

## HIGHLIGHTS

Zargon achieved record revenue, cash flow, and earnings in 2000.

| (\$ million, except per share amounts) | 2000  | 1999  | Percent Change |
|----------------------------------------|-------|-------|----------------|
| Production revenue                     | 53.31 | 24.05 | 122            |
| Cash flow from operations              | 27.50 | 10.64 | 158            |
| Per fully diluted share (\$)           | 1.77  | 0.70  | 153            |
| Earnings                               | 11.26 | 4.26  | 164            |
| Per fully diluted share (\$)           | 0.73  | 0.29  | 152            |
| Net capital expenditures               | 30.51 | 16.95 | 80             |

## DETAILED FINANCIAL ANALYSIS

### PRODUCTION REVENUE

Petroleum and natural gas revenue exclusive of hedges climbed 122 percent to \$53.31 million in 2000 from \$24.05 million in 1999 (\$14.26 million in 1998). Sharply higher oil prices, gas prices, and gas volumes all contributed to the significant increase in 2000 revenues.

Production revenue in 2000 was allocated 52 percent to the sale of natural gas and 48 percent to the sale of oil and liquids. The natural gas revenue allocation was up from a 35 percent weighting in 1999 and a 31 percent weighting in 1998. Increased gas volumes in 2001 will continue this trend to a more pronounced weighting to natural gas revenues.

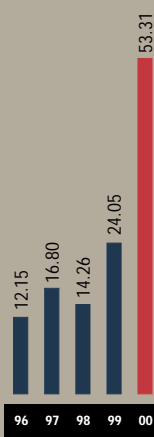
### CRUDE OIL PRICING

Canadian crude oil and liquid prices are referenced to an Edmonton light sweet reference price that is adjusted for transportation charges and oil quality differentials to arrive at an average Zargon field price. In 2000, Zargon's average oil and liquid field price, exclusive of price hedges, increased \$15.71 per barrel or 63 percent to \$40.73 per barrel. Zargon's blended average crude density is 30 degrees API. The field price for this blended crude stream averaged \$3.60 per barrel less than the Edmonton reference crude price, which compares to the 1999 differential of \$2.33 per barrel. The higher differential reflected the industry prevalent trend to the higher discounting of heavier gravity crude in the fourth quarter of 2000.

### NATURAL GAS PRICING

During 2000, Zargon's natural gas field price, exclusive of price hedges increased a remarkable 107 percent to \$5.20 per thousand cubic feet compared to \$2.52 per thousand cubic feet in 1999 and \$1.93 per thousand cubic feet in 1998. Approximately 50 percent of Zargon's gas production was sold under aggregator contracts with TransCanada Energy Ltd. (Jarrow – 37 percent) and ProGas Limited (Hamilton Lake – 13 percent). This total is down from the aggregators' 70 percent share in 1999. The bulk of the remaining volumes were sold by spot sale contracts and received Alberta index prices. As Zargon continues to develop new gas reserves outside of the original Jarrow and Hamilton Lake aggregator contract areas, it is anticipated that the aggregator share of total production will continue to decline.

Revenue  
(\$ million)



## HEDGING ACTIVITIES

Crude oil and natural gas prices climbed sharply throughout 2000 to levels well beyond expectations. Historically, Zargon has reduced pricing risk by employing a forward sales (hedging) program for up to 30 percent of its oil and natural gas volumes. In 2000, these hedging activities resulted in a reduction in revenue of \$2.73 million, compared to a \$1.10 million reduction in revenue reported in 1999.

During the year, crude oil and currency hedges resulted in a \$1.62 million reduction of 2000 revenues, which is equivalent to a \$2.56 per barrel charge against the year's total oil and liquid production. Natural gas hedges reduced Zargon's 2000 revenues by \$1.11 million, which is equivalent to a \$0.21 per thousand cubic feet charge against the year's total natural gas production. For 2001, Zargon has initiated a put option strategy to reduce commodity pricing risk. This strategy will allow for the retention of the upside associated with higher than anticipated prices. Approximately 10 percent of Zargon's projected 2001 natural gas and oil volumes remain hedged at levels less than current prices.

