



# Sterling Resources Ltd.

## Third Quarter Report

For the Nine Months Ended September 30, 2003

## Message to Shareholders

### Third Quarter Highlights:

- Discovered oil in Avington exploration well onshore UK
- Farmed out drilling costs of next well in Wessex Basin scheduled for fourth quarter 2003
- Awarded two offshore UK licenses
- Finalized preparations for infill drilling program in South Craiova block onshore Romania

In the Weald Basin onshore UK, the exploration well, Avington-2, was an oil discovery. The well reached total depth having drilled a 580-meter horizontal section within the Great Oolite reservoir and is now undergoing an extended production test, to gather data on producing sections, acidize certain sections, and obtain a stabilized flow rate. The well came in close to prognosis with the top of the reservoir encountered 45 meters up dip from the untested oil column found in the Avington-1 well drilled in 1987. Prior to going horizontal, a short-term test of rates up to 250 barrels of oil per day confirmed the presence of hydrocarbons. Sterling retains an 8.33 percent interest in the well having farmed out most of its share of the well costs for an 8.33 percent interest.

An exploration well at Waddock Cross, within license PL 090 in the Wessex Basin onshore UK, received planning approval. Site construction commenced in October and drilling operations are expected to start early December. Waddock Cross is the first of the Wessex High wells to be drilled to evaluate the Bridport and Sherwood reservoirs as they trend westwards from the Wytch Farm field. Sterling retains an 18.75 percent working interest in PL 090 following a farm out which will fund Sterling's share of the well cost.

In the Cleveland Basin, the planning application for the Westerdale natural gas exploration well was approved in September. Westerdale is one of two planned wells in PEDL 068, which Sterling operates with an 80 percent working interest. The well is designed to test the structural closure some 50 meters up dip from the original well drilled several years ago on the structure, which tested natural gas.

Sterling extended its UK activity to the offshore when, together with its partners, it was awarded two "Promote Licenses" in the United Kingdom 21st Offshore Licensing Round. One license covers Blocks 210/25b and 210/30 located in the northern North Sea. Sterling holds a 60 percent interest and is operator. These blocks are surrounded by producing fields and have been somewhat under explored since earlier drilling to evaluate Brent objectives. The early part of the work program will integrate the existing data, and reprocess key seismic as necessary. The initial focus will be an Upper Jurassic sediment "wedge" that thickens westwards from the 210/30-1 well which had thin Upper Jurassic sands with oil shows. The other license covers Blocks 47/1 and 47/2b located in the southern North Sea. Sterling holds a 40 percent interest. The blocks are located just to the west of several southern North Sea gas fields in an area where the prolific Rotliegendes sandstone trends westwards into Sterling's onshore license PEDL 071. Initial activity will involve the acquisition and evaluation of existing seismic and well data.

Onshore Romania, an infill seismic acquisition program was completed on September 30 in the northeast part of the Craiova Block, in which Sterling has a 100 percent operated interest. The 110 kilometer program was chosen to evaluate a large positive geochemical anomaly and provide modern data quality along the western edge of the Bailesti depression. This is one of two focus areas within the large 1.5 million acre concession and is close to the large producing fields Bradesti and Malu Mare. Data quality appears excellent and processing will be completed during the fourth quarter.

On behalf of the Board of Directors,

(signed) "Robert G. Welty"  
Chairman & Chief Executive Officer

November 10, 2003

(signed) "Stewart G. Gibson"  
President & Chief Operating Officer

# Consolidated Balance Sheets

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	Sept. 30, 2003 <i>(Unaudited)</i>	Dec. 31, 2002 <i>(Audited)</i>
<b>ASSETS</b>		
Current		
Cash and short term investments	\$ 674,041	\$ 284,674
Accounts receivable	296,104	49,075
Due from officer	-	115,000
	<u>970,145</u>	<u>448,749</u>
Capital assets		
Petroleum and natural gas properties and equipment	9,036,505	8,398,166
Furniture and fixtures	21,250	24,746
	<u>9,057,755</u>	<u>8,422,912</u>
	<u>\$ 10,027,900</u>	<u>\$ 8,871,661</u>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current		
Accounts payable and accrued liabilities	\$ 937,505	\$ 490,222
Shareholders' equity		
Share capital (note 2)	14,052,084	12,382,568
Contributed surplus	66,479	66,479
Deficit	(5,028,168)	(4,067,608)
	<u>9,090,395</u>	<u>8,381,439</u>
	<u>\$ 10,027,900</u>	<u>\$ 8,871,661</u>

