TETHYS PETROLEUM LIMITED

MANAGEMENT'S DISCUSSION AND ANALYSIS

for the year ended December 31, 2011

Summary of Annual results

(All references to $ are United States dollars unless otherwise noted)
(Tabular amounts are in thousands, unless otherwise stated.)

	2011	2010	2009
	$	$	$
Revenue	22,922	14,706	8,559
Other operating revenue	7,375	-	-
Total revenue and other income	30,297	14,706	8,559
Net loss	(26,989)	(29,649)	(21,720)
Basic and diluted loss ($) per share	(0.10)	(0.15)	(0.20)
Capital expenditure *	41,902	38,293	32,221
Total assets	263,391	267,748	137,082
Non-current liabilities	(4,676)	(11,535)	(18,345)
Cash balance	11,631	79,135	7,297
Cash and working capital surplus/(deficiency)	942	69,718	(157)
Common shares outstanding			
Basic and diluted	286,692,744	260,629,769	134,554,769

*The 2009 figure includes Tajikistan capital expenditure while in 2010 and until December 13, 2011 the Tajikistan capital expenditure was included in the jointly controlled entity Seven Stars Energy Corporation ("SSEC").

The following Management's Discussion and Analysis ("MD&A") is dated March 30, 2012 and should be read in conjunction with the Company's Audited Consolidated Financial Statements and related notes for the year ended December 31, 2011. The accompanying consolidated financial statements of the Company have been prepared by management and approved by the Company's Audit Committee and Board of Directors. The annual financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board and in accordance with the requirements of the Disclosure and Transparency Rules ("DTR") of the Financial Services Authority ("FSA") in the United Kingdom as applicable to annual financial reporting. Additional information relating to the Company can be found on the SEDAR website at *www.sedar.com*. Readers should also read the "Forward-Looking Statements" legal advisory wording contained at the end of this MD&A and also the Company's Annual Information Form ("AIF") for the year ended December 31, 2011 including the Glossary of Abbreviations and Technical terms, which is integrated herein by reference.

The Tethys Petroleum Limited Annual Report and Accounts for 2011 consists of three documents as detailed below:

1) Management's Discussion & Analysis: this includes the documents required to be disclosed pursuant to National Instrument 51-102 of Canadian Securities Administrators "Continuous Disclosure Obligations" ("Canadian NI 51-102") in respect of an annual Management's Discussion & Analysis and the documents required to be disclosed pursuant to UK's Disclosure & Transparency Rules with respect to DTR 4.1 "Annual Financial Report" (DTR 4.1);

2) Annual financial information: this includes the Consolidated Financial Statements, the documents required to be disclosed pursuant to Canadian NI 51-102 with respect to an annual financial report and the

documents required to be disclosed pursuant to DTR 4.1, Directors' Responsibility Statement and the Independent Auditor's Report to Tethys Petroleum Limited; and

3) The Annual Information Form ("AIF"): this includes the documents required to be disclosed pursuant to Canadian NI 51 – 102 and DTR 4.1 and the statement which is required to be presented in accordance with DTR 7.2 "Corporate Governance Statements".

Highlights and Significant Transactions

2011

On January 11, 2011, the Company received Kazakh State approval for the Pilot Production Project for the Doris oil discovery in the Akkulka block (the "Pilot Production Project"). This approval gives the Company the right to produce oil from the Doris accumulation during the exploration period and allows for the installation and operation of production facilities for the planned 4,000 barrels of oil per day ("bopd") (Phase 1) production target; currently estimated to commence in April 2012.

On February 7, 2011, the Company announced that the proposed amendments to the Kul-Bas Exploration and Production Contract had been incorporated into the contract by the Ministry of Oil and Gas ("MOG"), granting an extension to the exploration period by a further two years until November 11, 2013.

On February 17, 2011, the Company signed a Joint Venture agreement with Eurasia Gas LLP, subsequently assigned to Olisol Investments Limited, to build a joint venture oil terminal (named the "Aral Oil Terminal" or "AOT") so that oil production from the Akkulka block can be delivered and sold to market more effectively.

On April 17, 2011, the Company announced that it was one of five international companies pre-qualified and selected by the Ministry of Mines of the Afghanistan Government for a tender to explore and develop oil and gas deposits in northern Afghanistan. On September 5, 2011, the Company announced that the Chinese State Oil Company, CNPC, won the tender for the blocks in Afghanistan. The Company considers that the terms it would have needed to offer to win the tender would have made the project non-commercial.

On May 18, 2011, the Company announced it had signed a contract with the Institute of Geology and Prospecting for Oil and Gas Deposits of UNG, the state oil and gas company, to review materials on exploration areas in the Ustyurt region and the Bukhara-Khiva region with a view to applying for suitable projects in these areas.

On May 31, 2011, the Company announced that the AKD03 ("Dione") exploration well in Kazakhstan tested oil from the Cretaceous interval, the uppermost pay zone of the well. The well, which reached a total depth of 3,975 metres (13,041 feet) in the Triassic, tested oil at a rate of some 400 bopd from Jurrasic sands and also tested oil from the Cretaceous sandstone.

On July 25, 2011, the Company's entire issued ordinary share capital was admitted to the standard category of the Official List of the Financial Services Authority and commenced trading on the main market of the London Stock Exchange under the ticker symbol "TPL".

On July 26, 2011, the Company announced that, following acidisation, its AKD05 Doris appraisal well in Kazakhstan flowed some 2,088 barrels of fluid per day, of which 1,568 barrels per day was good quality (45° API) oil. The well flowed with good surface pressures although the flow was limited by the surface facilities. Flow data indicated that the well would be capable of flowing around 3,000 barrels per day with reconfiguration of the production facilities.

On August 8, 2011, the Company opened its Doris oil production facilities in Kazakhstan after receiving final Kazakh governmental approvals.

On September 7, 2011, the Company's KBD01 (Kalypso) exploration well on the Kul-Bas Block reached total depth at approximately 4,300 metres in what was interpreted to be rocks of the Carboniferous age. Initial logging results indicate more than 100 metres of gross potential hydrocarbon bearing zones in the well.

On September 12, 2011, the Company announced that its East Olimtoi EOL09 exploration well reached a total depth of 3,765 metres in the Akdzhar formation and was flowing a mixture of completion brine and oil from the Upper Alai sandstone interval. The oil was of good quality with an API gravity of 36 degrees. Sections open to testing included the upper Alai sandstone unit (a secondary target) where there was previously a strong flow of live oil to the surface accompanied by 33% gas in the drilling mud, the lower Alai limestone interval and the upper part of the Bukhara formation. There are two further sandstone zones in the Alai formation that appear oil bearing based on wireline logs. The flow testing of the well showed that the formation appeared to have been damaged during the drilling process, when the well required control using heavy drilling mud and further operations are planned to fully evaluate the commerciality of this oil discovery.

On September 12, 2011, the Company announced that the data collection for the gravity, gradiometry and magnetic aerial survey carried out over the Bokhtar PSC Area in Tajikistan was completed and that it would provide additional and more aerially extensive data to complement the existing seismic acquisition with the final processed data.

On October 20, 2011, the Company announced results of a successful workover of well BST20 in the Beshtentak oilfield in Tajikistan. The well tested oil at a rate of 533 bopd, accompanied by 12,500 cubic metres of gas per day on a restricted choke. The oil had an API gravity of 38 degrees and no water was being produced.

On November 15, 2011, the AKD06 Doris appraisal well tested oil at a rate of over 4,300 bopd from the Cretaceous sand interval. The flow was restricted but data indicated that open flow potential was in excess of 6,000 bopd.

On November 18, 2011, the Company signed a Memorandum of Understanding ("MOU") with UNG to establish a programme for Tethys to acquire two new Production Enhancement Contracts ("PECs") for two new existing oilfields in Uzbekistan. The MOU stated an agreed timetable up to May 1, 2012 to negotiate for the PECs. One for the Chegara Group of fields and one for the West Kruk field both located in the same area as North Urtabulak. Subsequently, following technical and commercial evaluation of the West Kruk field, the Company has decided to focus on the Chegara group of fields.

On December 9, 2011, the Company completed a private placement of 26,062,975 Ordinary Shares for gross proceeds of USD13,001,981. The net proceeds of the offering were to enable Tethys to exercise an option to purchase an additional 34% of shares in SSEC and to carry out additional work in Tajikistan.

On December 13, 2011, the Company completed the purchase of 34% of the shares in SSEC from its Tajik joint venture partner Sangam Limited, and increased its shareholding to 85% (from 51%). SSEC is the owner of the rights to the Bokhtar Production Sharing Contract ("Bokhtar PSC") in Tajikistan and is now a subsidiary of the Company. In the two years prior to December 13, 2011, SSEC was a Joint Venture as neither shareholder had control.

On December 19, 2011, the Company announced the initial results of its Persea 1 exploration well in Tajikistan. The well reached a total depth of 2,655 metres and wireline logs show a 50 metre gross zone of possible hydrocarbons within mixed sandstone and carbonate sequence assigned to the Alai formation. Testing is planned to be carried out in the first half of 2012.

2012

On January 30, 2012, the Company announced the official inauguration of AOT - a new storage and rail loading facility for its oil shipments from the Doris oilfield. The AOT is owned and operated through a 50:50 joint venture by Tethys and its Kazakh oil trading partner's company, Olisol Investment Limited (a subsidiary of Eurasia Gas). The Company plans to initially double production to approximately 4,000 bopd. It is planned to expand the capacity of the terminal to more than 12,000 bopd to accommodate future potential production growth dependent upon further drilling results.

On February 1, 2012, the Company announced it had signed an MOU with the Uzbek State oil and gas company, National Holding Company "Uzbekneftegaz" ("UNG"). The objective of this MOU is to provide the framework for a Joint Study and the negotiation process for an Exploration Agreement relating to certain exploration blocks in the North Ustyurt Basin of Uzbekistan.

On February 9, 2012, the Company confirmed the issue of a tender for the final stage of the seismic programme in Tajikistan. The seismic programme will involve the acquisition of approximately 870km of new 2D seismic in two areas; the Dushanbe Step and the Vaksh valley. It is expected that this data will be acquired this summer with initial interpreted results in Q4 2012. When completed, it will identify the location for the first deep pre-salt well to be drilled by Tethys. This seismic data will be used to firm up an initial deep well drilling location to exploit the very significant upside indicated by the gravity, gradiometry and magnetic aerial survey previously carried out.

On March 21, 2012 the company announced Total Net Oil and Gas Reserves (barrels of oil equivalent: BOE) consisting of 1P (Proved reserves) up 96% to 14.5 million BOE and 2P (Proved + Probable reserves) up 45% to 25.3 million BOE.

Total revenue in 2011 at USD30.297 million represented an increase of 106% on the 2010 figure of USD14.706 million while oil and gas revenue in 2011 at USD22.922 million was 56% higher than the oil and gas revenue of USD14.706 million in 2010.

The net loss for 2011 at USD26.989 million represented a reduction of 9% on the 2010 loss of USD29.649 million.

In the year to December 31, 2011, capital expenditure was USD41.902 million compared to USD38.293 million in the year ended December 31, 2010. These figures exclude any capital expenditure by the Joint Venture in Tajikistan in the period from January 1, 2011 to December 13, 2011 or in the twelve months to December 31, 2010.

Production costs in the year to December 31, 2011 were USD10.785 million compared to USD7.076 million in the year ended December 31, 2010 reflecting the additional production costs associated with the enhanced levels of gas and oil production achieved in Kazakhstan.

Administrative costs in the year to December 31, 2011 at USD20.549 million were 5% up on the USD19.520 million incurred in the year to December 31, 2010.

Nature of Business

Tethys Petroleum Limited and its subsidiaries (collectively "Tethys" or "the Company") has its principal executive office in Guernsey, British Isles. The domicile of Tethys Petroleum Limited is the Cayman Islands where it is incorporated. Tethys' principal activity is the exploration for and production of crude oil and natural gas. The Company currently has projects in the Republic of Kazakhstan, the Republic of Tajikistan and the Republic of Uzbekistan.

Financial and Operational Review

Reserves

Following the completion of the audit of the Kazakhstan reserves by an independent auditor, Gustavson & Associates Consultants Limited, independent oil and gas reservoir engineers of Calgary, Alberta, the company announced Total Net Oil and Gas Reserves (barrels of oil equivalent: BOE) consisting of 1P (Proved reserves) up 96% to 14.5 million BOE and 2P (Proved + Probable reserves) up 45% to 25.3 million BOE.

The growth of the Company's reserves is one of the Company's Key Performance Indicators ("KPIs").

Kazakhstan Gas Production (Kyzyloi contract)

	2011				2010			
	Mcm	Mcf	Mcm/d[1]	boe/d[2]	Mcm	Mcf	Mcm/d[1]	boe/d[2]
Q1	28,798	1,016,840	320	1,883	0	0	0	0
Q2	34,225	1,208,471	376	2,214	10,146	358,255	298	1,756
Q3	35,538	1,254,843	386	2,274	44,215	1,561,232	481	2,829
Q4	36,067	1,273,508	394	2,316	41,449	1,463,564	451	2,652
Total	134,628	4,753,662	369	2,171	95,810	3,383,051	439	2,587

Note 1 Mcm/d is thousands of cubic metres per day and in 2010 was calculated based on the actual production days in the quarter or year. In 2011 there were 365 production days while in 2010 there were 218.

