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Petrel Resources

Annual Report 2002

>>Chairman's Statement

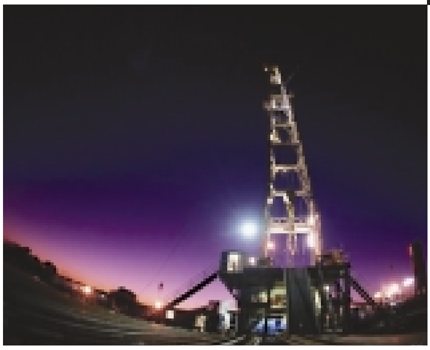
It may seem strange to relate but war has been good for Petrel. Our share price which was languishing at an all time low of 3p has risen 400 per cent in the first six months of 2003. Why is this?

It is the prospect of certainty replacing uncertainty. For years Petrel has ploughed a lonely track as the sole English speaking Western oil venture in Iraq. As the sanctions dragged on and on investors lost hope that we would ever be able to begin work on the Iraqi oilfields. We never wavered. Our conviction remains that Iraq has the best oil prospects in the world and will provide Petrel with a major project or projects. We have spent five years and much of the company's scarce equity in pursuit of an Iraq oil concession either production, exploration or both. That objective looks closer now than ever before. Order will emerge from the current chaos and anarchy in Iraq. When it does we will be ready and available to work. Toward that end, David Horgan and Guy Delbes, two of your directors, traveled to Baghdad to re-establish our office and our industry contacts. We now have staff, communications and experts on the ground ready to move.

Let me once again explain the importance of Iraq in world oil. The country is virtually unexplored yet holds proven reserves of 115 billion barrels, second only to Saudi Arabia. Exploration is likely to double these reserves. The oil is mainly top quality, ideal for refining into gasoline which the US badly needs. Cost of operations are the lowest in the world, running at less than $1.00 per barrel. Plans exist to double capacity from 3m barrels a day to 6m and possibly 9m barrels a day. There are 48 discovered, undeveloped or shut-in former producing fields waiting to be opened up.

That's the technical side of supply. Now look at demand. Existing and potential world supply is not sufficient for the expected growth in demand in the coming decades. Statistics can demonstrate whatever you like but the reality is that the major producing areas like the US, Colombia, Venezuela, Mexico and the North Sea are mature and are either declining already or will shortly decline. Alternative sources, like the Caspian, are expensive and politically difficult while the massive Heavy Oil Sands of Canada and Venezuela need very high oil prices to be viable.

Consider the political picture. What is going to happen in Saudi Arabia? It is difficult to believe that some form of political upheaval will not happen in the coming years. Venezuela is in even worse political shape, while Nigeria struggles to find stability. This leaves Iraq in a pivotal position. Iraq is not a natural entity. Created artificially by the Western powers, it has many tribes, a separate race, the Kurds, in the north and two groups – the Shia and the Sunni, each with a different approach to religion. To compound the problems, the Kurdish area holds the fabled Kirkuk oil fields, home of



the Ancient Lights, where gas has been burning for thousands of years. The Kirkuk oil fields are capable of producing 1m barrels of crude oil a day for many years to come. This asset is surely a prize worth fighting for. The Basra area in the South home of the Shia Marsh people, contains the vast Rumailah fields and the West Qurna reserve, the largest undeveloped oil reserve in the world containing somewhere between 8 and 20 billion barrels of oil. Why would the Shia want central control?

Can the US, or indeed the UN, cobble together a coalition which will unite the country to the extent that a government can be democratically elected? It is said that democracy is not the tyranny of the majority but it is very difficult to see how the 60% plus Shia majority can be denied the lion's share of power.

At this early stage of democratization it is not clear who will emerge as leaders, but the task to find a peaceful stable way forward is not easy. The Iraqi people are educated and cultivated, as befits a people living in the cradle of civilization. They have been bombed and sanctioned into poverty. The economy and much of the infrastructure is destroyed. Vast sums are required for rebuilding. These will come from oil. No matter who runs the government, oil development will be a top priority.

PETREL IN IRAQ

Petrel entered Iraq seeking a concession to develop and/or refurbish existing oil fields in Iraq. In 1999 we submitted a detailed tender to refurbish the Subba/Luhais oil fields in the Basra area. The feasibility study envisaged the following:

- Capital cost $355m.
- Daily output of 180,000 bbls rising to 240,000.
- 27-36 month refurbishment period.

The tender was well received and over the following months a detailed evaluation took place between the Iraqi Oil Ministry staff and Petrel staff and consultants.

As small junior oil venture Petrel lacked a track record. The Oil Ministry suggested that we cut our teeth on an exploration block and indicated that we should apply for Block 6 – a choice block in the Western Desert which lies between Baghdad and Jordan. Only 9 blocks in the area were offered for tender. Outstanding exploration areas in the North and South were not offered.