## ROYALTIES

Royalties include payments made to the Crown, freehold owners and third parties. Reported royalties include the offsets of credits received through the Alberta Royalty Tax Credit (ARTC) program and the cost of the Saskatchewan Resource Surcharge (SRC). During 2000, total royalties were \$10.72 million, up 166 percent from the \$4.03 million reported in 1999 (\$1.84 million in 1998). Royalties as a percentage of gross revenue (before hedging adjustments) increased to 20.1 percent up from 16.8 percent in 1999 and 12.9 percent in 1998. This substantial increase reflected the impact of the higher oil and gas prices on royalty rates and the increased production volumes from the more highly encumbered Jarrow, Alberta gas property.

During the year, 61 percent of the total royalties were paid to provincial governments with the remainder paid to freehold owners and other third parties. Royalties payable to the Province of Alberta on qualifying properties are reduced through the ARTC program. Zargon received a \$0.52 million ARTC rebate in 2000 compared to \$0.57 million of ARTC in 1999. Due to higher crude volumes and the sharply higher crude prices, the SRC charges increased to \$0.30 million in 2000, up from the prior year's charge of \$0.21 million.

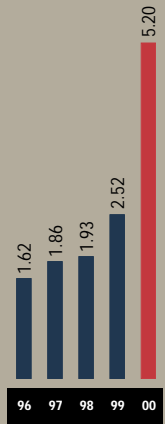
## PRODUCTION EXPENSES

Zargon's production expenses increased 41 percent to \$8.62 million in 2000. On a unit of production basis, expenses increased 16 percent to \$7.41 per barrel of equivalent from \$6.39 per barrel of equivalent in 1999 (\$6.50 per barrel of equivalent in 1998).

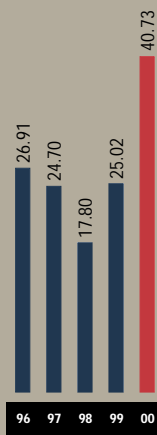
Production expenses for natural gas held steady at \$0.59 per thousand cubic feet compared to \$0.57 per thousand cubic feet in 1999 (\$0.61 per thousand cubic feet in 1998). During the year the benefit of increased Jarrow gas volumes was offset by increased compression leasing costs and third party gas processing charges.

Production expenses for crude oil of \$8.69 per barrel were 29 percent higher than the prior year's \$6.74 per barrel expense (\$6.68 per barrel in 1998). The year's much higher costs were a function of prior year adjustments on non-operated properties, reactivation costs to initiate production in shut-in wells that became economic to produce due to sharply higher crude prices, and additional cost pressures relating to third party services including electrical power. In 2001, Zargon will focus on reversing this concerning upward trend in oil production expenses.

Natural Gas Prices (\$/mcf)



**Oil and  
Liquid Prices  
(\$/bb)**



**OPERATING NETBACKS**

The sharply higher 2000 oil and natural gas prices resulted in very large increases in operating netbacks, despite increases in effective royalty rates and oil production expenses. During the year, Zargon's oil netback increased by 59 percent to \$20.92 per barrel from \$13.15 per barrel in 1999 (\$9.21 per barrel in 1998). Natural gas netbacks improved 152 percent to \$3.43 per thousand cubic feet from \$1.36 per thousand cubic feet in 1999 (\$1.10 per thousand cubic feet in 1998). On an equivalent basis (10:1), operating netbacks increased 101 percent to \$26.90 per barrel of equivalent up from \$13.35 per barrel of equivalent in 1999 (\$9.63 per barrel of equivalent in 1998).

**Operating Netbacks**

|                                                         | 2000                       |                         |                              | 1999                       |                         |                              |
|---------------------------------------------------------|----------------------------|-------------------------|------------------------------|----------------------------|-------------------------|------------------------------|
|                                                         | Oil and Liquids<br>(\$/bb) | Natural Gas<br>(\$/mcf) | Equivalents<br>(\$/boe 10:1) | Oil and Liquids<br>(\$/bb) | Natural Gas<br>(\$/mcf) | Equivalents<br>(\$/boe 10:1) |
| Revenues (adjusted for oil,<br>gas and currency hedges) | 38.17                      | 5.02                    | 43.53                        | 23.72                      | 2.42                    | 23.95                        |
| Royalties (net of ARTC and SRC)                         | (8.56)                     | (1.00)                  | (9.22)                       | (3.83)                     | (0.49)                  | (4.21)                       |
| Operating costs                                         | (8.69)                     | (0.59)                  | (7.41)                       | (6.74)                     | (0.57)                  | (6.39)                       |
| Operating netbacks                                      | 20.92                      | 3.43                    | 26.90                        | 13.15                      | 1.36                    | 13.35                        |