Note 2 boe is barrel of oil equivalent. A boe conversion ratio of 6,000 cubic feet (169.9 cubic metres) of natural gas = 1 barrel of oil has been used and is based on the standard energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

- Production commenced from the Kyzyloi field in 2007, following the construction of a 56 km, 325 mm diameter export pipeline from the Kyzyloi Field gathering station to the main Bukhara–Urals gas trunkline, where a compressor station was constructed at km910 on that trunkline. The gas flows into the main trunkline which is owned by Intergas Central Asia, a division of the Kazakh state natural gas company KazTransGas.

- Initial production from the Kyzyloi Field was sold under the long-term take-or-pay contract signed between TAG and gas trading company GazImpex in January 2006. This contract was assigned in December 2007 from GazImpex to the Kazakhstani Petrochemical Company Kemikal LLP, who utilized the gas in the domestic Kazakh market. This contract was further assigned on May 1, 2009 to Asia Gas NG LLP. The contract price is USD32 per Mcm excluding VAT or USD35.84 per Mcm including VAT at the current 12% rate.

  In Q1 2011, one of the compressors was out of commission while being repaired. This was the reason that production was slightly lower in the first quarter compared to the other three quarters.

- In contrast to prior years, there were few disruptions to the Kyzyloi gas production levels throughout 2011. In 2010, the Bukhara Urals pipeline was closed and did not re-open until May 27, 2010 when volumes through the pipeline were restricted to 360Mcmpd[1]. It was not until July 26, 2010 when volumes returned to pre-closure levels of 500Mcmpd.

- As stated above, the Kyzyloi Gas Supply Contract has a term until the earlier of the date when 850 MMcm of gas has been sold and December 1, 2012, the date on which all contracts and licences pursuant to which the gas to be delivered under the Gas Supply Contract terminate is based on a take–or–pay principle and covers all gas produced from the Kyzyloi Field Licence and Production Contract area up to the termination

[1]Thousand cubic metres
[2]Thousand cubic feet

of the Gas Supply Contract. To the end of Q4 2011 some 535 MMcm under the Gas Supply Contract had been delivered.

Kazakhstan Gas Production (Akkulka contract)

	2011				2010			
	Mcm[1]	Mcf[2]	Mcm/d	boe/d	Mcm[1]	Mcf[2]	Mcm/d	boe/d
Q1	17,182	606,693	191	1,124	0	0	0	0
Q2	22,651	799,796	249	1,465				
Q3	22,867	807,430	249	1,463				
Q4	20,204	713,403	220	1,293	24,244	856,056	279	1,640
Total	82,904	2,927,322	227	1,337	24,244	856,056	279	1,640

Note Mcm/d is thousands of cubic metres per day and has been calculated based on the actual production days in the quarter. In 2011 there were 365 production days while in the same period in 2010 there were 87 days.

- On September 16, 2010, the Company commenced the second phase of gas development (referred to as "Phase 2" of the Kyzyloi / Akkulka shallow gas development) with commencement of production from the Akkulka Field on October 6, 2010.
- In Q1 2011, one of the compressors was out of commission while being repaired. This was the reason that production was slightly lower in the first quarter compared to the other three quarters.
- In conjunction with this, the Company entered into a second gas sales contract with Asia Gas NG LLP pursuant to which gas is sold from the Akkulka Field at a price of USD33.93 per Mcm excluding VAT or USD38 per Mcm including VAT. Gas sold under this contract is for domestic sales and, as such, is subject to a Mineral Extraction Tax of approximately 0.5% to the Kazakh State. The Akkulka gas sales contract runs for a period of two years. First deliveries under this contract commenced on October 6, 2010.
- TAG has made eleven shallow gas discoveries in the Akkulka Exploration Licence and Contract area. The Akkulka Production Contract now covers seven of these wells and four are currently producing from a similar horizon to the Kyzyloi Field and are tied into the Company's existing pipeline infrastructure, with additional compression having been installed at the BCS. The development of the other gas discoveries already made in the Akkulka Block is planned as Phase 3.
- The Company has chosen not to advance both the Kyzloi and Akkulka gas projects fully due to the relatively low gas prices currently being obtained. The Company is hopeful however that with the completion of the Kazakhstan – China gas pipeline (which the Company understands is scheduled for 2013), better gas prices may be obtained with more competition from gas buyers for supply.

Kazakhstan Oil Production (Akkulka contract)

	2011					2010			
	Gross fluid		Net	Production		Gross fluid		Production	
	m3	Barrels	Barrels	days	bopd	m3	Barrels	days	bopd
Q1	4,219	32,359	30,030	26	1,155	-	-	-	-
Q2	10,269	78,143	74,244	52	1,428	-	-	-	-
Q3	18,622	156,129	144,624	92	1,725	1,393	10,952	21	522
Q4	21,292	178,493	165,324	92	1,797	5165	39,918	65	614
Total	54,402	445,124	414,222	262	1,581	6,558	50,870	86	591

- On September 10, 2010, the Company commenced selling untreated oil at the well site of AKD01 (under test production at a permitted level of up to 750 bopd) to an oil trading company which transports the oil by truck to an oil loading terminal north of the town of Emba, located 450 km to the northeast of the well site, where it is treated before being transported to local refineries. Tethys sold the unprocessed oil at the wellhead at an initial price of USD22/bbl. This test production scheme was implemented to gain reservoir information, realise early cash flow and also to prepare for the higher production and associated logistics for the next stage.
- On January 11, 2011, TAG received Kazakh State approval from MOG for the Pilot Production Project for the Doris oil discovery in the Akkulka Block. This approval granted TAG the right to produce oil from the Doris discovery under the exploration contract and allows the Company to install and operate production facilities for the planned (Phase 2) production target. Once the Pilot Production Project is fully completed, the relevant final reserve calculations will be submitted to MOG to receive a production contract that will allow for full field development and foreign or domestic sales. The Company is expected to apply for a production contract after the appraisal programme for the Doris oil discovery is complete.
- Between January 1, 2011 and March 31, 2011, due to a combination of weather problems and work on building the necessary facilities, only 26 days of pilot production were achieved from well AKD01 on the Doris discovery on the Akkulka contract.
- Between April 1, 2011 and June 30, 2011, due to the ongoing work on building the necessary facilities, only 52 days of pilot production were achieved on the Doris discovery on the Akkulka contract.
- On August 8, 2011, the Company announced the opening of its Doris oil production facilities. With the opening of the new rail-loading facility in April 2012, which will reduce the road trucking distance by half, it is planned to increase production initially to 4,000 bopd although the production facility and terminal are designed for potentially much greater production rates in the future with 5,000 - 6,000 bopd planned for later in the year. Completion of this terminal was originally anticipated to be in the fourth quarter of 2011 but this was subsequently moved back because of the extremely adverse weather conditions and is now anticipated to be completed and commissioned in April 2012.
- Test production from well AKD05 commenced in June and carried on into July 2011. There was then a gap in August and September before commercial production commenced in October 2011.
- In November 2011, commercial production commenced from AKD06.
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Joint Venture

On February 17, 2011, the Company signed a joint venture agreement to construct and operate AOT, a rail oil loading terminal at Shalkar in Kazakhstan. Transcontinental Oil Transportation ("TOT"), a wholly owned subsidiary of the Company, and Olisol Investments Limited, a local partner with strong experience in the oil distribution business in Kazakhstan each has a 50% interest in the project. With the opening of this new rail-loading facility in April 2012, which will reduce the road trucking distance by half, it is planned to increase production initially to 4,000 bopd although the production facility and terminal are designed for potentially much greater production levels in the future with 5,000 - 6,000 bopd planned for later in the year from existing drilled and tested wells.

Uzbekistan Oil Production (North Urtabulak PEC)

Total Production from TPU under PEC

	Total Production			Total Production		
	Tonnes	Barrels*	bopd	Tonnes	Barrels*	bopd
Three months ended March 31	14,945	115,076	1,278	20,869	160,691	1,785
Three months ended June 30	14,047	108,162	1,189	19,627	151,528	1,660
Three months ended September 30	10,891	83,859	912	17,512	134,842	1,466
Three months ended December 31	9,291	71,542	777	15,048	115,869	1,259
Total production	49,174	378,639	1,037	73,056	562,930	1,541

After State Take

Period	2011			2010		
	TPU[2] Share			**TPU Share**		
	Tonnes	Barrels*	bopd	Tonnes	Barrels*	bopd
Three months ended March 31	6,430	49,510	550	10,434	80,342	893
Three months ended June 30	5,808	44,720	497	9,814	75,565	830
Three months ended September 30	3,883	29,898	325	7,182	55,301	601
Three months ended December 31	2,629	20,246	220	6,444	49,619	539
Total production	18,750	144,374	396	38,874	260,827	714

* *using 7.7 barrels = 1 tonne*

- The Company, through Tethys Production Uzbekistan ("TPU"), owns a 100% contractor interest in the North Urtabulak PEC for the North Urtabulak Field, together with subsidiaries of Uzbekneftegaz ("UNG"). This field is located in southern Uzbekistan in the northern portion of the Amu Darya basin. The North Urtabulak PEC does not confer ownership of the North Urtabulak Field to TPU and no reserves or resources have been attributed to TPU's interest under the North Urtabulak PEC to date.
- Under the North Urtabulak PEC, the contractor receives 50% of all incremental production from each well from the North Urtabulak Field for the first three years of production, with the remaining 50% to be shared between the Uzbek State Partners. For the subsequent five years, the contractor receives 20%, and the Uzbek State Partners 80% of the same.
- As at December 31, 2011, the Company was producing approximately 689 bopd (gross) from 16 wells under the North Urtabulak PEC. Part of the North Urtabulak Field lies under a zone of active salt movement which has had limited production in the past due to drilling difficulties.
- A full-field dynamic reservoir model was completed and interpreted, and further production enhancement operations have been conducted on the North Urtabulak Field – including radial drilling, sidetracking, acid stimulation, water-injection and horizontal drilling but without any significant benefit.
- As a result of the consistent decline in the production levels of the North Urtabulak PEC, the Company carried out an estimate of the asset's recoverable amount. The result of this exercise was that the discounted cash flow indicated a value for the asset at USD6,078,254while the carrying value of the asset was USD15,061,146 and consequently an impairment adjustment of USD8,982,792 was recorded to bring the carrying value in line with the discounted cash flow. *See Impairment in Uzbekistan below.*

[2] TPU is Tethys Production Uzbekistan, the Tethys subsidiary which holds the PEC. Tethys Production Uzbekistan is the trading name of Baker Hughes (Cyprus) Limited.

- On November 18, 2011, the Company signed an MOU with UNG to establish a programme for Tethys to acquire two new PECs for two existing oilfields in Uzbekistan. The MOU stated an agreed timetable up to May 1, 2012 to negotiate for the PECs. The Company is currently negotiating for the Chegara Group of fields located in the same area as North Urtabulak. The Chegara Group of fields are producing oilfields but are less developed than North Urtabulak, and Tethys believes that these fields offer significant potential for additional oil production in the short term thereby enhancing its production and cash flow from Uzbekistan.

- The Company intends to focus future efforts in Uzbekistan on developing new contracts such as the Chegara PEC or on potential exploration activities. The North Urtabulak impairment must be taken in the context of the new projects which the Company is now developing in Uzbekistan. The North Urtabulak project is a late stage re-development and incremental production project on an old field, and the Company has used this project as a base to develop additional projects and a significant business presence in Uzbekistan. Currently these new projects include the Chegara PEC (Chegara is a much less developed producing field) and the potential exploration block in the North Ustyurt basin (which is south of the Doris discovery in Kazakhstan and which the Company believes has considerable exploration potential).

Tajikistan Oil Production (Beshtentak field)

		2011					2010			
		Total Production					Total Production			
		Tonnes	Barrels*	Production days	bopd		Tonnes	Barrels*	Production days	bopd
Total		2,481	18,468	76	243		817	5,923	86	592

* *using 7.4 barrels = 1 tonne*

- In 2010, oil production had re-commenced from the Beshtentak field in Q1, albeit on a small scale, and further work was initiated, aimed at increasing the production but without success.
- Further workovers were carried out in 2010 on other wells in the field but initially without success.
- On October 20, 2011, the Company announced that the Beshtentak well BST20, having been worked over by applying modern perforating and acidisation techniques and applying natural gas lift, tested oil at a rate of 533 bopd accompanied by 12,500 cubic metres (441 thousand cubic feet) of gas per day on a restricted choke (10 mm - 25/64 inch) with a flowing tubing head pressure of 26 atmospheres (377 psi).
- Initial sales agreements were signed and the first payments from oil sales received.

The well was placed on oil production and the gas was tied into the nearby local gas grid but subsequently production performance indicated possible communication with the nearby BST103 well which is producing gas from the field for the city of Kulob, this gas being part of the "base level" production on the field assigned to the Tajik State. As a result, the BST20 production is currently restricted and it is planned to acquire additional data to ascertain the extent of any possible communication. The well is now back on production but at lower rates than previously, currently less than 100 bopd, and the Company believes that this well needs work carried out on zonal isolation to increase production. This work is planned once the current bad weather conditions have improved. Meanwhile, three further workover candidates have been identified in other parts of the field (away from existing producers), which are interpreted to contain remaining bypassed oil and gas and work is progressing to fully assess these interesting opportunities, including potentially the acquisition of downhole seismic data. In addition to conducting recompletion work on these three wells, it is planned in the future to locate potentially one or two new high angle or horizontal crestal development wells, which would have the potential to achieve higher production rates than those obtained from the BST20 well.

