

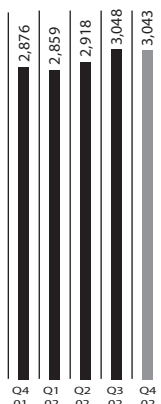
**CORPORATE  
HIGHLIGHTS**

In the fourth quarter of 2002, Zargon recorded strong gains in revenue, cash flow and earnings as natural gas prices surged upward. Compared to the third quarter of 2002 revenue, cash flow and earnings climbed 24 percent, 38 percent and 89 percent, respectively. Daily production increased five percent from the third quarter and 11 percent from the prior year's fourth quarter. Gains were similar on a per share basis: fourth quarter 2002 cash flow of \$0.59 per diluted share was 37 percent ahead of third quarter 2002 levels and earnings of \$0.24 per diluted share exceeded third quarter 2002 earnings by 85 percent. For the year, cash flow was \$32.12 million or \$1.81 per diluted share, earnings were \$10.68 million or \$0.60 per diluted share and production averaged 6,349 barrels of equivalent per day.

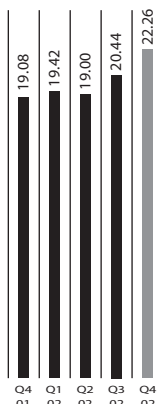
Capital expenditures in the 2002 fourth quarter were \$11.06 million gross and \$8.03 million net after the disposition of selected, smaller, non-core properties. Consistent with Zargon's 2002 focus to expand its natural gas exploration base, Zargon's undeveloped land inventory increased by 38 percent in 2002 to 331.3 thousand net acres by year end. Zargon's balance sheet remains strong with a bank indebtedness plus working capital deficiency of \$28.74 million representing only a 0.7 year multiple of annualized fourth quarter 2002 cash flow.

	Three Months Ended December 31,			Year Ended December 31,		
	2002	2001	% Change	2002	2001	% Change
<b>FINANCIAL</b>						
Income and Investments (\$ million)						
Production revenue	<b>20.67</b>	11.18	85	<b>65.54</b>	63.80	3
Cash flow from operations	<b>10.71</b>	5.81	84	<b>32.12</b>	32.67	(2)
Earnings	<b>4.28</b>	1.77	142	<b>10.68</b>	13.14	(19)
Net capital expenditures	<b>8.03</b>	9.28	(13)	<b>35.55</b>	55.18	(36)
Per Common Share, Diluted						
Cash flow from operations (\$/share)	<b>0.59</b>	0.34	74	<b>1.81</b>	2.03	(11)
Earnings (\$/share)	<b>0.24</b>	0.10	140	<b>0.60</b>	0.82	(27)
Balance Sheet at Period End (\$ million)						
Property and equipment, net				<b>141.01</b>	118.99	19
Bank indebtedness				<b>25.28</b>	24.14	5
Shareholders' equity				<b>86.60</b>	69.99	24
Shares Outstanding at Period End (million)				<b>17.64</b>	16.67	6
<b>OPERATIONS</b>						
Average Daily Production						
Crude oil and liquids (bbl/d)	<b>3,043</b>	2,876	6	<b>2,968</b>	2,441	22
Natural gas (mmcf/d)	<b>22.26</b>	19.08	17	<b>20.29</b>	18.67	9
Equivalents (boe/d)	<b>6,753</b>	6,057	11	<b>6,349</b>	5,553	14
Equivalents per million shares (boe/d)	<b>383</b>	363	6	<b>368</b>	357	3
Average Selling Price (before hedges)						
Crude oil and liquids (\$/bbl)	<b>35.79</b>	22.72	58	<b>34.45</b>	31.86	8
Natural gas (\$/mcf)	<b>5.20</b>	2.95	76	<b>3.81</b>	5.19	(27)
Wells Drilled, Net	<b>17.4</b>	11.4	53	<b>31.6</b>	47.7	(34)
Undeveloped Land at Period End (thousand net acres)				<b>331.3</b>	240.7	38

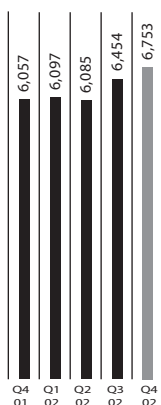
Crude Oil and Liquids Production (bbl/d)



Natural Gas Production (mmcf/d)



Production (boe/d)



Year Ended  
December 31,

	2002	2001	% Change
<b>RESERVES</b> (at period end)			
Proven Reserves			
Crude oil and liquids (mmbbl)	11.11	10.48	6
Natural gas (bcf)	64.54	60.74	6
Proven reserves (mmbbl)	21.87	20.61	6
Proven reserves per share (boe)	1.24	1.24	0
Proven & probable reserves (mmbbl)	26.76	25.79	4
Proven & risked probable reserves			
Net present value @ 12% (\$ million)	200.9	162.8	23
Net asset value (\$ per diluted share) (PV 12% incl. land & net debt)	10.65	8.83	21

Note: The calculation of barrels of equivalent (boe) is based on the conversion ratio of one barrel of oil is equivalent to six thousand cubic feet of natural gas.

