



**ENERCHEM**  
INTERNATIONAL INC.

2<sup>nd</sup> Quarter Interim Report 2008



# President's Message

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## To Our Shareholders,

On behalf of the Board of Directors of Enerchem International Inc. ("the Company") I am pleased to provide this report on the results of the Company's operations for the three and six months ended June 30, 2008.

Against the backdrop of an industry quarter that was essentially flat year-over-year, Enerchem's revenues increased by 186% when compared to the same quarter last year and by 56% for the first half of 2008 versus the same period in 2007. These increases reflect a significant increase in sales volume over the comparative periods in 2007 and are also a function of higher prices charged for our finished products as we attempt to remain aligned with the rise in crude oil prices. These results also reflect our effort to improve our plant output and efficiency as well as maximize our finished goods sales. We believe that having both manufacturing and distribution capability provides us with a competitive advantage in this price driven commodity market.

Throughout the quarter we have also concentrated on maximizing production out of our Slave Lake facility and increasing our storage capacity in order to be better prepared to meet the seasonal requirements of our clients. As a result, we have built up finished goods inventory over the quarter which is reflected on the balance sheet at June 30, 2008 by the approximately \$2.0 million increase in inventory over the \$8.7 million in inventory at the end of the first quarter of 2008 and \$4.8 million over the \$5.8 million of inventory at the end of 2007.

For both the second quarter and the year-to-date of 2008 we have posted a loss of \$1.1 million. This result includes a provision for restructuring costs of \$850,000 relating to the consolidation of our accounting and administrative offices from Leduc to Calgary, Alberta. The consolidation is expected to be completed by October 31, 2008. The net loss for both periods also reflects the effects of margin compression associated with the increase in feedstock costs caused by the dramatic rise in commodity prices. However, with the return to operation of our Sundre plant in the third quarter of this year, we anticipate lowering overall production costs and increased leverage on our fixed cost structure.

Over the reporting quarter of 2008 industry activity continued to track below 2007 levels with a 3% drop in wells drilled on a completion basis (3,148 compared to 3,232 in the second quarter of 2007); the year-to-date decline is 17% (8,134 compared to 9,822 in 2007).<sup>1</sup> Rig utilization rates improved slightly quarter-

over-quarter (19% compared to 17%), but trail 2007 year-to-date utilization rates at 38% vs. 39%. It has become somewhat commonplace to report that weather affected the second quarter; it did again this year particularly in June which provided the industry with only two weeks of productive activity.

There are some indications that the cycle's downward movement may have moderated. During this reporting quarter the Petroleum Services Association of Canada ("PSAC") increased its forecast for wells drilled on a rig-released basis in 2008 by 2,000 wells. In addition, although natural gas prices have weakened in recent weeks, US natural gas storage for the week of July 18th was estimated to be tracking about 11% below this time last year and slightly below the five year average. Provided that natural gas prices remain above economically viable levels, we see this trend together with the approximately 60% year-over-year reduction (July import figures) in LNG imports into North America, as positive for the Western Canadian natural gas producers and therefore gas drilling in this region.

## Strategy and Outlook

Our operating strategy remains unchanged from that outlined in the first quarter report for 2008. We continue to make investments in our fractionation plants to improve their operating efficiency. With respect to our Sundre plant, we announced on July 8, 2008 that we were re-installing its salt-bath heaters in order to return the plant into production during the busy drilling quarters of the year. This initiative is proceeding as planned, and we expect to soon announce its completion. The project to replace these salt-bath heaters with more efficient, re-designed direct-fired heaters is also continuing, and is in the early re-engineering phase.

Given the continued strength in commodity prices and record cash flows being generated by producers, there is growing industry consensus that these underlying fundamentals may provide for stronger than expected levels of oilfield activity during the second half of 2008 and in 2009. Enerchem is well positioned to take full advantage of this opportunity.



Kenneth Bagan  
President and Chief Executive Officer

<sup>1</sup> Source: Canadian Association of Drilling Contractors ("CAODC")



## Financial Highlights

(unaudited)

### Results of Operations

<b>Three months ended June 30</b>	<b>2008</b>	<b>2007</b>
	\$	\$
Revenues	21,390,234	7,467,779
Net loss for the period	(1,067,125)	(648,176)
Net loss per share		
Basic	(0.07)	(0.04)
Diluted	(0.07)	(0.04)
EBITDA (1)	152,987	(441,061)
EBITDA per share (2)	0.01	(0.03)

<b>Six months ended June 30</b>	<b>2008</b>	<b>2007</b>
	\$	\$
Revenues	55,137,155	35,344,180
Net (loss) earnings for the period	(1,137,484)	1,194,575
Net (loss) earnings per share		
Basic	(0.07)	0.08
Diluted	(0.07)	0.08
EBITDA (1)	705,943	2,827,247
EBITDA per share (2)	0.05	0.18

### Financial Position

<b>As at</b>	<b>June 30, 2008</b>	<b>June 30, 2007</b>
Total assets	66,686,455	65,589,250
Working capital (3)	13,144,756	20,172,629
Shareholders' equity	50,647,473	57,540,216

(1) EBITDA represents earnings from continuing operations before interest expense, taxes, depreciation, amortization, accretion expense, restructuring costs and write-downs.

(2) EBITDA per share is calculated as EBITDA divided by the basic weighted average common shares outstanding.

(3) Calculated as current assets less current liabilities.

## Management's Discussion and Analysis

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This Management's Discussion and Analysis ("MD&A") of the financial position and interim consolidated results of operations of Enerchem International Inc. for the period ended June 30, 2008 should be read in conjunction with the interim financial statements for the period ended June 30, 2008 and the audited financial statements and notes thereto, President's Message and MD&A for the year ended December 31, 2007. This MD&A is dated August 6, 2008.

Additional information relating to the Company, including the Company's Annual Information Form, is available on the System for Electronic Document Analysis and Retrieval ("SEDAR") at [www.sedar.com](http://www.sedar.com).

*Statements throughout this report that are not historical facts may be considered "forward looking statements." Such statements are based on current expectations that involve risks and uncertainties which could cause actual results to differ from those anticipated. Important factors that can cause anticipated outcomes to differ materially from actual outcomes include the impact of general economic conditions, industry conditions, competition from other industry participants, volatility of petroleum prices, the ability to attract and retain qualified personnel, changes in laws or regulations, currency fluctuations, continued ability to access capital from available facilities and environmental risks. References in this MD&A to "Enerchem", the "Company", "us", "we", and "our" mean Enerchem International Inc.*

### Use of Non-GAAP Measures

This MD&A contains references to certain financial measures that do not have any standardized meaning prescribed by Canadian Generally Accepted Accounting Principles ("GAAP"), and may not be comparable to similar measures presented by other companies or trusts. These measures are provided to assist investors in determining the Company's ability to generate cash from operations and to provide additional information regarding the use of its cash resources. These financial measures are identified below:

- EBITDA represents earnings from operations before interest expense, taxes, depreciation, amortization, accretion expense, restructuring costs and write-downs. It is used by management internally to measure the performance of the business as a whole. EBITDA is presented as supplemental information because management believes it is a widely used financial indicator of the Company's operating profitability and performance before the effects of capital investment and financing decisions.
- Cash provided by operations is derived from the Company's consolidated statement of cash flows and represents cash provided by operating activities before changes in non-cash components of working capital. Cash provided by operations is provided as supplemental information because management believes it provides investors with additional information regarding the Company's ability to generate funds to finance operations and its capital requirements.
- EBITDA per share represents EBITDA divided by the basic weighted average common shares outstanding.

### Overview of the Company's Operations

Enerchem is a manufacturer of hydrocarbon drilling and fracturing fluids, designed to provide cost effective solutions to the upstream oil and gas industry, and specialty solvents which are designed to resolve production and processing problems encountered by downstream producers. The Company's proprietary hydrocarbon products are manufactured through its facilities located in Sundre and Slave Lake, Alberta and are distributed through its network of sales and service representatives. The Company has also diversified its operations to capture energy marketing opportunities that are focused on maximizing value received by the Company for its hydrocarbon by-products, providing energy marketing management and expertise and to mitigate, in part, the Company's exposure to the seasonality of its operations. In addition, through its wholly owned subsidiary, Millard Trucking Ltd. ("Millard") based in Sundre, Alberta, the Company provides transportation services and other oilfield services to the oil and gas industry. The operations of the Company are conducted entirely within the Western Canadian Sedimentary Basin ("WCSB").

