

CORPORATE

HIGHLIGHTS

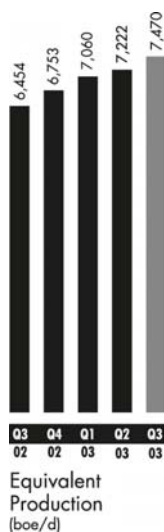
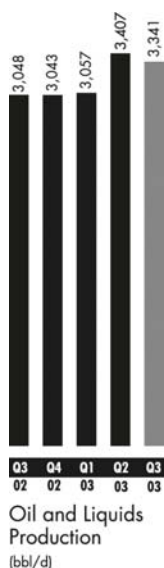
For the three and
nine months ended
September 30, 2003

With growing production volumes and continued high commodity pricing, Zargon reported strong financial results for the third quarter of 2003. Third quarter revenue of \$23.76 million, cash flow from operations of \$12.34 million (\$0.67 per diluted share) and earnings of \$4.51 million (\$0.24 per diluted share) were all sharply higher than the 2002 comparative results. High oil and natural gas commodity prices were the primary source of these gains with natural gas prices up 74 percent over the prior year quarter. Price gains were reinforced by natural gas production volume increases that, for the quarter, were 21 percent ahead of the comparative 2002 third quarter and eight percent over the preceding 2003 second quarter. Earnings continue to benefit from the recent federal tax reductions for resource companies, which reduce future tax provisions and provided Zargon a large one-time positive impact in the 2003 second quarter.

For the first nine months, record revenue of \$77.15 million, cash flow from operations of \$41.10 million (\$2.24 per diluted share) and net earnings of \$20.50 million (\$1.12 per diluted share) showed increases of 72, 92, and 220 percent, respectively over the comparable 2002 period. Net capital expenditures for the first nine months of 2003 totaled \$27.07 million with \$24.41 million allocated to field related activities, as Zargon focused its expenditures on natural gas exploration. Property acquisitions for the 2003 period were largely offset by dispositions of non-core, higher cost properties. During the nine month period, Zargon increased its natural gas exploration-focused undeveloped land base by 14 percent to 378,500 net acres. The high cash flows experienced throughout 2003 have funded a successful exploration program and brought debt net of working capital down to \$13.81 million at September 30, 2003, an amount equivalent to less than four months of the current cash flow from operations.

(unaudited)	Three months ended September 30			Nine months ended September 30		
	2003	2002	Percent Change	2003	2002	Percent Change
FINANCIAL						
INCOME AND INVESTMENTS (\$ million)						
Production revenue	23.76	16.65	43	77.15	44.87	72
Cash flow from operations	12.34	7.75	59	41.10	21.41	92
Net earnings	4.51	2.27	99	20.50	6.40	220
Net capital expenditures	12.11	10.89	11	27.07	27.52	(2)
PER COMMON SHARE, DILUTED						
Cash flow from operations (\$/share)	0.67	0.43	56	2.24	1.21	85
Net earnings (\$/share)	0.24	0.13	85	1.12	0.36	211
BALANCE SHEET AT PERIOD END (\$ million)						
Property and equipment, net				155.32	136.85	13
Bank indebtedness				8.92	28.71	(69)
Shareholders' equity				108.01	82.00	32
SHARES OUTSTANDING AT PERIOD END (million)						
				17.89	17.54	2
OPERATIONS						
AVERAGE DAILY PRODUCTION						
Oil and liquids (bbl/d)	3,341	3,048	10	3,269	2,942	11
Natural gas (mmcf/d)	24.77	20.44	21	23.90	19.63	22
Equivalent (boe/d)	7,470	6,454	16	7,252	6,213	17
Equivalent per million shares (boe/d)	418	368	14	408	363	12
AVERAGE SELLING PRICE (before hedges)						
Oil and liquids (\$/bbl)	36.39	38.09	(4)	37.95	33.98	12
Natural gas (\$/mcf)	5.51	3.17	74	6.63	3.28	102
WELLS DRILLED, NET						
	11.5	7.1	62	22.5	14.2	58
UNDEVELOPED LAND AT PERIOD END						
(thousand net acres)				379	318	19

Note: The calculation of barrels of equivalent (boe) is based on the conversion ratio that one barrel of oil is equivalent to six thousand cubic feet of natural gas. Average daily production per million shares uses the weighted average number of shares for the period.