See accompanying notes

# Consolidated Statements of Operations and Deficit

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*Unaudited*

	Three Months Ended Sept. 30		Nine Months Ended Sept. 30	
	2003	2002	2003	2002
<b>EXPENSES</b>				
General and administrative				
Corporate	\$ 165,986	\$ 94,053	\$ 405,094	\$ 398,873
Exploration projects	–	30,225	–	49,793
Depreciation	1,143	1,850	3,497	5,214
Exploration licenses relinquished – Denmark	–	–	555,871	–
	<b>167,129</b>	<b>126,128</b>	<b>964,462</b>	<b>453,880</b>
<b>OTHER INCOME</b>				
Interest	2,649	1,787	3,902	3,353
Net loss for the period	<b>164,480</b>	<b>124,341</b>	<b>960,560</b>	<b>450,527</b>
Deficit, beginning of period	<b>4,863,688</b>	<b>3,725,153</b>	<b>4,067,608</b>	<b>3,398,967</b>
Deficit, end of period	<b>\$ 5,028,168</b>	<b>\$ 3,849,494</b>	<b>\$ 5,028,168</b>	<b>\$ 3,849,494</b>
Net loss attributable per common share				
Basic	\$ (0.01)	\$ (0.01)	\$ (0.05)	\$ (0.03)
Diluted	\$ (0.01)	\$ (0.01)	\$ (0.05)	\$ (0.03)
Weighted average number of shares outstanding	<b>24,041,467</b>	<b>16,105,090</b>	<b>19,686,569</b>	<b>15,359,927</b>

*See accompanying notes*

# Consolidated Statements of Cash Flows

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Unaudited

	Three Months Ended Sept. 30		Nine Months Ended Sept. 30	
	2003	2002	2003	2002
<b>OPERATING ACTIVITIES</b>				
Net loss for period	\$ (164,480)	\$ (124,341)	\$ (960,560)	\$ (450,527)
Items not affecting cash				
Depreciation	1,143	1,850	3,497	5,214
Exploration licenses relinquished – Denmark	–	–	555,871	–
Cash loss from operations	(163,337)	(122,491)	(401,192)	(445,313)
Change in non-cash working capital	1,012,227	105,335	315,254	188,858
Cash provided by (used in) operating activities	848,890	(17,156)	(85,938)	(256,455)
<b>INVESTING ACTIVITIES</b>				
Petroleum and natural gas properties and equipment additions	(872,795)	(400,034)	(1,194,210)	(548,421)
Furniture and fixtures additions	–	(172)	–	(2,452)
Cash used in investing activities	(872,795)	(400,206)	(1,194,210)	(550,873)
<b>FINANCING ACTIVITIES</b>				
Issue of common shares, net of issue costs	(1,522)	772,570	1,669,515	772,570
Cash provided by (used in) financing activities	(1,522)	772,570	1,669,515	772,570
Increase (decrease) in cash	(25,427)	355,208	389,367	(34,758)
Cash and short term investments, beginning of period	699,468	244,586	284,674	634,552
Cash and short term investments, end of period	\$ 674,041	\$ 599,794	\$ 674,041	\$ 599,794

See accompanying notes

# Selected Notes to Consolidated Financial Statements

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Nine months ended September 30, 2003  
(Unaudited)

## NOTE 1. BASIS OF PRESENTATION

The interim consolidated financial statements of Sterling Resources Ltd. have been prepared by management in accordance with accounting principles generally accepted in Canada. The interim consolidated financial statements have been prepared following the same accounting policies and methods of computation as the consolidated financial statements for the fiscal year ended December 31, 2002. The disclosures included below are incremental to those included with annual consolidated financial statements. The interim consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto in the Company's annual report for the year ended December 31, 2002.