The Company's activities are divided into three distinct business segments:

- *Oilfield Services*, which represents the manufacture and sale of hydrocarbon products;
- *Energy Marketing*, which represents the purchasing, gathering and marketing of petroleum for resale to refiners and other customers; and
- *Transportation Services*, which represents the operations of Millard.

Our customers include large multi-national and independent oil and gas producers, as well as smaller independent producers and major land based drilling contractors with operations in the WCSB. The primary factor influencing demand for our products and services is the level of drilling and workover activity in the WCSB, which in turn, depends on our current and anticipated future oil and gas prices and the levels of cash flows allocated by the industry to drilling and workover activities. As a result, demand for our products and services is cyclical and substantially depends on oilfield activity levels in the WCSB and is highly sensitive to current and expected oil and natural gas prices. Drilling and well service rig counts and rigs utilized by depth are leading indicators of anticipated demand for the Company's products and services. The Company's drilling and fracturing fluids provide cost effective solutions for deep well drilling and workover activities that are at well depths greater than 1,850 metres.

## Seasonality of Operations

Weather conditions can affect the sale of the Company's products and services. The ability to move heavy equipment in the Canadian oil and natural gas fields is dependent on weather conditions. As a result, spring months in Western Canada and the duration of this "spring break-up" has a direct impact on the Company's activity levels. In addition, exploration and production in many of the northern regions of the WCSB are accessible only in winter months when the ground is frozen hard enough to support the weight of heavy equipment. The timing of freeze-up and spring break-up affects the ability to move equipment in and out of these areas. As a result, late March through May is traditionally the Company's slowest period.

## Divestiture

During 2007, the Company sold its 25% interest in the Egyptian Canadian Company for Chemicals Industries - F.Z. ("ECC"), for total proceeds of \$750,000 U.S. (\$826,000 Cdn.), less transaction fees of \$2,278 U.S., to a privately held Egyptian company based in Cairo, Egypt. During 2007, the Company recorded a \$58,000 (December 31, 2006 - \$230,000) write down in respect of the carrying value of its Egyptian investment. The sale completed the disposition of the Company's investment in ECC.

## Results of Operations – Three and Six Months Ended June 30, 2008

### Overview

Oilfield activity levels in the WCSB and overall industry conditions continued to provide a challenging business climate for the oil and gas service sector during the second quarter and first half of 2008. The number of wells drilled in the second quarter of 2008 declined by 3% to 3,148 from 3,232 in the same period last year and declined by 17% to 8,134 for the six months ended June 30, 2008 versus 9,822 in the same period last year. Drilling rig utilization rates averaged 19% in the second quarter of 2008, modestly ahead of the 17% average rig utilization rate during the same period last year, but declined for the comparative six months to 38% in 2008 versus 39% in 2007. Utilization rates in the second quarter of 2008 were also negatively impacted by wet weather or "spring break-up" conditions that reached well into May which delayed the usual seasonal start of oilfield activity until the latter portion of June.

While we experienced improved sales activities during the second quarter of 2008 when compared to the same period last year, overall margins achieved by the Oilfield Services segment declined on a comparative quarter basis as a result of the continued rise in crude oil prices which increased our feedstock costs. The foregoing combined with the effects of a very competitive pricing environment limited our ability to reflect underlying product values in our prices despite the rise in crude oil. In addition, the Company has continued to experience issues with the new heating units which have affected the operating capacity of the Sundre plant since early in the first quarter of 2008. As a result, the Company is re-installing its original salt-bath heaters in order to return the plant to an operational state while addressing the issues with the new heaters.

### Revenues

*Consolidated Revenues.* Consolidated revenues for the three months ended June 30, 2008 increased by \$13,922,000, or 186%, to \$21,390,000 from \$7,468,000 for the same period last year, and increased by \$19,793,000, or 56%, to \$55,137,000 for the six months ended June 30, 2008 versus \$35,344,000 for the first half of 2007. Revenues by business segment were as follows:

- *Oilfield Services.* Segment revenues for the three months ended June 30, 2008 increased by 177% to \$10,478,000 from \$3,787,000 for the same period last year and increased by 29% to \$29,508,000 for the six months ended June 30, 2008 versus \$22,938,000 for the first half in 2007. The increase in revenues, in the second quarter of 2008 when compared to the same period last year, was attributable to stronger demand from the segment's existing customer base and the establishment of several new customer relationships for the Company's fracturing and drilling fluids and solvent products. As a result, the Oilfield Services segment experienced a significant increase in the volume of products sold during the second quarter of 2008 when compared to the same period last year, which also contributed to the

improvement in the total volume of products sold in the first half of 2008 when compared to the same period last year.

- *Energy Marketing.* Segment revenues increased by \$7,400,000, or 458%, to \$9,014,000 in the second quarter of 2008 from \$1,614,000 in the same quarter last year and increased by \$12,700,000, or by 165%, to \$20,404,000 for the first half of 2008 versus \$7,704,000 for the same period last year. The volume of by-products available to the energy marketing segment is a function of the volume of feedstock put into production during a period. As the volume of feedstock put into production during the second quarter and first six months of 2008 significantly exceeded the comparative periods in 2007, the volume of by-products available for sale increased. In addition, the increase in energy marketing revenues for the comparative periods of 2008 and 2007 reflects the increase in the underlying value of crude oil.
- *Transportation Services.* Segment revenues decreased by \$168,000, or 8%, to \$1,899,000 in the second quarter of 2008, excluding inter-segment revenues of \$1,448,000, from \$2,067,000 in the same period last year, excluding inter-segment revenues of \$614,000, as a result of the shift in utilization of the segment's fluid hauling fleet. During the second quarter of 2008 versus the same quarter of 2007, more of the segment's fluid hauling fleet was directed to providing services to the Company's Oilfield Services segment as a result of the increase in its manufacturing and sales activities. For the six months ended June 30, 2008, Transportation Services revenues increased by 11% to \$5,226,000, excluding inter-segment revenues of \$3,595,000, when compared to revenues of \$4,702,000, excluding inter-segment revenues of \$2,218,000, for the same period last year. The increase in revenues, excluding inter-segment revenues, for the comparative first six months of 2008 and 2007 resulted from new business arrangements secured by this segment.

## Operating Expenses

Operating expenses represent the Company's product and service costs associated with the manufacture and sale of its hydrocarbon products and its transportation services. In addition, operating expenses include all costs directly related to the support and maintenance of the Company's fractionation plants and other operating equipment.

### Operating Expenses as a Percentage of Consolidated Revenue (1)

For the three months ended June 30	2008	2007	Change
	%	%	%
Oilfield Services	46	45	1
Energy Marketing	37	20	17
Transportation Services	11	27	(16)
<b>Total</b>	<b>94</b>	<b>92</b>	<b>2</b>

For the six months ended June 30	2008	2007	Change
	%	%	%
Oilfield Services	50	53	(3)
Energy Marketing	34	18	16
Transportation Services	11	15	(4)
<b>Total</b>	<b>95</b>	<b>86</b>	<b>9</b>

(1) Operating expenses as a percentage of consolidated revenues for the three and six months ended June 30, 2008 and 2007 are after the elimination of significant inter-segment transactions.

The overall increase in operating expenses as a percentage of revenues largely reflects the effects of the period-over-period increase in feedstock costs precipitated by the dramatic rise in crude oil prices over the respective comparative periods. By way of example, the average posted price of light sweet crude oil in the second quarter of 2008 was \$795 per cubic metre compared to \$453 per cubic metre in the same period last year, representing a quarter-over-quarter increase of 76%. Similarly, for the first half of 2008 the average posted price of light sweet crude was \$705 per cubic metre versus \$439 per cubic metre for the same period last year, representing a year-over-year increase of 61%. The increase in operating expenses associated with the Energy Marketing segment for the comparative quarters and first six months of 2008 and 2007 was primarily due to the increase in by-product volumes resulting from the increase in manufacturing activities and the effects of the sharp rise in crude oil prices.

## General and Administrative

General and administrative (“G&A”) expenses include salaries and other related expenses for the Company’s administrative, finance, information technology and human resource functions. G&A expenditures for the three months ended June 30, 2008 increased by \$75,000, or 7%, to \$1,125,000 from \$1,050,000 for the same period last year, and increased by \$19,000, or 1%, to \$2,215,000 in the first six months of 2008 from \$2,196,000 for the same period last year. The increase in G&A expenditures was largely due to the increase operational consulting services utilized by the Company during the current period offset by the decrease in stock based compensation costs and the capitalization of labour costs directly identifiable with several of the Company’s construction projects.