**RESERVES**

The reserve values tabulated above are from Zargon's year-end reserve report prepared by the independent engineering firm McDaniel & Associates Consultants Ltd. ("McDaniel"). During 2002, Zargon spent \$35.55 million of net capital investment to increase proven oil and liquids reserves by six percent to 11.11 million barrels and also increase proven natural gas reserves by six percent to 64.54 billion cubic feet. These additions replaced the year's oil and natural gas production by 156 percent and 152 percent respectively. On an equivalent basis, proven reserves rose six percent to 21.87 million barrels of equivalent.

Approximately 83 percent of the total proven reserves are classified as proven producing. McDaniel assigned year-end proven and probable reserves of 77.88 billion cubic feet of natural gas and 13.78 million barrels of oil and liquids. Proven non-producing reserves are primarily natural gas reserves from unconnected wells at Pembina and Sturgeon Lake and behind-pipe natural gas reserves at Jarrow. Proven undeveloped reserves are less than one percent of proven reserves. Based on fourth quarter 2002 production rates, Zargon's proven reserve life index is 10.0 years and 7.9 years for oil and natural gas respectively. The corresponding proven and probable reserve life indices are 12.4 years and 9.6 years for oil and natural gas respectively.

Based on the McDaniel independent report, Zargon's 2002 proven finding and development costs were \$9.92 per barrel of equivalent. These costs compare with a 2000-2002 three-year and a 1998-2002 five-year historical proven average of \$7.90 and \$6.84 per barrel of equivalent, respectively. The 2002 finding and development costs are after a negative proven natural gas reserve revision of 5.62 billion cubic feet on certain wells in East Central Alberta at the Jarrow, Ukalta and Hamilton Lake properties. The revisions relate primarily to reserve reappraisals for 2000-2001 vintage natural gas wells that had been originally evaluated with volumetric reserve assignments in the absence of production data. Excluding these revisions, the 2002 proven finding and development cost would be reduced to \$8.19 per barrel of equivalent.

Zargon's year-end net asset value increased 21 percent in 2002 to \$10.65 per diluted share from the prior year's estimate of \$8.83 per diluted share. This net asset value is calculated using a McDaniel 12 percent discounted present value pretax estimate of proven and risked probable reserves, with adjustments for net debt and a 2002 year-end Seaton Jordan independent undeveloped land appraisal of \$22.37 million.

**PRODUCTION**

Production of oil and liquids averaged 3,043 barrels per day in fourth quarter 2002, unchanged from the third quarter and a six percent increase over fourth quarter 2001 as the majority of the 2002 capital budget targeted natural gas opportunities. Natural gas production averaged 22.26 million cubic feet per day in fourth quarter

2002, a nine percent improvement over the preceding third quarter and 17 percent over fourth quarter 2001. Natural gas production rates increased throughout the fourth quarter as wells from the summer/fall drilling program were tied-in to reach the January 2003 rate of 23.77 million cubic feet per day. Production at Jarrow, Zargon's largest natural gas property, averaged 14.69 million cubic feet per day in the fourth quarter and has been relatively stable over the last four quarters.

On an equivalent basis, production in fourth quarter 2002 of 6,753 barrels of equivalent per day was five percent above the preceding third quarter and 11 percent above the 6,057 barrels per day produced in fourth quarter 2001.

## **EXPLORATION AND EXPLOITATION**

Following our basic growth strategy of building inventories of undeveloped natural gas lands and oil-in-place resources when reasonable prices are available, Zargon deferred an active drilling program and concentrated on undeveloped land acquisitions in the low commodity price period during the 2002 first half. Commodity prices began to show renewed strength by mid-year and our drilling program was correspondingly accelerated. Following only an eight gross (7.1 net) well program in the first half, eight gross (7.1 net) wells were drilled in the third quarter and nineteen gross (17.4 net) wells in the fourth quarter, the latter a new quarterly high for Zargon.