PRODUCTION

Natural gas production volumes averaged 24.77 million cubic feet per day in third quarter 2003, a 21 percent increase over the 20.44 million cubic feet per day reported in the 2002 third quarter, and an eight percent improvement from the 22.89 million cubic feet per day reported in second quarter 2003. Over the last eighteen months, Zargon's natural gas growth has primarily been generated from successful exploration initiatives located at the West Central Alberta properties of Highvale, Pembina and Peace River Arch. During the third quarter an additional two million cubic feet per day of production was added from the tie-in of winter 2002-03 exploratory gas wells at the Pembina shallow gas project. By quarter-end, more than three additional million cubic feet per day of natural gas was tied-in from a recently drilled Progress well on the Peace River Arch. Zargon's working interest natural gas production currently exceeds 28 million cubic feet per day. These natural gas production gains demonstrate the initial successful results of Zargon's West Central Alberta exploration strategy. Since January 2002, Zargon has increased its West Central Alberta undeveloped lands from 38.0 thousand net acres to 154.5 thousand net acres. West Central Alberta natural gas production volumes have grown commensurately from 2.0 million to over 10 million cubic feet per day. During this time East Central Alberta natural gas production volumes have been maintained at steady rates with a modest maintenance-drilling program.

Production of oil and liquids averaged 3,341 barrels per day in third quarter 2003, ten percent higher than in third quarter 2002 but two percent less than the second quarter 2003 rate. Zargon's oil production growth is based on the exploitation and enhancement of Williston Basin (Southeast Saskatchewan and North Dakota) long-life, shallow-decline properties plus complementary acquisitions. In North Dakota, an enhanced Haas Unit waterflood program and a Truro Unit property acquisition have provided the majority of this year's oil production growth. Further Williston Basin production gains are expected this winter from horizontal development drilling programs and waterflood implementation and modification projects.

On an equivalent basis, Zargon has shown a consistent growth trend for the first three quarters of 2003. Third quarter production of 7,470 barrels of equivalent per day increased three percent over the second quarter, which was in turn two percent over the 2003 first quarter rate. For the first nine months, production of 7,252 barrels of equivalent per day was 17 percent higher than the corresponding nine months of 2002 volumes. On a per share basis, the 2003 third quarter production registered a 14 percent gain over the 2002 third quarter.

EXPLORATION AND EXPLOITATION

Zargon has based its growth on the twin strategies of exploring for natural gas reserves and exploiting existing oil reservoirs. The key input resource for our natural gas exploration program is undeveloped land and over the last few years, Zargon has successfully built a 378.5 thousand net acre undeveloped land inventory. During the 2003 nine month period, 75.9 thousand net acres of Crown and freehold leases were acquired with the largest additions located in the Highvale area, but also with sizeable additions at Pembina and Peace River Arch in West Central Alberta. The average cost of the Crown purchases in this nine month period was \$87 per acre.

This growing undeveloped land inventory has broadened the scope of our drilling programs and after a slow first half, Zargon had an active and successful third quarter drilling program with twelve operated gross wells (10.5 net) plus eight non-operated gross wells (1.0 net). This program delivered 8.5 net gas wells, 2.0 net oil wells and one net dry hole for a 91 percent success ratio. The gas wells included 1.8 net gas wells at the West Central Alberta Pembina property, 2.0 net gas wells on the Peace River Arch property and 4.7 net gas wells at the East Central Alberta Jarrow property. Oil wells were drilled at Taber, Alberta and Weyburn, Saskatchewan and a dry hole was drilled at the Peace River Arch property.

In the 2003 nine month period, Zargon has implemented oil reservoir waterflood initiation or enhancement projects at East Frys, West Frys and Weyburn (Elswick) in Saskatchewan and at Taber, Alberta. Once the oil reservoirs are repressurized, our exploitation programs proceed with 3D seismic reservoir characterization and horizontal drilling. In the third quarter, five 3D seismic shoots were completed in the Williston Basin and this winter we will proceed with the drilling of a minimum of five horizontal development wells. Oil reservoir analysis and exploitation programs

form an important part of Zargon's growth strategy and, over the years, have provided steady growth from a portfolio of long-life shallow-decline properties.

Zargon is planning a very active drilling program in the 2003 fourth quarter. Five net wells originally scheduled for September were deferred to October and have now been drilled. During the remainder of the year an additional ten net wells are projected to be drilled, resulting in a 2003 well count total of approximately 37 net wells. Capital expenditures will continue to focus on expanding our natural gas exploration activities in West Central Alberta, while maintaining steady natural gas production rates from East Central Alberta. Oil expenditures will continue to be directed to the efficient exploitation of our large Williston Basin oil development and waterflood project inventory.

ACQUISITIONS/DISPOSITIONS

The largest property acquisition made in the first nine months of 2003 was the \$4.95 million Cdn. purchase of a 92.5 percent interest in the Truro Unit in Renville County, North Dakota. The Unit is currently producing about 200 barrels of oil per day net to Zargon, of long-life production and has good exploitation potential. Total property acquisitions for the period were \$7.82 million and were largely offset by \$5.16 million realized through the sale of small, non-core properties as Zargon took advantage of the opportunities presented by an extremely strong property market. As an additional benefit, these dispositions plus those made in the fourth quarter of 2002 have had a major impact in delivering the current trend of improving per unit operating costs.

