

Third Quarter Report

STERLING RESOURCES LTD.

For the Nine Months ended September 30, 2004

Message to Shareholders

Sterling significantly increased its presence in the North Sea with the award on September 14 of eight new Blocks under six “Promote Licenses” in the UK’s 22nd Offshore Licensing Round. This brings Sterling’s UK offshore holdings to interests in eleven Blocks. The Blocks awarded consist of Block 210/29 in the Northern North Sea, adjacent to existing Block 210/30 (Sterling 60%), three Blocks in the Central North Sea, 19/5b (partial), 21/23a and 22/26b (all Sterling 100%), and four Blocks in the Southern Gas Basin, Blocks 42/13, 42/19, 42/20 and 42/24 (all Sterling 100%).

Prior to making the applications for the Blocks, Sterling had access to modern 3D seismic coverage over most of them. The new Blocks contain multiple prospects and leads and two have older wells with proven hydrocarbons. Sterling now has a superior portfolio of UK offshore exploration projects and this is now a strong core area for the Company.

On Block 210/30 in the Northern North Sea, mapping and interpretation of the 3D seismic dataset indicated three untested structures in the Middle Jurassic Brent Formation. Also high amplitude anomalies were identified within the Upper Jurassic sequence that indicate the potential for substantial hydrocarbon bearing sands. Given these positive results, Sterling (60% interest) has begun the process of bringing in an industry partner through farmout of a portion of its interests.

Onshore UK, extended well testing of the Waddock Cross oil discovery well (Sterling 18.75%) is showing positive results.

Shortly after the quarters’ end, Sterling negotiated a farmout of a portion of its 100% interest in its onshore South Craiova Concession in Romania. The agreement is subject to government approval. Under the farmout agreement, the farmee will earn a 40% interest by paying promoted percentages, based on AFE costs, of two wells plus a 140 kilometer 2D seismic program. The first well, named Cetatua, will be drilled to a depth of approximately 2,700 meters to test a multi-target prospect on the western edge of the Bailesti Depression in the northeast part of the Concession. The primary target reservoirs are in the Tertiary and Triassic sections. The prospect is analogous to producing fields on the eastern edge of the Depression in which all target reservoirs are oil and gas productive. Drilling tenders have been received and location preparation is scheduled to begin shortly.

On the remainder of the South Craiova Concession, detailed studies are underway to follow up on initial technical work that identified many leads. This work is planned to be completed in time to enable additional seismic and potential drilling during 2005, after integration of the results of the first well.

On behalf of the Board of Directors,

(signed)

Robert G. Welty
Chairman & Chief Executive Officer

November 15, 2004

(signed)

Stewart G. Gibson
President & Chief Operating Officer

Management's Discussion and Analysis

The following Management's Discussion and Analysis (MD&A) is dated November 15, 2004 and should be read in conjunction with the accompanying unaudited consolidated interim financial statements and the audited consolidated financial statements and MD&A for the year ended December 31, 2003.

The Company's financial statements and the financial data included in the MD&A have been prepared in accordance with Canadian generally accepted accounting principles (GAAP). All financial amounts are expressed in Canadian dollars, except as otherwise indicated.

Forward-looking Statements

Certain statements contained in the MD&A are forward-looking statements. Forward-looking statements are based on current expectations, estimates and projections that involve a number of risks and uncertainties, which could cause actual results to differ materially from those anticipated by the Company and described in the forward-looking statements. These risks and uncertainties include:

- the risks of the oil and gas industry, such as operational risks in exploring for, developing and producing crude oil and natural gas;
- risks and uncertainties involving geology of oil and gas deposits;
- potential delays or changes in plans with respect to exploration or development projects or capital expenditures;
- uncertainties as to the availability and cost of financing;
- risks in conducting foreign operations; and
- the possibility that government policies or laws may change or governmental approvals may be delayed or withheld.

Forward-looking statements are based on the estimates and opinions of the Company's management at the time the statements are made. The Company assumes no obligation to update forward-looking statements should circumstances or management's estimates or opinions change.