- Further wells are available on the field for workover and potential oil production, as well as the possible development of undrained fault compartments in the field.
- Throughout 2010 and until December 13, 2011, Tethys had a 51% shareholding in SSEC but under the terms of a loan agreement with SSEC, Tethys was due to receive all revenues from production sales attributable to SSEC, the jointly controlled entity until the loan was repaid. With effect from December 13, 2011, Tethys increased its shareholding in SSEC to 85%. See *Acquisition of Shares in SSEC* below.

Production Summary

In the year ended December 31, 2011, the oil and gas production levels achieved (before the deduction of local governments share or taxation) were as follows:

Country	**Oil**	**Gas**		**Combined**
	bopd	Mcm/d	boe/d	boe/d
Kazakhstan	1,581	596	3,508	5,089
Uzbekistan	1,037	-	-	1,037
Tajikistan	243	-	-	243
Total	**2,861**	**596**	**3,508**	**6,369**

While in the same period of 2010 the figures were as follows:

Country	**Oil**	**Gas**		**Combined**
	bopd	Mcm/d	boe/d	boe/d
Kazakhstan	591	730	4,292	4,883
Uzbekistan	1,259	-	-	1,259
Tajikistan	16	-	-	16
Total	**1,866**	**730**	**4,292**	**6,158**

- Gas production days in the Kyzyloi field in Kazakhstan were 365 in 2011 and 218 days in 2010.
- Gas production days in the Akkulka field in Kazakhstan were 365 in 2011 and 87 days in 2010.
- Oil production days in the Akkulka field in Kazakhstan were 262 in 2011 and 86 days in 2010.
- Oil production days in the Beshtentak field in Tajikistan were 76 in 2011 and 86 days in 2010.

The combined boe/d is another of the Company's KPIs.

Financial Review

Loss before tax

The Company recorded a net loss after taxation of USD26.989 million in the year ended December 31, 2011, compared to a net loss of USD29.649 million in the same period of 2010. In the three months to December 31, 2011, the net loss incurred was USD9.424 million compared to USD11.210 million in the same period of 2010.

	Three months ended December 31			Year ended December 31		
	2011	**2010**	**Movement**	**2011**	**2010**	**Movement**
	$	$		$	$	
Sales and other revenues	7,416	3,387	119%	22,922	14,706	56%
Other operating income	747	-	100%	7,375	-	100%
Total revenue and other income	**8,163**	**3,387**	141%	**30,297**	**14,706**	106%
Production expenses	(3,867)	(2,965)	30%	(10,785)	(7,076)	52%
Depreciation, depletion and amortization	(3,427)	(2,200)	56%	(13,111)	(5,885)	123%
Impairment charge	(8,983)	-	100%	(8,983)	-	100%
Unsuccessful exploration & evaluation expenditure	-	94	-100%	(1,807)	-	100%
Listing expenses	-	(58)	-100%	(606)	(1,288)	-53%
Business development expenses	(437)	(35)	1149%	(2,363)	(35)	6651%
Administrative costs	(5,029)	(6,345)	-21%	(20,549)	(19,520)	5%
Stock-based compensation	(703)	(2,360)	-70%	(3,814)	(5,956)	-36%
Finance income/(loss) net	187	(40)	-568%	1,100	(129)	-953%
Foreign exchange gains/(loss) net	41	-	100%	74	(337)	-122%
Fair value gains/(loss)	(71)	242	-129%	(625)	(24)	2,504%
Gain on previously held equity interest in SSEC	27,381	-	100%	27,381	-	100%
Loss on settlement of pre-existing loan relationship	(24,423)	-	100%	(24,423)	-	100%
Loss from jointly controlled entity	80	(212)	-138%	(722)	(634)	14%
Loss before taxation	**(11,088)**	**(10,492)**	**6%**	**(28,936)**	**(26,178)**	**11%**
Taxation	1,664	(718)	332%	1,947	(3,471)	-156%
Loss for the year	**(9,424)**	**(11,210)**	**16%**	**(26,989)**	**(29,649)**	**9%**
Loss attributable to:						
Shareholders	(9,374)	(11,210)	16%	(26,939)	(29,649)	9%
Non-controlling interest	(50)	-	100%	(50)	-	100%
Loss for the year	**(9,424)**	**(11,210)**	**15%**	**(26,989)**	**(29,649)**	**9%**

Note

Revenue from the oil sales in Tajikistan is included in the financial statements of SSEC. Between December 31, 2009 and December 13, 2011, SSEC was a joint venture and as such its revenue was not included in the Company's consolidated revenue.

Sales and other revenue

	Three months ended December 31			Year ended December 31		
	2011 $	**2010** $	% Change	**2011** $	**2010** $	Change
Gas sales	1,800	1,982	-9%	7,027	3,767	87%
Oil sales	3,682	748	392%	8,185	748	994%
Refined product sales	1,869	631	196%	7,255	9,851	-26%
Other revenue	65	26	150%	455	340	34%
	7,416	3,387	119%	22,922	14,706	56%

Note 1 Gas sales in Kazakhstan are reported net of mineral Extraction Tax (MET) which amounted to USD40k in 2011 and USD22k in 2010.

Note 2 Oil sales in Kazakhstan are reported net of water content plus compensation for natural wastage, transportation costs of water from the well head to the terminal at Emba, and MET.

The growth of gas, oil and refined product sales is one of the Company's KPIs.

Gas sales

- The gas sales are generated from both the Kyzyloi and the Akkulka contracts in Kazakhstan and, as referred to in *Kyzyloi Gas Production* above, are sold to Asia Gas NG LLP at agreed prices of USD32 per Mcm excluding VAT for the Kyzyloi gas and USD38 including VAT for the Akkulka gas.
- Gas sales in Kazakhstan in 2010 were affected by stoppages and production restrictions detailed in *Kyzyloi Gas Production* above. In 2011, there were no such disruptions and steady sales were achieved throughout the year reflecting the consistent production levels of approximately 600Mcm/d.
- Total volumes sold in the year to December 31, 2011 were 134.2MMcm (2010: 94.5MMcm) from Kyzyloi and 81.8MMcm (2010: 24.2MMcm) from Akkulka.
- Gas sales for the year to December 31, 2011 were USD7,027,000 compared to USD3,767,000 in the prior year.
- Gas sales for Q4 2011 were USD1,800,000 compared to USD1,982,000 in 2010.
- Total volumes sold in the three months to December 31, 2011 were 36.2MMcm (2010: 40.2MMcm) from Kyzyloi and 19.2MMcm (2010: 24.2MMcm) from Akkulka.

Oil sales

- Q4 2010 was the first period in which oil sales were generated by the Company in Kazakhstan. Oil sales achieved in Q4 2011 at USD3,682,000 were significantly higher than the USD748,000 achieved in Q4 2010.
- The volumes of oil sales achieved in 2011 reflected the steady increase in production referred to in *Kazakhstan Oil Production* above.
- Full details of the progress of both sales volumes and prices through the course of 2011 are as follows:

	bbls	Revenue	Price (at the well head)	Compensation	VAT	MET	Net sales
			$/bbl				
Q1	24,856	598	24.1	26	55	10	507
Q2	63,190	1,503	23.8	231	144	27	1,101
Q3	133,466	3,667	27.5	343	361	68	2,895
Q4	149,322	4,383	29.4	175	444	82	3,682
Total/Avg	370,834	10,151	27.4	775	1,004	187	8,185

Net figures exclude the compensation for water content plus compensation for natural wastage, transportation costs of water from the well head to the terminal at Emba, and MET.

Refined products sales (Uzbekistan)

	Three months ended December 31			Year ended December 31		
	2011	**2010**	%	**2011**	**2010**	%
	$	$	Change	$	$	Change
Refined product sales	1,869	631	196%	7,255	9,851	-26%

- Refined product sales for the year to December 31, 2011 were USD7,255,000 compared to USD9,851,000 in the same period of 2010. This reduction was a combination of the reduced production levels achieved in 2011 combined with the Company's reduced share of that production with several wells having completed the initial three years of production.
- Under the North Urtabulak PEC, TPU receives 50% of all incremental production from each well from the North Urtabulak Field for the first three years of production, with the remaining 50% to be shared between the Uzbek State Partners. For the subsequent five years, the company receives 20%, and the Uzbek State Partners 80% of the same. As at December 31, 2011 more than half of these wells were past the initial three years of production.
- The sales achieved in the three months to December 31, 2011 were in fact higher than in the same period of 2010 but this was the result of the virtual absence of deliveries from the refinery in the final quarter of 2010.
- Deferred revenue from refined product sales, i.e. goods sold and paid for but awaiting delivery, at December 31, 2011 was USD1,839,000 (2010: USD2,449,856).

Other operating income

	Three months ended December 31			Year ended December 31		
	2011	**2010**	%	**2011**	**2010**	%
	$	$	Change	$	$	Change
Other operating income	747	-	100%	7,375	-	100%

Since the beginning of 2010, through a wholly owned subsidiary, the Company has leased its ZJ30 drilling rig together with associated equipment to a subsidiary of its jointly controlled entity SSEC in Tajikistan. This rig and equipment was used in Tajikistan in drilling both of the Komsomolsk wells and then to drill the Persea well. The renting of the equipment is on a full commercial basis and appropriate invoices have been issued to cover the entire rental period. In accordance with the SSEC shareholders agreement, the amounts receivable in respect of the rentals were added to the loan due from that entity. When preparing the 2010 annual financial statements and the interim financial statements for Q1 2011, these amounts were eliminated in full rather than proportionate to the group's equity accounted interest, and no income was recognized.

On May 27, 2011, the Company issued a holding statement with regard to oil being encountered in its Tajik exploration well East Olimtoi EOL09, noting that the interval, which showed oil in the drilling mud at surface together with high gas levels, had not been fully evaluated or tested but the observed oil flow was obviously a positive indication. This was followed on June 9, 2011, by an announcement that electric logs had now been run in the well which confirmed the probable presence of moveable hydrocarbons in the interval from 3,341 to 3,500 metres. Independent petrophysical interpretation indicated up to 32 metres of net hydrocarbon bearing pay in the section with porosities of up to 17%. No oil-water contact was interpreted in this section of the well. These positive developments in Tajikistan were further supported by the Beshtentak well announcement on October 20, 2011 and subsequent oil production achieved in the final months of 2011. See *Tajikistan Operations Update* below.

As a result of these developments, which indicated that oil sales would commence in Tajikistan in the future, the directors revisited this matter and considered it appropriate to include that revenue from the rig rentals in the Q2 2011 interim financial statements and subsequent financial statements. Accordingly, 'Other operating income' for the year ended December 31, 2011 includes USD7.374 million in respect of these transactions, of which USD3.835 million relates to the year ended December 31, 2010. The invoices have still to be settled and there is consequently no impact on the Company's cash flows. There is also no impact on tax expense as a result of this income being recognised. Refer to *Note 7 in the Audited Consolidated Financial Statements for the year ending December 31, 2011.*

Following the purchase of 34% of the shares in SSEC from its Tajik joint venture partner Sangam Limited, increasing its shareholding to 85% (from 51%), this income will be eliminated on consolidation when preparing future financial statements.

Operating expenses

	Three months ended December 31			Year ended December 31		
	2011	**2010**	%	**2011**	**2010**	%
	$	$	Change	$	$	Change
Kazakhstan	2,950	1,673	76%	7,429	2,224	234%
Uzbekistan	888	134	563%	3,327	3,238	3%
Other	29	1,158	-97%	29	1,614	-98%
Total	3,867	2,965	30%	10,785	7,076	52%

Kazakhstan

The split between the gas and oil production in Kazakhstan was as follows:

Kazakhstan gas production	USD3,662,000	(2010:USD1,531,000)
Production cost per boe	USD2.86	
Kazakhstan oil production	USD3,767,000	(2010: USD 693,000)
Production cost per barrel	USD8.46	(2010: USD13.621)

The majority of production costs in Kazakhstan are fixed.

Control of the production cost per barrel of oil is another of the Company's KPIs.

Total production costs in Kazakhstan were higher in the year ended December 31, 2011 compared to the same period in 2010 primarily as a result of the increased levels of oil production. There had been no oil production in the first nine months of 2010 and in the final three months of 2010 there was only test production from well AKD01.

A second significant contributory factor in Kazakhstan figures related to the Akkulka gas operating costs in 2011 as production did not commence on the contract until October 2010 meaning that there were no production costs for Akkulka gas in the first nine months of 2010.

In Kazakhstan, the time writing calculations and cost allocation process was reviewed and updated, resulting in a one off cost of USD0.6 million of expenditure being transferred in Q4 2011 from Administrative to gas and oil Production expenses.

Included in the Operating expenses of each contract is a charge for property tax relating to the NBV of the operating assets, which in 2011 amounted to USD0.15 million (2010: USD0.16 million) for the Kyzyloi contract, USD0.14 million (2010: USD0.15 million) for the Akkulka gas contract and USD0.18 million (2010: nil) for the Akkulka gas contract.

Each contract also incurred project documentation costs of USD0.13 millionin Kyzyloi, USD0.11million in Akkulka gas contract and USD0.8 million in Akkulka oil contract.