GUIDANCE*

Last May, Zargon provided 2003 year-end production guidance at 3,600 barrels of oil per day and 26.5 million cubic feet of natural gas per day, for a combined rate of 8,020 barrels of equivalent per day. In the 2003 third quarter, Zargon tied-in more than five million cubic feet per day of West Central Alberta natural gas production at the Peace River Arch and Pembina project areas, taking current rates to more than 28 million cubic feet per day. Current oil production remains at the average third quarter rate of approximately 3,350 barrels per day. Oil production gains should come late in the fourth quarter from Williston Basin drilling at Frys and Pinto, Saskatchewan plus Haas, North Dakota, but oil production volumes may not reach exit rate guidance levels until the first quarter of 2004. Natural gas production volumes are anticipated to exceed the 28 million cubic feet per day level throughout the fourth quarter, and on an equivalent basis average fourth quarter production is anticipated to exceed exit rate guidance levels.

Zargon's 2004 capital program budget is to be primarily sourced from cash flow and has been initially set at \$45 million with the drilling of 45 net wells. This budget is allocated \$40 million to exploration and development field activities and \$5 million to property acquisitions. The budget reflects our view that the current property acquisition market is fully priced. Should value added property or corporate acquisitions become available, our unutilized \$40 million of bank lines would permit us to greatly expand the acquisition component of our budget.

Based on the \$45 million capital budget, mid-year 2004 production guidance has been set at 30 million cubic feet of natural gas per day and 3,750 barrels of oil per day, for a combined rate of 8,750 barrels of equivalent per day, which would represent a 16 percent gain over the 2003 mid-year guidance levels. Natural gas production gains are forecast from exploration-related growth in the West Central Alberta exploration initiatives at the Peace River Arch, Pembina and Highvale properties. Oil production gains are projected from Williston Basin exploitation horizontal drilling and/or Williston Basin property acquisitions.

We are pleased to report that J. Graham Weir of Calgary has joined the Zargon Board of Directors as of October 15, 2003. Graham has had broad experience at a senior level in corporate finance, most recently with Raymond James Ltd. in Calgary, with a focus on the oil and gas industry. While at Goepel Shields in 1993, he played a lead role in Zargon's initial public offering and has continued to support our activities. Graham holds an M.Sc in actuarial mathematics and is working part time on an advanced degree from Oxford. He is currently an officer and director of Graymont Limited and a director of two junior companies. We look forward to his participation with Zargon.

** Please see comments on "Forward Looking Statements" on the last page of this report.*

MANAGEMENT'S
DISCUSSION AND
ANALYSIS

Management's discussion and analysis (MD&A) should be read in conjunction with the unaudited interim financial statements for the three and nine months ended September 30, 2003 and the audited consolidated financial statements and MD&A for the year ended December 31, 2002. The calculation of barrels of equivalent (boe) is based on the conversion ratio that one barrel of oil is equivalent to six thousand cubic feet of natural gas.

FINANCIAL ANALYSIS

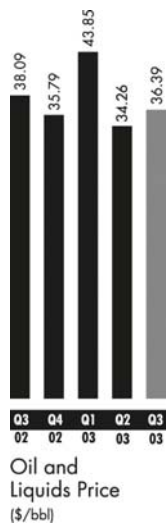
In the first nine months of 2003 Zargon increased oil and liquids production by 11 percent and natural gas production by 22 percent over the 2002 comparative period. The gain in oil and liquid volumes generally came from Williston Basin exploitation drilling and acquisitions while the expanded natural gas volumes were primarily the result of successful West Central Alberta natural gas exploration initiatives. These production gains were enhanced by a 102 percent improvement in field gas prices to \$6.63 per thousand cubic feet, and a 12 percent increase in oil prices to \$37.95 per barrel when compared to the 2002 nine month period. The result of these production gains and price improvements were record nine month 2003 revenues of \$77.15 million, a 72 percent improvement over the \$44.87 million recorded in the 2002 comparative period.

Similarly, third quarter 2003 revenues of \$23.76 million were 43 percent higher than the 2002 third quarter revenues due to a combination of higher natural gas prices and improved oil and natural gas volumes. Compared to the 2003 second quarter, revenues declined by two percent as the impact of increased natural gas production volumes was more than offset by lower natural gas prices.

Zargon's commodity price risk management policy uses forward sales, options and costless collars for, on average, 20 to 30 percent of our net oil and natural gas sales in order to partially offset the effects of large price fluctuations. The net hedging loss of \$2.22 million experienced in the first quarter of 2003 declined to a \$0.47 million loss in the second quarter and a \$0.35 million loss in the third quarter. The first quarter hedging losses were especially large due to certain fixed price natural gas swaps and collars whose price levels had been greatly exceeded by the first quarter's extremely high natural gas prices. For the first nine months of 2003, the net hedging loss was \$3.05 million compared to a gain of \$1.38 million in first nine months of 2002 when natural gas prices were substantially lower.