Block 6 is a 10,000 sq kilometre block about halfway between Baghdad and the Jordanian border. It had some work done in the early 1980's and has pipelines running along the edges of the block.

Over the following two years long and torturous negotiations took place to agree a work programme and then to negotiate commercial and financial terms. In Spring 2001, we signed an agreement with the Oil Ministry. Together with other applicants such as ONGC of India and Petronas of Indonesia we awaited the Proclamation of the Agreement. In December 2002 we were informed that the Proclamation was approved and would be made on December 15th 2002. That is where events remain.

Where are we now? We are open for business in Baghdad. We have presented an interim work programme on Block 6 to the current executives in the Oil Ministry. We have re-affirmed our interest in the development of the Subba and Luhais oil fields. If we get approval we proceed. If we do not we fight. It is as simple as that. We will be flexible not intransigent. I hope and expect that commercial sense prevails and that all realise how we can develop oil

projects far quicker than new entrants. It is not as if there is a scarcity of projects. There is oil development work for the next generation. We would like to have a local Iraqi partner as well as the Oil Ministry. We are not averse to taking in an international oil industry partner. The opportunities are so good that to use an old expression "half a loaf is better than no bread".

Rest assured that we are, and will remain, at the head of the queue. We have laid down our markers.

SUDAN

While the focus of our efforts is Iraq our application to obtain a concession in Sudan is on the cabinet table in Khartoum. In recent years Sudan has had a terrible press due to an ongoing civil war in the South. What has been largely ignored is the emergence of Sudan as a significant oil producer with production at 450,000 barrels a day and rising. The potential has attracted many of the world's, most powerful oil companies, but none of the Seven Sisters. Petrel was invited three years ago to apply for a licence. Having reviewed the terms and the potential we applied for Block 15 in the shallow waters offshore Port Sudan. This block was surveyed and drilled in the 1970s by one of the majors but the discoveries were not large enough. We negotiated a joint venture with Sudapet the Sudanes State Oil company and submitted a proposal. Negotiations have taken a great deal of time but we believe that a decision is imminent. Should we be successful we would expect to drill within 12 months.

FINANCE

Petrel has been run on a shoestring for the past three years yet even the lowest level of operations cost money. It costs in excess of £100,000 stg. a year to maintain an AIM listed company. In recent years small placings mainly with the directors and friends has funded ongoing activities. In the Spring of 2003 we agreed a small placing with a City institution which raised £136,000 stg. Since then our price has quadrupled. We will continue a policy of small placements to minimize dilution until we need to raise money for development and/or exploration.

PEOPLE

I cannot complete this report without commenting on the people involved in Petrel, particularly our directors David Horgan and Guy Delbes. They have taken significant personal risks and suffered hardship to venture into Iraq to re-establish our operations. Our success will be in large part to their efforts. I am delighted to welcome Stefano Borghi to our board. It will be my pleasure to propose him for re-election at our Annual General Meeting. Stefano is an experienced international manager with Iraqi oil experience. He is currently managing an Italian venture capital company. His experience, contacts and advice will be valuable.

John J. Teeling

John J. Teeling
Chairman

June 27, 2003

>>Managing Director's Report

Geology is why we're interested in Iraq. Officially Iraq has 115 billion barrels proven, with probables of 200 to 300 billion. This is usually stated as 11% of proven world reserves, but may be closer to 15% on a fair comparison.

Probables are so high because Iraq is virtually unexplored: amazingly, only about 2,000 wells have been drilled – compared to over a million in similarly sized Texas. Nearly all of those wells are relatively shallow and in the main river valleys. There have been few wells in northwestern Kurdistan or the western desert. Only two wells have scratched the Jurassic – which is the main producer in Saudi Arabia and Kuwait. The Mesozoic is virtually untouched, the Paleozoic unknown. This explains the Oil Ministry's interest in exploration despite having 42 major fields shut-in even pre-war. Exploring the relatively shallow drilling targets western desert gives clues about deeper potential nationwide.

Pre-war Iraq's total production of 2.5 million barrels a day came from just 12 fields, which have been maintained despite desperate shortage of new capital investment and essential spares.

So Iraq is the cornucopia, the best oil exploration and development play worldwide. What will happen now and how to exploit the opportunity?

Driving back to our work place in Iraq is a strange experience. The stable, if repressive Ba'athist régime has been replaced by legal and administrative chaos. The occupying power was shocked at the kaleidoscope of loyalties that is Iraq, and the Middle East generally. Those of us familiar with the faiths, traditions and language of the area are not surprised.

Many of the old certainties are gone: infrastructure destroyed by war, sanctions and latterly looting. Baghdad is no longer a safe place for foreigners. The interior of our representative office was not broken into, but twice our manager escaped attempted car theft. It is not safe to commute, so he has established an emergency office at his residence.