Because of the remoteness of the location, the Company has to maintain a fleet of vehicles with the associated fuel costs and because of the terrain the vehicles also incur significant maintenance costs.

Production costs in the three months to December 31, 2011 were also higher in Kazakhstan when compared to the same period of 2010 as a result of the time writing adjustment referred to above.

The other principal factor contributing to the increase in costs in the three months to December 31, 2011 compared to the same period in 2010 was the higher oil production level, with the oil being produced from three wells and 92 days of production as opposed to only AKD01 in 2010 and 65 days of production.

Uzbekistan

Despite the overall production being down from 562,930 bbls in 2010 to 378,639 barrels in 2011(see *Uzbekistan oil production and Refined product sales* above) there was an increase in the Operating costs from USD3,238,000 in 2010 to USD3,327,000, which was the result of two factors:

- A large proportion of the production costs are fixed and, as such, do not decrease in line with production.
- There was a reduction in the stock of finished goods.

The operating costs in Q4 2011 were significantly higher than in the same period of 2010 because of the reduced level of sales achieved in Q4 2010 which was the result of the virtual absence of deliveries from the refinery in that period.

Depreciation, depletion and amortization expense

	Three months ended December 31			Year ended December 31		
	2011	**2010**	%	**2011**	**2010**	%
	$	$	Change	$	$	Change
DD&A costs	3,427	2,200	56%	13,111	5,885	123%
Impairment charge	8,983	-	100%	8,983	-	100%

Impairment in Uzbekistan

As a result of the consistent decline in the production levels of the North Urtabulak PEC, the Company carried out an estimate of the recoverable amount from the contract. The result of this exercise was that the discounted cash flow indicated a value for the asset at USD6,078,254 while the carrying value of the asset was USD15,061,146 and consequently the impairment adjustment of USD8,982,792 was recognised to bring the carrying value in line with the discounted cash flow. See *Uzbekistan Oil Production North Urtabulak PEC* above. Should the actual future performance of the PEC prove to be better than has been estimated then this impairment adjustment or part thereof could be reversed at a later date.

Unsuccessful exploration and evaluation expenditures

	Three months ended December 31			Year ended December 31		
	2011 $	**2010** $	% Change	**2011** $	**2010** $	% Change
Unsuccessful exploration and evaluation expenditures	-	(94)	-100%	1,807	-	100%

The costs incurred in Q3 2011 related to two shallow wells drilled on the Kul Bas contract in Kazakhstan.

Listing expenses

	Three months ended December 31			Year ended December 31		
	2011 $	**2010** $	% Change	**2011** $	**2010** $	% Change
Listing expenses	-	58	-100%	606	1,288	-53%

- The 2011 figures include costs related to the London listing that was completed in July 2011.
- The 2010 figures relate to the aborted listing on the Hong Kong Stock Exchange.

Business development expenses

	Three months ended December 31			Year ended December 31		
	2011 $	**2010** $	% Change	**2011** $	**2010** $	% Change
Business development expenses	437	35	1,149%	2,363	35	6,651%

- Business development costs relate primarily to costs incurred in the Company's pursuit of new contracts in Central Asia.
- The majority of the costs in 2011 were incurred with respect to the tender held by the government of Afghanistan for an Exploration and Production Sharing Contract relating to three exploration / development areas located in the north of the country within the Amu Darya basin.
- On April 17, 2011, the Company announced that it was one of five international companies pre-qualified and selected by the Ministry of Mines of the Afghanistan Government for a tender to explore and develop oil and gas deposits in northern Afghanistan. On September 5, 2011, the Company announced that the Chinese State Oil Company, CNPC, won the tender for the blocks in Afghanistan. The Company considers that the terms it would have needed to offer to win the tender would have made the project non-commercial.
- The Company incurred USD330,000 in connection with a contract with the Institute of Geology and Prospecting for Oil and Gas Deposits (the "Institute") in Uzbekistan to study the potential of two separate prospective areas in Uzbekistan with a view to Tethys applying for suitable projects in these areas. The study involved the assessment of existing data and the oil and gas bearing prospectivity of the areas on the basis to prepare proposals for the Government of Uzbekistan for further exploration activities. Tethys views both areas as having very good oil and gas potential but has chosen to focus on the North Ustyurt area and has now signed an MOU with a view to obtaining an exploration contract for this area.

Administrative costs

	Three months ended December 31			Year ended December 31		
	2011	**2010**	%		**2010**	%
	$	$	Change	$	$	Change
Staff costs	2,356	3,358	-30%	8,751	8,741	-
Travel costs	894	1,034	-14%	3,700	3,380	9%
Office costs	586	369	59%	2,634	2,080	27%
Professional fees	705	727	-3%	2,653	2,577	3%
Marketing costs	155	260	-40%	1,269	835	52%
Other costs	333	597	-44%	1,542	1,907	-19%
	5,029	6,345	-21%	20,549	19,520	5%

General and Administration expenses for the year ended December 31, 2011 were up on the same period of the previous year as a result of the following:

- There was an increase in staff costs in the year to December 31, 2011, as a result of increased levels of staff particularly in Kazakhstan and other operational areas. In 2010, bonuses were paid in relation to the fund raising completed in the first and final quarters of the year.
- Travel costs in the year to December 31, 2011, increased as a result of more staff travelling throughout the area as the Company looks to develop its operations and revenue.
- In Kazakhstan, the time writing calculations, being the staff costs allocated on time sheets completed by the employees, and the cost allocation process was updated and as a result USD0.6 million of expenditure was transferred from G&A to Operating expenses and USD0.3 million to Capital expenditure. *(See Operating Costs above.)* Within the staff costs, some costs were incurred in the final quarter of 2010 in connection with the successful fund raising completed in October 2010.
- Year on year there was little movement in the total expenditure for Professional Fees while certain "one off" computer software costs and legal costs incurred in the early part of the year were offset by savings in the final quarter.
- The principal factor in the increased marketing costs was a number of contributions to various social programmes at a combined cost of USD250,000. These programmes were linked primarily to the development of the Shalkar region in Kazakhstan, where the Company's projects lie, and were incurred by both of the Company's subsidiaries, Tethys-Aral-Gaz and Kul Bas. The Company also incurred costs with the contracting of a new company involved in public and governmental relations.

General and Administration expenses for the three months ended December 31, 2011 were up on the same period of the previous year as a result of the following:

- Within staff costs, certain costs were incurred in the final quarter of 2010 in connection with the successful fund raising completed in October 2010.
- In Kazakhstan the time writing calculations and the cost allocation process was updated and as a result USD0.6 million of expenditure was transferred in Q4 2011 from G&A to Operating expenses and USD0.3 million to Capital expenditure
- There was an increase in office costs in Q4 2011 compared to Q4 2010 as a result of an increase in floor space to accommodate the increased staffing levels.

Share based payments

	Three months ended December 31			Year ended December 31		
	2011	**2010**	%	**2011**	**2010**	%
	$	$	Change	$	$	Change
Share based payments	703	2,360	-70%	3,814	5,956	-36%

- Share based payment expenses relate to stock options and warrants issued in 2011 and prior years. The decrease is due to fewer options issued during 2011 compared with 2010 combined with the fall in the share price.

Finance expenses

	Three months ended December 31			Year ended December 31		
	2011	**2010**	%	**2011**	**2010**	%
	$	$	Change	$	$	Change
Foreign exchange (gain) / loss	(41)	-	100%	(74)	337	-122%
Fair value loss / (gain)	71	(242)	-129%	625	24	2,504%
Loss from joint venture	(80)	212	-138%	722	634	14%
Finance (income) / costs net	(187)	40	-568%	(1,100)	129	-953%

- The Fair Value gain or loss on derivative financial instruments reflects the movement in the fair value of warrants issued by the Company that are denominated in a currency other than the Company's functional currency for financial reporting purposes and the impact of interest rate swaps and forex hedging.
- In addition to the operating income, the Directors have given similar consideration to the position of interest on the loan to jointly controlled entity SSEC, with the result that cumulative interest income of USD1.113 million on the loan of USD18.443 million as at December 13, 2011 (up until the date SSEC became consolidated into the Company's financial statements) has been recognised for the year to December 31, 2011. Of this amount, USD0.420 million relates to the year ended December 31, 2010. This change also has no effect on tax expense or cash flows. Refer to *Note 16 to the 2011 Audited Consolidated Financial Statements.*

Acquisition of 34% of SSEC

	Three months ended December 31			Year ended December 31		
	2011	**2010**	%	**2011**	**2010**	%
	$	$	Change	$	$	Change
Gain on previously held interest in SSEC	(27,381)	-	100%	(27,381)	-	100%
Loss on settlement of pre-existing loan relationship	24,423	-	-100%	24,423	-	-100%

- On December 13, 201,1 the Company completed the purchase of 34% of the shares in SSEC from its Tajik joint venture partner Sangam Limited, and increased its shareholding to 85% (from 51%). SSEC is the owner of the rights to the Bokhtar PSC in Tajikistan.

- For full details of loss on acquisition of subsidiary see *Acquisition of Shares in SSEC* below and refer to *Note 25 of the 2011 Audited Consolidated Financial Statements.*

Taxation

	Three months ended December 31			Year ended December 31		
	2011	**2010**	%	**2011**	**2010**	%
	$	$	Change	$	$	Change
Tax	1,664	(718)	-332%	1,947	(3,471)	-156%

The tax charge reflects the change in deferred tax arising as a result of the movement in timing differences between the accounting value of assets and liabilities and their respective values for tax purposes. The recovery in 2011 was due in part to the impairment of Uzbekh assets (see *notes 12 and 13 of the Audited Consolidated Financial Statements*) and a favourable increase in asset tax pools in Kazakhstan.

For details as to why the provision for income taxes is different from the expected provision for income refer to *Note 10 of the Audited Consolidated Financial Statements.*

Acquisition of shares in SSEC

The Group, through Tethys Tajikistan Limited (TTL), established the joint venture company SSEC with Sangam to explore for and develop oil and gas resources in Tajikistan, with TTL holding 51% and Sangam holding 49% of SSEC's shares; however with neither party having voting control. The management of Sangam are experienced in operating businesses in Tajikistan and the Company views this experience as being very valuable in assisting SSEC to develop its business in Tajikistan. Operations were managed and directed by TTL. TTL provided the financing for SSEC by way of a shareholder loan from TTL to SSEC. In November 2011, TTL and Sangam concluded an option agreement for TTL to acquire 34% of SSEC (and full control of the company) from Sangam for cash consideration of USD7 million and the waiver of USD49.92m of the outstanding loan between TTL and SSEC, this option to expire on December 31, 2011. At the time of acquisition, SSEC owed TTL USD66,772,000 with respect to the loan. On December 9, 2011, Tethys announced that it had completed the private placement of 26,062,975 Ordinary Shares for gross proceeds of USD13,069,187, with the private placement being primarily to exercise the option to acquire the Sangam interest. On December 13, 2011 the Company announced that the option had been exercised and that TTL now owned 85% of SSEC and controlled the company.

The non-cash consideration part of the purchase involved the Company agreeing to waive an amount of USD49,920,000 with respect to the loan between SSEC and TTL, being the loan balance at April 1, 2011. The fair value of the joint venture partner's benefit from the loan waiver is the fair value of 15% of the amount waived, representing the future benefit that the joint venture partner will now receive from future distributions by SSEC. The Company involved an independent external expert to fair value 15% of the amount of USD49,920,000 that was waived and full details are provided in *Note 25 of the Company's 2011 Audited Consolidated Financial Statements.*

On completion, TTL increased its shareholding from 51% to 85% and holds a controlling interest in SSEC. The shareholder loan was discharged with effect from April 1, 2011 however continues from April 2, 2011 pursuant to which TTL agrees to finance work programmes and field development of its subsidiaries in Tajikistan. The loan bears interest at the rate of the London inter bank offer rate plus 1% . The loan will be repaid by SSEC from free cash flow before any distribution of profit to SSEC's shareholders. TTL will continue to manage SSEC and subsidiaries in all day to day operations in accordance with the Management Agreement as oil and gas experts.

Subsequent to this transaction the Company now holds 85% economic interest in the contractor share of the Bokhtar PSC which covers an area of 34,797.8 km^2 in the southwest of the country (representing approximately 21.6% of the total land area of Tajikistan). The Bokhtar PSC is for a term of 25 years and covers a large highly prospective region, which has previously produced oil and gas. This transaction has provided the Company with valuable benefits including the acquisition of over 388 million barrels of prospective resources, reducing the interest of a non-funding partner and thereby increasing the Return on Capital Employed going forward, and obtaining control of the Tajikistan joint-venture.

Capital Expenditure

Capital expenditure during the quarter ended December 31, 2011 was USD5.068 million.

	Three months ended December 31			Year ended December 31		
	2011	**2010**	%	**2011**	**2010**	%
	$	$	Change	$	$	Change
Kazakhstan	4,002	13,794	-71%	37,020	33,058	12%
Uzbekistan	167	1,303	-87%	3,772	4,937	-24%
Other and Corporate	899	(13)	-7,015%	1,110	298	272%
	5,068	15,084	-66%	41,902	38,293	9%

Major items of capital expenditure in the three months to December 31, 2011 were:

Kazakhstan

- Akkulka appraisal wells USD4.22 million
- Shalkar rail terminal USD3.10 million
- Kalypso (Kul Bas) USD1.55 million

Uzbekistan

- Workovers USD0.27 million

Tajikistan

- Well EOL09 USD0.48 million
- Persea well USD1.73 million
- Aeromagnetic survey USD0.27 million

Major items of capital expenditure in the year to December 31, 2011 were:

Kazakhstan

- Doris oil production USD 5.40 million
- Akkulka appraisal wells USD22.02 million
- Kalypso (Kul Bas) USD 7.85 million

Note Through its new Joint Venture in Kazakhstan the Company invested USD3.1 million which was spent on the rail terminal at Shalkar.