Royalties, inclusive of Alberta Royalty Tax Credit and Saskatchewan Resource Surcharge, were \$5.70 million for the third quarter of 2003, an increase of 13 percent from the second quarter and an increase of 49 percent from \$3.82 million in the 2002 third quarter. The increase over the prior year quarter is due primarily to a corresponding 43 percent gain in revenue. As a percentage of gross revenue, third quarter 2003 royalties were 24.0 percent of revenue compared to 20.9 percent in the second quarter and 23.0 percent in the 2002 period. In the current year, significant natural gas production gains have come from high rate wells that incur a higher royalty rate. For the first nine months, royalties of \$16.99 million were 73 percent higher than the 2002 first nine months, corresponding to a 72 percent increase in revenue.

Production expenses were \$4.34 million in the 2003 third quarter, a nine percent increase from the second quarter and five percent higher than the third quarter of 2002. However, on a unit of production basis, 2003 production expenses have improved significantly, showing response to field cost containment initiatives and a disposition program of non-core, higher cost properties. Third quarter 2003 production costs were \$6.32 per barrel of equivalent compared to \$6.05 per barrel of equivalent in the 2003 second quarter and \$6.98 per barrel of equivalent the 2002 third quarter. For the first nine months of 2003, production costs were \$6.34 per barrel of equivalent, a three percent decrease from the same period 2002 levels, and a six percent decrease from the 2002 annual rate of \$6.75 per barrel.



OPERATING NETBACKS

Nine months ended September 30	2003		2002	
	Oil and Liquids (\$/bbl)	Natural Gas (\$/mcf)	Oil and Liquids (\$/bbl)	Natural Gas (\$/mcf)
Revenue	37.95	6.63	33.98	3.28
Hedging	(1.10)	(0.31)	(0.16)	0.28
Royalties	(7.53)	(1.58)	(6.64)	(0.84)
Production costs	(8.97)	(0.69)	(9.33)	(0.67)
Operating netbacks	20.35	4.05	17.85	2.05

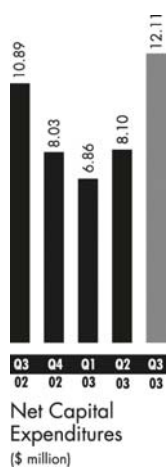
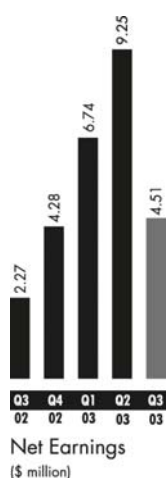
General and administrative expenses of \$0.88 million in the third quarter of 2003 were 14 percent above the second quarter and 13 percent below the 2002 third quarter. On a unit of production basis, general and administrative costs in the first nine months of 2003 decreased 22 percent to \$1.28 per barrel of equivalent as compared to \$1.64 per barrel of equivalent in the first nine months of 2002 and \$1.49 per barrel of equivalent for all of 2002. This encouraging trend in general and administrative costs on a unit of production basis is due to increased production volumes, increased general and administrative cost recoveries from expanded field capital programs, and the disposition of a substantial number of small, overhead-intensive properties.

CORPORATE NETBACKS

Nine months ended September 30 (\$/boe)	2003	2002
Revenue	38.96	26.46
Hedging	(1.54)	0.81
Royalties	(8.58)	(5.80)
Production costs	(6.34)	(6.53)
Operating netbacks	22.50	14.94
General and administrative	(1.28)	(1.64)
Interest	(0.33)	(0.47)
Foreign exchange	0.07	–
Capital and current income taxes	(0.20)	(0.21)
Cash flow netbacks	20.76	12.62
Depletion and depreciation	(6.44)	(5.70)
Site restoration	(0.50)	(0.56)
Unrealized foreign exchange	0.04	(0.05)
Future income taxes	(3.50)	(2.54)
Net earnings	10.36	3.77

Depletion and depreciation expense for the third quarter of 2003 of \$4.67 million was 13 percent higher than the second quarter and 34 percent above third quarter 2002, due in part to increased production volumes. Comparisons on a unit of production basis show an eight percent increase over the 2003 second quarter and a 16 percent increase over the 2002 third quarter to \$6.79 per barrel of equivalent. The increase in unit charges reflects the ongoing industry-wide trend, also experienced by Zargon, to higher finding and development costs.

Cash flow from operations in third quarter 2003 of \$12.34 million (see note below) was 59 percent higher than the 2002 third quarter levels due to the effect of higher natural gas prices and higher production volumes. Third quarter 2003 cash flow from operations was however nine percent lower than in the preceding second quarter, because of a 15 percent decrease in natural gas prices. Strong prices and higher production volumes have provided record cash flow from operations for the first nine months of 2003 on both a corporate and per share basis. For the first nine months of 2003, cash flow from operations of \$41.10 million (\$2.24 per diluted share) showed a gain of 92 percent from the prior year's nine-month period.