We travelled widely through Baghdad visiting offices and key people at their homes. Oil Ministry buildings are now secured by the US military. In the back streets, there are groups of armed men of military age in mufti. There are increasingly sophisticated demonstrations. Resentments against westerners exist where they never did before. Unaccompanied women are strangely absent. Formerly westernised women now appear in traditional Islamic dress.

But old friends survived, proving that while politicians come and go, friendships between people and nations persist. They were delighted to see us and tell their story which was in many ways worse than we'd feared. But sanctions are lifted and in the trauma which exists there is more scope to work together for the benefit of Iraqi people, energy consumers worldwide and Petrel shareholders. The Iraqi oil opportunity is wide open.

As I write in late June 2003 the Iraqi oil industry is in dire straits: production is at a low proportion of pre-war levels. Contractors retained

View of Block 6 – The Western Desert ➤

under non-competitive tenders funded by the US taxpayer are still based in Kuwait, rather than in Iraq. They commute daily under heavy US military guard. If inadequate security is available they do not work.

Most ministry officials are now at their desks, but seem paralysed by events. They have lost their bosses and some of their best people to purges and uncertainty. Much of their data and even office equipment was stolen. They believe that only a legitimate sovereign Iraqi government can take policy decisions. They define such a government as one enjoying broad internal and international recognition, particularly among Arab countries.

Iraq cannot restore production; much less develop its oil potential without massive international investment of capital, skills and technology. Yet US companies will not work except in secure situations under heavy military guard. And there is a shortage of coalition troops available for static security. Overt military activity aggravates locals, creating additional security hazards. So the industry is in a vicious circle. Companies from non-threatening, neutral countries are therefore advantaged: we are watched and sometimes challenged by Iraqi men of military bearing – but not threatened by them. Bandits without political motivation are a threat to everyone, foreign and Iraqi, but normal security precautions should adequately protect. We expect to start some fieldwork shortly.

Often the apparently shortest route is the longest way home. Trying to turn a fast buck in the Middle East often ends in tears. This is especially so in Iraq, where you have a highly educated and proud ‘permanent government’ suspicious of carpetbaggers. Many top people worked right up to the Baghdad battle and risked their lives to save invaluable data. The deteriorating situation forced many to stay at home. They were only returning permanently to their desks during June 2003. Up to a century of data and files were looted. Ministry officials are rebuilding their files and databases, but a comprehensive inventory is months away.

Facilities were not systematically sabotaged or hit by air attack. But looters wreaked havoc in the hours between defeat and conquest. Geophysical data, critical for the world’s energy future, now lies burnt and scattered. Much of the seismic tapes and other key information was stored in non-military areas, unlikely to be struck by air attack or fought over. But looters broke in, smashed and destroyed scientific records and files without apparent logic. Boxes containing priceless drilll cores were smashed open, their contents now a pile of useless rubble.

The industry’s development has been set back years by the war and its aftermath. Pre-war there were 40 oilrigs working, now there are none. Complete rigs vanished, involving over 50 truckloads. Officials risked their lives to save material, challenging intruders, risking being mistaken for thieves themselves. The damage was devastating, but Petrel staff are already working with the Oil Ministry to help restore their files from our own databanks. During the Baghdad battle, our local manager went to the ministry and helped officials rescue files. Later he drove 400km to Basra but found the Southern Oil Company offices there destroyed by air attack and gutted by looters. We saw no other foreign companies engaged in such efforts and believe our efforts will generate future goodwill for Petrel.

The security situation is challenging, with bandits and rebels roaming the city streets. The coalition military presence seems limited to Baghdad throroughfares and main oilfields. There is minimal coalition presence at borders and negligible overt presence throughout the country.

A purge is underway of former ruling party officials of officer rank. Though many key oil ministry people were apolitical, others were party members. We know from direct experience that those purged include reformers and even dissidents outspoken against the

“Oil Ministry with US Guard” ➤

former regime. The current indiscriminate purge of such officials seems to offend common sense. This imposes additional stresses on an already over-stretched infrastructure.

Post war policy is literally catastrophic: they fired the professional army and police – without back pay – and wonder why there’s no security. Only a few police officers are acceptable re-hires. Private weapons are widespread, essential for personal security – but forbidden. The police are unarmed, but rebels and gangsters are not. Ten weeks after Baghdad’s fall there is still no regular power and virtually no phones.

Emergency measures are authorised by UN resolution 1483. Otherwise the current administration can decide nothing. No official, whether collaborating or not, is content. They are safe as long as they do nothing. But take a controversial decision such as awarding contracts to foreign companies – necessary to attract risk capital – and you risk appearing corrupt or anti-national. The rational decision is to avoid making enemies.