Uzbekistan

- Well NU96 USD2.76 million
- Workovers USD1.59million

Tajikistan

- Well EOL09 USD4.98 million
- Persea well USD5.18 million
- Aeromagnetic survey USD3.65 million
- KOM201 well USD1.30 million

Transfer of assets

The Company has established a wholly-owned Cayman subsidiary, Imperial Oilfield Services Limited ("IOSL"), to own some of its drilling rigs and other production equipment. At the end of 2011, the Company restructured the ownership of the rigs Telesto and Tykhe and their respective equipment by transferring them from Asia Oilfield Equipment B.V. and AOE Tyke S.A. to IOSL. These transfers were between wholly owned subsidiaries of Tethys and were carried out at Net Book Value. Lenders participating in the USD10 million loan facility, as detailed in "Liquidity and Capital resources" section below, have security against the shares of Imperial Oilfield Services Limited.

Use of Funds

Set out below are details of the planned use of funds as detailed in the prospectus dated October 4, 2010:

The primary differences were in relation to:

1. The well drilling programme in Kazakhstan is ongoing with a further two appraisal wells planned for 2012 and testing of the exploration well in Kul Bas.
2. Phase 1 of the production and processing infrastructure is almost complete though there is some work ongoing including road improvements.
3. While the Company has incurred USD3,100,000 in relation to the Shalkar rail terminal costs further expenditure will be incurred in 2012.
4. There is no significant production yet in Tajikistan and so few costs have been incurred in relation to Production and Processing infrastructure.
5. In Uzbekistan no seismic work has yet been undertaken.
6. While only one well has been drilled in Uzbekistan there have been a number of workovers.

	Prospectus dated Oct 04, 2010	**Incurred to Dec 31, 2011**	**Balance**
Kazakhstan			
Appraisal and Exploration Wells	47,500	34,089	13,411
Production and Processing Infrastructure	19,800	12,650	7,150
Seismic Data	6,000	3,070	2,930
Tajikistan			
Production and Processing Infrastructure	3,760	-	3,760
Seismic Data	3,000	3,000	-
Exploration and Appraisal Drilling Wells	4,000	4,000	-
Uzbekistan			
Seismic Data	2,000	-	2,000
Production Drilling	5,940	2,763	3,177
Total	92,000	59,572	32,428

The primary explanation of the difference between the "Balance" of USD32.4 million per the above table and the cash balance of USD11.6 million per the Company's financial statements are as follows:

Increased spending on Komsomolsk wells
Drilling of EOL09 oil discovery exploration well in Tajikistan
Testing of EOL09
Reduced cash from 2011 Kazakhstan Revenue primarily due to adverse weather conditions
Reduced cash from 2011 Uzbek sales
Business development costs

Set out below are details of the planned use of funds as detailed in the prospectus dated June 11, 2009.

The primary differences were in relation to:

- The Komsomolsk wells KOM 200 and KOM 201, encountered unexpected drilling challenges and cost more than was anticipated and are currently suspended awaiting completion at some future date. As a result the processing plant has not yet been constructed. Additional costs were however incurred on the Beshtentak and Komsomolsk fields.
- Installation of a Gas Lift Compression system in North Urtabulak has now been cancelled following detailed technical and commercial analyses.

	Jun 12, 2009 Prospectus	**Incurred Sept 30, 2011**	**Balance**
Tajikistan			
East Komsomolsk - KOM 200 appraisal well Phase 1	3,500	3,500	-
Infrastructure - Komsomolsk gas Processing plant Phase 1	2,000	-	2,000
East Komsomolsk - gas development well KOM 201 Phase 2	3,500	3,500	-
Additional seismic on Bokhtar PSC	3,660	3,660	-
Uzbekistan			
North Urtabulak Gas Lift Compression System	1,190	-	1,190
North Urtabulak new well.	4,000	4,000	-
Radial drilling and water injection			
Workovers			
	17,850	14,660	3,190

Summary of Quarterly Results

Financials	Mar 31 2010 $	Jun 30 2010 $	Sep 30 2010 $	Dec 31 2010 $	Mar 31 2011 $	Jun 30 2011 $	Sep 30 2011 $	Dec 31 2011 $
Revenue	2,116	6,030	3,173	3,387	4,480	9,883	7,771	8,163
Net loss	(7,999)	(3,322)	(7,118)	(11,210)	(6,294)	(2,696)	(8,575)	(9,424)
Basic and diluted loss ($) per share	(0.05)	(0.02)	(0.04)	(0.04)	(0.02)	(0.01)	(0.03)	(0.04)
Capital expenditure	4,443	7,316	11,950	14,584	10,852	14,834	11,148	5,068
Total assets	186,405	184,082	182,081	267,748	259,477	261,144	255,066	263,391
Total long term liabilities	(13,419)	(14,938)	(15,963)	(11,535)	(10,492)	(8,434)	(8,295)	(4,676)
Cash balance	48,927	30,232	12,917	79,135	57,400	35,855	18,425	11,631
Cash and working capital surplus/(deficit)	38,372	24,408	6,046	69,718	49,893	24,137	4,893	942

The figures in the table above have been prepared under IFRS requirements.

Significant factors influencing quarterly results:

Oil sales from oil test production from Doris commenced in Q4 2010 resulting in revenue of USD748,000 in Q4 2010, USD507,000 in Q1 2011, USD1,101,000 in Q2 2011, USD2,895,000 in Q3 2011 and USD3,682,000 in Q4 2011. See *Oil Sales* above.

Revenue from rig rentals to the JV in Tajikistan was first included in Q2 2011. See *Other operating income* above.

Refined product shipments were delayed in the first two quarters in 2011. See *Refined product sales (Uzbekistan)* above.

Akkulka gas production commenced in Q4 2010. See *Kazakhstan Gas Production (Akkulka contract)* above

During the course of Q2 2010, a number of Uzbekistan refined product shipments were completed which related to 2009 production resulting in higher revenue recognized in Q2 2010. See *Refined product sales (Uzbekistan)* also above.

In December 2009, the Company's Tajikistan operations were transferred to a jointly controlled venture (SSEC). See *Acquisition in SSEC* above.

Financial position

The following table outlines significant movements in the consolidated balance sheets from December 31, 2010 to December 31, 2011:

	Dec 31, 2011	Dec 31, 2010	Movement	Movement Details
Property, plant and equipment	128,918	115,653	13,265	Continuing investment in Akkulka Deep oil property offset by DD&A
Intangible assets	99,959	16,892	83,067	Expenditure on Kul Bas and acquisition of SSEC assets
Non-current other receivables	10,217	12,320	(2,103)	Partial movement of long term VAT receivable to current
Loan receivable from joint controlled entity	2,013	35,460	(33,447)	Full disclosure in note 16 of the 2011 audited consolidated financial statements
Investment in jointly controlled entity	1,113	-	1,113	Investment in the JV - Aral Oil Terminal
Inventories	2,025	2,121	(96)	Movement in finished product - Uzbekistan
Trade and other receivables	5,478	3,680	1,798	Partial movement of long term VAT receivable to current in anticipation of recovery in 2012.
Cash and cash equivalents	10,746	79,135	(68,389)	Refer to Consolidated Statement of Cash Flows in the annual financial statements
Restricted cash	885	-	885	Required in relation to a hedge on foreign currency plus security against credit cards.
Derivative financial instruments - interest rate swap	630	1,472	(842)	Movement in fair value valuation
Other reserves	38,530	34,261	4,269	Stock based compensation expense for the year to December 31
Accumulated deficit	(144,962)	(118,023)	(26,939)	Loss incurred for the year ended December 31. Refer to Financial Review above
Non-controlling interest	8,918	-	8,918	15% non-controlling interest in SSEC
Non-current financial liabilities - borrowings	1,632	2,853	(1,221)	Movement of older loans to current liabilities less new equipment based loan.
Deferred taxation	2,111	4,070	(1,959)	The deferred tax liability arises in Kazakhstan and Uzbekistan as a result of timing differences between the accounting value of assets and liabilities and their respective values for tax purposes.
Current financial liabilities - borrowings	8,396	5,047	3,349	Movement from long term borrowings plus new equipment based loan.
Derivative financial instruments - warrants	264	405	(141)	Movement in the fair value of the liability together with expiry of some warrants
Derivative financial instruments - forex hedge	157	-	157	Movement in the fair value of a foreign currency hedge
Deferred revenue	1,839	2,450	(611)	Net release of Uzbekistan sales awaiting shipment.
Trade and other payables	10,179	8,788	1,391	Increase in trade payables primarily in Kazakhstan

Contractual obligations and liabilities as at December 31, 2011

The following are the contractual maturities of financial liabilities, including estimated interest payments:

		Payments Due by Period $'000s				
	Carrying amount	Contractual cash flow	Less than 1 Year	1 - 3 Years	4 - 5 Years	After 5 years
Trade and other payables	10,726	11,108	10,289	437	382	-
Financial borrowings	10,028	11,029	9,537	1,492	-	-
Commitments	5,162	5,162	5,162	-	-	-
Operating leases	1,055	1,055	670	290	95	-
Total	26,971	28,354	25,658	2,219	477	-

The Company is confident that it will satisfy these obligations and liabilities as and when they fall due.

Liquidity and Capital Resources

In December 2011, the Company closed on the first tranche of a maximum USD10 million loan facility amounting to USD3,965,240, which is secured by the ZJ70 and ZJ30 rigs and other equipment. This facility gives lenders the choice of two methods of repayment designated Option A and Option BUnder Option A, which has a term of one year, lenders have the option to receive monthly repayments on an interest only basis followed by a single balloon repayment of the principal amount to be paid at the maturity date. Option B, which has a term of two years, gives lenders the right to receive equal monthly instalments, incorporating interest and capital, together with a single balloon repayment of half of the principal amount to be paid at the maturity date. These borrowings are held at amortized cost and their carrying amounts approximate to their fair value at the balance sheet date. The interest payable on the borrowed funds is 12% per annum under both options.

In addition, lenders were granted warrants to acquire ordinary shares of the borrower equal to half of each USD100,000 principal amount of the loan advanced to the Company. As at December 31, 2011, 1,982,620 such warrants have been granted to lenders. Under the USD10 million loan facility, a total of 5 million warrants are issuable.

Such warrants will be exercisable at a 25% premium to the price of the volume weighted average CAD price of the shares on the TSX for the 5-day period prior to the day the borrower receives the funds in its bank account. As at December 31, 2011, 1,982,620 warrants had been issued in connection with the first tranche of the loan. The Company has recorded a discount to the loan in the amount of USD232,746 based on the relative fair value of the warrants. USD3,611,005 was then amortised using the effective rate interest method. Lenders have security over the shares of IOSL which has no other assets except the drilling rigs and associated equipment.

The Company completed the second tranche of this loan for a further USD3.2 million was completed in February and of the final tranche of USD2.8 million, USD2.3 million has been received and USD0.5 million has been committed.

For details of other avenues that the Company is pursuing to improve liquidity refer to the "*Funding*" section below.

Cash Flows

The movement in the cash balance during the year to December 31, 2011 compared to what happened in the same period of 2010 can be broken down as follows:

	December 31 2011 $	December 31 2010 $	% Change
Net cash used in operating activities	(12,558)	(16,824)	34%
Net cash used in investing activities	(67,928)	(56,643)	20%
Net cash generated from financing activities	12,107	145,304	-92%
Foreign exchange difference	(10)	1	-1,100%
	(68,389)	71,838	5%

Operating activities

The reduction in the Net cash used in operating activities in the year to December 31, 2011 compared to the previous year can be attributed to the increased level of sales achieved in 2011 *See Sales and Other Revenue above.*

Investing activities

The primary items contributing to Net cash used in investment activity are as follows:

- Purchase of 34% of SSEC USD7,000,000
- Increase in payments made on behalf of SSEC USD18,292,000
- Capital expenditure USD41,902,000

Financing activities

Cash generated from financing activities relates to equity based funding in both years.

Capital management

The Company's capital structure is comprised of shareholders' equity and debt.

The Company's objectives when managing capital is to maintain adequate financial flexibility to preserve its ability to meet financial obligations, both current and long term. The capital structure of the Company is managed and adjusted to reflect changes in economic conditions.

The Company funds its capital expenditures from existing cash and cash equivalent balances, primarily received from issuances of shareholders equity and some debt financing. None of the outstanding debt is subject to externally imposed capital requirements.

Financing decisions are made by management and the Board of Directors based on regularly updated forecasts of the expected timing and level of capital and operating expenditure required to meet both the Company's commitments and development plans. Factors considered when determining whether to issue new debt or to seek equity financing include the amount of financing required, the availability of financial resources, the terms on which financing is available and consideration of the balance between shareholder value creation and prudent financial risk management.