Future taxes were \$2.61 million for the third quarter of 2003, an increase of 63 percent from the 2002 third quarter and a very large increase from the near-zero provision in the 2002 second quarter. The increase from the prior year quarter basically reflects an 82 percent increase in earnings before taxes while the second quarter 2003 future taxes were distorted by an adjustment resulting from future federal tax rate reductions. These tax changes and their effects on Zargon's tax provisions were described in detail in our 2003 second quarter report.

Earnings are normally leveraged to cash flow and the combined effect of high cash flow from operations and favourable tax changes increased third quarter 2003 earnings to \$4.51 million, approximately double the earnings reported in third quarter 2002. Comparisons with the preceding 2003 quarter are distorted by the major future tax adjustments booked in that quarter. For the first nine months of 2003, the strong prices and higher production volumes experienced plus the favourable tax changes provided record earnings of \$20.50 million, a 220 percent increase from the prior year period. Earnings per diluted share were \$1.12 for the 2003 nine month period and \$0.36 for the same 2002 period, a 211 percent gain.

Note: Cash flow from operations is a non-GAAP term that represents net earnings adjusted for non-cash items. The Company evaluates its performance based on net earnings and cash flow from operations. The Company considers cash flow from operations to be a key measure as it demonstrates the Company's ability to generate the cash necessary to repay debt or fund future growth through capital investment. Cash flow from operations per share is calculated using the diluted weighted average number of shares for the period.

CAPITAL EXPENDITURES

Nine months ended September 30 (\$ million)	2003	2002
Undeveloped land	5.96	3.00
Geological and geophysical (seismic)	4.11	1.75
Drilling and completion of wells	9.72	6.11
Well equipment and facilities	4.62	3.09
Exploration and development	24.41	13.95
Property acquisitions	7.82	6.28
Property dispositions	(5.16)	(0.10)
Net property acquisitions	2.66	6.18
Hadrian acquisition assigned to property and equipment	-	7.39
Total capital expenditures (net)	27.07	27.52

LIQUIDITY AND CAPITAL RESOURCES

Zargon's capital expenditure program has expanded steadily throughout 2003, from \$6.86 million in the first quarter to \$8.10 million in the second and \$12.11 million in the third quarter, reaching \$27.07 million for the first nine months. The exploration program in the first half of 2003 was constrained by a combination of strategic resource allocations and a long, wet spring that deferred field activities. For the first nine months of 2003, net capital expenditures were \$27.07 million with \$24.41 million attributed to exploration and development costs. Total net capital expenditures in the 2003 nine month period were approximately equal to those in the corresponding 2002 period but were significantly different in allocation. In 2003, Zargon's \$7.82 million of property acquisitions were offset by dispositions of a number of small non-core properties aggregating \$5.16 million. Consequently, net property acquisitions totaling \$2.66 million were only 20 percent of the 2002 corresponding period's total property and corporate acquisitions of \$13.57 million. In 2003, the only significant property acquisition was the second quarter \$4.95 million Cdn. purchase of the Truro Unit in North Dakota.

The 2003 exploration and development spending of \$24.41 million represented an increase of 75 percent over the \$13.95 million spent in the corresponding nine months of 2002 and demonstrates Zargon's current emphasis on internally generated field activities. Reflecting Zargon's expanded focus on exploration, Zargon spent \$10.07 million on undeveloped land and geological/geophysical expenditures in the first nine months of 2003,

a 112 percent increase over the \$4.75 million spent in 2002. The continuing high cash flows in the 2003 period of \$41.10 million funded the full capital expenditure program while still applying \$16.36 million to the reduction of bank debt. At September 30, 2003, Zargon's debt net of working capital had declined to \$13.81 million, an amount equivalent to less than four months of the current cash flow from operations.

As at November 18, 2003, Zargon has issued 17.90 million common shares and has granted stock options to acquire an additional 1.37 million shares.

CAPITAL SOURCES

Nine months ended September 30 (\$ million)	2003	2002
Cash flow from operations	41.10	21.41
Changes in working capital and other	1.42	(4.41)
Change in bank indebtedness	(16.36)	4.57
Issuance of common shares	0.91	5.95
Total capital sources	27.07	27.52

OUTLOOK

Zargon's strong financial position and ongoing successful natural gas exploration and oil exploitation programs provide much encouragement for the future. Although oil and natural gas prices have receded from record levels, current prices remain very strong. The combination of an unlevered balance sheet and the large 2003 cash flows provide financial resources that will continue to be deployed on our exploration and exploitation growth programs and can still fund a sizeable acquisition if and when value-added opportunities become available.