Yet Iraqis remain determined to get on with life, and put aside the last wasted two decades. They will be masters of their own fate. They will build a society that reflects their own aspirations, and hopefully ancient traditions of religious tolerance.

The earlier wars and sanctions wreaked havoc. The oil industry was starved of resources. Since 1999 Petrel did as much work as under applicable laws. But public companies could not import geophones, industrial explosives or other necessary items while the embargo existed.

GEOPOLITICAL CONTEXT

There’s no point crying over spilt blood: either that of the wars, sanctions or previous government. Order and stability are required for the serious work necessary.

Infrastructure is dilapidated. Operating power plants generate only a fraction of the needed electricity. Even that is possible only through the skill of Iraqi engineers forced to improvise without necessary spares.

US officials acknowlege that decisions on Iraq's utilities and new oil concessions must wait until an interim Iraqi government takes charge.

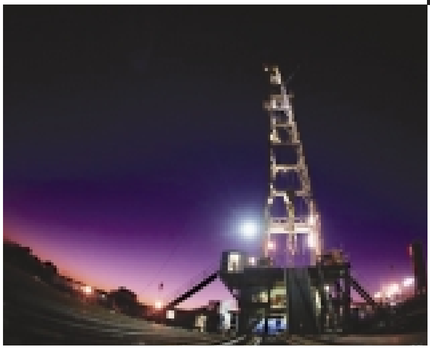
Early US Aid contracts are not a future model for Iraqi reconstruction and particularly not for the oil sector. There will be no sweetheart deals. The 1991 Kuwaiti liberation and long-standing defence of Saudi Arabia did not yield oil concessions for Britain or the USA.

There are few short cuts in the Middle East. It’s about hard work, levering your unique competence and patience. You must understand and respect local sensitivities. You bring many things they need: access to western technology, skills and capital markets. But a proud people have been humiliated by the west – first via war, then sanctions and then war again. They perceive our regional policies as displaying double standards.

THE CORROSIVE EFFECT OF SANCTIONS

It’s been 23 tough years for the Iraqi oil industry. Most of the damage was done not by war but by sanctions. This appeared to be a surprise to newcomers, but was well known by oils people familiar with Iraq’s industry. It will take ten years and maybe €100 billion to correct past mistakes, achieve the industry’s potential and rival Saudi Arabia.

Between August 1990 and early 1997, when the humanitarian ‘oil-for-food’ programme was introduced, there were no legal exports of Iraqi crude. Yet Jordan received about 90,000 barrels daily; pleading the UN Charter article exempting nations from enforcing Security Council resolutions where this would threaten essential national interests. Though Turkey never stated so publicly, they



practised a similar policy with about 140,000 barrels daily of smuggled oil. The much-maligned Syrians were late in the game, commissioning their pipeline only in 2000 and pumping only about 75,000 barrels daily – much less than that claimed. Sanctions corrupted everone they touched: many pointed fingers at the Syrians and Iran, but they knew that the real smuggling involved pro-western Jordan and Turkey.

Similar hypocrisy applied to the surcharges paid to the Iraqi Ministry of Oil, as well as official kick-backs to the Ministry, which were used for local expenses, including security. These were well-known, often complained about and behind the ‘smart sanctions’ scheme in 2000. For most of the ‘oil-for-food’ programme the majority of buyers made such payments.

We would have liked to have taken oil uplifts but could never work out a way of doing so legally. Standard practices of plausible deniability simply compounded dishonesty. We opted for the long-term but less immediately profitable path of working within the letter of UN rules. Time will tell whether we were right or just naïve. The Oil Ministry never pressured us to break the UN rules or our nation’s laws in any way. Nor have we experienced pressure or difficulties from other quarters.

Some think that judicious payments are a quick and trouble-free route to success. But Iraq’s oil industry is not traditionally corrupt, despite lurid western media coverage based on poor understanding of what really happened under sanctions. The relative lack of corruption was largely due to a strict police state.

Petrel Resources’ position has strengthened in recent months, though not in a peaceful way that we would have preferred. We expected war and knew that conquest was inevitable. The argument for economic, civilian (as opposed to military) sanctions has long since lost its persuasive power. Nonetheless, the UN put humanitarian concerns and common sense over geopolitical squabbles and legal disputes: Resolution 1483 lifted the sanctions. There are now no legal constraints on working in Iraq.

Petrel is restarting work in Iraq. Our Iraqi people are safe and highly motivated to re-build their country and careers. Our contacts survived the war. Purging of top people compromised by alleged links with the Ba’ath Party makes available world class engineers and scientists – many of them Imperial College graduates – with unparalleled knowledge of reservoirs and local conditions.