## NOTE 2. SHARE CAPITAL

### a) Authorized

Unlimited common shares without nominal or par value

### b) Issued and outstanding

	September 30, 2003		September 30, 2002	
	Number of Shares	Amount (\$)	Number of Shares	Amount (\$)
Common shares				
Balance, beginning of year	16,675,967	12,382,568	14,981,967	11,612,046
Issued during period	7,365,500	1,841,375	1,694,000	847,000
Share issue costs	–	(171,859)	–	(74,430)
Balance, end of period	24,041,467	14,052,084	16,675,967	12,384,616

In June of 2003 the Company issued 7,200,000 units at \$0.25 per unit for an aggregate cash consideration of \$1,800,000. Each unit consists of one common share and one common share purchase warrant. Each warrant entitles the holder to purchase one additional common share for a period of 24 months at a price of \$0.30 per common share during the first twelve months after the closing date of the private placement or at a price of \$0.35 per common share during the second twelve month period. Commissions in the amount of \$100,000 cash and 165,500 units, on the same terms and conditions as the placement to subscribers, were paid to finders in connections with the placement of certain units.

### c) Stock options

The Company has a stock option plan under which employees, directors, officers and consultants are eligible to receive grants. On September 30, 2003 there were 1,662,500 common shares reserved for issuance under the plan with exercise prices between \$0.30 and \$0.60. Options granted under the plan are generally fully exercisable after three years and expire five years after the grant date.

	September 30, 2003		September 30, 2002	
	Number of Options	Weighted Average Exercise Price	Number of Options	Weighted Average Exercise Price
Outstanding at beginning of year	1,007,500	\$ 0.47	932,500	\$ 0.54
Granted	655,000	\$ 0.36	320,000	\$ 0.37
Outstanding at end of period	1,662,500	\$ 0.43	1,252,500	\$ 0.51
Exercisable at end of period	657,503	\$ 0.48	575,835	\$ 0.61

As the Company is following the intrinsic value method of accounting for employee options, no compensation expense has been recorded with respect to employee options. The following table provides pro forma measures of net loss and net loss per share, had compensation expense been recognized based on the estimated fair value of the employees options on the grant date in accordance with the fair value method of accounting for stock-based compensation.

	Nine months ended	
	Sept. 30, 2003	Sept. 30, 2002
Reported net loss	\$ 960,560	\$ 450,527
Compensation expense	\$ 12,104	\$ 8,445
Pro forma net loss	\$ 972,664	\$ 458,972
Reported basic and diluted net loss per share	\$ 0.05	\$ 0.03
Pro forma basic and diluted net loss per share	\$ 0.05	\$ 0.03

655,000 options were granted during the second quarter of 2003; 320,000 options were granted during the second quarter of 2002. The estimated fair value of stock options issued during 2003 and 2002 was determined using Black-Scholes model using the following weighted average assumptions, resulting in a weighted average fair value of \$0.17 per option for 2003 and \$0.11 per option for 2002.

	Nine months ended	
	Sept. 30, 2003	Sept. 30, 2002
Risk-free interest rate	3.33%	3.55%
Expected hold period to exercise	3 years	3 years
Volatility factor of the Company's shares	0.640	0.596
Dividend yield	0%	0%

#### d) Warrants Outstanding

Expiry Dates	September 30, 2003		September 30, 2002	
	Number of Warrants	Exercise Price	Number of Warrants	Exercise Price
July 17, 2003	-	\$ -	1,703,812	\$ 0.75
July 26, 2003	-	\$ -	333,372	\$ 0.75
January 17, 2003	-	\$ -	103,956	\$ 0.90
July 31, 2004	1,694,000	\$ 0.60	-	\$ -
June 6, 2005	4,115,000	\$ 0.30/0.35	-	\$ -
June 16, 2005	3,250,500	\$ 0.30/0.35	-	\$ -
	9,059,500		2,141,140	