## Depreciation

Depreciation expense increased by \$65,000, or 12%, to \$625,000 in the second quarter of 2008 compared to \$561,000 for the same quarter last year and for the first six months ended June 30, 2008 increased by \$134,000, or 12%, to 1,262,000 from \$1,128,000 for the same period in 2007. The increase in depreciation expense is largely attributable to commencing with the depreciation of: the flowback facility in the latter half of 2007; the desalter and blend facility at the Slave Lake plant; and other equipment purchases completed in 2008.

At June 30, 2008, \$2,089,000 of costs largely associated with the construction of the Company’s direct fired heaters at the Sundre fractionation plant and the land activated custody transfer connection for the bi-directional pipeline at the Slave Lake fractionation plant have not been depreciated as the projects were not completed and put into use as at June 30, 2008. Enerchem has continued to experience issues with the new direct-fired heaters installed at its Sundre fractionation plant. These issues have affected the operating capacity of the plant since early in the first quarter of 2008. As a result, the Company has decided to re-install its original salt-bath heaters in order to return the plant to an operational state while it works to address the issues with the new heaters. The re-installation of the salt bath heaters should be completed during the third quarter of 2008, bringing the plant back on line prior to commencement of the anticipated strong level of drilling activity normally experienced in the fourth and first quarters of each year.

## Restructuring Costs

During the second quarter of 2008, the Company recorded a provision for restructuring costs of \$850,000 relating to the consolidation of its accounting and administrative offices from Leduc to Calgary, Alberta. Restructuring costs include severance provisions of \$555,000 and \$295,000 in other transitioning costs. The consolidation is expected to be completed by October 31, 2008.

## Income Tax Expense (Recovery)

The provision for current income taxes in second quarter of 2008 includes a recovery of \$364,000 compared to a recovery of \$450,000 in the same period last year. For the first six months ended June 30, 2008, the provision for income taxes includes a recovery of \$375,000 versus income tax expense of \$562,000 for the same period in 2007.

The effective rate for the six months ended June 30, 2008 was 21% compared to 25% for the same period in the prior year. The reduction in the effective rate for the period ended June 30, 2008 was largely due to the effects of non-deductible permanent differences combined with the effects of a \$46,000 increase in tax expense resulting from a recent tax review affecting the Company’s 2004 and 2005 taxation years.

## Net (Loss) Earnings

For the three months ended June 30, 2008, the Company reported a net loss of \$(1,067,000), or \$(0.07) per common share diluted, compared to a net loss of \$(648,000), or \$(0.04) per common share diluted, for the three months ended June 30, 2007. For the six months ended June 30, 2008, the Company reported a net loss of \$(1,137,000) or \$(0.07) per common share diluted, compared to net earnings of \$1,195,000, or \$0.08 per common share diluted, for the same period last year. The significant decline in the Company’s financial performance for the three and six months ended June 30, 2008 resulted from: the effects of the oil and gas producers’ overall focus on reducing service costs which combined with the increase in feedstock costs has squeezed margins on products offered by the Oilfield Services business segment; restructuring costs of \$850,000 relating to the consolidation of the Company’s accounting and administrative offices from Leduc to Calgary, Alberta; and operational issues with the new heaters at the Sundre fractionation plant which affected the availability of the plant in processing clean flowback in the manufacture of its fracturing fluids.

EBITDA (refer to “Use of Non-GAAP Measures”) for the three months ended June 30, 2008 improved by \$594,000 to \$153,000 from \$(441,000) for the same quarter last year, and for the six months ended June 30, 2008, EBITDA decreased by \$2,121,000, or 75%, to \$706,000 from \$2,827,000 for the same period last year. EBITDA for the three and six months ended June 30, 2008 reflect the reduction in the Company’s earnings for the periods as explained in this MD&A.

## Liquidity and Capital Resources

Cash used in operations before changes in non-cash components of working capital (refer to "Use of Non-GAAP Measures") for the three months ended June 30, 2008 totaled \$208,000 compared to cash provided by operations of \$232,000 for the same quarter last year. For the six months ended June 30, 2008, cash provided by operations before changes in non-cash components of working capital totaled \$590,000 compared to \$2,839,000 for the same period last year. The decrease in cash provided by operations for the three and six months ended June 30, 2008 was largely the result of the decline in operating earnings. The Company's working capital was \$13,145,000 at June 30, 2008 compared to \$15,991,000 at December 31, 2007. The Company's current ratio (defined as current assets divided by current liabilities) was 2.1 to 1 at June 30, 2008 compared to 2.8 to 1 at December 31, 2007. The decline in the Company's current ratio was largely influenced by the increase in accounts payable and accrued liabilities in respect of feedstock purchased in June 2008.

Net cash used by the Company for investing activities totaled \$1,228,000 for the three months ended June 30, 2008 compared to \$1,200,000 for the same period last year, and totaled \$3,360,000 for the six months ended June 30, 2008 compared to \$3,188,000 for the same period last year. Cash used for investing activities were primarily directed to the completion of the blend facility and desalter project at the Slave Lake fractionation plant, plant turnaround programs and work on the direct fired heater project at the Sundre fractionation plant.

Net cash used in financing activities in the second quarter of 2008 totaled \$4,717,000 and largely represented the Company's repayment of advances drawn from its available revolving operating line of credit. During the second quarter of 2008, the Company purchased 29,100 of its common shares at an average price of \$2.10 per common share, including transaction fees, totaling \$61,239. For the six months ended June 30, 2008, the Company purchased 37,000 of its common shares at an average price of \$2.07 per common share, including transaction fees, totaling \$76,751. All of the common shares purchased in the first six months of 2008 have been cancelled and returned to treasury.

Subsequent to June 30, 2008, as part of its annual review, the Company entered into a new credit facility with a Canadian chartered bank consisting of: a \$10,500,000 revolving operating line of credit that bears interest at the bank's prime rate plus 0.40%; Bankers' Acceptances facility of \$10,000,000 which bears interest at Bankers' Acceptance rates plus a margin; an \$8,000,000 demand revolving loan facility at the bank's prime rate plus 0.90%; and a bank guarantee facility of \$17,000,000 that bears a fee of 1.35% per annum at the time of issuance of the bank guarantee.

## Summary of Contractual Obligations and Off-Balance Sheet Arrangements

The following table summarizes the Company's contractual obligations including payments due for each of the next five years and thereafter.

Contractual obligations	Payments due by period				
	Total	Less than 1 year	1 - 3 years	4 - 5 years	After 5 years
	\$	\$	\$	\$	\$
Operating leases (1)	886,040	438,452	447,588	-	-
Commitments and capital expenditures (2)	162,980	162,980	-	-	-
<b>Total contractual obligations</b>	<b>1,049,020</b>	<b>601,432</b>	<b>447,588</b>	<b>-</b>	<b>-</b>

(1) Represents normal operating leases comprised of vehicles, trailers and office space.

(2) Represents an agreement with a third party for the construction of new heaters to be installed at the Sundre plant in the amount of \$745,900 of which \$162,980 remains outstanding at June 30, 2008.

In the normal course of business, the Company may become contingently liable for performance under letters of guarantee and credit with certain of its vendors. In this regard, the Company has arranged an \$11,000,000 bank guarantee facility available as security for its feedstock arrangements and purchase commitments. At June 30, 2008, the Company had provided letters of guarantee totaling \$7,062,640, which terminated in July, 2008, in favour of two suppliers for the purchase of petroleum feedstock from those suppliers.

For 2008 the Company expects cash flow from operations and from its available credit facilities to be sufficient to meet its contractual obligations and off-balance sheet arrangements.

## Share Capital

At June 30, 2008 the Company had 15,216,107 common shares outstanding. In addition, as at June 30, 2008, the Company has reserved 520,000 common shares for issuance under outstanding stock options.

On June 27, 2007, the Company announced a normal course issuer bid to purchase up to 766,465 of its issued and outstanding common shares at the market price at the time of acquisition beginning on July 3, 2007 and ending on July 2, 2008, or such earlier time as the bid is completed or terminated by the Company. During the first half of 2008, 37,000 common shares were purchased at an average price of \$2.07 per common share, including transaction fees. The cost of common shares purchased totaled \$76,751 of which \$71,877 was recorded as a charge against share capital at the average carrying value of the Company's common shares issued and outstanding, with the balance of \$4,874 charged against retained earnings.

Subsequent to June 30, 2008, the Company announced that it will commence a new normal course issuer bid to purchase up to 760,805 of its issued and outstanding common shares. Purchases under the normal course issuer bid will commence on July 15, 2008 and will terminate on July 14, 2009, or such earlier time as the bid is completed or terminated by the Company. All shares purchased under the issuer bid will be cancelled.