We remain, as we have long been, firmly committed to work, as a good corporate citizen under law, with the proper authorities irrespective of their political or religious complexion. Our work is of a technical and business nature. We take no side in the internal politics of any country in which we do business. Petrel as a company, our staff and contractors as individuals and indeed our host country, Ireland, has excellent relations with Iraqi people for many years. We are committed to playing a part in the development of Iraqi oil. We honoured our obligations in full under Iraqi as well as Irish and UN rules. There was never a dispute with the Ministry or purported withdrawal of our contract. We do not anticipate any serious title problems. If any such issues were to arise Petrel will participate in international arbitration and legal procedures to preserve our interests. There are some technical and security issues but these will be overcome.

We have re-launched our work, reopened our representative office, which was temporarily shut during, and are actively recruiting. As soon as the security situation permits we will push on with the detailed land survey and bedrock sampling programme in our western desert block. The immediate target is the large anticline that runs through the centre of the block. I have walked sections of this

one million hectare block: it is hard limestone, similar to that of Ireland though without much overburden. It is a sparsely populated, tribal area so we must be aware of Bedouin sensitivities.

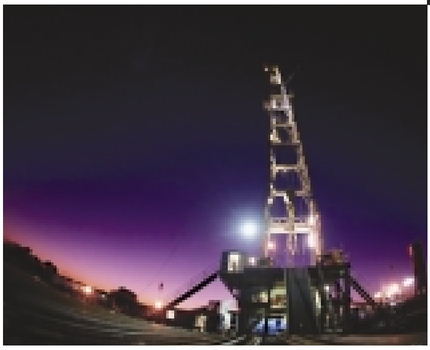
DEVELOPMENT PROJECTS

Iraq's immediate priority is in restoring production, rather than exploration. Parallel with our exploration work we are studying ways we can be involved in the development of existing fields. In 2000 we submitted a full feasibility study on the twin field development of Subba and Luhais, in the Shia-dominated south close to the Saudi and Kuwait borders and existing infrastructure. For €350 million we could bring production up to 160,000 barrels of light crude daily, with scope for further increases of up to 200,000 barrels daily. Our international group of contactors, employees and consultants are poised to start work within 3 weeks of concluding a contract. Until recently we were unable to pursue the commercial negotiations as the terms required would then have put us in breach of applicable rules. These barriers ended with the lifting of sanctions.

The immediate problem is that only the Ministry of Oil can conduct such work. The constitution expressly forbids contracts with other entities except where properly authorised and ratified by a sovereign Iraqi government. Ministry officials confirmed that there is no legal basis to contract with any foreign entity. Even UN Security Council resolutions do not appear to have any status in domestic Iraqi law. Effectively no such decisions can be taken until there is at least a reasonably legitimate interim authority. This is now the critical political and economic imperative. Petrel is in close contact with local players, ready to move as soon as there is reasonable legal and practical security.

There have been several approaches and some discussions with International companies about possible cooperation in Iraq. Petrel's objective is to maximise shareholder value. The preference of our institutional and large private investors consulted is to maintain our independence. I have discussed likely investment programmes with existing and potential institutional investors in London, Scotland and elsewhere. We do not believe that funding sensible work programmes given a acceptable level of security will be problematic. One advantage of the conflict is that it highlighted Iraq's huge reserve base, even greater exploration potential and very low costs. Investment analysts, as well as industry insiders now realise that Iraqi oil is the best minerals play for a generation. The failure of any British or US company to receive an oil concession in Kuwait or Saudi Arabia underline this point, recently confirmed by collapse of negotiation over Saudi gas. There is nothing worldwide that matches its potential.

The situation is complicated for new entrants and especially majors by the fact that Public International Law (the Fourth Geneva Convention) forbids enterprises from concluding long-term deals with transitional authorities, including occupying forces. This is why a UN resolution was necessary to permit temporary oil sales pending establishment of a transitional Iraqi authority, which it is agreed must eventually yield power to a legitimate, sovereign and representative government. Though some companies, including Lukoil and Agip, have made contact with interim administration they are usually groups with existing contracts or negotiations well underway. Any large-scale development involving super-majors must wait for legal and security reasons. Consequently those with existing knowledge and relationships remain advantaged. BP and Shell have confirmed that they require a clear and transparent legal and political framework. Total says that it will be 2 to 3 years before there are 'multi-billion dollar developments'. The interim administration does not have power to sign major



development projects. It can only concern itself with existing relationships and immediate operations, maintenance and repair work. Production remains at only a fraction of pre-war levels, itself only about half Iraq's pre-1990 capacity. Pre-war claims about the rapidity of restoring Iraqi production swiftly ignored the practical and legal difficulties. Even if existing administrators were prepared to contract with new entrants, which they are currently not, it's hard to see adequate legal security for expenditure of the hundreds of millions of dollars necessary to develop existing oilfields.