(\$ million, except per share amounts)

Quarter	Net Earnings	Earnings/ Diluted Share	Cash Flow	Cash Flow/ Diluted Share	Production Revenue	Total Assets	Bank Debt
2003 Q3	\$4.51	\$0.24	\$12.34	\$0.67	\$23.76	\$166.89	\$8.92
2003 Q2	\$9.25	\$0.51	\$13.53	\$0.74	\$24.20	\$160.05	\$11.47
2003 Q1	\$6.74	\$0.37	\$15.23	\$0.84	\$29.19	\$159.34	\$20.78
2002 Q4	\$4.28	\$0.24	\$10.71	\$0.59	\$20.67	\$153.66	\$25.28
2002 Q3	\$2.27	\$0.13	\$7.75	\$0.43	\$16.65	\$146.00	\$28.71
2002 Q2	\$2.55	\$0.14	\$7.47	\$0.42	\$15.50	\$137.76	\$28.00
2002 Q1	\$1.58	\$0.09	\$6.19	\$0.36	\$12.73	\$128.97	\$25.26
2001 Q4	\$1.77	\$0.10	\$5.81	\$0.34	\$11.18	\$127.93	\$24.14
2001 Q3	\$2.60	\$0.15	\$7.66	\$0.44	\$14.67	\$119.06	\$19.27

"Signed" C.H. Hansen
President and Chief Executive Officer

Calgary, Alberta
November 18, 2003

CONSOLIDATED
BALANCE SHEETS

(\$ thousand)

September 30, 2003 December 31, 2002

(unaudited)

ASSETS

Current

Accounts receivable	11,089	11,942
Prepaid expenses and deposits	485	712

Property and equipment, net

LIABILITIES

Current

Bank indebtedness	8,919	25,279
Accounts payable and accrued liabilities	16,465	16,118

Future site restoration

Future income taxes (note 8)

	5,650	4,746
	27,846	20,922

SHAREHOLDERS' EQUITY

Share capital (note 3)	41,911	40,997
Retained earnings	66,098	45,598

	108,009	86,595
	166,889	153,660

See accompanying selected notes

CONSOLIDATED
STATEMENTS OF
EARNINGS AND
RETAINED EARNINGS

(unaudited)	Three months ended September 30		Nine months ended September 30	
	2003	2002	2003	2002
(\$ thousand, except per share amounts)				
Revenue				
Oil and gas sales	23,755	16,647	77,146	44,873
Hedging (note 7)	(354)	447	(3,050)	1,381
Royalties	(5,695)	(3,821)	(16,991)	(9,831)
	17,706	13,273	57,105	36,423
Expenses				
Production	4,344	4,146	12,550	11,077
General and administrative	876	1,003	2,530	2,776
Interest	152	262	661	803
Foreign exchange	69	75	(210)	84
Site restoration	344	333	990	950
Depletion and depreciation	4,667	3,475	12,759	9,671
	10,452	9,294	29,280	25,361
Earnings before taxes	7,254	3,979	27,825	11,062
Taxes				
Future (note 8)	2,607	1,596	6,924	4,306
Current	133	116	401	359
	2,740	1,712	7,325	4,665
Net earnings for the period	4,514	2,267	20,500	6,397
Retained earnings, beginning of period	61,584	39,049	45,598	34,919
Retained earnings, end of period	66,098	41,316	66,098	41,316
Earnings per common share (note 4)				
Basic	0.25	0.13	1.15	0.37
Diluted	0.24	0.13	1.12	0.36

See accompanying selected notes

CONSOLIDATED
STATEMENTS OF
CASH FLOW

(unaudited)	Three months ended		Nine months ended	
	September 30	2002	September 30	2002
2003	2003	2003	2003	2002
(\$ thousand)				
Operating activities				
Net earnings for the period	4,514	2,267	20,500	6,397
Add non-cash items:				
Depletion and depreciation	4,667	3,475	12,759	9,671
Site restoration	344	333	990	950
Unrealized foreign exchange	209	75	(70)	84
Future income taxes	2,607	1,596	6,924	4,306
Cash flow from operations	12,341	7,746	41,103	21,408
Changes in non-cash working capital	(853)	(536)	306	(1,225)
	11,488	7,210	41,409	20,183
Financing activities				
Advances (repayment) of bank indebtedness	(2,555)	708	(16,360)	4,570
Exercise of stock options	88	37	914	955
	(2,467)	745	(15,446)	5,525
Investing activities				
Additions to property and equipment	(12,218)	(10,901)	(32,223)	(20,233)
Proceeds on disposal of property and equipment	110	15	5,155	97
Acquisition of Hadrian Energy Corp. (cash portion)	-	-	-	(4,857)
Site restoration expenditures	(35)	(157)	(86)	(204)
Changes in non-cash working capital	3,122	3,088	1,191	(712)
	(9,021)	(7,955)	(25,963)	(25,909)
Decrease in cash	-	-	-	(201)
Cash, beginning of period	-	-	-	201
Cash, end of period	-	-	-	-

See accompanying selected notes

SELECTED NOTES TO
CONSOLIDATED
FINANCIAL
STATEMENTS

For the three and nine months
ended September 30, 2003
and 2002 (unaudited)

1. BASIS OF PRESENTATION

The interim consolidated financial statements of Zargon Oil & Gas Ltd. (the "Corporation") 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 in computation as the consolidated financial statements for the fiscal year ended December 31, 2002. The interim consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto in the Corporation's annual report for the year ended December 31, 2002.