## Summary of Quarterly Results

The following tables provide selected unaudited financial information relating to the Company's quarterly activities in 2008, 2007 and 2006 and are prepared in accordance with Canadian generally accepted accounting principles with respect to the preparation of interim financial statements.

Three month period ended (unaudited)	June 30, 2008	March 31, 2008	December 31, 2007	September 30, 2007
	\$	\$	\$	\$
Revenues	21,390,234	33,746,921	25,133,073	19,822,532
Net (loss) earnings for the period	(1,067,125)	(70,359)	642,814	(6,318,781)
Net (loss) earnings per share for the period				
Basic	(0.07)	0.00	0.04	(0.41)
Diluted	(0.07)	0.00	0.04	(0.41)

Three month period ended (unaudited)	June 30, 2007	March 31, 2007	December 31, 2006	September 30, 2006
	\$	\$	\$	\$
Revenues	7,467,779	27,876,401	24,199,343	29,138,305
Net (loss) earnings for the period	(648,176)	1,842,751	373,246	2,036,051
Net (loss) earnings per share for the period				
Basic	(0.04)	0.12	0.02	0.13
Diluted	(0.04)	0.12	0.02	0.13

## Trends and Outlook

Given the strong outlook provided by the continued strength in commodity prices and record cash flows being generated by producers, there is growing industry consensus that these underlying fundamentals may provide for stronger than expected levels of oilfield activity during the second half of 2008 and into 2009

In this regard, over the past months, we have directed significant resources to make the necessary infrastructure and plant optimization improvements focused on aligning our operations to the achievement of our strategic goals which we anticipate will contribute to improve our overall financial performance and competitive capabilities. We continue to maintain a strong balance sheet with a focused management team and are well positioned to take advantage of opportunities that may develop.

## Changes in Accounting Policies

### a) Capital Disclosures

Effective January 1, 2008, the Company adopted CICA Section 1535, "Capital Disclosures" which requires that an entity disclose information that enables users of its financial statements to evaluate an entity's objectives, policies and processes for managing capital including disclosures of any externally imposed capital requirements and the consequences of non-compliance. The adoption of this standard does not impact the Company's financial statements as it only addresses disclosure requirements. Information regarding the Company's capital disclosures is further described in note 5, "Capital Disclosures", of the Notes to the Interim Consolidated Financial Statements for the period ended June 30, 2008.

### b) Financial Instruments – Presentation and Disclosure

Effective January 1, 2008, the Company adopted CICA Sections 3862 and 3863 which replaced CICA Section 3861, "Financial Instruments – Disclosure and Presentation." This new standard requires an increased emphasis on disclosures about the nature and extent of risk arising from financial instruments and how an entity manages those risks. The adoption of this standard does not impact the Company's financial statements as it only addresses disclosure requirements. Information regarding the nature and extent of risk arising from the Company's financial instruments and how it manages those risks is further described in note 6, "Financial Instruments", of the Notes to the Interim Consolidated Financial Statements for the period ended June 30, 2008.

### c) Inventories

Effective January 1, 2008, the Company adopted CICA Section 3031, "Inventories" which harmonizes accounting for inventories under Canadian GAAP with International Financial Reporting Standards. This standard requires the measurement of inventories at the lower of cost and net realizable value and includes guidance on the determination of cost, including allocation of overheads and other costs to inventory. The standard also requires the consistent use of either first-in, first-out (FIFO) or weighted average cost formula to measure the cost of other inventories and requires the reversal of previous write-downs to net realizable value when there is a subsequent increase in the value of inventories. Information regarding the Company's inventory disclosures is further described in note 7, "Inventories", of the Notes to the Interim Consolidated Financial Statements for the period ended June 30, 2008.

## Recent Canadian Accounting Pronouncements

### a) International Financial Reporting Standards ("IFRS")

The Canadian Accounting Standards Board has confirmed that the use of IFRS will be required for publicly accountable profit-oriented enterprises. IFRS will replace Canada's current generally accepted accounting principles for those enterprises. These new standards are applicable to fiscal years beginning on or after January 1, 2011. Companies will be required to provide comparative IFRS information for the previous fiscal year. The Company will implement this standard in its first quarter of the year ending December 31, 2011 and is currently evaluating the impact of these standards on its consolidated financial statements.

### b) Goodwill and Intangible Assets

In February 2008, the CICA issued Section 3064, "Goodwill and Intangible Assets", replacing Section 3062, "Goodwill and Other Intangible Assets" and Section 3450, "Research and Development Costs". The new pronouncement establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. Standards concerning goodwill are unchanged from the previous standards included in the previous Section 3062. The new standard applies to interim and annual financial statements relating to fiscal years beginning on or after October 1, 2008. The Company is currently evaluating the impact of adopting this standard.

## Critical Accounting Estimates

The preparation of the financial statements, in conformity with GAAP, requires management of the Company to make estimates and assumptions that affect the reported amounts of assets and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Management regularly evaluates these estimates and assumptions which are based on past experience and other factors that are deemed reasonable under the circumstances. This involves varying degrees of judgment and uncertainty and, therefore, amounts currently reported in the financial statements could differ in the future. There have been no changes in these accounting estimates from those reported in the Company's Annual Report at December 31, 2007.

## **Risk and Uncertainties**

The MD&A of the Annual Report for the year ended December 31, 2007 includes an overview of the risks and uncertainties affecting the Company on pages 17 and 18. These risks and uncertainties are unchanged as at June 30, 2008.

## **Disclosure Controls and Internal Controls over Financial Reporting**

The Company's Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") are responsible for establishing and maintaining disclosure controls and procedures ("Procedures") which provide reasonable assurance that information required to be disclosed by the Company under various securities legislation ("Required Filings") is reported within the time periods specified. The Procedures are designed to ensure that material information relating to the Company is accumulated and communicated to management, the CEO and CFO and to allow for timely decisions regarding the Required Filings.

Enerchem's CEO and CFO evaluate the effectiveness of the Company's Procedures on a regular basis throughout the year and have concluded that the Procedures in place as of the end of the period covered by the Required Filings are effective.

In addition, management is responsible for establishing and maintaining adequate internal control over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. The CEO and CFO have evaluated whether there were any changes to internal control over financial reporting during the quarter ended June 30, 2008 that have materially affected, or are reasonably likely to materially affect, its internal control over financial reporting. No such changes were identified through their evaluation.

# Consolidated Balance Sheets

As at	June 30, 2008 (unaudited)	December 31, 2007 (audited)
	\$	\$
<b>Assets</b>		
<b>Current assets</b>		
Cash and cash equivalents	194,266	2,711,136
Accounts receivable	13,586,881	16,074,755
Income taxes receivable	516,695	305,609
Inventories (note 7)	10,607,210	5,839,545
Prepaid expenses	218,573	117,184
Current portion of future tax asset	73,200	73,200
	<u>25,196,825</u>	<u>25,121,429</u>
<b>Other assets</b>	400,144	315,582
<b>Property, plant and equipment</b>	<u>41,089,486</u>	<u>39,488,530</u>
	<u>66,686,455</u>	<u>64,925,541</u>
<b>Liabilities</b>		
<b>Current liabilities</b>		
Bank indebtedness	60,883	-
Accounts payable and accrued liabilities	11,991,186	9,130,388
	<u>12,052,069</u>	<u>9,130,388</u>
<b>Asset retirement obligations</b>	211,672	204,937
<b>Future income taxes</b>	<u>3,775,241</u>	<u>3,746,478</u>
	<u>16,038,982</u>	<u>13,081,803</u>
<b>Contingent liabilities and commitments</b> (note 9)		
<b>Shareholders' equity</b>		
Share capital (note 8 (b))	29,559,491	29,631,368
Contributed surplus (note 8 (c))	1,518,539	1,500,569
Retained earnings	19,569,443	20,711,801
	<u>50,647,473</u>	<u>51,843,738</u>
	<u>66,686,455</u>	<u>64,925,541</u>

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

# Consolidated Statement of Operations, Comprehensive Loss and Retained Earnings

(unaudited)