**GENERAL AND ADMINISTRATION EXPENSES**

Gross general and administration costs increased 32 percent in 2000 to \$3.53 million, largely as a result of costs associated with adding staff members and consultants to handle increased activity levels. Higher staff salaries, benefits and office space requirements also added to costs. Increased operated capital activity resulted in an increase in overhead cost recoveries to \$1.34 million. Since 1995, Zargon has maintained a policy of not capitalizing any portion of its general and administrative costs.

**General and Administration Expenses**

| (\$ million)                               | 2000   | 1999   | 1998   |
|--------------------------------------------|--------|--------|--------|
| Gross general and administration expense   | 3.53   | 2.68   | 1.98   |
| Overhead recoveries                        | (1.34) | (1.22) | (0.73) |
| Net general and administration expense     | 2.19   | 1.46   | 1.25   |
| Net expense after recoveries (\$/boe 10:1) | 1.88   | 1.53   | 1.60   |
| Number of employees at year-end            | 24     | 21     | 17     |

General and administration expenses on a unit of production basis increased 23 percent in 2000 to \$1.88 per barrel of equivalent. In 2001, it is anticipated that continued production gains will more than offset increased general and administration costs, and this will result in a small improvement in general and administration costs on a unit of production basis.

**INTEREST EXPENSE**

Zargon's primary borrowings are through its bank line of credit. In 2000, interest expense increased 115 percent to \$1.27 million from \$0.59 million in 1999 (\$0.38 million in 1998). Zargon's effective interest rate was 7.1 percent on an average bank debt of \$18.0 million in 2000, compared to a 6.0 percent effective interest rate on an average bank debt of \$9.8 million in 1999 (6.3 percent on \$6.0 million in 1998). Bank debt increased \$1.78 million in 2000 to \$15.90 million at year-end. In 2001, further moderate bank debt increases are anticipated to result in higher interest expenses.

## CAPITAL AND INCOME TAX

Zargon did not pay current income taxes in 2000, but did remit \$0.29 million of federal and provincial capital taxes (\$0.10 million remitted in 1999). At year-end the Company has \$46 million in resource tax pools available to reduce future taxable income. Since it is anticipated that these pools will not be large enough to shelter all of the 2001 taxable income, it is expected that substantial cash income taxes will be paid in 2001.

## CORPORATE NETBACKS

Driven by sharply higher oil and gas prices, Zargon's corporate netbacks climbed by 114 percent in 2000. Corporate netbacks, defined as operating netbacks less general and administration costs, financial costs and cash taxes, \$23.67 per barrel of equivalent, up from \$11.10 per barrel of equivalent in 1999 (\$7.45 per barrel of equivalent in 1998).

### Corporate Netbacks

| (\$/boe 10:1)                    | 2000   | 1999   | 1998   |
|----------------------------------|--------|--------|--------|
| Operating netbacks               | 26.90  | 13.35  | 9.63   |
| General and administration       | (1.88) | (1.53) | (1.60) |
| Financial charges                | (1.10) | (0.62) | (0.48) |
| Capital and current income taxes | (0.25) | (0.10) | (0.10) |
| Corporate netbacks               | 23.67  | 11.10  | 7.45   |

## CASH FLOW FROM OPERATIONS

Substantially improved prices combined with higher gas production volumes were responsible for a 158 percent increase in Zargon's 2000 cash flow from operations to \$27.50 million as compared to \$10.64 million in 1999 (\$5.82 million in 1998). Seventy-two percent of the year's incremental \$16.86 million gain in cash flow can be attributed to improved price-driven netbacks and the balance to increased production volumes.

Fully diluted cash flow per share climbed 153 percent in 2000 to \$1.77, up from \$0.70 in 1999 and \$0.43 in 1998.