The fourth quarter drilling program resulted in five additional Pembina shallow natural gas wells that continue to expand the scope of this project. In East Central Alberta three natural gas wells and one dry hole were drilled in Hamilton Lake and two natural gas wells were drilled at Jarrow. Four wells were drilled at Taber, resulting in one natural gas well and three oil wells. One horizontal oil well was drilled at Weyburn, Saskatchewan and one oil well was drilled as an eastern extension to the Haas, North Dakota property. Dry holes were drilled at the West Central Alberta exploration properties of Dunvegan and Judy Creek. The fourth quarter program resulted in 4.9 net oil wells, 9.5 net natural gas wells and 3.0 dry holes. During the year, Zargon drilled 31.6 net wells, which resulted in 20.7 net natural gas wells, 6.9 net oil wells and 4.0 net dry holes. Zargon operated 34 of these 35 gross wells with an average working interest of 90 percent. The year's program delivered an 87 percent success ratio, despite a 73 percent weighting to exploration wells.

Throughout the fourth quarter, Zargon tied-in wells relating to the successful 2002 summer/fall drilling program that were responsible for growing natural gas production from the third quarter average of 20.44 million cubic feet per day to reach the year-end exit rate projection of \$23.50 million cubic feet per day. The largest gains were from three summer exploratory gas wells at Highvale that averaged 2.76 million cubic feet of natural gas per day to Zargon's 60 percent interest in January 2003. Other tie-ins occurred at Judy Creek and at the East Central Alberta Jarrow, Hamilton Lake and Ukalta properties.

In 2002, Zargon participated aggressively in Crown land sales, taking advantage of lower Crown sale prices to expand our undeveloped land inventory. The result was a 38 percent increase in undeveloped lands to 331,300 net acres by year-end, with the bulk of the gains in our West Central Alberta natural gas exploration areas. The average price paid at Crown sales during 2002 was \$58 per acre, which compares favourably to the prior year's average cost of \$95 per acre. In the fourth quarter a total of 19,800 net acres were acquired at an average cost of \$71 per acre. This Crown posting and acquisition strategy has maintained the East Central Alberta undeveloped inventory at 170,300 net acres and increased the West Central Alberta undeveloped inventory from 38,400 net acres at the beginning of the year to a year-end 109,100 net acres. Over the year Zargon focused on building interests in the three West Central Alberta exploration areas of Peace River Arch, Pembina shallow and greater Highvale, reaching respective year-end inventories of 45,200, 28,100, and 18,200 net acres.

Zargon had good success with its oil exploitation programs in the second half of 2002, adding waterflood pressure support programs at the Haas Unit in North Dakota and the Frys East property in Southeast Saskatchewan. The Haas property has shown good early response from the commencement of October 2002 water injections, with a strong 37 percent increase in production from the existing producers to 690 barrels per day. Additional waterflood implementation programs are proceeding in West Central Alberta and in Southeast Saskatchewan.

## ACQUISITIONS

With higher property values becoming apparent, Zargon was not active in acquiring properties in the fourth quarter of 2002. However, consistent with its counter cyclical strategy, Zargon was successful in selling seventeen minor properties in ten transactions in the fourth quarter for a total of \$3.04 million. These sale properties had generally been acquired in recent corporate acquisitions and were either very small, were medium-heavy oil properties or had high operating costs. Further minor property sales are anticipated in the first half of 2003. The sales are expected to have only a minor effect on production, but will improve corporate efficiencies in terms of overheads and operating costs.

## GUIDANCE

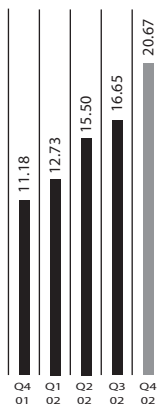
Last August, Zargon adjusted its 2002 year-end production rate guidance to 23.5 million cubic feet of natural gas per day and 3,200 barrels of oil per day, for a combined rate of 7,115 barrels of equivalent per day. These targets were mostly attained as evidenced by January 2003 production rates of 23.77 million cubic feet of natural gas per day and 3,005 barrels of oil per day, that equate to 6,967 barrels of equivalent per day. Total equivalent production was about two percent less than guidance levels, with oil production coming below targets primarily as a result of fourth quarter oil property sales, and natural gas production exceeding targets due to strong initial natural gas production rates from new natural gas well tie-ins at the West Central Alberta Highvale property.

Mid-year 2003 production guidance is reaffirmed at 25 million cubic feet per day of natural gas and 3,400 barrels per day of oil, which equates to a combined rate of 7,570 barrels of equivalent per day. Forecasted natural gas production growth will come from the June 2003 tie-in of about two million cubic feet per day at the West Central Alberta Pembina shallow gas property, which may be partially offset by the second quarter disposition of selected minor non-operated gas properties. Oil production volume growth is forecasted to come from first and second quarter drilling on exploitation projects located in our Southeast Saskatchewan core area.