	Three months ended June 30		Six months ended June 30	
	2008	2007	2008	2007
	\$	\$	\$	\$
<b>Revenues</b>	21,390,234	7,467,779	55,137,155	35,344,180
<b>Expenses</b>				
Operating	20,124,497	6,862,339	52,247,001	30,376,057
General and administrative	1,124,894	1,049,546	2,215,335	2,196,112
Restructuring costs (note 10)	850,000	-	850,000	-
Depreciation and amortization	625,437	560,539	1,262,127	1,128,286
Accretion expense	3,367	3,160	6,734	6,320
Amortization of pre-operating costs	-	21,718	-	43,436
Interest expense	18,524	-	24,782	8,116
	22,746,719	8,497,302	56,605,979	33,758,327
<b>(Loss) earnings from operations before other income (expense)</b>	(1,356,485)	(1,029,523)	(1,468,824)	1,585,853
<b>Other income (expense)</b>				
Interest income and other	10,809	(2,235)	25,800	58,890
Loss on write-down of investment in foreign operations	-	(13,916)	-	(58,358)
Gain (loss) on disposal of property, plant and equipment	1,335	5,280	5,324	(3,654)
	12,144	(10,871)	31,124	(3,122)
<b>(Loss) earnings from operations before income taxes</b>	(1,344,341)	(1,040,394)	(1,437,700)	1,582,731
<b>Income tax expense (recovery)</b>				
Current	(318,479)	(449,978)	(328,979)	561,745
Future	41,263	57,760	28,763	(173,589)
	(277,216)	(392,218)	(300,216)	388,156
<b>Net (loss) earnings and comprehensive (loss) income for the period</b>	(1,067,125)	(648,176)	(1,137,484)	1,194,575
<b>Retained earnings, beginning of period</b>	20,641,276	27,096,977	20,711,801	25,254,226
<b>Common shares repurchased and cancelled</b>	(4,708)	-	(4,874)	-
<b>Retained earnings, end of period</b>	19,569,443	26,448,801	19,569,443	26,448,801
<b>(Loss) earnings per share</b>				
Basic	(0.07)	(0.04)	(0.07)	0.08
Diluted	(0.07)	(0.04)	(0.07)	0.08
<b>Weighted average shares outstanding (note 8 (e))</b>				
Basic	15,237,340	15,301,285	15,243,467	15,298,313
Diluted	15,237,340	15,348,658	15,243,467	15,375,014

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

# Consolidated Statement of Cash Flows

(unaudited)

	Three months ended June 30		Six months ended June 30	
	2008	2007	2008	2007
	\$	\$	\$	\$
<b>Operating activities</b>				
Net (loss) earnings from operations	(1,067,125)	(648,176)	(1,137,484)	1,194,575
Items not affecting cash -				
Depreciation, amortization and accretion expense	628,804	585,417	1,268,861	1,178,042
Stock based compensation	11,704	94,342	17,970	188,344
Amortization of plant turnaround costs	178,489	134,402	417,534	389,863
(Gain) loss on disposal of property, plant and equipment	(1,335)	(5,280)	(5,324)	3,654
Write-down of investment in foreign operations	-	13,916	-	58,358
Future income tax expense (recovery)	41,263	57,760	28,763	(173,589)
	(208,200)	232,381	590,320	2,839,247
Changes in non-cash components of working capital				
Net change in accounts receivable	9,757,022	10,569,839	2,487,874	10,921,062
Net change in inventories and prepaid expenses	(1,938,346)	1,413,395	(4,869,054)	(570,132)
Net change in accounts payable and accrued liabilities	(1,727,550)	(4,378,487)	2,860,798	(3,673,884)
Net change in income taxes receivable	(103,345)	(1,778,967)	(211,086)	(767,244)
	5,987,781	5,825,780	268,532	5,909,802
Net cash provided by operating activities	5,779,581	6,058,161	858,852	8,749,049
<b>Investing activities</b>				
Purchase of property, plant and equipment	(771,882)	(1,526,443)	(2,891,939)	(3,625,530)
Decrease in promissory note	-	30,251	-	61,127
Proceeds on disposal of property, plant and equipment	10,280	25,000	34,180	87,600
Increase in other assets	(466,284)	(555,026)	(502,095)	(537,120)
Proceeds received on sale of foreign investment	-	826,083	-	826,083
Net cash used in investing activities	(1,227,886)	(1,200,135)	(3,359,854)	(3,187,840)
<b>Financing activities</b>				
Issue of common shares	-	103,700	-	103,700
Net change in bank indebtedness	(4,656,252)	-	60,883	-
Repurchase of common shares under normal course issuer bid	(61,239)	-	(76,751)	-
Repayment of long-term debt	-	-	-	(287,062)
Net cash (used in) provided by financing activities	(4,717,491)	103,700	(15,868)	(183,362)
<b>(Decrease) increase in cash and cash equivalents</b>	<b>(165,796)</b>	<b>4,961,726</b>	<b>(2,516,870)</b>	<b>5,377,847</b>
<b>Cash and cash equivalents - beginning of period</b>	<b>360,062</b>	<b>2,829,643</b>	<b>2,711,136</b>	<b>2,413,522</b>
<b>Cash and cash equivalents - end of period</b>	<b>194,266</b>	<b>7,791,369</b>	<b>194,266</b>	<b>7,791,369</b>

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

# Notes to the Interim Consolidated Financial Statements

## For the Period Ended June 30, 2008 (unaudited)

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### 1. Basis of Presentation and Accounting Policies

The accompanying unaudited interim consolidated financial statements of Enerchem International Inc. (“Enerchem” or the “Company”) are prepared in accordance with generally accepted accounting principles (“GAAP”) in Canada with respect to the preparation of interim financial statements. Accordingly, they do not include all of the information and disclosures required by Canadian GAAP in the preparation of annual statements.

These unaudited interim consolidated financial statements include the accounts of the parent company and its wholly owned subsidiary Millard Trucking Ltd. (“Millard”). All significant inter-company balances and transactions have been eliminated. With the exception of items (a), (b) and (c) as described below, these unaudited interim consolidated financial statements follow the same accounting policies and methods of computation as, and should be read in conjunction with, the most recent audited annual financial statements for the year ended December 31, 2007.

#### a) Capital Disclosures

Effective January 1, 2008, the Company adopted CICA Section 1535, “Capital Disclosures” which requires that an entity disclose information that enables users of its financial statements to evaluate an entity’s objectives, policies and processes for managing capital, including disclosures of any externally imposed capital requirements and the consequences of non-compliance. The adoption of this standard does not impact the Company’s financial statements as it only addresses disclosure requirements. Information regarding the Company’s capital disclosures is further described in note 5.

#### b) Financial Instruments – Presentation and Disclosure

Effective January 1, 2008, the Company adopted CICA Sections 3862 and 3863 which replaced CICA Section 3861, “Financial Instruments – Disclosure and Presentation”. This new standard requires an increased emphasis on disclosures about the nature and extent of risk arising from financial instruments and how an entity manages those risks. The adoption of this standard does not impact the Company’s financial statements as it only addresses disclosure requirements. Information regarding the nature and extent of risk arising from the Company’s financial instruments and how it manages those risks is further described in note 6.

#### c) Inventories

Effective January 1, 2008, the Company adopted CICA Section 3031, “Inventories” which harmonizes accounting for inventories under Canadian GAAP with International Financial Reporting Standards. This standard requires the measurement of inventories at the lower of cost and net realizable value and includes guidance on the determination of cost, including allocation of overheads and other costs to inventory. The standard also requires the consistent use of either first-in, first-out (FIFO) or weighted average cost formula to measure the cost of other inventories and requires the reversal of previous write downs to net realizable value when there is a subsequent increase in the value of inventories. Information regarding the Company’s inventory disclosures is further described in note 7.

### 2. Recent Canadian Accounting Pronouncements

#### a) International Financial Reporting Standards (“IFRS”)

The Canadian Accounting Standards Board has confirmed that the use of IFRS will be required for publicly accountable profit-oriented enterprises. IFRS will replace Canada’s current generally accepted accounting principles for those enterprises. These new standards are applicable to fiscal years beginning on or after January 1, 2011. Companies will be required to provide comparative IFRS information for the previous fiscal year. The Company will implement this standard in its first quarter of the year ending December 31, 2011 and is currently evaluating the impact of these standards on its consolidated financial statements.

## 2. Recent Canadian Accounting Pronouncements (continued)

### b) Goodwill and Intangible Assets

In February 2008, the CICA issued Section 3064, "Goodwill and Intangible Assets", replacing Section 3062, "Goodwill and Other Intangible Assets" and Section 3450, "Research and Development Costs". The new pronouncement establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. Standards concerning goodwill are unchanged from the previous standards included in the previous Section 3062. The new standard applies to interim and annual financial statements relating to fiscal years beginning on or after October 1, 2008. The Company is currently evaluating the impact of adopting this standard.