Business and Strategy

Sterling Resources Ltd. is a Calgary, Canada based energy company actively engaged in the exploration and development of crude oil and natural gas in selected areas of the world. The Company's strategy for achieving growth is to source and initiate international projects with the potential for larger reserves. High initial working interests are taken where possible, and financial exposure and risk are managed by obtaining industry participations. Current landholdings are focused in the United Kingdom and Romania.

Discussion of Operations and Financial Results

For the third quarter ended September 30, 2004, the Company recorded a loss of \$179,200, compared with a loss of \$176,513 for the quarter ended September 30, 2003.

There is no material revenue at the present time. Sterling participated in two small oil discoveries onshore UK, Avington-2 and Waddock Cross-2, in 2003 and 2004 respectively. Extended well tests have and are being conducted and revenues and expenses during this period are being offset against capital expenditures on the licenses.

Expenses for the quarter were \$196,348 compared with \$179,162 in 2003. The major increases in expenses were third party consulting fees, business travel and stock based compensation. Foreign exchange losses for the three months ended September 30, 2004 decreased to \$248 from \$20,864 for the three months ended September 30, 2003, principally due to the strengthening of the Canadian dollar. For the nine months ended September 30, 2004 the loss on foreign exchange was \$21,908 compared with a

gain of \$21,894 for the nine months period in 2003. The variance was again related to exchange rates between the Canadian dollar and the British pound during these two periods.

Changes in Accounting Policy

The Company adopted the intrinsic value method of accounting for stock options as of January 1, 2002 and as at December 31, 2003 adopted the new Canadian Institute of Chartered Accountants (“CICA”) standard for reporting. As permitted by this new pronouncement, the change has been applied retroactively for grants awarded after January 1, 2002. Results for the 2003 periods have been restated to conform to this new form of disclosure using the fair value method of accounting for stock options.

As of January 1, 2004 the Company adopted the CICA Handbook Section 3110, “Asset Retirement Obligations” and Accounting Guide AcG-6 “Oil and Gas Accounting - Full Cost”. The effect of adopting these policies is explained in Note 2 to the September 30, 2004 financial statements.

Petroleum Properties and Capital Expenditures

Sterling had invested \$10,055,863 in its oil and gas properties to September 30, 2004, compared with \$9,227,590 as at December 31, 2003.

Cash capital expenditures on oil and gas activities for the quarter were \$361,326 compared with \$872,795 for the third quarter of 2003. Expenditures during the 2004 quarter were primarily for geophysical analyses of the seismic acquired onshore Romania and Block 210/30 in the North Sea, plus the extended well test of the Waddock Cross-2 discovery. Expenditures during the third quarter of 2003 were comprised primarily of seismic acquisition costs onshore Romania.

Financing, Liquidity and Solvency

As at September 30, 2004 Sterling had working capital of \$3,561,232 compared to a negative working capital of \$323,834 as at December 31, 2003.

On June 30, 2004 Sterling completed a private placement to an international investment fund, consisting of 15,350,000 common shares at a price of \$0.32, for gross proceeds of \$4,912,000. Proceeds will be used to fund Sterling’s ongoing work programs and to augment working capital. During the quarter, 140,000 warrants were exercised for proceeds of \$49,000 and during the nine months ended September 30, 2004, 1,516,575 warrants were exercised for proceeds of \$461,973.

As at September 30, 2004 there were 42,408,042 common shares outstanding and a further 2,595,000 common shares reserved for the issuance of stock options. In addition, warrants attached to common share issues completed in 2003 reserve 5,848,925 common shares at \$0.35 per share until June 2005.

As is typical of companies in Sterling’s stage, future exploration and development activities will require substantial amounts of additional capital which the Company may raise through debt or equity financing and by farming out of partial interests in certain properties. Financings and farm outs are subject to prevailing market conditions at the time. Successful completion of financings and farm outs of partial interests are required for Sterling to carry out its activities on each of its projects. Sterling may also raise capital by monetization of certain of its existing assets.

There are no material commitments on oil and gas properties. The majority of costs associated with Phase 3 of the Exploration Period onshore Romania, which Sterling elected to enter effective June 23, 2004, will be covered by a farmout completed in October, 2004 to an industry partner. Commitments on its offshore Romanian contract areas have been suspended with the agreement of the Romanian Government pending resolution of the Romanian/Ukrainian maritime boundary delineation. All licenses in the UK and France have only minor expenditure commitments for geological and geophysical activities.