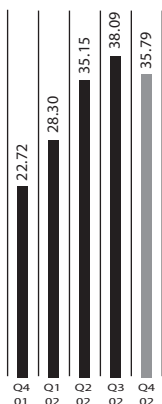
Zargon's 2003 capital program budget continues to be set at \$45 million. This budget is allocated \$30 million to exploration and development field activities and calls for the drilling of 40 net wells of which 75 percent will be related to natural gas projects. The majority of these all-season access locations will be drilled in the spring/summer/fall period, when field services are projected to be less expensive than the high cost winter months. The 2003 field-related capital expenditures will focus on continuing to expand our gas activities in West Central Alberta (18 net wells), while maintaining steady gas production rates from East Central Alberta (12 net wells). Oil expenditures will continue to be directed to the efficient exploitation of our very large Southeast Saskatchewan (10 net wells) oil development and water-flood project inventory. The remaining \$15 million of the capital budget is allocated to either property or corporate acquisitions, which will be pursued if value-added opportunities are available.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

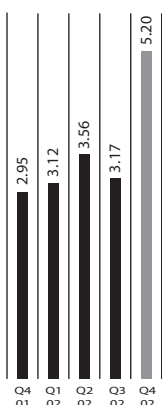
Production Revenue  
(\$ million)



Oil and Liquids  
Prices  
(\$/bbl)



Natural Gas Price  
(\$/mcf)



Management's discussion and analysis (MD&A) should be read in conjunction with the unaudited interim financial statements for the three months ended December 31, 2002 and the audited consolidated financial statements and MD&A for the years ended December 31, 2001 and December 31, 2002. The calculation of barrels of equivalent (boe) is based on the conversion ratio of one barrel of oil is equivalent to six thousand cubic feet of natural gas.

### FINANCIAL ANALYSIS

Fourth quarter 2002 before hedging production revenue of \$20.67 million increased strongly, 24 percent over third quarter 2002 and 85 percent over fourth quarter 2001. These large gains are due primarily to steep price increases in both oil and natural gas and secondarily to increased production. In the fourth quarter of 2002, production of oil and natural gas averaged 6,753 barrels of equivalent per day, a five percent increase over third quarter 2002 levels and an 11 percent improvement over fourth quarter 2001. Natural gas production increased to 22.26 million cubic feet per day, due in part to the November tie-in of three new Highvale natural gas wells.

Zargon's field price for oil and liquids in the fourth quarter of \$35.79 per barrel was six percent below third quarter 2002 and 58 percent above the prior year fourth quarter. The transportation and quality differential from the FOB Edmonton posted price for the fourth quarter averaged \$5.90 per barrel, a 15 percent increase over the \$5.12 per barrel recorded in the third quarter. For the year ended December 31, 2002, the average field oil price of \$34.45 per barrel was eight percent higher than the 2001 average.

Zargon's field natural gas price for the fourth quarter of 2002 was \$5.20 per thousand cubic feet, 64 percent above third quarter 2002 and 76 percent above the fourth quarter of 2001. For the full year, the average field price of \$3.81 per thousand cubic feet in 2002 was 27 percent below 2001, which had been bolstered by the record high prices of the 2001 first quarter.

Zargon's commodity price risk management policy is to use forward sales, options and costless collars for 20 to 30 percent of our net oil and natural gas sales to partially offset the effects of wide price swings. High natural gas prices in the fourth quarter produced a net hedging loss of \$0.71 million compared to a hedging gain of \$0.45 million in the preceding third quarter and a hedging gain of \$0.88 million in the 2001 fourth quarter. For the full 2002 year, the hedging program added \$0.67 million of revenue, primarily related to natural gas commodity prices. For 2003, Zargon currently entered into oil swaps for an average of 692 barrels per day at \$24.65 US per barrel (WTI). The natural gas hedging program has outstanding swaps for 4,000 gigajoule per day to March 31, 2003 averaging \$3.85 per gigajoule (AECO) and 2,000 gigajoule per day from April 1, 2003 to October 31, 2003 at \$4.85 per gigajoule. Zargon has also entered into two natural gas collars, one for 4,000 gigajoule per day at a put/call of \$3.85/\$8.05 per gigajoule to March 31, 2003 and one for 2,000 gigajoule per day at a put/call of \$4.00/\$6.10 per gigajoule from April 1, 2003 to October 31, 2003 (AECO). A third costless collar in place for 1,000 gigajoule per day from November 1, 2003 to March 31, 2004 at a put/call of \$5.50/\$7.90 per gigajoule (AECO).