Political instability, though regrettable, may even work to Petrel's benefit: it is true that contractors, including Halliburton and Bechtel, work under the US military's guns on programmes paid for by US taxpayer-funded US Aid programmes. But contractors often lack the perspective and commitment to the country shared by long term investors risking their own capital. Petrel and our institutional shareholders are keen to make that investment. We are familiar with the challenges, are not frightened by the problems and are fortunate in the warmth of our friendships with Iraqi people as well as the American and British authorities.

Many were mystified that the sanctions, seemingly in defiance of the original mandate, have been lifted but control of immediate oil revenues have effectively been handed to a country without the necessary UN mandate. The UN Security Council conducts its business through diplomatic horse-trading in smoke-filled rooms. The decision was unanimous (though Syria abstained) and was the only intelligent policy. We understand from diplomatic sources in several countries that the USA undertook to respect the rule of Private International Law. In effect, resolution 1483 codifies the duties and rights of occupying powers under existing law and practice. They can use oil revenues but only for the good of the people in the occupied territories. They cannot legally misappropriate oil or invalidate existing contracts. They cannot sign long-term contracts to develop or explore for Iraqi oil.

THE FUTURE

Right or wrong, the conflict finally brought the Iraqi standoff to a head. This offers an opportunity for those with the skills, capital and attitude necessary to develop Iraq's reserves. This is not how most industry people wanted the crisis resolved. Conflict is bad for business because it increases costs and risks while ordinarily reducing revenues – all of which are bad for shareholders. But uncertainty deters the larger companies, opening up special opportunities for agile players open to taking chances.

Western pundits and Iraqi émigrés rarely give reliable briefings. Radio interviewers want comprehensible sound-bite replies. But now there's legal and administrative chaos. Don't hold your breath for liberal democracy. US Defense Secretary Donald Rumsfeld declared that the USA wouldn't accept an Islamist electoral victory – though a nationalist and Shia-dominated outcome is likely. The future is uncertain, so shrewd players keep options open and maximise flexibility. Ironically there is more instability than before. Iraq is a kaleidoscope of different tribes, families, religions, sects and political groups. No one knows how the many Iraqi factions will behave. The invasion aggravated sectarian divisions. The majority Shia are close to Islamist Iran and hostile to the west. Kurds have never united in two millennia. Secular Sunni Arabs and Christians ran the area for centuries, but are associated with Saddam's party. Democracy cannot work in such circumstances, at least not in tandem with western interests.

Iraq will play a key role in the world's energy future. Iraq will be extensively explored and will probably rival Saudi Arabia by 2015. The real prize is long

term. There are no short cuts. We don't know how things will evolve but Petrel will be a part of Iraq's oil development. We can resist anything except temptation!

INITIAL WORK PROGRAMME

WESTERN DESERT IRAQ: BLOCK 6

PRE-SEISMIC EXPLORATION PROGRAMME

Acting on the recommendations of leading international geological advisors, we developed the following work programme, the phase at which will be carried out in parallel, so that the company can carry out seismic acquisition during the coming winter season:

1. Field data collection
The Mesozoic section in western Iraq crops out north west of Block 6, and to a lesser extent on the Block itself. We need to examine, and get familiar with, this sequence and also collect samples. This work could be carried out in two stages. The first phase, subject to security considerations, would involve the immediate collection on Block 6 of suitable samples for micro-palaeontological, source and maturation analysis, to act as verification of the surface mapping and also to provide background control for the later drilling programme. A second phase of fieldwork, possibly in September, would collect additional samples and make a more detailed examination of potential reservoir and source rock sequences outside Block 6. GPS hand-held control would be required for the second phase of the operation. It is possible that we would require permission to carry out work outside Block 6 – assistance from the Geological Survey would in any case be valuable.

The target Palaeozoic section is exposed in western Jordan and again, should be studied and samples collected.

2. Sample analysis
Prof. Geoff. Clayton in Trinity College Dublin and Prof. Ken Higgs at University College Cork have been involved in the project to establish palynological zonation for the Palaeozoic in Saudi Arabia. The company will make use of this Irish expertise to provide sample dating, TOC (Total Oil Content) and maturation data from the field samples.

The end product of the field and sample work is to have knowledge and confidence in the stratigraphic sequence which is in the subsurface in Block 6, and to have sufficient data to critically assess any play concepts from the point of view of source, seal, reservoir and timing of migration. The data will also provide control during the drilling phase.

3. Satellite interpretation.
Petrel's current seismic interpretation has possible plays/leads controlled by major lineaments and folds. These structural controls are visible on remote sensing imagery and a structural interpretation and fracture analysis will assist the seismic interpretation. There is considerable expertise in Ireland for the processing and interpretation of these data. The end product would be in digital format for adding to other datasets on the base maps. It is essential at an early stage in the work to have available good digital format map bases. We could produce good bases from satellite data allied with existing topographic maps

4. Regional data collection
Through the Iraqi authorities we should acquire any additional useful wells, examining the critical sections if samples are available, and obtain copies of any logs etc. There are probably informative water wells in addition to the deeper petroleum exploration tests. Other wells from Saudi or Jordan should also be accessed. Any important logs can be scanned into digital format for future use.