Net debt is calculated as total borrowings (including 'current and non-current borrowings' as shown in the consolidated statement of financial position) less cash and cash equivalents. Total borrowings at December 31, 2011 were higher than at the same point in 2010 primarily due to the new drilling equipment loan less the repayments on the Tykhe loan. *See Liquidity and Capital Resources above.*

Total capital is calculated as 'equity' as shown in the consolidated statement of financial position plus net debt.

There was no net debt at December 31, 2011.

	December 31 2011	December 31 2010
	$	$
Total financial liabilities - borrowings	10,028	7,900
Less: cash and cash equivalents	(11,631)	(79,135)
Net (funds)	(1,603)	(71,235)
Total equity	237,880	239,523
Total capital	236,277	168,288

If the Company was in a net debt position, the Company would assess whether the projected cash flow was sufficient to service this debt and support ongoing operations. Consideration would be given to reducing the total debt or raising funds through an alternative route such as the issuing of equity.

Funding

The directors have considered the Company's current activities, funding position and projected funding requirements for the period of at least twelve months from the date of approval of the consolidated financial statements, in concluding whether it is appropriate to adopt the going concern basis in preparing the consolidated financial statements for the year ended 31 December 2011. The Company's activities, together with the factors likely to affect its future development, performance and position are set out in the Annual Information Form and Management Discussion & Analysis document. The key issues impacting the cash flows of the Company are the commissioning of the AOT rail terminal due at the beginning of April and receipt of the USD5 million Kazakh bank facility. The financial position of the Company, its cash flows and liquidity position are as set out in the Management Discussion & Analysis document on pages 23 to 26 and in Note 20 to the 2011 audited consolidated financial statements. The Company reports a loss for the year ended 31 December 2011 of USD26.989 million (2010: USD29.649 million). As at 29 February 2012, the Company held cash of USD6.7 million.

The AOT rail terminal at Shalkar has been completed and will allow the Company to increase shipments once approved by the local State Commission. The Company believes that the increased oil sales resulting from the production of 4,000 – 6,000 bopd, will generate sufficient levels of cash to fund its ongoing activities and its current capital expenditure plans. Completion of this terminal was originally anticipated to be in the fourth quarter of 2011 but due to adverse weather this was moved back to the first quarter of 2012 and is now due to be commissioned at the beginning of April.

Existing oil operations were disrupted as a result of severe winter weather conditions in Kazazhstan which reduced the sales revenue and so the cash available to the Company. In December 2011 the Company was committed to meet the balloon payments of USD0.7 million due on the expiring Tykhe rig loan and then in the first quarter of 2012 the loans associated with the Uzbekistan NU116 well, drilled in late 2009, were due for settlement with USD4.1 million due in January 2012 and USD3.4 million in March 2012. The Company settled USD1.05 million of the USD4.1 million loan in December 2011 and the remaining funds then rolled over into the new equipment secured loan (see below). All other loan balances were settled on the due dates.

To assist with these commitments, the Company put in place a loan secured against drilling equipment. The total amount of the loan is USD10 million and the first tranche of USD4 million was completed in December 2011, the second tranche of USD3.2 million was completed in February and of the final tranche of USD2.8 million, USD2.3 million has been received and USD0.5 million has been committed.

While as stated above, management is confident that, with the increased production levels at 4,000 – 6,000 bopd, the Company will have sufficient funding for its ongoing activities and its current capital expenditure plans, it is aware that until the terminal is fully commissioned additional funds may be necessary to meet planned outflows. The Company has a number of options with respect to capital expenditure and can defer, delay or cancel several planned capital items. Given the low level of committed capital expenditure, the Directors believe that the Company has sufficient funds but would like to progress other activities if funding allows. For this reason, the Company is exploring a number of alternative funding arrangements including discussions which are close to being finalised with the Company's Kazakh bank with regard to a USD5 million loan facility. In addition, the Company would also like to fund a further USD8 – 10 million of seismic work in Tajikistan, in order to finalise the location of the first deep sub-salt well. This is not a contractual commitment but the Company would like to advance its programme which should assist with bringing in a suitable farm-in partner to fund the drilling of the deep well. The Company is currently adopting a prudent approach to cash management and will proceed with such projects when certain milestones have been met. Discussions have also been initiated with regard to reserve based lending and on other corporate and project related financing options.

With regard to longer term requirements, the Company regularly considers farm-out/farm-in and joint venture opportunities as a means of developing its business and sharing financial and/or commercial risks. As at the date of this report, the Company is in discussions with several parties with regard to a potential farm in and/or joint ventures.

The Directors have examined these issues to form a view on the Company's ability to realise its assets and discharge its liabilities in the normal course of business. After making enquiries and considering the circumstances referred to above, the Directors have a reasonable expectation that the company has adequate resources and potential to continue operations for at least the next twelve months. For these reasons they continue to adopt the going concern basis of accounting in preparing the consolidated financial statements.

Off-Balance Sheet arrangements

The Company has no off-balance sheet arrangements.

Stockholder Equity

As at December 31, 2011, the Company had authorized share capital of 700,000,000 Ordinary Shares of which 286,692,744 (2010: 260,629,769) had been issued and 50,000,000 preference shares of which none had been issued. The preference shares have the rights as set out in the Memorandum and Articles of Association approved at the AGM on April 24, 2008.

On December 9, 2011, the Company completed a previously announced private placement of 26,062,975 Ordinary Shares for gross proceeds of USD13,001,981. The net proceeds of the Offering were to enable Tethys to purchase an additional 34% of shares in SSEC and to carry out additional work on the Beshtentak oilfield in Tajikistan.

As at the date of this report, March 30, 2011, a total of 31,115,572 (2010: 22,100,372) ordinary shares were reserved under the Company's Long Term Stock Incentive Plan and Warrants granted by the Company. The number of options outstanding as at the date of this report is 28,923,000 and the number of warrants outstanding is 6,903,226.

Auditors

At the AGM held in Grand Cayman on June 27, 201,1 KPMG Audit Plc were appointed as auditors of the Company to hold office until the close of the 2012 Annual General Meeting of Shareholders. PriceWaterhouseCoopers had been the previous auditors.

OUTLOOK

The information provided under this heading is considered as forward looking information, as such please refer to *Forward Looking Statements* on page 38 of this MD&A.

The Company's objective is to build a diversified oil and gas exploration and production company with a mixture of short-term cash flow projects and long-term high potential exploration projects focused in the Central Asian region. The Company's approach involves a mix of early cashflow production and development projects, for natural gas and oil, as well as high potential exploration prospects looking to generate significant commercial upside. The Company produces both oil and natural gas in order to balance its product portfolio, and operates in three separate jurisdictions in Central Asia in order to mitigate the political, fiscal and taxation risk that would be inherent with operations solely conducted in one jurisdiction.

While the Company's long-term ambition is to occupy a significant role in the production and delivery of hydrocarbons from the Central Asian region to local and global markets, the specific focus of management in the short term is to:

- fully appraise the Doris oil field discovery in the Akkulka Block, Kazakhstan;
- increase production from the Doris field to 6,000 bopd.
- test and evaluate the Kalypso (KBD01) exploration well with the aim of producing hydrocarbons, subject to having appropriate governmental permissions and available prioritised cash resources;
- continue exploration drilling and evaluation of the Akkulka and Kul-Bas licence blocks in Kazakhstan;
- acquire contracts on new existing oil fields and exploration acreage in Uzbekistan;
- complete the final stage of the seismic programme in Tajikistan;
- fully test the East Olimtoi EOL09 exploration well in Tajikistan;
- fully test the Persea well –PER01 in Tajikistan subject to available prioritised cash resources; and
- further evaluation and testing of the Beshtentak Field in Tajikistan including construction of additional field facilities, completion of a new geological and reservoir model and plan for further workovers and possible drilling to increase oil and gas production.

In common with many oil and gas companies, in implementing its strategies, the Company regularly considers farm-out/farm-in and joint venture opportunities as a means of developing its business and sharing financial and/or commercial risks and is actively pursuing farm outs and similar arrangements on its Tajik and Uzbek assets.

Kazakhstan Operations Update

On November 15, 2011, the AKD06 Doris appraisal well tested oil at a rate of over 4,300 bopd from the Cretaceous sand interval. The flow was restricted but data indicated that open flow potential was in excess of 6,000 bopd. This well commenced production in November and along with wells AKD01 and AKD05 will contribute to the increased production levels when the AOT rail terminal is fully operational.

On January 30, 2012, the Company announced the official inauguration of its AOT terminal – a new storage and rail loading facility for its oil shipments from the Doris oilfield. The AOT is owned and operated through a 50:50 joint venture by Tethys and its Kazakh oil trading partner's company, Olisol Investment Limited. The facilities are fully complete and ready to commence commercial operations and the Company anticipates that these facilities will be fully operational following the visit of a Kazakh governmental State Commission which is planned imminently. The AOT is initially planned to enable the Company to increase production to approximately 4,000 bopd. It is planned to expand the capacity of the terminal to more than 12,000 bopd to accommodate future potential production growth dependent upon further drilling results. Production from Akkulka area is planned to increase to 5,000 - 6,000 bopd later in the year from the existing drilled wells, and further production increases are expected but are dependent on the results of the appraisal / exploration drilling planned for 2012. Further evaluation of the 3D seismic dataset acquired using state of the art processing and interpretation techniques is revealing the probable presence of sand fans in the Cretaceous sandstone sequence and these data are being integrated with the results of the well data to plan future appraisal well locations in the greater Doris area.

The next appraisal well, AKD07, is expected to spud in Q2 2012 and will be located to the south-east of the original AKD01 discovery well and will target 3P reserves at the Cretaceous Aptian sand level in what is believed to be a channel sand system, whilst simultaneously targeting an exciting exploration prospect (named "Dyna") that has been identified on the new seismic data from a bright amplitude anomaly at a slightly shallower level and is interpreted to be part of a different, larger sand fan system. The prospective resource for this new target will be disclosed after the completion of a new independent Kazakhstan Resource Report, which is expected to be issued in Q2 2012.

Additional exploration/appraisal prospects have been identified using the newly interpreted 3D and 2D data. This data has led to the identification of a number of other attractive exploration prospects at the Doris reservoir levels and other horizons. All these will be included in the new resource report.

Tajikistan Operations Update

On October 20, 2011, the Company announced that the Beshtentak well BST20, having been worked over by applying modern perforating and acidisation techniques and applying natural gas lift, tested oil at a rate of 533 bopd accompanied by 12,500 cubic metres (441 thousand cubic feet) of gas per day on a restricted choke (10 mm - 25/64 inch) with a flowing tubing head pressure of 26 atmospheres (377 psi). The oil has an API gravity of 38 degrees.

Initial sales agreements were signed and the first payments from oil sales received. The well was placed on oil production and the gas was tied into the nearby local gas grid but subsequently production performance indicated possible communication with the nearby BST103 well which is producing gas from the field for the city of Kulob, this gas being part of the "base level" production on the field assigned to the Tajik State. As a result the BST20 production is currently restricted and additional data was acquired to ascertain the extent of any possible communication. The well is now back on production but at lower rates than previously and the Company believes that this well needs work carried out on zonal isolation to increase production. This work is planned once the current bad weather conditions have improved. Meanwhile three further workover candidates have been identified in other parts of the field (away from existing producers), which are interpreted to contain remaining bypassed oil and gas and work is progressing to fully assess these interesting opportunities, including potentially the acquisition of downhole seismic data. In addition to conducting recompletion work on these three wells it is planned in the future to locate potentially one or two new high angle or horizontal crestal development wells, which would have the potential to achieve higher production rates than those obtained from the BST20 well.

Testing operations on the East Olimtoi EOL09 exploration well located south of the town of Kulob, some 10 km north of the Afghan border, were initiated in Q3 and Q4. This well reached a total depth of 3,765 metres in the Akdzhar formation in August 2011. The initial results from the raw logs indicated several zones of interest in the Bukhara limestone sequence with potential high oil saturations but testing has shown this reservoir to be unproductive and may require hydraulic fracturing. The Alai formation showed both good oil and gas shows while drilling (with oil and gas to surface) and the electric logs through this interval indicate several hydrocarbon bearing zones with no evidence of any oil-water contact. The well required heavy drilling mud to control the well and it is likely that this has damaged the formation. The well testing programme is planned to be continued in Q2 2012 once specialist equipment is available and operational to stimulate and attempt to establish continual flow of oil from the Alai zone, where oil has been recovered. The EOL 09 well is the first exploration oil discovery in Tajikistan since independence. There are other similar salt swell flank prospects to be explored nearby which was one of the first subjects of the recent deep seismic survey. Some of these salt swells break surface forming "salt mountains" such as the Khoja Mumin salt dome, which has oil and gas prospects around and under it and is located close to East Olimtoi.

The Persea 1 exploration well, located near the town of Kurgon-Teppa in the south-west part of the Bokhtar PSC area, was drilled primarily targeting the Bukhara limestone formation in a four-way dip closed structure with the overlying Alai formation forming a potential secondary target. On December 19, 2011, the Company announced the initial results of its Persea 1 exploration well in Tajikistan. The well reached a total depth of 2,655 metres and wireline logs show a 50 metre gross zone of possible hydrocarbons within mixed sandstone and carbonate sequence assigned to the Alai formation. Testing will be carried out on a cash flow prioritised basis with the cost to be financed by internally generated cash flow.