Future Plans

Sterling plans to continue with its growth strategy. Over the next two years the major initiatives will be to:

- drill at least six exploration wells on the key prospects, which have been matured within the currently held acreage. It is intended to continue the successful farm out strategy adopted to date for the majority of these wells.
- continue geological and geophysical work to evaluate the many other prospects and leads that exist on the current licenses, in addition to those identified in the drilling program. In particular, this work will focus on offshore UK and both onshore and offshore Romania, where significant additional prospectivity exists.
- consider divesting of the UK onshore assets which contain two oil discoveries, to allow concentration on the UK offshore.
- appraise and develop existing discoveries. The Doina gas discovery awaits drilling of further nearby prospects on the Block and the privatization of Petrom, the Romanian national oil company, which was completed in July 2004 when OMV, the Austrian Oil Company, acquired control.
- acquire more blocks through promote license applications in the UK North Sea and pursue the acquisition of “Fallow Blocks” and “Fallow Discoveries”. Generally, these are license areas that have been so designated by the Department of Trade and Industry where the initial term of the license has expired and there has been no drilling or dedicated seismic or other significant activity for four years.

Estimated minimum capital expenditures and general administrative expenditures for 2004 are \$2,300,000 net of planned farmouts on certain properties. Sterling has flexibility over most of its capital expenditures and as to the percentage of its working interests farmed out.

For the past four years, Sterling’s strategy for growth and financing has proved to be a workable one. Furthermore, during this time the Company has increased its holdings of exploration lands as well as the geological prospectivity of many of its properties. Accordingly plans are to increase the amount of drilling activity over the next two years. Successful drilling would result in production and cash flow with which to finance further activity.

Business Risks

The Company’s business risks have not changed materially from the disclosure presented in the 2003 year end MD&A.

Review of Interim Financial Statements

Under National Instrument 51-102, if an auditor has not performed a review of the interim financial statements, they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor.

The accompanying unaudited interim financial statements (“financial statements”) of the Company have been prepared by Sterling Resources Ltd.’s management. The Company’s independent auditor has not performed a review of the accompanying financial statements in accordance with standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statement by an entity’s auditor.

Additional information about Sterling Resources Ltd. and its business activities, including the Company’s Annual Information Form, is available on SEDAR at www.sedar.com.

Consolidated Balance Sheets

<i>Unaudited</i>	September 30	December 31
	2004	2003
	\$	\$
Assets		
Current		
Cash and short term investments	3,724,751	17,227
Accounts receivable and prepaid expenses	150,332	84,390
	3,875,083	101,617
Capital assets		
Petroleum and natural gas properties (<i>note 2</i>)	10,055,863	9,227,590
Furniture, fixtures and other	34,821	20,155
	10,090,684	9,247,745
	13,965,767	9,349,362
Liabilities and Shareholders' Equity		
Current		
Bank indebtedness	–	75,000
Accounts payable and accrued liabilities	313,851	350,451
	313,851	425,451
Asset retirement obligation (<i>note 2</i>)	11,761	–
Shareholders' equity		
Share capital (<i>note 3</i>)	19,329,505	14,052,083
Contributed surplus	170,417	105,988
Deficit	(5,859,767)	(5,234,160)
	13,640,155	8,923,911
	13,965,767	9,349,362

See accompanying notes

Consolidated Statements of Operations and Deficit

Unaudited

	Three Months Ended Sept. 30		Nine Months Ended Sept. 30	
	2004	2003	2004	2003
	\$	\$	\$	\$
		<i>(Restated— see note 2)</i>		<i>(Restated— see note 2)</i>
EXPENSES				
General and administrative	160,108	142,122	552,761	426,988
Foreign exchange (gain) loss	248	20,864	21,908	(21,894)
Stock-based compensation	34,488	12,033	64,429	17,921
Depreciation and accretion	1,504	1,143	4,078	3,497
Exploration licenses relinquished	—	—	—	555,871
	196,348	179,162	643,176	982,383
OTHER INCOME				
Interest	17,148	2,649	17,569	3,902
Net loss for the period	179,200	176,513	625,607	978,481
Deficit, beginning of period	5,680,567	4,869,576	5,234,160	4,067,608
Deficit, end of period	5,859,767	5,046,089	5,859,767	5,046,089
Net loss attributable per common share				
Basic	(0.01)	(0.01)	(0.01)	(0.05)
Diluted	(0.01)	(0.01)	(0.01)	(0.05)