## DEPLETION AND DEPRECIATION

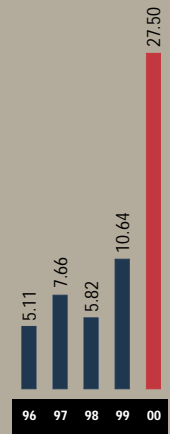
In 2000, Zargon's depletion and depreciation provision increased 18 percent to \$5.85 per barrel of equivalent, up from \$4.96 per barrel of equivalent (\$4.68 per barrel of equivalent in 1998). Depletion, depreciation and site restoration charges calculated on a unit of production method are based on total proven reserves with a conversion of 10 thousand cubic feet of natural gas being equivalent to 1 barrel of oil. The 2000 depletion calculation includes \$3.49 million of future capital expenditures to develop the Company's reserves but excludes \$6.70 million of unproven properties relating to undeveloped land. Using the assumption that 6 thousand cubic feet of natural gas is equivalent to 1 barrel of oil, the 2000 depletion and depreciation charge would be \$4.64 per barrel of equivalent. Zargon's relatively low per unit depletion and depreciation charges are a result of the Company's historically low finding and development costs.

In 2000, Zargon's depletion and depreciation provision increased 43 percent to \$6.80 million as compared to \$4.75 million in 1999 (\$3.66 million in 1998). The higher charges reflected increased production volumes and higher per unit charges relating to both Zargon's and the industry's current trend towards higher finding and development costs.

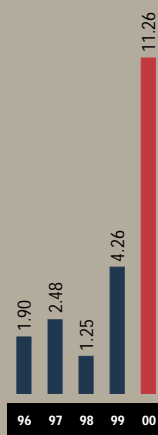
## SITE RESTORATION AND RECLAMATION

Zargon provided for \$0.72 million of site restoration and reclamation charges in 2000 compared to a \$0.59 million provision in 1999 (\$0.48 million in 1998). This charge of \$0.62 per barrel of equivalent (\$0.51 on a 6:1 equivalent basis) is essentially unchanged from the 1999 and 1998 charges of \$0.61 and \$0.62 per barrel of equivalent, respectively. Zargon accrues the estimated future restoration and reclamation charges on a unit of production basis assuming a \$25,000 net after salvage abandonment charge for each net working interest well. Actual

### Cash Flow From Operations (\$ million)



## Earnings (\$ million)



site restoration and reclamation costs incurred in 2000 were \$0.38 million compared to the 1999 expenditures of \$0.18 million (\$0.23 million in 1998).

### FUTURE INCOME TAXES

In accordance with CICA recommendations, Zargon has adopted the liability method of tax allocation in accounting for income taxes in 2000. Zargon's 2000 future taxes increased 730 percent to \$8.71 million from \$1.05 million in 1999 (\$0.43 million in 1998). This very large increase in future taxes reflects the impact of a 274 percent increase in before tax earnings combined with an increase in the effective tax rate to 43 percent from the 1999 tax rate of 20 percent (25 percent in 1998). The 1999 and 1998 effective tax rates had been reduced due to the substantial benefits associated with non-capital losses relating to the 1997 Oasis corporate acquisition.

On a unit of production basis, future income taxes were \$7.50 per barrel of equivalent, up 588 percent from the prior year's future income taxes of \$1.09 per barrel of equivalent (\$0.55 per barrel of equivalent in 1998).

### NET EARNINGS

Zargon's 2000 net earnings were \$11.26 million, a 164 percent increase from the \$4.26 million recorded in 1999 (\$1.25 million in 1998). On a fully diluted per share basis, the 2000 net earnings climbed 152 percent to \$0.73 from the prior year's \$0.29 net earnings (\$0.10 in 1998). The substantial increase in earnings was primarily due to higher natural gas and oil prices plus higher natural gas sales volumes.

### Net Earnings

| (\$/boe 10:1)                    | 2000   | 1999   | 1998   |
|----------------------------------|--------|--------|--------|
| Corporate netbacks               | 23.67  | 11.10  | 7.45   |
| Depletion and depreciation       | (5.85) | (4.96) | (4.68) |
| Site restoration and reclamation | (0.62) | (0.61) | (0.62) |
| Future income taxes              | (7.50) | (1.09) | (0.55) |
| Net earnings                     | 9.70   | 4.44   | 1.60   |

On a unit of production basis, the 2000 net earnings were \$9.70 per barrel of equivalent, which represented a 118 percent increase over the prior year's earnings of \$4.44 per barrel of equivalent (\$1.60 per barrel of equivalent in 1998). In 2000, net earnings represented 41 percent of cash flow, essentially unchanged from a 40 percent ratio in 1999 (21 percent in 2000).