Regional data points and any maps produced should all be on a standard regional base. There is a geological map of the region, together with many publications relating to the surface geology. All these data need to be synthesised into a single geological database. This will provide control for the second phase of field sampling, and also assist in the planning of the seismic programme and in interpretation of the seismic data.

5. Seismic interpretation
Petrel carried out an interpretation of the seismic data provided by the Iraqi authorities. However, more refined velocity information was provided at a later stage and these new data need to be applied to the interpretation to provide a second-generation suite of subsurface maps for Block 6, which will also incorporate the results arising from the satellite interpretation and the regional data set.

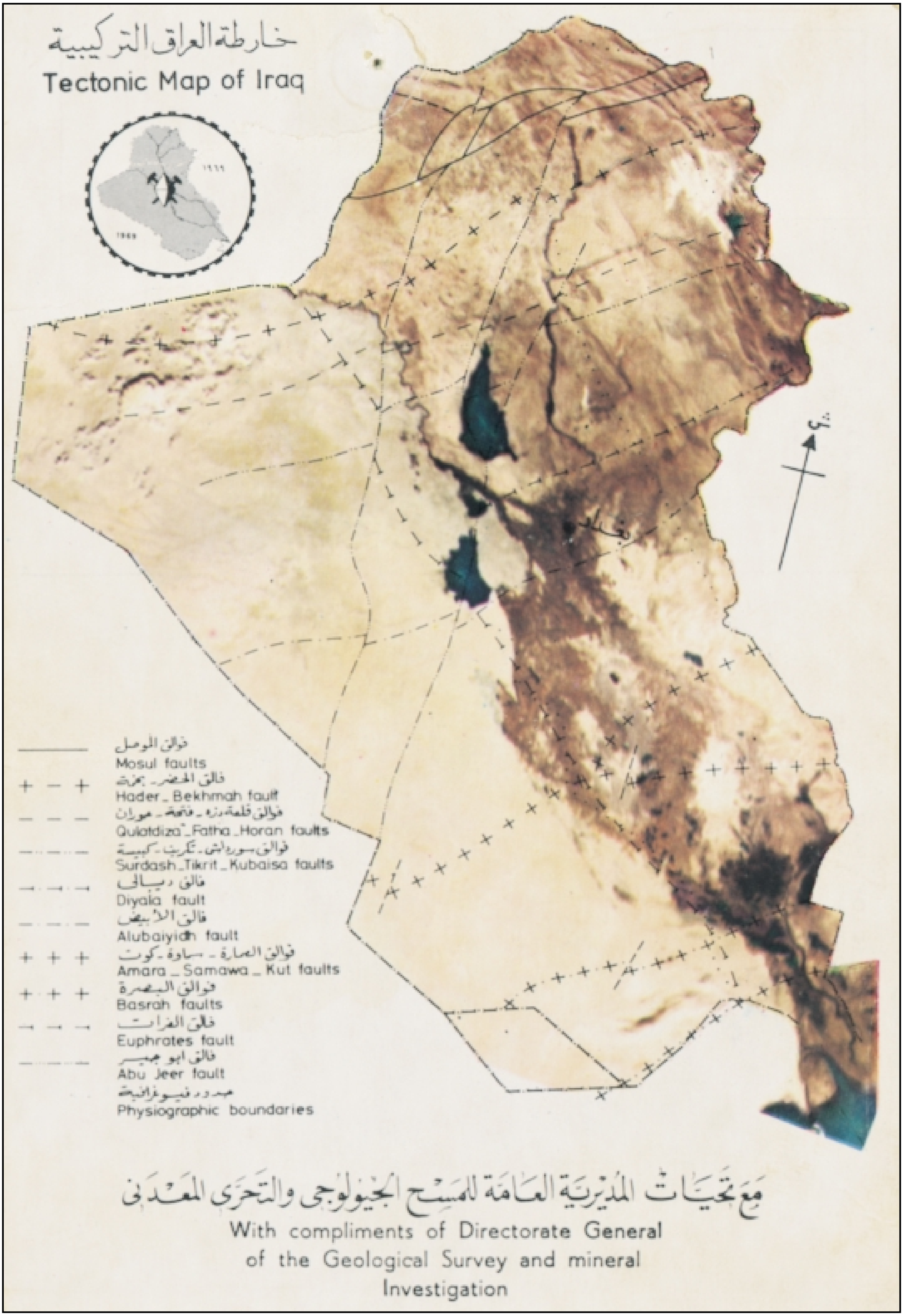
6. Seismic reprocessing
We can improve the quality of the older seismic data by reprocessing the tapes. The approach would be to reprocess a few trial lines first to judge the level of improvement, before reprocessing larger parts of the data. The Ministry of Oil quote 3325 km of data on Block 6 from 4 surveys in 1979-81 period, all from vibroseis. It could be that some of the surveys give better results than others, or that there are parts of the block, which we consider to be of lower interest. However, if the results are good and the per/km costs reasonable, then the recommendation is to reprocess much of the data. The cost of seismic reprocessing will depend on the state of the data presented to the contractor, and particularly whether the surveying data, shot-point & geophone location data are in digital or paper form.