In 2011, Tethys carried out an aeromagnetic graviometry survey over more than half of the Bokhtar PSC Area. The initial analysis of the data from the aerial graviometry survey completed at the end of 2011 has revealed several attractive prospective areas with the potential presence of very large deep sub-salt and sub-thrust prospects within the Bokhtar PSC Area. This area lies within the Afghan-Tajik basin whose extension, the Amu Darya basin contains some of the world's largest gas and condensate fields, many located in the sub-salt section. No well has ever been drilled through the salt zone to the sub-salt section in the Tajik part of this basin. It is now planned to acquire additional seismic which will target these areas and provide the final data in a comprehensive programme to optimally locate a deep well. It is expected that this data will be acquired this summer with initial interpreted results in Q4 2012. It is also expected that Tethys' large drilling rig "Telesto" will be mobilized to Tajikistan before the end of this year in order to drill this well.

The seismic programme will involve the acquisition of approximately 870km of new 2D seismic in two areas. The programme has been designed to target these areas as the graviometry survey has identified them to be the most likely to contain large deep prospects including potential Jurassic reefs located on the edge of likely Permian basement high features. Jurassic reefs form some of the most prolific fields in the Amu Darya basin and no wells have ever been drilled through to the Jurassic horizon through the overlying salt layer in Tajikistan to date. The data also reveals significant potential in other parts of the Bokhtar PSC Area, including the Kulob area.

It is planned to carry out a new resource report in 2012 based on the results of this work.

The Company has previously stated that it is seeking a suitable farm-in partner for its exploration programme in Tajikistan and the seismic data are an important part of the information relating to such a potential farm-in. Discussions continue with several parties.

Uzbekistan Operations Update

The Company intends to focus future efforts in Uzbekistan on developing new contracts such as the Chegara PEC or on potential exploration activities. The North Urtabulak impairment (See *Impairment Adjustment in Uzbekistan* above) must be taken in the context of the new projects which the Company is now developing in Uzbekistan. The North Urtabulak project is a late stage re-development and incremental production project on an old field and the Company has used this project as a base to develop additional projects and a significant business presence in Uzbekistan. Currently these new projects include the Chegara PEC (Chegara is a much less developed producing field) and the potential exploration block in the North Ustyurt basin (which is south of the Doris discovery in Kazakhstan and which the Company believes has considerable exploration potential).

In November 2011, the Company announced it had signed an MOU with UNG, establishing a programme for Tethys to obtain a new PEC on an existing oilfield in Uzbekistan. The MOU presented an agreed timetable up to May 1, 2012 to negotiate for a new PEC for the Chegara Group of fields. The Chegara Group of fields is located in the same geographical area as North Urtabulak. The Chegara Group of fields is less developed than North Urtabulak, and Tethys believes that these fields offer significant potential for additional oil production in the short term.

In February 2012, the Company announced it had signed an additional MOU with UNG. The objective of this MOU was to continue providing the framework for a Joint Study and the negotiation process for an Exploration Agreement relating to certain exploration blocks in the North Ustyurt Basin of Uzbekistan.

Transactions with Related Parties

Vazon Energy Limited

Vazon Energy Limited ("Vazon") is a corporation organized under the laws of the Bailiwick of Guernsey, of which Dr. David Robson, Chief Executive Officer, is the sole owner and managing director. Tethys has a management services contract with Vazon that came into effect from June 27, 2007 whereby the services of Dr. Robson and other Vazon employees are provided to the Company. The total cost charged to Tethys for services under a "not for profit flow through" contract from Vazon in the year ended December 31, 2011 was USD3, 295,754 (December 31, 2010 USD2,525,885). 34% of the increase was as a result of remuneration increases, 66% as a result of new staff/internal transfers.

Vazon as a Guernsey based company plays, amongst other things, a pivotal role in the obtaining and maintaining of residence licences for senior staff in Guernsey.

Oilfield Production Consultants

Oilfield Production Consultants (OPC) Limited, Oilfield Production Consultants (OPC) Asia LLC and Oilfield Production Consultants (OPC) USA LLC, both of which have one common director with the Company, has charged Tethys for work on projects in Tajikistan, Kazakhstan and Uzbekistan. Total fees for the year ended December 31, 2011 were USD11,422 (December 31, 2010 – USD182,470). OPC participated in the 2011 loan financing described in *Liquidity and Capital Resources* above, advancing USD200,000 under Option B of the facility. As a result, OPC received 100,000 warrants valued at a fair value of USD15,030. The loan was advanced under the same conditions and terms disclosed in note 20.1 afforded to non-related parties.

Two officers of the Company participated in the 2011 loan financing described in *Liquidity and Capital Resources* above, for which they received 75,000 and 232,620 warrants valued at a fair value of USD6,143 and USD21,983 respectively. Loans advanced were USD150,000 and GBP300,000 respectively for a one year term under the same conditions and terms disclosed in note 20.1 afforded to external parties.

Transactions with affiliates or other related parties including management of affiliates are to be undertaken on the same basis as third party arms-length transactions.
Related party transactions with SSEC are disclosed in *Other operating income* above.

There have been no changes in the related parties transactions described in the last annual report.

New and amended accounting standards adopted by the Company

There were no significant new or amended standards introduced for the current accounting year relevant for the Company for these financial statements.

Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Company.

The following standards and amendments to existing standards have been published and are mandatory for the Company's accounting periods beginning on or after January 1, 2012 or later periods, but the Company has not early adopted them:

- IFRS 9 'Financial instruments' – issued in November 2009. This standard is the first step in the process to replace IAS 39, 'Financial instruments: recognition and measurement'. IFRS 9 introduces new requirements for classifying and measuring financial assets and liabilities, which may affect the Company's accounting for its financial assets. The standard is not applicable until January 1, 2015 but is available for early adoption. This standard will have no impact on the Company's consolidated financial statements as currently reported.
- IFRS 10 'Consolidated Financial Statements' – issued in May 2011. This standard is part of a new suite of standards on consolidation and related standards, replacing the existing accounting for subsidiaries and joint ventures (now joint arrangements), and making limited amendments in relation to associates. It supersedes IAS 27 'Consolidated and Separate Financial Statements' and SIC-12 'Consolidation – Special Purpose Entities' (SPEs). It provides a single model to be applied in the control analysis for all investees, including entities that currently are SPEs in the scope of SIC-12. This standard is not applicable until January 1, 2013. The amendments will not result in a material impact on the Company's consolidated financial statements.
- IFRS 11 'Joint Arrangements' – issued in May 2011. This standard is part of a new suite of standards on consolidation and related standards, replacing the existing accounting for subsidiaries and joint ventures (now joint arrangements), and making limited amendments in relation to associates. All parties to a joint arrangement are within the scope of IFRS 11. IFRS 11 carves out from IAS 31 'Interests in Joint Ventures', those cases in which there is a separate vehicle but that separation is overcome by form, contract

or other facts and circumstances. It also removes the choice of equity or proportionate accounting for jointly controlled entities. Although this standard is not applicable until January 1, 2013 and is not available for early adoption, the Company has considered the potential impact this standard will have on the accounting for existing jointly controlled entities. There will be no impact as the Company will still be able to account for its existing joint arrangements under equity accounting.

- IFRS 12 'Disclosure of Interests in Other Entities' – issued in May 2011. This standard is part of a new suite of standards on consolidation and related standards, replacing the existing accounting for subsidiaries and joint ventures (now joint arrangements), and making limited amendments in relation to associates. It contains the disclosure requirements for entities that have interests in subsidiaries, joint arrangements, associates and/or unconsolidated structured entities. This standard is not applicable until January 1, 2013 and will not result in a material impact to the Company's consolidated financial statements.
- IFRS 13 'Fair Value Measurement' – issued in May 2011. The is a new standard to replace existing guidance on fair value measurement in different IFRSs with a single definition of fair value, a framework for measuring fair values and disclosures about fair value measurements. The standard applies to assets, liabilities and an entity's own equity instruments that, under other IFRSs are required or permitted to be measured at fair value or when disclosure of fair value is provided. This standard is not applicable until January 1, 2013 and will not result in a material impact to the Company's consolidated financial statements.

RISKS AND UNCERTAINTIES AND OTHER INFORMATION

Tethys' business may be impacted by various risks not all of which are within its control. Readers are encouraged to read and consider the risk factors and additional information regarding the Company, included in its 2011 Annual Information Form filed with the Canadian securities regulators, a copy of which is posted on the SEDAR website at www.sedar.com. All risks which were detailed at that time have not changed and remain appropriate.

Risk management is carried out by senior management, in particular, the Executive Board of Directors.

The Company has identified its principal risks for 2012 to include:

- Exploration and development expenditures and success rates, though considerable technical work is undertaken to reduce related areas of risk and maximise opportunities.
- Oil and gas sales volumes and prices;
- Retention and extension of existing licences; and
- Liquidity.

Financial Risk Management

The Company's activities expose it to a variety of financial risks including credit risk, liquidity risk, interest rate risk and foreign exchange. The Company's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Company's financial performance.

Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to financial instruments fails to meet its contractual obligations. Credit risk arises from the Company's cash and cash equivalents and accounts receivable balances.

With respect to the Company's financial assets the maximum exposure to credit risk due to default of the counter party is equal to the carrying value of these instruments. The maximum exposure to credit risk as at the reporting date was:

	Dec 31, 2011	Dec 31, 2010
	$	$
Trade receivables	837	1,661
Cash and cash equivalents	10,746	79,135
Loan receivable from jointly controlled entity	2,013	35,460
Restricted cash	2,292	1,015
	15,888	117,271

Concentration of credit risk associated with the above trade receivable balances in Kazakhstan is as a result of contracted sales to three customers during the year. The Company does not believe it is dependent upon these customers for sales due to the nature of gas products and the associated market. The Company's sales in Kazakhstan commenced in December 2007 and the Company has not experienced any credit loss to date. At December 31, 2011, the trade receivable balance amounted to USD836,837 (2010 - USD1,661,015), none of which was greater than 30 days overdue. The Company has therefore not recorded a provision against this amount as it does not consider the balance to be impaired.

Included in the restricted cash balance at December 31, 2011 is USD0.885 million security deposit held by HSBC Bank in support of the hedging arrangement put in place in May 2011 and in support of company credit cards. *See Hedging Arrangement below.*

In Uzbekistan, the Company makes use of three customers where full payment is in US Dollars and is required before delivery of the oil and therefore there is limited exposure to credit risk in this country. In Tajikistan, oil is currently being purchased by two buyers where prepayment in full is also required before delivery.

Although a significant amount of the deposits at financial institutions are not covered by bank guarantees, the Company does not believe there to be a significant risk of credit loss as the majority of the counterparties are banks with high credit ratings (BBB or equivalent) assigned by international ratings agencies (Fitch and Standard and Poors). Previously the Company's minimum rating for any bank was A- but after careful consideration a decision was taken to place funds with Investec Bank plc which has a BBB rating. Within the Central Asian countries, banks with the international ratings are generally not available.

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. This risk relates to the Company's ability to generate or obtain sufficient cash or cash equivalents to satisfy these financial obligations as they become due. Since inception, the Company has incurred significant consolidated losses from operations and negative cash flows from operating activities, and has an accumulated deficit at December 31, 2011.

The Company's processes for managing liquidity risk includes preparing and monitoring capital and operating budgets, co-ordinating and authorizing project expenditures and ensuring appropriate authorization of contractual agreements. Revenue and expenditure levels, both actual and projected, are reviewed on a regular basis and forecasts updated accordingly. These forecasts enable the Company to identify when additional financing might be needed or expenditure plans adjusted.

The timing of cash outflows relating to financial liabilities and commitments at the reporting date are summarized on page 21 above in *Contractual obligations and liabilities as at December 31, 2011.*

Particularly in the current climate, there can be no assurance that debt or equity financing will be available or sufficient to meet the Company's requirements or if debt or equity financing were available, that it would be on terms acceptable to the Company. The inability of the Company to access sufficient capital for its operations could have a material impact on the Company's financial condition, timing of activities and results of operations and prospects.

Interest rate risk

Interest rate risk is the risk that the value of a financial instrument will be affected by changes in market interest rates. Existing long term debt is agreed at fixed interest rates and consequently has limited exposure to volatility in market interest rates.

Because of the current level of deposit interest rates on USD being less than 1%, the Company's exposure to interest rate risk on short term deposits is minimal.

Foreign exchange risk

The Company is exposed to risks resulting from fluctuations in a number of foreign currency exchange rates. A material change in the value of any such foreign currency could result in a material adverse effect on the Company's cash flow and future profits. The Company is exposed to exchange rate risk to the extent that balances and transactions are denominated in a currency other than the USD. A significant portion of expenditures in Kazakhstan are denominated in local currency, the Tenge. There is limited availability in exchange rate derivatives to manage exchange rate risks with this currency.

During the year, the Company used an exchange rate derivative to manage its risk as a result of the significant exchange rate fluctuation of the USD against GBP (note 20.4).

The Company holds the majority of its cash and cash equivalents in US dollars. However, the Company does maintain deposits in other currencies, as disclosed in the following table, in order to fund ongoing general and administrative activity and other expenditure incurred in these currencies.