### RETURN ON EQUITY

Zargon's pre-tax return on shareholder's equity in 2000 climbed to 53.5 percent, from 17.2 percent in the previous year (6.5 percent in 1998). The after tax return on shareholder's equity in 2000 improved to 30.0 percent from 13.8 percent in the prior year (4.8 percent in 1998). Zargon's after tax rates of return on equity have averaged 17.8 percent over the past three years and 15.1 percent over the Company's eight-year corporate history.

### CAPITAL EXPENDITURES

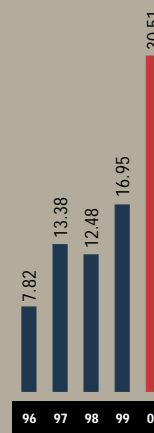
Net capital expenditures in 2000 increased 80 percent to \$30.51 million from the prior year's \$16.95 million (\$12.48 million in 1998). During the year, Zargon continued to support an active exploration program by spending \$5.99 million or 20 percent of the total budget on geological, geophysical and undeveloped land acquisition activities. Zargon's record field activities in 2000 resulted in an expenditure of \$15.06 million or 49 percent of the year's capital allocation to the drilling, and completion of wells and the construction of related facilities.

During the year, Zargon's net property acquisitions increased sharply to \$9.35 million or 31 percent of the total capital program. The majority of these property acquisitions related to oil exploitation opportunities. In 2001, Zargon is projecting to spend \$35 million of capital expenditures with an emphasis on gas exploration and oil exploitation projects.

## Capital Expenditures

| (\$ million)                               | 2000   | 1998   | 1998   |
|--------------------------------------------|--------|--------|--------|
| Property, plant and equipment assets       |        |        |        |
| Undeveloped land                           | 2.93   | 3.98   | 0.81   |
| Geological and geophysical (seismic)       | 3.06   | 1.91   | 0.92   |
| Drilling and completion of wells           | 11.28  | 6.20   | 3.05   |
| Well equipment and facilities              | 3.78   | 2.52   | 1.57   |
| Exploration and development                | 21.05  | 14.61  | 6.35   |
| Property acquisitions                      | 10.09  | 3.70   | 6.57   |
| Property dispositions                      | (0.74) | (1.45) | (0.59) |
| Net property acquisitions                  | 9.35   | 2.25   | 5.98   |
| Total property, plant and equipment assets | 30.40  | 16.86  | 12.33  |
| Administration assets                      | 0.11   | 0.09   | 0.15   |
| Total capital expenditures (net)           | 30.51  | 16.95  | 12.48  |

## Net Capital Expenditures (\$ million)



## LIQUIDITY AND CAPITAL RESOURCES

Zargon relies on three sources of funding to support its capital expenditure programs:

- Internally generated cash flow provides the basic level of funding for the Company's annual capital expenditures program.
- Debt may be utilized to expand capital programs when it is deemed appropriate. The Company maintains a conservative debt policy.
- New equity, if available and if on favourable terms, will be utilized to expand capital programs. Conversely, if Zargon's equity is valued by the stock market at levels perceived to be at a substantial discount to the underlying net asset value, Zargon will consider the repurchase of Zargon shares through an issuer bid.

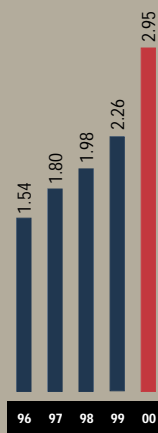
In calendar 2000, over 91 percent of Zargon's capital program was funded by cash flow with the remaining expenditures funded from working capital or by the issuance of debt.

During 2000, Zargon repurchased 340 thousand common shares pursuant to June 1999 and November 2000 issuer bids. Including commissions the total cost for these shares was \$1.19 million, which equates to an average cost of \$3.50 per share. In 1999 the Company had repurchased 388 thousand common shares at an average cost of \$2.71 per share. Pursuant to the Company's stock option plan, Zargon issued 235 thousand shares for \$0.43 million, to employees, consultants and directors of the Company in 2000, at an average cost of \$1.84 per share (nil shares issued in 1999).