## 3. Nature of Operations

Enerchem is a manufacturer and distributor of hydrocarbon drilling and fracturing fluids designed to provide cost effective solutions to the upstream oil and gas industry and specialty solvents to help resolve production and processing problems to the downstream producers. The Company also provides energy marketing services and, through its wholly-owned subsidiary company, Millard, provides fluid transportation and other related oilfield services.

The Company's activities are divided into three distinct business segments: Oilfield Services, which represents the manufacture and sale of hydrocarbon products; Energy Marketing, which represents the purchasing, gathering and marketing of crude oil for resale to refiners and other customers; and Transportation Services, which represents the operations of Millard.

## 4. Seasonality of Operations

Weather conditions can affect the sale of the Company's products and services. Spring months in Western Canada tend to effect operations negatively as road bans and wet weather conditions ("spring break-up") make it difficult to drill for oil and gas and to access service sites. The Company traditionally experiences increased activity levels during the fall and winter seasons and decreased activity during spring break-up.

## 5. Capital Disclosures

The Company's objectives in managing capital are:

- 1) to ensure sufficient liquidity to enable the internal financing of capital projects thereby facilitating its expansion,
- 2) to maintain a strong capital base so as to maintain investor, creditor and market confidence, and
- 3) to provide an adequate return to shareholders.

The Company's capital is composed of long-term debt, including the current portion, and shareholders' equity. The Company's primary uses of capital in the past have been to finance its plant and equipment expenditures. The Company currently funds these requirements out of its internally-generated cash flows. The Company maintains a secured operating line of credit with a Chartered bank that it uses from time to time for its business activities. The Company has not drawn on its available long-term credit facility therefore net earnings generated from operations are available for reinvestment in the Company. The Board of Directors does not establish quantitative return on capital criteria for management; but rather promotes year over year sustainable profitable growth. The Board of Directors also monitors the share repurchase program activities. The Company does not have a defined share repurchase plan and buy and sell decisions are made on a specific transaction basis and depend on market prices and regulatory restrictions. The Company is not subject to any externally imposed capital requirements.

## 6. Financial Instruments

The Company's financial instruments consist of cash and cash equivalents, accounts receivable, bank indebtedness and accounts payable and accrued liabilities.

### a) Fair Value Disclosure

The fair values of cash and cash equivalents, accounts receivable, bank indebtedness and accounts payable and accrued liabilities approximate their carrying values due to the relatively short periods to maturity of these instruments.

## 6. Financial Instruments (continued)

### b) Financial Risk Management

The Company's activities are exposed to a variety of financial risks: credit risk, liquidity risk and market risk. The Company's overall risk management program focuses on the unpredictability of financial and economic markets and seeks to minimize potential adverse effects on the Company's financial performance. Risk management is carried out by financial management in conjunction with overall Company governance.

#### i) Credit Risk

The Company is exposed to credit risk through its cash and cash equivalents and accounts receivable. The Company has deposited the cash and cash equivalents with reputable financial institutions, from which management believes the risk of loss to be remote. The Company has accounts receivable from customers in the oil and gas industry and risk is mitigated due to: the Company's diverse customer base; conducting a majority of its business with large companies in the industry; following a program of credit evaluation; and limiting the amount of customer credit where deemed necessary.

As at June 30, 2008 the Company's exposure to credit risk for these financial instruments was as follows:

Aging of financial assets:	Total	Current Amount	Not more than three months past due	More than three months but less than six months past due
	\$	\$	\$	\$
Accounts Receivable	13,586,881	11,094,915	1,925,303	566,663

#### ii) Liquidity Risk

Prudent liquidity risk management implies maintaining sufficient cash and cash equivalents and the availability of funding through an adequate amount of committed credit lines and bank guarantee facility. Due to the dynamic nature of the business, the Company aims to maintain flexibility in funding by keeping committed credit lines available. The contractual maturity of accounts payable and accrued liabilities as at June 30, 2008 totaled \$11,991,186 of which \$11,141,186 requires payment within thirty days and \$850,000, representing restructuring costs, upon completion of the required services. As at June 30, 2008, the Company has a \$5,500,000 revolving operating line of credit with a Canadian chartered bank (June 30, 2007 - \$5,500,000). During the first quarter of 2008, the Company increased its bank guarantee facility to \$11,000,000 from \$10,000,000 to accommodate its feedstock purchase commitments with two suppliers. Advances under the operating line are available at either the bank's prime rate plus 0.40%, Bankers' Acceptance rates plus 1.65%, or a combination thereof, and are repayable on demand. The guarantee facility bears a fee of 1.35% per annum at the time of issuance of the bank guarantee.

Subsequent to June 30, 2008, as part of its annual review, the Company entered into a new credit facility with a Canadian chartered bank consisting of: a \$10,500,000 revolving operating line of credit that bears interest at the bank's prime rate plus 0.40%; Bankers' Acceptances facility of \$10,000,000 which bears interest at Bankers' Acceptance rates plus a margin; an \$8,000,000 demand revolving loan facility at the bank's prime rate plus 0.90%; and a bank guarantee facility of \$17,000,000 that bears a fee of 1.35% per annum at the time of issuance of the bank guarantee.

#### iii) Market Risk

Market risk comprises three types of risk: currency risk, interest rate risk and other price risk.

- *Currency Risk*: Foreign currency risk arises from fluctuations in foreign exchange rates and the degree of volatility of these rates relative to the Canadian dollar. The Company is not significantly exposed to foreign currency risk.

## 6. Financial Instruments (continued)

### b) Financial Risk Management (continued)

#### iii) Market Risk (continued)

- *Interest Rate Risk:* The Company has a credit facility with a Canadian chartered bank which when utilized by the Company provides loans that are subject to interest rate fluctuation. The Company manages its interest risk on borrowings by utilizing a combination of short term fixed rates through the use of 30 to 90 day Bankers' Acceptance instruments and floating rates on debt. Management's assessment is that a 25 basis point decrease or increase is the most reasonable possible change in market interest rates. The effect of this possible change in market interest rates on the Company's pre-tax earnings for the six months ended June 30, 2008 affecting the Company's floating rate debt outstanding of \$60,883 at the balance sheet date is not material.

- *Other Price Risk:* The Company's exposure to other price risk arises from changes in petroleum and natural gas prices as a result of its use of petroleum feedstock and natural gas for processing at its Sundre and Slave Lake fractionation plants. The potential fluctuations in petroleum and natural gas prices, without a corresponding increase in the underlying value of the Company's products to the end user, could have a significant impact on the cost of producing its products and the profitability of the Company. This risk is reduced in part, from time to time, through the use of crude oil and natural gas forward purchase contracts. The contracts are not used for speculative trading purposes. Realized gains or losses on these contracts are reported as adjustments to petroleum and natural gas costs in the related production period.

The Company did not have any outstanding crude oil and natural gas forward purchase contracts as at June 30, 2008 or June 30, 2007.

The Company's purchase of petroleum feedstock and natural gas and forward purchase contracts are not considered to be financial instruments under CICA Section 3855.

## 7. Inventories

Inventories are comprised as follows:

As at	June 30, 2008	December 31, 2007
	\$	\$
Raw materials	2,512,614	3,153,345
Finished product	8,094,596	2,686,200
Total	10,607,210	5,839,545

For the three months and six months ended June 30, 2008, operating expenses include inventories recognized as an expense, using the weighted cost method, in the amount of \$16,162,000 and \$43,255,000, respectively (three and six months ended June 30, 2007 - \$3,915,000 and 22,670,000, respectively).

The Company's inventories have been pledged as collateral on its demand revolving operating loans, bank guarantees and long-term credit facility with a Canadian chartered bank.

## 8. Share Capital and Contributed Surplus

### a) Authorized -

- 20,000,000 non-voting, preferred shares, rights to be determined upon issue
- Unlimited number of common shares

### b) Issued -

- Common

	June 30, 2008		December 31, 2007	
	#	\$	#	\$
Balance - beginning of period	15,253,107	29,631,368	15,295,307	29,675,698
Issue of shares for cash upon exercise of stock options	-	-	34,000	103,700
Redemption pursuant to normal course issuer bid	(37,000)	(71,877)	(76,200)	(148,030)
<b>Balance - end of period</b>	<b>15,216,107</b>	<b>29,559,491</b>	<b>15,253,107</b>	<b>29,631,368</b>

On June 27, 2007, the Company announced a normal course issuer bid to purchase up to 766,465 of its issued and outstanding common shares at the market price at the time of acquisition beginning on July 3, 2007 and ending on July 2, 2008, or such earlier time as the bid is completed or terminated by the Company. During the first half of 2008, 37,000 common shares were purchased at an average price of \$2.07 per common share, including transaction fees. The cost of common shares purchased totaled \$76,751 of which \$71,877 was recorded as a charge against share capital at the average carrying value of the Company's common shares issued and outstanding, with the balance of \$4,874 charged against retained earnings.