Royalties, inclusive of Alberta Royalty Tax Credit and Saskatchewan Resource Surcharge, were \$3.68 million for the fourth quarter of 2002, a decrease of four percent from the preceding third quarter and up 59 percent from the 2001 fourth quarter. For the full year of 2002, royalties and revenues were each very similar to those of 2001. As a percentage of gross revenue, 2002 royalties were 20.6 percent of revenue, comparable to 22.3 percent in the 2001 period.

Production expenses were \$4.57 million in the 2002 fourth quarter, 10 percent higher than in the preceding third quarter and 31 percent higher than in the fourth quarter of 2001. For the year, production expenses were \$15.65 million in 2002, an increase of 31 percent from 2001. On a unit of production basis, the 2002 production costs were \$6.75 per barrel of equivalent compared to \$5.89 per barrel of equivalent in the 2001 period, a 15 percent increase. Fourth quarter expenses were especially heavy due the booking of a series of third party adjustments. The reversal of the increasing trend in operating costs is a key focus for Zargon. In fourth quarter of 2002 the first of a series of proposed dispositions of high-cost, non-core properties was concluded, taking advantage of the current high commodity/property prices. Other field initiatives are underway to control and improve production costs, but material improvements in our cost structure will require the disposition of the higher cost component of our property base.

## Operating Netbacks

Year ended December 31	2002		2001	
	Oil and Liquids	Natural Gas	Oil and Liquids	Natural Gas
	\$/bbl	\$/mcf	\$/bbl	\$/mcf
Revenue	<b>34.45</b>	<b>3.81</b>	31.86	5.19
Hedging	<b>(0.33)</b>	<b>0.14</b>	(0.33)	(0.04)
Royalties	<b>(6.86)</b>	<b>(0.82)</b>	(6.31)	(1.26)
Production costs	<b>(9.72)</b>	<b>(0.69)</b>	(8.85)	(0.59)
<b>Operating netbacks</b>	<b>17.54</b>	<b>2.44</b>	16.37	3.30

General and administrative expenses of \$0.68 million in the fourth quarter of 2002 were 32 percent below the preceding third quarter and 18 percent below the 2001 fourth quarter. The fourth quarter expenses were especially low due to large overhead recoveries associated with the expanded fourth quarter field-related capital program. For 2002, general and administrative costs of \$3.46 million were 12 percent above 2001 and on a unit of production basis decreased two percent to \$1.49 per barrel of equivalent in 2002 from \$1.52 in 2001. During the period, Zargon maintained its policy of not capitalizing any portion of its general and administrative costs.

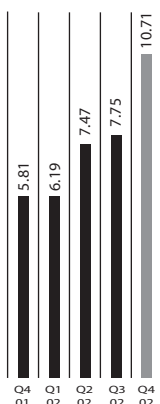
Interest expense of \$0.30 million in the fourth quarter and \$1.10 million for 2002 compares to \$0.24 million in the fourth quarter and \$0.96 million for the full year of 2001. Short-term interest rates have been at record low levels in 2002, but the related savings were partially offset by the increased bank debt levels. In accordance with new CICA recommendations, bank debt is now presented as a current liability on the balance sheet and not as long-term debt as in previous year's statements.

## Corporate Netbacks

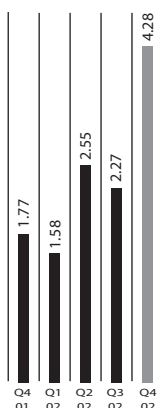
Year ended December 31	2002	2001
	\$/boe	\$/boe
Revenue	<b>28.28</b>	31.48
Hedging	<b>0.29</b>	(0.29)
Royalties	<b>(5.83)</b>	(7.01)
Production costs	<b>(6.75)</b>	(5.89)
<b>Operating netbacks</b>	<b>15.99</b>	18.29
General and administrative	<b>(1.49)</b>	(1.52)
Financing charges	<b>(0.47)</b>	(0.47)
Capital and current income taxes	<b>(0.17)</b>	(0.18)
<b>Cash flow netbacks</b>	<b>13.86</b>	16.12
Depletion and depreciation	<b>(5.84)</b>	(5.22)
Site restoration	<b>(0.55)</b>	(0.52)
Foreign exchange	<b>(0.03)</b>	(0.05)
Future income taxes	<b>(2.83)</b>	(3.85)
<b>Net earnings</b>	<b>4.61</b>	6.48

Depletion and depreciation expense for the fourth quarter of 2002 of \$3.87 million was 11 percent higher than the preceding third quarter 2002 and 25 percent above fourth quarter 2001. For the full year depletion and depreciation expense increased 28 percent to \$13.54 million in 2002 from \$10.58 million in 2001. Production volumes have increased 14 percent year-over-year and on a unit of production basis, depletion and depreciation charges have risen 12 percent to \$5.84 per barrel of equivalent from \$5.22 in 2001. The fourth quarter 2002 depletion and depreciation charge was \$6.22 per barrel of equivalent. The increase in unit charges arose mainly from the ongoing industry-wide trend, also experienced by Zargon, to higher finding and development costs.