2. ACQUISITION

On June 17, 2002, the Corporation acquired all of the outstanding shares of Hadrian Energy Corp. ("Hadrian"), a private oil and gas company, for \$9.60 million. Consideration consisted of \$4.745 million cash and the issuance of 542,340 Zargon common shares valued at \$8.75 per share. Costs of \$0.112 million were incurred to effect the transaction and were charged to share capital. The acquisition was accounted for by the purchase method and the purchase price has been allocated as follows:

(\$ thousand)	2002
Working capital	(816)
Property and equipment	7,386
Future tax asset	3,792
Future site restoration	(760)
Total consideration	<u>9,602</u>

3. SHARE CAPITAL

The Corporation is authorized to issue an unlimited number of common shares with no par value and an unlimited number of first preferred shares and second preferred shares.

Common Shares

(thousand)	September 30, 2003		September 30, 2002	
	Number of Shares	Amount (\$)	Number of Shares	Amount (\$)
Shares issued				
Balance, beginning of year	17,637	40,997	16,666	35,066
Shares issued for Hadrian	-	-	542	4,658
Stock options exercised	253	914	327	955
Balance, end of period	17,890	41,911	17,535	40,679

A summary of the status of the Corporation's stock option plans as at September 30, 2003 and 2002, and changes during the nine months ended on those dates is presented below:

Stock Options

	September 30, 2003		September 30, 2002	
	Weighted Number of Shares (thousand)	Average Exercise Price (\$)	Weighted Number of Shares (thousand)	Average Exercise Price (\$)
Outstanding at beginning of year	1,215	5.10	1,199	3.36
Granted	429	9.36	454	7.66
Exercised	(253)	3.61	(327)	2.92
Cancelled	(22)	9.30	(9)	7.25
Outstanding at end of period	1,369	6.64	1,317	4.92
Options exercisable at end of period	944	5.42	852	3.43

Stock Based Compensation

The Corporation recognizes no compensation expense when stock options are granted to employees and directors. Pro forma information regarding net earnings is required and has been determined as if the Corporation had accounted for its stock options granted after December 31, 2001 under the fair value method. The fair value for these options was estimated at the date of grant using a Black-Scholes Option Pricing Model.

The assumptions made for the options granted in the three month period ended September 30, 2003 include a volatility factor of expected market price of 20.80 percent, a weighted average risk-free interest rate of 3.53 percent, no dividend yield and a weighted average expected life of options of four years.

For purposes of pro forma disclosures, the estimated fair value of options is amortized to expense over the options' vesting periods. The Corporation's net earnings would be reduced by \$75,000 for the three months ended September 30, 2003 and \$400,000 for the nine months ended September 30, 2003. Basic and diluted earnings per share figures would have both been unchanged for the 2003 quarter and would have both been reduced by \$0.02 for the 2003 nine months.

Comparatively, the Corporation's prior period net earnings would be reduced by \$159,000 for the three months ended September 30, 2002 and \$464,000 for the nine months ended September 30, 2002. Basic and diluted earnings per share figures would have both been reduced by \$0.01 for the 2002 quarter and by \$0.03 for the 2002 nine months.

4. WEIGHTED AVERAGE NUMBER OF COMMON SHARES

(thousand)	Three months ended September 30		Nine months ended September 30	
	2003	2002	2003	2002
Basic	17,867	17,527	17,788	17,104
Diluted	18,430	18,081	18,324	17,695

5. SEGMENTED INFORMATION

(\$ thousand)	Three months ended September 30		Nine months ended September 30	
	2003	2002	2003	2002
Oil and Gas Sales				
Canada	20,685	14,588	68,465	39,680
United States	3,070	2,059	8,681	5,193
Total	23,755	16,647	77,146	44,873
Net Capital Expenditures				
Canada	11,827	10,234	21,546	26,849
United States	281	652	5,522	673
Total	12,108	10,886	27,068	27,522
Total Assets				
Canada			157,384	140,540
United States			9,505	5,463
Total			166,889	146,003

6. SUPPLEMENTAL CASH FLOW INFORMATION

(\$ thousand)	Three months ended September 30		Nine months ended September 30	
	2003	2002	2003	2002
Cash interest paid	117	159	540	926
Cash taxes paid	37	117	305	359

7. FINANCIAL INSTRUMENTS

The Corporation is a party to certain off-balance sheet derivative financial instruments which have fixed the price of a portion of its oil and natural gas production. The Corporation enters into these contracts for hedging purposes only, in order to protect a portion of its future Canadian cash flow from the volatility of crude oil and natural gas commodity prices.