Subsequent to June 30, 2008, the Company announced that it will commence a new normal course issuer bid to purchase up to 760,805 of its issued and outstanding common shares. Purchases under the normal course issuer bid will commence on July 15, 2008 and will terminate on July 14, 2009, or such earlier time as the bid is completed or terminated by the Company. All shares purchased under the issuer bid will be cancelled.

### c) Contributed Surplus

	June 30, 2008	December 31, 2007
	\$	\$
Balance – beginning of period	1,500,569	1,123,673
Stock based compensation expensed during the period	17,970	376,896
<b>Balance – end of period</b>	<b>1,518,539</b>	<b>1,500,569</b>

### d) Stock Options

The Company has reserved 2,700,000 common shares which may be granted to directors and employees of the Company pursuant to an approved stock option plan ("Option Plan"). Stock options granted to employees vest after varying terms from the date of grant and expire up to ten years after the date of grant. The exercise price of each option equals the market price of the Company's common shares at the date of grant. A summary of the status of the Company's Option Plan is presented below:

	June 30, 2008	
	Options	Weighted Average Exercise Price
	#	\$
Common shares under option - beginning of period	540,000	3.26
Share options cancelled	(220,000)	3.40
Share options granted	200,000	2.21
<b>Common shares under option - end of period</b>	<b>520,000</b>	<b>2.79</b>
<b>Options exercisable at end of period</b>	<b>320,000</b>	<b>3.16</b>

## 8. Share Capital and Contributed Surplus (continued)

### d) Stock Options (continued)

During the three months ended June 30, 2008, the Company granted 100,000 stock options to an employee of the Company with an exercise price of \$2.21 (three months ended June 30, 2007 – NIL). During the six months ended June 30, 2008, the Company granted a total of 200,000 stock options (six months ended June 30, 2007 – 100,000) to two employees of the Company with exercise prices of \$2.20 and \$2.21. The stock options vest with the employees over a five year period and expire seven years after the date of grant. The weighted average fair value of the options granted during the six months ended June 30, 2008 were \$1.05 and \$1.30 per option grant and were estimated using the Black-Scholes model with the following assumptions: risk-free interest rate ranging from 3.1 to 3.7 percent; vesting period of five years per grant; volatility ranging from 50 to 68 percent and zero dividend yield.

The impact of expensing stock options for the three and six months ended June 30, 2008 was \$11,704 and \$17,970, respectively (three and six months ended June 30, 2007 – \$94,342 and \$188,344, respectively), with a corresponding increase in contributed surplus.

### e) Weighted Average Shares Outstanding

The following table summarizes the common shares used in calculating the net earnings per common share.

	Three months ended June 30		Six months ended June 30	
	2008	2007	2008	2007
	#	#	#	#
Weighted average share reconciliation				
- Basic				
Common shares - opening	15,245,207	15,295,307	15,253,107	15,295,307
Weighted average common shares (repurchased) issued during the period	(7,867)	5,978	(9,640)	3,006
	15,237,340	15,301,285	15,243,467	15,298,313
- Diluted				
Basic weighted average common shares - opening	15,237,340	15,301,285	15,243,467	15,298,313
Dilutive effect of stock options and equivalents	-	47,373	-	76,701
	15,237,340	15,348,658	15,243,467	15,375,014

## 9. Contingent Liabilities and Commitments

- Letters of guarantee are provided by the Company on an on-going basis and for varying amounts for its petroleum feedstock purchases from suppliers. At June 30, 2008, the Company had provided letters of guarantee totaling \$7,062,640 which terminated in July 2008, in favour of two suppliers for purchases of feedstock from those suppliers.
- In the normal course of business, the Company is party to various claims and legal proceedings. While the final outcome with respect to the claims and legal proceedings pending, as at June 30, 2008, cannot be determined with certainty, it is the opinion of management that their resolution will not have a material adverse effect on the Company's financial position or results of operations.
- The Company has accrued environmental costs of \$240,000 related to the clean-up of its tank farm in Sundre, Alberta. The \$240,000 is an estimate and the Company is in the process of gathering third party quotations. The Company carries insurance against such risks and anticipates that a portion of the environmental costs will be insured. The insurance underwriter is presently examining the Company's claim for the environmental clean-up. The accrual for the clean-up has been reported on the balance sheet under the caption accounts payable and accrued liabilities.

## 9. Contingent Liabilities and Commitments (continued)

- d) On April 30, 2007, the Company entered into an agreement with a third party for the construction of new heating units for the Sundre plant in the amount of \$745,900 of which \$162,980 is outstanding at June 30, 2008. The Company has continued to experience issues with the new heating units which have affected the operating capacity of the plant since early in the first quarter of 2008. As a result, the Company is re-installing its original salt-bath heaters in order to return the plant to an operating state while addressing the issues with the new heaters.

## 10. Restructuring Costs

During the second quarter of 2008, the Company recorded a provision for restructuring costs of \$850,000 relating to the consolidation of its accounting and administrative offices from Leduc to Calgary, Alberta. Restructuring costs include severance provisions of \$555,000 and \$295,000 of other transitioning costs. The consolidation is expected to be completed by October 31, 2008.

## 11. Segmented Information

The Company's activities are divided into three distinct business segments: Oilfield Services, which represents the manufacture and sale of hydrocarbon products; Energy Marketing, which represents the purchasing, gathering and marketing of crude oil for resale to refiners and other customers, and Transportation Services, which represents the operations of Millard. All of these business segments operate in one geographic region being the Western Canadian Sedimentary Basin. In the following tables, the elimination of significant inter-segment transactions are reflected under the caption "Inter-segment Eliminations".

Three months ended June 30, 2008

	Oilfield Services	Energy Marketing	Transportation Services	Inter-Segment Eliminations	Consolidated
	\$	\$	\$	\$	\$
Revenues	10,477,534	9,013,762	1,898,938	-	21,390,234
Inter-segment revenues	-	-	1,448,199	(1,448,199)	-
Total revenues	10,477,534	9,013,762	3,347,137	(1,448,199)	21,390,234
Operating expenses	11,054,151	8,107,285	2,430,081	(1,467,020)	20,124,497
Depreciation, amortization & accretion expense	348,504	10,716	269,584	-	628,804
Interest expense	18,524	-	-	-	18,524
Other income	12,144	-	-	-	12,144
Subtotal	(931,501)	895,761	647,472	18,821	630,553
Less: General and administrative					1,124,894
Less: Restructuring costs					850,000
Loss before income taxes					(1,344,341)

Three months ended June 30, 2007

	Oilfield Services	Energy Marketing	Transportation Services	Inter-Segment Eliminations	Consolidated
	\$	\$	\$	\$	\$
Revenues	3,786,720	1,614,242	2,066,817	-	7,467,779
Inter-segment revenues	-	-	614,357	(614,357)	-
Total revenues	3,786,720	1,614,242	2,681,174	(614,357)	7,467,779
Operating expenses	3,857,338	1,584,824	2,006,033	(585,856)	6,862,339
Depreciation, amortization & accretion expense	305,052	-	280,365	-	585,417
Other income (expense)	(16,151)	-	5,280	-	(10,871)
Subtotal	(391,821)	29,418	400,056	(28,501)	9,152
Less: General and administrative					1,049,546
Loss before income taxes					(1,040,394)

## 11. Segmented Information (continued)

Six months ended June 30, 2008

	Oilfield Services	Energy Marketing	Transportation Services	Inter-Segment Eliminations	Consolidated
	\$	\$	\$	\$	\$
Revenues	29,507,900	20,403,669	5,225,586	-	55,137,155
Inter-segment revenues	-	-	3,595,048	(3,595,048)	-
Total revenues	29,507,900	20,403,669	8,820,634	(3,595,048)	55,137,155
Operating expenses	30,506,434	19,095,927	6,243,029	(3,598,389)	52,247,001
Depreciation, amortization & accretion expense	676,482	10,716	581,663	-	1,268,861
Interest expense	24,782	-	-	-	24,782
Other income	27,135	-	3,989	-	31,124
Subtotal	(1,672,663)	1,297,026	1,999,931	3,341	1,627,635
Less: General and administrative					2,215,335
Less: Restructuring Costs					850,000
Loss before income taxes					(1,437,700)