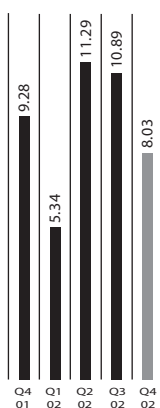
Cash Flow from Operations  
(\$ million)



Earnings  
(\$ million)



Net Capital Expenditures  
(\$ million)



Cash flow in fourth quarter 2002 of \$10.71 million rose sharply from \$7.75 million in the preceding third quarter and \$5.81 million in fourth quarter 2001. For the full year cash flow in 2002 of \$32.12 million was two percent below 2001. The exceptional gas prices and cash flow experienced in first quarter 2001 offset a steadily improving price trend in the final three quarters of 2002. The earnings pattern was similar but with wider quarterly swings; earnings of \$4.28 million in fourth quarter 2002 were 89 percent above the preceding third quarter of 2002 and 142 percent above the prior year quarter. Full year earnings in 2002 of \$10.68 million were 19 percent below the previous year and were impacted by 2002 increases in future income tax provisions and higher depletion and depreciation charges.

### Capital Expenditures

Year ended December 31 (\$ million)	2002	2001
Undeveloped land	4.46	5.08
Geological and geophysical (seismic)	2.47	3.80
Drilling and completion of wells	12.49	17.44
Well equipment and facilities	4.48	4.87
Exploration and development	23.90	31.19
Property acquisitions	7.39	4.83
Property dispositions	(3.13)	(4.23)
Net property acquisitions	4.26	0.60
Corporate acquisitions assigned to property and equipment	7.39	23.39
<b>Total capital expenditures (net)</b>	<b>35.55</b>	<b>55.18</b>

### LIQUIDITY AND CAPITAL RESOURCES

During the year ended December 31, 2002 Zargon's capital expenditures were \$35.55 million with \$23.90 million or approximately 67 percent assigned to exploration and development activities. Funding for the 2002 expenditures was \$32.12 million from operating cash flow and \$5.87 million through the issuance of common stock pertaining to the second quarter Hadrian acquisition and employee stock options, and \$1.14 million bank debt. Zargon's balance sheet remains very strong with total net current liabilities (including bank debt) of \$28.74 million being only a 0.7 year multiple of annualized fourth quarter 2002 cash flow. Zargon's total authorized banking credit facilities are \$50.0 million Cdn. plus \$4.3 million US and we continue to maintain the financial strength and flexibility to deal with opportunities that may appear as the industry cycle proceeds.

As at March 13, 2003, Zargon has issued 17,721,600 common shares and has granted stock options to acquire an additional 1,535,200 shares.

### Capital Sources

Year ended December 31 (\$ million)	2002	2001
Cash flow from operations	32.12	32.67
Changes in working capital and other	(3.58)	0.39
Bank indebtedness	1.14	8.23
Issuance of common shares	5.87	13.89
<b>Total capital sources</b>	<b>35.55</b>	<b>55.18</b>

## OUTLOOK

The increasing strength of oil and natural gas prices experienced in 2002 and particularly in the fourth quarter provided cash flows sufficient to support a strong exploration effort. In the 2003 first quarter, increased production volumes and even higher oil and natural gas prices will provide excellent cash flows and earnings, with surplus cash flows providing some debt reduction.

Zargon is particularly well positioned for this current period of higher commodity prices and the inevitable increase in undeveloped land, property and field services input costs. The lower Crown land prices prevailing in 2002 were opportune as they allowed us to substantially expand our West Central Alberta gas exploration area on favourable terms. Over its history, Zargon has assembled a large inventory of exploitable oil properties that continues to provide numerous long-term opportunities for efficient capital deployment. With inventories of over 331,000 net acres of undeveloped land and 130 million barrels of working interest oil-in-place available, we expect that our growth strategy of exploring for gas and exploiting oil properties will continue to be successful.