See accompanying notes

Consolidated Statements of Cash Flow

Unaudited

	Three Months Ended Sept. 30		Nine Months Ended Sept. 30	
	2004	2003	2004	2003
	\$	\$	\$	\$
		<i>(Restated— see note 2)</i>		<i>(Restated— see note 2)</i>
OPERATING ACTIVITIES				
Net loss for the period	(179,200)	(176,513)	(625,607)	(978,481)
Items not affecting cash				
Depreciation and accretion	1,504	1,143	4,078	3,497
Stock-based compensation	34,488	12,033	64,429	17,921
Exploration licenses relinquished	—	—	—	555,871
Cash loss from operations	(143,208)	(163,337)	(557,100)	(401,192)
Change in non-cash working capital	(179,752)	1,012,227	(102,542)	315,254
Cash provided by (used in) operating activities	(322,960)	848,890	(659,642)	(85,938)
INVESTING ACTIVITIES				
Petroleum and natural gas properties	(361,326)	(872,795)	(817,412)	(1,194,210)
Furniture, fixtures and other	(10,865)	—	(17,844)	—
Cash used in investing activities	(372,191)	(872,795)	(835,256)	(1,194,210)
FINANCING ACTIVITIES				
Issue of common shares net of share issue costs	(1,720)	(1,522)	5,277,422	1,669,515
Bank indebtedness	—	—	(75,000)	—
Due to related party	—	—	—	—
Cash provided by (used in) financing activities	(1,720)	(1,522)	5,202,422	1,669,515
Increase (decrease) in cash	(696,871)	(25,427)	3,707,524	389,367
Cash and short term investments, beginning of period	4,421,622	699,468	17,227	284,674
Cash and short term investments, end of period	3,724,751	674,041	3,724,751	674,041

See accompanying notes

Selected Notes to Consolidated Financial Statements

Unaudited

Nine Months Ended September 30, 2004

1. Basis of Presentation

The interim consolidated financial statements of Sterling Resources Ltd. have been prepared by management in accordance with Canadian generally accepted accounting principles. 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, 2003. The disclosures included below are incremental to those included with the 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, 2003.

2. Changes in Accounting Policies

As of January 1, 2002, the Company adopted the recommendations of the Canadian Institute of Chartered Accountants (CICA) on accounting for stock-based compensation. As permitted by this new pronouncement, the Company has applied this change retroactively for grants awarded after January 1, 2002, and restated the 2003 results to conform to this new form of disclosure using the fair value method of accounting for stock options.

As of January 1, 2004, the Company adopted CICA Handbook Section 3110 "Asset Retirement Obligations" to account for future costs of abandonment of existing facilities. As a result of this change, the Consolidated Financial Statements at March 31, 2004 were changed as follows: petroleum and natural gas properties was increased by \$10,861 with a corresponding amount recorded as a liability, asset retirement obligation. The change was applied retroactively. The Company estimates the undiscounted cash flows related to asset retirement obligations, adjusted for inflation, to be incurred over the estimated reserve life of the underlying assets will total approximately \$49,915. The fair value at January 1, 2004 was \$10,861, using a discount rate of 10% and an inflation rate of 4%.

As of January 1, 2004, the Company adopted guideline AcG-16 "Oil and Gas Accounting – Full Cost" issued by the CICA. Under AcG-16 impairment is recognized if the carrying amount of the capital assets exceeds the sum of the undiscounted cash flows expected to result from the Company's proved reserves. Previously impaired was tested based on undiscounted future net revenues using proved reserves, and providing for future general and administrative expenses, carrying costs and taxes. The adoption of AcG-16 had no effect on the Company's financial results.

