payable to Petaquilla Copper Ltd. The fair value of these financial instruments approximates their carrying values due to the immediate or short-term maturity of these financial instruments

The Company's senior secured notes are measured on initial recognition using the residual method (see Note 11). Subsequent fair value measurement is based on a discounted cash flow model using a discount rate of 26.65% and a maturity date of two years from issue.

**(b) Financial instrument risk exposure**

***Credit risk***

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. Financial instruments that potentially subject the Company to credit risk consist of cash and cash equivalents, restricted cash, and accounts receivable. The Company has reduced its credit risk by investing its cash and cash equivalents and restricted cash in term deposits with financial institutions that operate globally. Also, as the majority of its receivables are with the governments of Canada in the form of sales tax and, the credit risk is minimal. Therefore, the Company is not exposed to significant credit risk and overall the Company's credit risk has not changed significantly from the prior year

***Liquidity risk***

Liquidity risk is the risk that the company will not be able to meet its financial obligations as they fall due. 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 has historically relied on issuance of shares, senior secured debt and leasing arrangements to develop the project and may require doing so again in the future.

The Company holds shares in Petaquilla Copper Ltd with a market value at August 31, 2008 of \$44,308,286. The daily exchange traded volume of these shares, is not sufficient for the Company to liquidate its position in a short period of time without potentially affecting the price of the shares. These shares are held for strategic purposes and are considered long-term investments and therefore as part of the Company's planning, budgeting and liquidity analysis process, these investments are not relied upon to provide operational liquidity. The Company may sell these shares in order to extinguish its senior secured notes.

***Market risk***

**(i) *Currency risk***

Financial instruments that impact the Company's net earnings or other comprehensive income due to currency fluctuations include: United States dollar denominated cash and cash equivalents, restricted cash, accounts receivable, operating credit line facility, accounts payable, leases, long-term debt and senior secured notes. The sensitivity of the Company's net earnings and other comprehensive income due to changes in the exchange rate between the Canadian dollar and the United

**PETAQUILLA MINERALS LTD.**  
(An Exploration Stage Company)  
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited, expressed in Canadian Dollars)  
August 31, 2008 and July 31, 2007

**18. FINANCIAL INSTRUMENTS AND CAPITAL MANAGEMENT (continued)**

States dollar is summarized in the table below:

|   | As at August 31, 2008                       |   |
|---|---|---|
|   | 10% Increase in the<br>United States Dollar | 10% decrease in the<br>United States Dollar |
| (Decrease) increase in net earnings               | \$ (5,144,463)                              | \$ 5,144,463                                |
| (Decrease) increase in other comprehensive income | -   | -   |
| Comprehensive income                              | \$ (5,144,463)                              | \$ 5,144,463                                |

**(ii) Interest rate risk**

Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate due to changes in market interest rates. Cash and cash equivalents, and restricted cash bear interest at fixed rates.

Other current financial assets and liabilities are not exposed to interest rate because they are non-interest bearing.

The operating credit line facility, leases, long-term debt and senior secured notes bear interest at a fixed rate and are also not exposed to interest rate risk.

**(C) Capital Management**

The Company's objectives of capital management are intended to safeguard the entity's ability to support the Company's normal operating requirements on an ongoing basis, continue the development and exploration of its mineral properties and support any expansionary plans.

The capital structure of the Company consists of long-term debt (Note 8), leases (Note 10) and senior secured notes (Note 11) and equity attributable to common shareholders, comprising of issued capital, contributed surplus and deficit. The Company manages the capital structure and makes adjustments in light of changes in economic conditions and the risk characteristics of the Company's assets.

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 has historically relied on issuance of shares, senior secured debt and leasing arrangements to develop the project and may require doing so again in the future.

The Company is monitoring market conditions to secure the funding at the lowest cost of capital. The Company is exposed to various funding and market risks which could curtail its access to funds.

**19. ASSET RETIREMENT OBLIGATIONS**

The Company's asset retirement obligation relates to site-restoration and clean-up costs related to its Molejon gold project located in Panama.

A reconciliation of the provision for asset retirement obligations is as follows:

|  |    |           |
|--|----|-----------|
| Balance at May 31, 2008                | \$ | 4,308,083 |
| Accretion                              |    | 85,112    |
| Foreign exchange loss on remeasurement |    | 307,898   |
| Balance at August 31, 2008             | \$ | 4,701,093 |

**PETAQUILLA MINERALS LTD.**

(An Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

(Unaudited, expressed in Canadian Dollars)

August 31, 2008 and July 31, 2007

**19. ASSET RETIREMENT OBLIGATIONS (continued)**

The provision for asset retirement obligations is based upon the following assumptions:

- a) The total undiscounted cash flow required to settle the obligation is approximately \$6,626,000 (US\$ 6,225,000);
- b) Asset retirement obligation payments are expected to occur during fiscal years 2014 and 2015;
- c) A credit adjusted risk-free rate of 7.65% has been used to discount cash flows.

**20. SUPPLEMENTAL DISCLOSURE WITH RESPECT TO CASH FLOWS**

|  | Three months ended<br>August 31, 2008 | Three months ended<br>July 31, 2008 |
|--|---------------------------------------|-------------------------------------|
| Non-cash investing activities                                |                                       |                                     |
| Property and equipment acquired through credit line facility | \$ 946,705                            | -                                   |
| Stock-based compensation capitalized to mineral properties   | \$ 22,337                             | -                                   |
|  | Three months ended<br>August 31, 2008 | Three months ended<br>July 31, 2008 |
| Interest paid in cash  | \$ 4,439,069                          | -                                   |
| Income taxes paid in cash                                    | -                                     | -                                   |

**21. CONTINGENCIES**

The Company is engaged in certain legal actions in the ordinary course of business and believe that the ultimate outcome of these actions will not have a material adverse effect on our operating results, liquidity or financial position.

**22. SUBSEQUENT EVENTS**

Subsequent to August 31, 2008:

- i. The Company granted 60,000 options at an exercise price of \$1.25.
- ii. The Company sold its 20,418,565 Petaquilla Copper Shares for proceeds of \$44,920,843
- iii. The Company repaid \$38,355,744 (US\$ 36,032,376) of the face value of its senior secured notes. Total amount paid including the 20% premium on redemption is \$44,920,843 (US\$ 43,238,852).
- iv. The Company issued US\$ 20,000,000 of its senior secured notes. Net proceeds received US\$ 15,875,000.
- v. As a result of the Inmet Mining Corporation's offer for Petaquilla Copper Ltd. the proceeds allocated to the pre-plan of arrangement options is based on the option price multiplied by the ratio of the five day weighted average price of each of the PTQ and Copper shares during the first five trading days of Copper.