(\$ million, except per share amounts)

Quarter	Earnings	Earnings/ Diluted Share	Cash Flow	Cash Flow/ Diluted Share	Revenue	Total Assets	Bank Debt
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
2001 Q2	\$3.49	\$0.22	\$8.59	\$0.57	\$16.90	\$108.27	\$13.19
2001 Q1	\$5.28	\$0.36	\$10.61	\$0.71	\$21.04	\$90.91	\$10.09
2000 Q4	\$4.75	\$0.32	\$10.93	\$0.74	\$19.32	\$86.88	\$15.90

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

Calgary, Alberta  
March 13, 2003

CONSOLIDATED  
BALANCE  
SHEETS

(\$ thousand)	<b>December 31, 2002</b>	December 31, 2001
<b>ASSETS</b>		
<b>Current</b>		
Cash	–	201
Accounts receivable	<b>11,942</b>	7,990
Prepaid expenses and deposits	<b>712</b>	741
	<b>12,654</b>	8,932
<b>Property and equipment, net</b>	<b>141,006</b>	118,994
	<b>153,660</b>	127,926
<b>LIABILITIES</b>		
<b>Current</b>		
Bank indebtedness	<b>25,279</b>	–
Accounts payable and accrued liabilities	<b>16,118</b>	12,440
	<b>41,397</b>	12,440
<b>Long-term debt</b>	–	24,137
<b>Future site restoration</b>	<b>4,746</b>	3,141
<b>Future income taxes</b>	<b>20,922</b>	18,223
	<b>67,065</b>	57,941
<b>SHAREHOLDERS' EQUITY</b>		
Share capital	<b>40,997</b>	35,066
Retained earnings	<b>45,598</b>	34,919
	<b>86,595</b>	69,985
	<b>153,660</b>	127,926

See accompanying selected notes.

CONSOLIDATED  
STATEMENTS OF  
INCOME AND  
RETAINED  
EARNINGS

(\$ thousand, except per share amounts)	Three Months Ended December 31,		Year Ended December 31,	
	2002	2001	2002	2001
<b>Income</b>				
Oil and gas sales	20,665	11,184	65,538	63,795
Hedging	(712)	878	669	(573)
Royalties	(3,677)	(2,306)	(13,508)	(14,222)
	<b>16,276</b>	9,756	<b>52,699</b>	49,000
<b>Expenses</b>				
Production	4,572	3,493	15,649	11,933
General and administrative	679	833	3,455	3,083
Interest	297	241	1,100	957
Foreign exchange	2	59	86	107
Site restoration	318	309	1,268	1,045
Depletion and depreciation	3,865	3,102	13,536	10,576
	<b>9,733</b>	8,037	<b>35,094</b>	27,701
<b>Income Before Income Taxes</b>	<b>6,543</b>	1,719	<b>17,605</b>	21,299
<b>Income Taxes</b>				
Future	2,242	516	6,548	7,806
Current	19	(570)	378	358
	<b>2,261</b>	(54)	<b>6,926</b>	8,164
<b>Net Income for the Period</b>	<b>4,282</b>	1,773	<b>10,679</b>	13,135
<b>Retained Earnings, Beginning of Period</b>	<b>41,316</b>	33,146	<b>34,919</b>	21,855
<b>Repurchase of Common Shares</b>	-	-	-	(71)
<b>Retained Earnings, End of Period</b>	<b>45,598</b>	34,919	<b>45,598</b>	34,919
<b>Earnings Per Common Share</b>				
Basic	0.24	0.11	0.62	0.84
Diluted	0.24	0.10	0.60	0.82

See accompanying selected notes.

CONSOLIDATED  
STATEMENTS OF  
CASH FLOWS

(\$ thousand, except per share amounts)	Three Months Ended December 31,		Year Ended December 31,	
	2002	2001	2002	2001
<b>Operating Activities</b>				
Net income for the period	4,282	1,773	10,679	13,135
Add non-cash items:				
Depletion and depreciation	3,865	3,102	13,536	10,576
Site restoration	318	309	1,268	1,045
Foreign exchange	2	107	86	107
Future income taxes	2,242	516	6,548	7,806
Cash flow from operations	10,709	5,807	32,117	32,669
Changes in non-cash working capital	(1,362)	(2,364)	(2,587)	(1,189)
	9,347	3,443	29,530	31,480
<b>Financing Activities</b>				
Bank indebtedness	(3,428)	4,871	1,142	8,235
Exercise of stock options	307	58	1,262	886
Issuance of common shares	-	-	-	13,106
Repurchase of common shares	-	-	-	(105)
	(3,121)	4,929	2,404	22,122
<b>Investing Activities</b>				
Acquisition of property and equipment	(11,063)	(9,667)	(31,296)	(36,014)
Disposal of property and equipment	3,037	745	3,134	4,230
Corporate acquisitions (cash portion)	-	-	(4,875)	(19,831)
Site restoration expenditures	(219)	(84)	(423)	(340)
Changes in non-cash working capital	2,019	646	1,325	(1,605)
	(6,226)	(8,360)	(32,135)	(53,560)
<b>Increase (decrease) in Cash</b>	-	12	(201)	42
<b>Cash, Beginning of Period</b>	-	189	201	159
<b>Cash, End of Period</b>	-	201	-	201
Cash interest paid	224	289	1,150	956
Cash taxes paid	19	40	378	218
<b>Cash Flow from Operations Per Share</b>				
Basic	0.61	0.35	1.86	2.10
Diluted	0.59	0.34	1.81	2.03
<b>Weighted Average Number of Shares (million)</b>				
Basic	17.62	16.64	17.23	15.56
Diluted	18.10	17.26	17.79	16.11

See accompanying selected notes.