The carrying amounts of the Company's significant foreign currency denominated monetary assets and liabilities at the reporting dates are as follows:

In USD equivalent at December 31, 2011	**CAD '000**	**GBP '000**	**EUR '000**	**KZT '000**
Cash and cash equivalents	137	810	62	1,647
Trade and other receivables	-	31	42	12,651
Trade and other payables	-	(229)	-	(4,187)
Financial liabilities - borrowings	-	(433)	-	-
Net exposure	**137**	**179**	**104**	**10,111**

In USD equivalent at December 31, 2010	**CAD '000**	**GBP '000**	**EUR '000**	**KZT '000**
Cash and cash equivalents	1,201	1,123	60	492
Trade and other receivables	-	19	24	10,434
Trade and other payables	(1)	(131)	-	(4,402)
Financial liabilities - borrowings	-	(287)	-	-
Net exposure	**1,200**	**724**	**84**	**6,524**

The following table details the Company's sensitivity to a 10% movement in USD against the respective foreign currencies, which represents management's assessment of a reasonably likely change in foreign exchange rates.

2011 Effect in USD'000	CAD	GBP	EUR	KZT
Profit or (loss) before tax	14	18	10	1,011

2010 Effect in USD'000				
Profit or (loss) before tax	120	72	8	652

A 10% strengthening of the USD against the currencies above at December 31, 2011 would have had an equal but opposite effect on the amounts shown above, assuming all other variables remained constant.

Hedging arrangement

On May 12, 2011 the Company took out foreign currency hedge contracts to hedge exposure to the USD/GBP exchange rate. The contracts are in the form of a put option to sell US dollars with a strike price of 1.6495, with a clause that if a barrier level in the foreign currency exchange rate of 1.5675 is breached on the date of expiry, the option converts to a forward contract at the strike price of USD1.6495. The fair value of the foreign currency contract was calculated using a valuation technique based on observable market inputs. Should the foreign currency exchange rate on the date of expiry be above the barrier of 1.5675 then no settlement would be required. Should the USD/GBP foreign currency rate be above 1.6495 then the options could be exercised at a gain to the Company.
In this arrangement each month up to and including December 2011, the Company could convert up to USD1 million on a set day each month at the lower of the market rate or a maximum secured rate of USD1.6495. From January to April 2012, the sum involved each month reduced to USD0.75 million. In support of this arrangement, the Company has to hold funds in the form of a security deposit with the bank though the balance required reduces during the period of the hedge. At December 31, 2011, this balance was USD0.35 million.

Foreign currency risk

Currently, there are no significant restrictions on the repatriation of capital and distribution of earnings from Kazakhstan or Tajikistan to foreign entities. While there are in fact restrictions on repatriation of capital and distribution of earnings from Uzbekistan to foreign entities, the Company has not been affected by this as it is paid for its refined product sales in US Dollars outside of Uzbekistan. There can be no assurance, that restrictions on repatriation of capital or distributions of earnings from Kazakhstan or Tajikistan will not be imposed in the future. Moreover, there can be no assurance that the Tenge, Somoni or Soum will continue to be exchangeable into U.S. Dollars or that the Company will be able to exchange sufficient amounts of Tenge, Somoni or Soum into U.S. Dollars or Pounds Sterling to meet its foreign currency obligations.

Market risk

Market risk is the risk of loss that may arise from changes in market factors such as marketability of production and commodity prices.

Marketability of Production

The marketability and ultimate commerciality of oil and gas acquired or discovered is affected by numerous factors beyond the control of the Company. These factors include reservoir characteristics, market fluctuations, the proximity and capacity of oil and gas pipelines and processing equipment and government regulation. The Company currently produces gas into the transcontinental gas trunkline system which ultimately supplies gas to Russia and Europe. Political issues, system capacity constraints, export issues and possible competition with Russian gas supplies may in the future cause problems with marketing production, particularly for export. Oil and gas operations (exploration, production, pricing, marketing and transportation) are subject to extensive controls and regulations imposed by various levels of government, which may be amended from time to time. Restrictions on the ability to market the Company's production could have a material adverse effect on the Company's revenues and financial position.

Commodity price risk

Oil and gas prices are unstable and are subject to fluctuation. Any material decline in oil and/or natural gas prices could result in a reduction of the Company's net production revenue and overall value and could result in ceiling test write downs. In Kazakhstan the Company has fixed price gas contracts up to the end of 2012 but its oil contract in Kazakhstan and its refined products in Uzbekistan are subject to commodity price fluctuation and it may become uneconomic to produce from some wells as a result of lower prices, which could result in a reduction in the volumes and value of the Company's reserves. The Company might also elect not to produce from certain wells at lower prices. All of these factors could result in a material decrease in the Company's net production revenue causing a reduction in its acquisition and development activities. Beyond 2012 fluctuations in oil and gas prices could materially and adversely affect the Company's business, financial condition, results of operation and prospects. There is no government control over the oil and gas price in the countries where the Company operates.

Although the Company believes that the medium to long term outlook for oil and gas prices in the region is good, the recent events in Africa and the Middle East demonstrate the volatility and uncertainties of the oil and gas industry. Also, there needs to be consideration of production and other factors such as OPEC, refinery shut-ins and inventory. Any discussion of price or demand is subjective and as such there are many differing opinions on the cause of recent price changes.

As previously stated production from both the Kyzyloi and Akkulka contracts in Kazakhstan are sold at fixed prices, at least until the end of 2012, and so the fluctuation in world commodity prices should have no effect on the Company's revenue from the Kazakh gas operations. In Uzbekistan, the Company sells refined petroleum products on a monthly basis and is consequently also subject to movements in the oil price.

Sensitivities

The price of gas sales from gas produced from the Kyzyloi gas field under the Gas Supply Contract is fixed in US dollars until December 1, 2012 and the Akkulka gas field under the Gas Supply Contract is fixed in US dollars until September, 2012 and consequently there is no sensitivity to currency movements or market movements in the gas price.

The price of oil sales from the Doris discovery planned at 4,000 bopd (Phase 1) due to commence in April 2012 has yet to be agreed and therefore would be sensitive to movements in the market price. On a production level of 4,000 bopd, a movement of USD1 per barrel on the price received by the Company would result in a plus or minus movement in the sales revenue of USD1,460,000 per annum.

The sales revenue in Uzbekistan is sensitive to fluctuations in the price of oil. At net production levels of 225 bopd, a movement of USD1 per barrel on the price received by the company would result in a maximum plus or minus movement in the sales revenue of USD82,125 per annum.

Environmental

The Company's operations are subject to environmental, safety and health and sanitary regulations in the jurisdictions in which it operates. Whilst the Company believes that it carries out its activities and operations in material compliance with these environmental, safety and health and sanitary regulations, there can be no guarantee that this is the case. In Kazakhstan, quarterly reports are required to be submitted by the Company to the Shalkar (Bozoi) Tax Committee. The Company is also required to prepare reports on any pollution of air, toxic waste and current expenses on environmental protection which have been made by the Company and which are submitted to the appropriate Kazakh authorities. Reports are submitted on a semi-annual basis for information purposes and no payments are applicable. In Tajikistan, the Company is subject to environmental regulation and its activities are subject to inspection by the appropriate authority in that country.

At present, the Company believes that it meets satisfactory environmental standards in all material respects in all of the areas in which it operates, and has included appropriate amounts in its capital expenditure budget to continue to meet its current environmental obligations. However, the discharge of oil, natural gas or other pollutants into the air, soil or water may give rise to liabilities to foreign governments and third parties and may require the Company to incur significant costs to remedy such discharge. No assurance can be given that changes in environmental laws or their application to the Company's operations will not result in a curtailment of production or a material increase in the costs of production, development or exploration activities or otherwise adversely affect the Company's financial condition, results of operations or prospects.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The annual and interim consolidated financial statements of the Company are prepared in accordance with International Financial Reporting Standards ("IFRSs") and IFRIC Interpretations issued by the IFRS Interpretations Committee.

Please refer to the Audited Consolidated Financial Statements for the year ended December 31, 2011 *Note 2 Summary of Significant Accounting Policies* for details of the Company's accounting policies which is accompanied herein by reference.

INTERNAL CONTROLS OVER FINANCIAL REPORTING

The Chief Executive Officer (CEO) and the Chief Financial Officer (CFO) of Tethys are responsible for establishing and maintaining internal control over financial reporting (ICFR) as that term is defined in National Instrument 52-109 – Certification of Disclosure in Annual and Interim Filings. The CEO and the CFO of Tethys are responsible for designing a system of internal controls over financial reporting, or causing them to be designed under their supervision, in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external reporting purposes in accordance with IFRS.

Management of Tethys has designed and implemented, under the supervision of its CEO and CFO, a system of internal controls over financial reporting as of December 31, 2011 which it believes is effective for a company of its size. Management of Tethys has not identified any material weaknesses relating to the design of the internal controls over financial reporting as at December 31, 2011. The Company's control system and procedures are reviewed periodically and adjusted or updated as necessary. In addition, where any new or additional risks have been identified then the management of Tethys has put in place appropriate procedures to mitigate these risks.

Under the supervision of the CEO and the CFO, an evaluation of the effectiveness of internal control over financial reporting based on "Internal Control – Integrated Framework" issued by the Committee of Sponsoring Organisations of the Treadway Commission was carried out in Q4 of 2011. Based on this evaluation management concluded that the Company's internal control over financial reporting was effective as at December 31, 2011. No material weakness relating to the design of the Company's system of ICFR or relating to the Company's operations as at December 31, 2011 have been identified.

DISCLOSURE CONTROLS AND PROCEDURES

The CEO and the CFO are responsible for establishing and maintaining disclosure controls and procedures (DC+P) as that term is defined in NI 52-109. Disclosure controls and procedures have been designed by the Tethys Management, under the supervision of the CEO and CFO, to ensure that information required to be disclosed by the Company is accumulated, recorded, processed and reported to the Company's management as appropriate to allow timely decisions regarding disclosure.

FORWARD-LOOKING STATEMENTS

In the interest of providing Tethys' shareholders and potential investors with information regarding the Company and its subsidiaries, including management's assessment of Tethys' and its subsidiaries' future plans and operations, certain statements contained in this MD&A constitute forward-looking statements or information (collectively referred to herein as "forward-looking statements") within the meaning of the "safe harbour" provisions of applicable securities legislation. Forward-looking statements are typically identified by words such as "anticipate", "believe", "expect", "plan", "intend", "forecast", "target", "project" or similar words suggesting future outcomes or statements regarding an outlook. Forward looking statements in this MD&A include, but are not limited to, statements with respect to: the projected 2012 capital investments projections, and the potential source of funding therefore. Readers are cautioned not to place undue reliance on forward-looking statements, as there can be no assurance that the plans, intentions or expectations upon which they are based will occur. By their nature, forward-looking statements involve numerous assumptions, known and unknown risks and uncertainties, both general and specific, that contribute to the possibility that the predictions, forecasts, projections and other forward-looking statements will not occur, which may cause the Company's actual performance and financial results in future periods to differ materially from any estimates or projections of future performance or results expressed or implied by such forward-looking statements. These risks, uncertainties and assumptions include, among other things: volatility of and assumptions regarding oil and gas prices; fluctuations in currency and interest rates; sufficiency of capital resources; ability to successfully complete proposed equity financings; product supply and demand; market competition; ability to realise current market gas prices; risks inherent in the Company's and its subsidiaries' marketing operations, including credit risks; imprecision of reserve estimates and estimates of recoverable quantities of oil and natural gas and other sources not currently classified as proved; the Company's and its subsidiaries' ability to replace and expand oil and gas reserves; unexpected cost increases or technical difficulties in constructing pipeline or other facilities; unexpected delays in its drilling operations; delays in the delivery of its drilling rigs; unexpected difficulties in, transporting oil or natural gas; risks associated with technology; the Company's ability to generate sufficient cash flow from operations to meet its current and future obligations; the Company's ability to access external sources of debt and equity capital; the timing and the costs of well and pipeline construction; the Company's and its subsidiaries' ability to secure adequate product transportation; changes in royalty, tax, environmental and other laws or regulations or the interpretations of such laws or regulations; political and economic conditions in the countries in which the Company and its subsidiaries operate; the risk of international war, hostilities, civil insurrection and instability affecting countries in which the Company and its subsidiaries operate and terrorist threats; risks associated with existing and potential future lawsuits and regulatory actions made against the Company and its subsidiaries; and other risks and uncertainties described from time to time in the reports and filings made with securities regulatory authorities by Tethys.

With regard to forward looking information contained in this MD&A, the Company has made assumptions regarding, amongst other things, the continued existence and operation of existing pipelines; future prices for natural gas; future currency and exchange rates; the Company's ability to generate sufficient cash flow from operations and access to capital markets to meet its future obligations; the regulatory framework representing mineral extraction taxes, royalties, taxes and environmental matters in the countries in which the Company conducts its business: gas production levels; and the Company's ability to obtain qualified staff and equipment in a timely and cost effective manner to meet the Company's demands. Statements relating to "reserves" or "resources" or "resource potential" are deemed to be forward-looking statements, as they involve the implied assessment, based on certain estimates and assumptions that the resources and reserves described exist in the quantities predicted or estimated, and can be profitably produced in the future. Although Tethys believes that the expectations represented by such forward-looking statements are reasonable, there can be no assurance that such expectations will prove to be correct. Readers are cautioned that the foregoing list of important factors is not exhaustive. Furthermore, the forward-looking statements contained in this MD&A are made as of the date of this MD&A, and except as required by law Tethys does not undertake any obligation to update publicly or to revise any of the included forward looking statements, whether as a result of new information, future events or otherwise. The forward-looking statements contained in this MD&A are expressly qualified by this cautionary statement.

Bernard Murphy, Chief Financial Officer