3. Share Capital

a) Authorized

Unlimited common shares without nominal or par value

b) Issued and outstanding

	Number of Shares	Amount \$
Common shares		
Balance outstanding as at December 31, 2003	24,041,467	14,052,083
Issued during period	18,366,575	5,853,973
Share issue costs	–	(576,551)
Balance, September 30, 2004	42,408,042	19,329,505

In June of 2004 the Company issued 15,350,000 common shares for an aggregate cash consideration of \$4,912,000. Commissions in the amount of 1,500,000 common shares were paid to finders in connection with the placement and the attributed value of \$480,000 has been included in share issue costs. During the period, 1,516,575 warrants were exercised for proceeds of \$461,973.

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, 2004 there were 2,595,000 common shares reserved for issuance under the plan with exercise prices between \$0.32 and \$0.60. Stock options granted prior to June 30, 2004 have a five year term and vested in full on June 30, 2004. Options granted on June 30, 2004 have a term of three years and vest as to one third after 12 months, 24 months and 35 months.

	Number of Options	Weighted Average Exercise Price \$
Outstanding as at December 31, 2003	1,642,500	0.47
Granted	1,210,000	0.33
Cancelled/Expired during the period	(257,500)	0.44
Outstanding at September 30, 2004	2,595,000	0.38
Exercisable at September 30, 2004	1,485,000	0.42

As mentioned in Note 2, the Company has adopted the fair value method of accounting for all stock options granted to directors, officers, employees and consultants retroactively to January 1, 2002 using the Black-Scholes option pricing model using the following assumptions for the options granted in 2004.

	2004
Risk-free interest rate	3.68%
Expected hold period to exercise	3 Years
Volatility in the price of the Company's shares	99.0%
Dividend yield	0%

d) Warrants Outstanding

Expiry Date	Number Outstanding January 1, 2004	Exercised During Nine Month Period	Expired During Nine Month Period	Number Outstanding Sept. 30, 2004	Exercise Price \$
	July 31, 2004	1,694,000	–	1,694,000	–
June 6, 2005	4,115,000	864,000	–	3,251,000	0.35
June 16, 2005	3,250,500	652,575	–	2,597,925	0.35
	9,059,500	1,516,575	1,694,000	5,848,925	

e) Weighted Average Shares

The weighted average shares outstanding for the three months ended September 30, 2004 and September 30, 2003 were 42,290,868 and 24,041,467 respectively and for the nine months ended on these dates were 28,259,247 and 19,374,831 respectively.

Corporate Information

Directors

Raj K. Agrawal

President

NRG Engineering Ltd.

Robert B. Carter ^{(1) (2)}

Independent Businessman

Ian Connor

Managing Director, Meridian

Capital Limited

Stewart G. Gibson

President & Chief Operating Officer

Sterling Resources Ltd.

Teck Soon Kong ⁽¹⁾

Independent Businessman

David E. Powell ⁽¹⁾

Independent Businessman

Robert G. Welty

Chairman & Chief Executive Officer

Sterling Resources Ltd.

⁽¹⁾ Audit Committee

⁽²⁾ Chairman, Audit Committee

Officers

Robert G. Welty

Chairman & Chief Executive Officer

Stewart G. Gibson

President & Chief Operating Officer

David A. Findlater

Vice President Exploration

Sherry L. Cremer

Treasurer & Corporate Secretary

Corporate Headquarters

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E-Mail: info@sterling-resources.com

Website: www.sterling-resources.com

Auditors

Ernst & Young LLP

Banker

The Royal Bank of Canada

Legal Counsel

Stikeman Elliott

Registrar and Transfer Agent

Inquiries regarding change of address, registered shareholdings, stock transfers or lost certificates should be directed to:

Computershare Investor Services Inc.

9th Floor, 100 University Avenue,

Toronto, Ontario, Canada M5J 2Y1

Telephone: (800) 564-6253

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(416) 263-9394

E-Mail: service@computershare.com

Stock Exchange Listing

The TSX Venture Stock Exchange

Trading Symbol: SLG

Sterling Resources (UK) Ltd.

(wholly owned)

Directors

Stewart G. Gibson

Aboyne, Scotland

David Miller

London, United Kingdom

Robert G. Welty

Calgary, Canada

Officers

Robert G. Welty

Chairman

Stewart G. Gibson

Managing Director

David A. Findlater

Vice President Exploration & Business Development

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