SELECTED  
NOTES TO  
CONSOLIDATED  
FINANCIAL  
STATEMENTS  
For the three months  
and year ended  
December 31, 2002  
and 2001

**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 years ended December 31, 2002 and December 31, 2001. 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, 2001.

**2. ACQUISITIONS**

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 \$0.13 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)

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

On July 10, 2001, the Corporation acquired all of the outstanding shares of Herc Oil Corp. ("Herc"), a private oil and gas company, for cash consideration of \$19.83 million. The acquisition was accounted for by the purchase method as follows:

(\$ thousand)

Working capital	1,972
Property and equipment	23,392
Future tax asset	993
Long-term debt	(5,696)
Future site restoration	(830)
<b>Cash consideration</b>	<b>19,831</b>

**3. BANK INDEBTEDNESS**

The Corporation has a \$50 million credit facility consisting of a revolving demand loan with a Canadian chartered bank that bears interest at the bank's prime rate. The Corporation has pledged an assignment of accounts receivable, a first floating charge on all of the Canadian assets and a fixed charge over certain property and equipment as collateral under this facility. The Corporation also has a revolving demand loan in the United States for \$4.3 million (U.S.) bearing interest at U.S. prime plus 3/4% percent and has pledged a first floating charge on all of the U.S. assets and a fixed charge over certain U.S. property and equipment as collateral.

Effective January 1, 2002, the Corporation adopted the recommendations of the Emerging Issues Committee of the Canadian Institute of Chartered Accountants concerning the presentation of revolving demand loans. These new recommendations require that the classification of debt in a debtor's balance sheet be based upon the facts existing at the balance sheet date rather than expectations. Prior to the adoption of the new recommendations, the Corporation presented the demand loan as long-term on the basis that the bank had indicated it was not its intention to call for repayment within one year provided there was no adverse change in the financial position of the Corporation. However, these loans are demand in nature and therefore are now presented as a current liability.

#### 4. 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)	December 31, 2002		December 31, 2001	
	Number of Shares	Amount \$	Number of Shares	Amount \$
Shares issued,				
Balance, beginning of year	16,666	35,066	14,315	20,667
Shares issued for Hadrian	542	4,669	-	-
Issuance of common shares	-	-	2,000	13,547
Stock options exercised	429	1,262	374	886
Normal course issuer bid	-	-	(23)	(34)
Balance, end of period	<b>17,637</b>	<b>40,997</b>	16,666	35,066

A summary of the status of the Corporation's stock option plans as at December 31, 2002 and 2001, and changes during the year ended on those dates is presented below:

Stock Options:	December 31, 2002		December 31, 2001	
	Number of Shares (thousand)	Weighted Average Exercise Price \$	Number of Shares (thousand)	Weighted Average Exercise Price \$
Outstanding at beginning of year	1,199	3.36	1,290	2.71
Granted	466	7.69	298	4.94
Exercised	(429)	2.94	(374)	2.37
Cancelled	(21)	7.37	(15)	4.28
Outstanding at end of period	<b>1,215</b>	<b>5.10</b>	1,199	3.36
Options exercisable at period end	<b>750</b>	<b>3.49</b>	916	2.85

#### 5. SEGMENTED INFORMATION

(\$ thousand)	Three Months Ended December 31,		Year Ended December 31,	
	2002	2001	2002	2001
<b>Oil and Gas Sales</b>				
Canada	18,680	10,019	58,360	60,999
United States	1,985	1,165	7,178	2,796
Total	<b>20,665</b>	11,184	<b>65,538</b>	63,795
<b>Total Assets</b>				
Canada			148,119	123,262
United States			5,541	4,664
Total			<b>153,660</b>	127,926

# ZARGON OIL AND GAS LTD.

## Corporate Information

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### 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

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

Toronto Stock Exchange  
Trading Symbol: ZAR

### Head Office

700, 333 – 5th Avenue S.W.  
Calgary, Alberta T2P 3B6  
Phone: (403) 264-9992  
Fax: (403) 265-3026  
Email: [zargon@zargon.ca](mailto:zargon@zargon.ca)

### Website

[www.zargon.ca](http://www.zargon.ca)

*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.*