## Capital Sources

| (\$ million)                        | 2000   | 1999   | 1998   |
|-------------------------------------|--------|--------|--------|
| Cash flow from operations           | 27.50  | 10.64  | 5.82   |
| Changes in working capital          | 1.98   | (0.57) | (0.16) |
| Bank debt                           | 1.79   | 7.94   | 1.31   |
| Issuance (buyback) of common shares | (0.76) | (1.06) | 5.51   |
| Total capital sources               | 30.51  | 16.95  | 12.48  |

**Shareholders  
Equity  
(\$/share)**



**CASH FLOW**

It is anticipated that the majority of Zargon's 2001 capital budget will be financed through the reinvestment of the Company's cash flow from operations. Cash flow is influenced by factors which the Company cannot control such as commodity prices, the US/Canadian dollar exchange rates and interest rates. Zargon's 2001 sensitivity to moderate fluctuations in these key business parameters is shown in the accompanying table.

**Cash Flow Sensitivities Summary**

|                                                  | Change in 2001 Cash Flow |            |
|--------------------------------------------------|--------------------------|------------|
|                                                  | (\$ million)             | (\$/share) |
| Change of \$1.00 US/bbl in the price of WTI oil  | 0.61                     | 0.04       |
| Change in oil production of 100 bbl/d            | 0.50                     | 0.03       |
| Change of \$0.10/mcf in the price of gas         | 0.62                     | 0.04       |
| Change in gas production of 1 mmcf/d             | 1.12                     | 0.07       |
| Change of \$0.01 in the \$US/\$Cdn exchange rate | 0.61                     | 0.04       |

**BANK DEBT AND LIABILITY**

At December 31, 2000 the Company had lines of credit totalling \$32.60 million of which \$15.90 million was drawn, a 13 percent increase from the prior year-end drawn balance of \$14.12 million. In late March 2001, this line of credit was increased to \$45 million. Reflecting a very active year-end capital program, the Company's working capital deficiency increased to \$2.51 million at December 31, 2000, which compares to the prior year-end's \$0.14 million working capital deficiency.

Zargon's combined debt and working capital deficiency was \$18.41 million at December 31, 2000, which represented a conservative 0.67 times Zargon's 2000 corporate cash flow of \$27.50 million.

**EQUITY**

At year-end 2000, Zargon had 14.31 million shares outstanding. Including the 1.29 million shares reserved (0.84 million exercisable at December 31, 2000) under the Company stock option plan, Zargon's fully diluted year end shares outstanding total 15.60 million.

During 2000, 4.89 million Zargon shares traded on The Toronto Stock Exchange with a high of \$4.65 per share, a low of \$3.00 per share and a close of \$4.45 per share. The 2000 trading statistics represent a 22 percent year over year increase in trading volume, and a 48 percent increase in the closing stock price. Zargon's market capitalization at year-end 2000 was \$64 million.

**BUSINESS RISKS AND OUTLOOK**

**BUSINESS RISKS**

Zargon's external business risks arise from the uncertainty of crude oil and natural gas pricing, the uncertainty of interest and exchange rates, environmental and safety issues, and financial and liquidity considerations. Additional risk exists regarding the production performance of producing properties and regarding the uncertain results from capital expenditure programs.

Zargon attempts to minimize pricing uncertainty with a risk management program which has in the past encompassed forward sales of crude oil and natural gas production complemented by U.S. dollar currency hedges for up to 30 percent of its oil and gas volumes. In 2001, the Company is making use of put option strategies that allow minimum price expectations to be reached in a manner that does not eliminate the Company's exposure to higher prices. However more moderate levels of crude and natural gas forward sales may still be contemplated. Environmental and safety risks are mitigated through compliance with provincial and

federal environmental and safety regulations, by maintaining adequate insurance, and by adopting appropriate emergency response and employee safety procedures.

Financial and liquidity risks are reduced by limiting debt financing to self-imposed debt to cash flow guidelines. Zargon actively manages the risks of its capital programs by concentrating drilling and subsequent development activities in areas where Zargon has demonstrated proven technical capabilities. Finally, Zargon's capital budget is managed to limit Zargon's capital exposure to any one project or concept.

## 2001 CORPORATE BUDGET

Zargon anticipates strong prices and continued gas and oil production growth in calendar 2001. The following table sets forth the current estimate of our Company's cash flow and earnings for the year. The analysis assumes that Zargon's effective cash tax rate will be 15 percent of the 2001 before tax cash flow from operations.