The Corporation enters into currency contracts for hedging purposes because the price received for its products varies in close relationship to the US dollar currency exchange rate.

The Corporation has outstanding contracts at September 30, 2003 as follows:

	Volume	Rate	Price	Range of Terms
Oil swaps	64,400 bbl	700 bbl/d	\$24.96 US/bbl	Oct. 1/03 – Dec. 31/03
	36,400 bbl	200 bbl/d	\$26.44 US/bbl	Jan. 1/04 – Jun. 30/04
Oil collars	36,400 bbl	200 bbl/d	\$22.50 US/bbl Put \$26.85 US/bbl Call	Jan. 1/04 – Jun. 30/04
	36,400 bbl	200 bbl/d	\$24.00 US/bbl Put \$27.65 US/bbl Call	Jan. 1/04 – Jun. 30/04
Natural gas swaps	36,800 bbl	200 bbl/d	\$24.00 US/bbl Put \$27.80 US/bbl Call	Jul. 1/04 – Dec. 31/04
	62,000 gj	2,000 gj/d	\$4.85/gj	Oct. 1/03 – Oct. 31/03
Natural gas put	304,000 gj	2,000 gj/d	\$7.50/gj	Nov. 1/03 – Mar. 31/04
	428,000 gj	2,000 gj/d	\$5.10/gj	Apr. 1/04 – Oct. 31/04
Natural gas put	456,000 gj	3,000 gj/d	\$5.00/gj	Nov. 1/03 – Mar. 31/04
Natural gas collars	62,000 gj	2,000 gj/d	\$4.00/gj Put \$6.10/gj Call	Oct. 1/03 – Oct. 31/03
	152,000 gj	1,000 gj/d	\$5.50/gj Put \$7.90/gj Call	Nov. 1/03 – Mar. 31/04
Currency collar	428,000 gj	2,000 gj/d	\$5.00/gj Put \$6.85/gj Call	Apr. 1/04 – Oct. 31/04
	\$1,000,000 Cdn./month	–	\$1.56 Put \$1.62 Call	Oct. 1/03 – Dec. 31/03

8. TAX RATE ADJUSTMENT

In the March 2003 budget, the Government of Canada announced federal corporate income tax changes affecting resource companies to be phased in over a five year period that include reducing the federal tax rate from 28% to 21%, allowing the deductibility of crown charges and eliminating the resource allowance. As a result of both federal and provincial corporate income tax changes, which are considered to be "substantively enacted" for Canadian GAAP purposes, the provision for future income taxes for the three months ended June 30, 2003 and nine months ended September 30, 2003 include a recovery and liability reduction in the amount of \$3.59 million.

CORPORATE
INFORMATION

BOARD OF DIRECTORS

Craig H. Hansen
Calgary, Alberta

K. James Harrison
Oakville, Ontario

H. Earl Joudrie
Toronto, Ontario

Kyle D. Kitagawa
Calgary, Alberta

John O. McCutcheon
Vancouver, British Columbia

James D. Peplinski
Calgary, Alberta

Byron J. Seaman
Calgary, Alberta

J. Graham Weir
Calgary, Alberta

William J. Whelan
Calgary, Alberta

Grant A. Zawalsky
Calgary, Alberta

OFFICERS

John O. McCutcheon
Chairman

Craig H. Hansen
President and Chief Executive Officer

Mark I. Lake
Vice President, Exploration

Daniel A. Roulston
Vice President, Operations

Sheila A. Wares
Vice President, Accounting

Kenneth W. Young
Vice President, Land

STOCK EXCHANGE LISTING

The Toronto Stock Exchange
Trading Symbol: ZAR

TRANSFER AGENT

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Forward Looking Statements – Certain information regarding Zargon set forth in this document, including management's assessment of Zargon's future plans and operations, contains forward-looking statements that involve substantial known and unknown risks and uncertainties. These forward-looking statements are subject to numerous risks and uncertainties, certain of which are beyond Zargon's control, including the impact of general economic conditions, industry conditions, volatility of commodity prices, currency fluctuations, imprecision of reserve estimates, environmental risks, competition from other producers, the lack of availability of qualified personnel or management, stock market volatility and ability to access sufficient capital from internal and external sources. Zargon's actual results, performance or achievement could differ materially from those expressed in, or implied by, these forward-looking statements and, accordingly, no assurance can be given that any of the events anticipated by the forward-looking statements will transpire or occur, or if any of them do so, what benefits that Zargon will derive therefrom.