Six months ended June 30, 2007

	Oilfield Services	Energy Marketing	Transportation Services	Inter-Segment Eliminations	Consolidated
	\$	\$	\$	\$	\$
Revenues	22,938,477	7,703,592	4,702,111	-	35,344,180
Inter-segment revenues	-	-	2,218,223	(2,218,223)	-
Total revenues	22,938,477	7,703,592	6,920,334	(2,218,223)	35,344,180
Operating expenses	20,608,613	6,788,083	5,180,492	(2,201,131)	30,376,057
Depreciation, amortization & accretion expense	589,218	-	588,824	-	1,178,042
Interest expense	-	-	8,116	-	8,116
Other income (expense)	(7,155)	-	4,033	-	(3,122)
Subtotal	1,733,491	915,509	1,146,935	(17,092)	3,778,843
Less: General and administrative					2,196,112
Earnings before income taxes					1,582,731

As at June 30, 2008

Total assets	57,202,334	6,345,800	8,539,260	(5,400,939)	66,686,455
Capital expenditures	2,453,783	459,707	480,544	-	3,394,034

December 31, 2007

Total assets	57,215,981	4,744,887	8,901,277	(5,936,604)	64,925,541
Capital expenditures	6,691,673	1,405,267	1,870,644	-	9,967,584

## 12. Comparative figures

Certain comparative figures have been reclassified to conform with the current year's presentation.

## Health, Safety and Environment

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Enerchem places the importance of safety above all other aspects of the Company's business. Enerchem recognizes that its employees represent its most valuable asset and must be provided with the tools and systems necessary to carry out their work in a safe environment.

We have initiated comprehensive policies and procedures to ensure the health and safety of all our employees, contractors, sub-contractors and visitors.

Enerchem holds a Certificate of Recognition ("COR") for all of its business operations. The COR recognizes that our health and safety management systems meet the Standards of Partnerships developed by Alberta Human Resources and Employment. We are proud that our employees have maintained an excellent safety performance record and that all facilities have operated lost-time incident free throughout the year. In recognition of our exceptional performance in workplace health and safety, we received a **Work Safe 2006 Alberta Best Safety Performer Award** which is presented to only 300 employers out of a possible 140,000 employers.

We also have implemented programs and guidelines to minimize our environmental exposures. All environmental laws and regulations are adhered to, including Alberta's Environmental Protection and Enhancement Act, the Canadian Environmental Protection Act, the Transportation of Dangerous Goods Act, and the Environmental Operating Guidelines for the Alberta Petroleum Industry.

## Corporate Governance

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The Board of Directors and management of the Company consider good corporate governance to be central to the effective operation and success of the Company.

The Board of Directors is responsible for the overall stewardship of the Company and has full power and authority to manage and control the affairs and business of the Company. It establishes the overall policies and standards for the Company. While delegating certain of its authority and responsibilities to its committees and management of the Company, it retains full effective control over the Company and monitors senior management. The directors are kept informed of the Company's operations at meetings of the Board, of its committees and through reports, analyses and discussions with management.

The Board is also responsible for overseeing the formulation by management of long-term strategic, financial and organizational and related objectives. The mandate of the Board also establishes a requirement that it implement structures and procedures to ensure that it functions independently of management, such as the Board's practice of conducting in-camera sessions as part of each regularly scheduled meeting.

### Composition of the Board of Directors and Committees

Enerchem's Board of Directors comprises seven members, six of whom qualify as unrelated directors by virtue of their independence from management or any interest, business or other relationship that could materially interfere with the directors' ability to act in the best interests of the Company, and all Audit Committee members qualify as independent within the meaning of Multilateral Instrument 52-110 – "Audit Committees". It believes that such number of directors is large enough to allow the directors to benefit from a wide variety of ideas and viewpoints without compromising communication among the directors, and between the directors and management.

The Board of Directors has four committees to which the Board has delegated certain of its authority and responsibilities, as well as certain advisory functions and power to make recommendations and reports to the Board. The standing committees of the Board are: the Audit Committee; the Compensation Committee; the Health, Safety and Environment Committee; and the Strategic Planning and Priorities Committee.

The Audit Committee meets on a regular basis with the Chief Financial Officer of the Company and the independent auditors to, among other things, review and inquire into: (a) matters affecting financial reporting; (b) the adequacy of internal controls and procedures for financial reporting and accounting; (c) the audit procedures and audit plans; and (d) the financial and business risks or exposures of the Company and the steps that management has taken to control such risks. It also recommends to the Board of Directors the external auditors to be appointed and their remuneration. The Audit Committee annually reviews the independence of the external auditors.

The Audit Committee reviews and recommends to the Board, for its approval: (a) the Company's interim unaudited financial statements and Management's Discussion and Analysis related thereto; (b) the Company's audited annual financial statements and Management's Discussion and Analysis related thereto; (c) prospectuses and other offering memoranda, if applicable; and (d) the annual and interim earnings press releases and other public disclosure documents containing audited or unaudited financial information required by regulatory authorities.

The responsibilities of the Audit Committee, including those responsibilities described above, are reviewed by the Board of Directors annually. All the members of the Audit Committee are considered to be financially literate and a majority have accounting or related financial expertise.

The Compensation Committee is responsible for reviewing matters of remuneration for senior executive positions, including that of the President and Chief Executive Officer, and making recommendations to the Board of Directors thereon. It is also responsible for reviewing and making recommendations to the Board for the appointment of persons to senior executive positions, for considering their terms of employment and for succession planning.

The Health, Safety and Environment Committee is responsible for reviewing and making recommendations and reports to the Board of Directors relating to the policies, standards, practices and programs of the Company on matters pertaining to both the environment and occupational health and safety. The committee monitors the Company's performance in relation to its own policies, as well as in relation to applicable legislation pertaining to both the environment and occupational health and safety. It also reviews and reports to the Board of Directors on the Company's state of readiness to respond to crisis situations.

The Company has set up a Strategic Planning and Priorities Committee whose mandate involves considering and advising the Board of Directors on matters of strategic importance to the Company.

#### **Code of Ethics and Business Conduct**

The Board has adopted a Code of Business Conduct and Ethics which applies to all directors, officers and employees of the Company. The Code calls for the highest standard of ethical conduct and personal integrity.

Enerchem is committed to maintaining its business in compliance with applicable laws, statutes and regulations. Additional information about our commitment to corporate governance practices are detailed in our 2008 Information Circular which can be found at [www.sedar.com](http://www.sedar.com).





## Directory

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### Corporate Office

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Enerchem International Inc.  
1950, 777 - 8th Avenue S.W.  
Calgary, Alberta  
CANADA T2P 3R5

T: 403.269.1500  
F: 403.269.1559  
www.enerchem.com

### Board of Directors

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Larry B. Phillips  
Chairman of the Board  
Director (2), (4)

David F. Potter  
Director (2), (4)

William D. Burch, FCA  
Director (1)

Gordon J. Hoy, P.Eng., MBA, CFA  
Director (3), (4)

Kenneth A. Klein, B. Comm.  
Director (1), (2)

Kevin M. Maguire, P. Eng., MBA  
Director (1), (4)

Bruce K. Gibson, B.Comm., CA  
Director (1)

### Officers

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Kenneth Bagan, LLB  
President and Chief Executive Officer

Brian M. Zubach, B. Admin., CMA  
Chief Financial Officer

J. Barrie Brookman  
Vice President, Corporate Development

Member of:

- (1) Audit Committee
- (2) Compensation Committee
- (3) Health, Safety and Environment Committee
- (4) Strategic Planning and Priorities Committee

### Registrar and Transfer Agent

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CIBC Mellon Trust Company  
320 Bay Street  
Toronto, Ontario CANADA M5H 4A6  
T: 800.387.0825  
www.cibcmellon.com

### Principal Bank

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HSBC Bank Canada  
Edmonton, Alberta

### Auditors

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PricewaterhouseCoopers LLP  
Edmonton, Alberta

### Legal Counsel

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Chamberlain Hutchison  
Edmonton, Alberta

### Stock Exchange Listing

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Toronto Stock Exchange: trading symbol "ECH"  
United States - Over the Counter 12g-3-2(b)

### Shareholder Information

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Shareholders may obtain copies of annual and quarterly reports, news releases, product information and other company information by contacting:

Investor Relations  
Mr. Kenneth Bagan  
Enerchem International Inc.  
First Alberta Place  
1950, 777 - 8th Avenue S.W.  
Calgary, Alberta T2P 3R5

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[www.enerchem.com](http://www.enerchem.com)