### PRICING ASSUMPTIONS

|                                        |                              |
|----------------------------------------|------------------------------|
| Oil and liquids (\$25.00 US/bbl – WTI) | \$32.00 Cdn./bbl field price |
| Natural gas (\$4.50 US/mmbtu – NYMEX)  | \$5.75 Cdn. /mcf field price |
| Exchange rate                          | \$0.68 Cdn./US Dollar        |

### AVERAGE PRODUCTION

|                 |             |
|-----------------|-------------|
| Oil and liquids | 1,900 bbl/d |
| Natural gas     | 19.0 mmcf/d |
| Equivalents     | 3,800 boe/d |

### CAPITAL EXPENDITURES

\$35.0 million

### REVENUE

\$62.0 million

### CASH FLOW FROM OPERATIONS

\$29.0 million

### NET EARNINGS

\$13.5 million

### CASH FLOW PER FULLY DILUTED SHARE

\$1.90

### EARNINGS PER FULLY DILUTED SHARE

\$0.90

## CORPORATE OUTLOOK

Zargon remains confident of its ability to maintain its record of consistent and sustainable growth. For calendar 2001, Zargon has budgeted \$35 million of capital expenditures allocated to promising gas exploitation and exploration opportunities and the acquisition and exploitation of long life oil properties. With its inherently strong financial condition, disciplined approach, new exploration initiatives, expanded undeveloped acreage base, and increased gas exposure, Zargon is well positioned to achieve substantial and profitable growth in 2001.

## Selected Quarterly Information

| (\$ million, except per share amounts) | 2000 |       |       |       | 1999 |      |      |      |
|----------------------------------------|------|-------|-------|-------|------|------|------|------|
|                                        | Q1   | Q2    | Q3    | Q4    | Q1   | Q2   | Q3   | Q4   |
| Production revenue                     | 9.13 | 10.62 | 14.24 | 19.32 | 4.28 | 5.06 | 6.82 | 7.89 |
| Cash flow from operations              | 4.36 | 5.04  | 7.17  | 10.93 | 1.64 | 2.16 | 3.17 | 3.67 |
| Per fully diluted share (\$/share)     | 0.29 | 0.32  | 0.46  | 0.70  | 0.11 | 0.14 | 0.20 | 0.25 |
| Earnings                               | 1.77 | 1.85  | 2.88  | 4.76  | 0.30 | 0.70 | 1.31 | 1.95 |
| Per fully diluted share (\$/share)     | 0.12 | 0.12  | 0.18  | 0.31  | 0.02 | 0.50 | 0.08 | 0.14 |
| Total assets                           | 62.4 | 68.5  | 74.6  | 86.9  | 44.2 | 45.1 | 50.4 | 56.0 |
| Long-term debt                         | 19.3 | 19.4  | 17.6  | 15.9  | 8.4  | 9.1  | 11.5 | 14.1 |

## Management's Report

The financial statements of Zargon Oil & Gas Ltd. were prepared by management in accordance with accounting principles generally accepted in Canada. The financial and operating information presented in this annual report is consistent with that shown in the financial statements.

Management has designed and maintains a system of internal controls to provide reasonable assurance that all assets are safeguarded and to facilitate the preparation of financial statements for reporting purposes. Timely release of financial information sometimes necessitates the use of estimates when transactions affecting the current accounting period cannot be finalized until future periods. Such estimates are based on careful judgements made by management.

External auditors appointed by the shareholders have conducted an independent examination of the corporate and accounting records in order to express their opinion on the financial statements.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control. The Board exercises this responsibility through its Audit Committee. The Audit Committee, which consists of non-management directors has met with the external auditors and management in order to determine that management has fulfilled its responsibilities in the preparation of the financial statements. The Audit Committee has reported its findings to the Board of Directors who have approved the financial statements.



J. O. McCutcheon  
Chairman



C. H. Hansen  
President and Chief Executive Officer

## Auditors' Report

### To the Shareholders of Zargon Oil & Gas Ltd.

We have audited the balance sheets of Zargon Oil & Gas Ltd. as at December 31, 2000 and 1999 and the statements of income and retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Canada. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 2000 and 1999 and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in Canada.

Calgary, Canada  
March 2, 2001



Chartered Accountants