The second-generation seismic maps would probably be sufficient for planning of the new seismic programme and for laying out the additional lines. The total seismic set, both newly acquired and reprocessed, could then be interpreted to provide the final prospect maps for drill site selection.

PETREL IN SUDAN

Because of the delays and uncertainties over the lifting of Iraqi sanctions, Petrel has looked at projects in Sudan. The ongoing Middle Eastern conflict exacerbated by 9/11 and its aftermath, led to the retreat of much western, and especially US, investment in Muslim countries. Where countries, such as Sudan, are cooperating with anti-terrorism efforts this has improved inter-governmental relations and eased working there. The EU has lifted its sanctions on Sudan. However, suspicion of the Arab world after 9/11 makes it politically impossible for Washington to lift its sanctions against Sudan. Paradoxically, US companies are therefore prejudiced by domestic politics. This offers a potential advantage for Petrel, provided we can negotiate attractive terms.

We have concluded a joint venture with the Sudanese national oil company Sudapet on offshore block 15 in northern Sudan. We are now in negotiations with the Sudanese authorities that may lead to the signing of an exploration and development licence. This project is additional and complementary to and in no way undermines our commitment to Iraq. There will be no signing bonuses or other up-front cash. Any bonus will be payable after production or in the event that Petrel sells its interest within two years of signature. The work programme negotiated is reasonable, as are the proportions of cost and profit oil, and fixed contributions.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فالق الحضر - بخمة
Hader_Bekhmah fault
فوالق قلعة دزه - فتحة - حوران
Quiatdiza_Fatha_Horan faults
فوالق سورداش - تكريت - كبيسة
Surdash_Tikrit_Kubaisa faults
فالق ديالى
Diyala fault
فالق الأبيض
Alubaiyidh fault
فوالق العمارة - سماوة - كوت
Amara_Samawa_Kut faults
فوالق البصرة
Basrah faults
فالق الفرات
Euphrates fault
فالق ابو جير
Abu Jeer fault
حدود فيزوغرافية
Physiographic boundaries
مع تحيات المديرية العامة للمسح الجيولوجي والتحري المعدني
With compliments of Directorate General
of the Geological Survey and mineral
Investigation

Report of the Directors

The directors present their annual report and the audited financial statements for the year ended December 31, 2002.

REVIEW OF ACTIVITIES AND FUTURE DEVELOPMENTS

The company is engaged in oil and gas exploration.

Further details of the group's activities and future developments are given in the Chairman's Statement.

RESULTS FOR THE YEAR

The consolidated loss for the year after taxation was €238,080 (2001 : loss after taxation €276,821).

The directors do not recommend that a dividend be declared for the year ended December 31, 2002.

SUBSEQUENT EVENTS

Subsequent to the balance sheet date the company raised €221,945 through the issue of ordinary shares.

BOOKS OF ACCOUNT

To ensure that proper books and accounting records are kept in accordance with Section 202 of the Companies Act, 1990, the directors have employed appropriately qualified accounting personnel and have maintained appropriate computerised accounting systems. The books of account are located at the company's office at 162 Clontarf Road, Dublin 3.

DIRECTORS

The current directors are set out on the inside back cover.

H. Wilson resigned as a director on 27 February 2002.
S. Borghi was appointed as director on 15 April 2003.

DIRECTORS' AND SECRETARY'S INTERESTS IN SHARES

The directors and secretary at December 31, 2002 held the following beneficial interest in the shares of the company:

	1/05/2003 Ordinary Shares of €0.0125 '000	1/05/2003 Options - Ordinary Shares of €0.0125 '000	31/12/2002 Ordinary Shares of €0.0125 '000	31/12/2002 Options - Ordinary Shares of €0.0125 '000	1/01/2002 Ordinary Shares of €0.0125 '000	1/01/2002 Options - Ordinary Shares of €0.0125 '000
J. Teeling	3,500	1,700	3,500	1,700	2,100	2,200
D. Horgan	2,600	1,400	2,600	1,400	1,100	2,200
G. Delbes	140	100	140	100	—	100
J. Finn (Secretary)	900	670	900	670	100	770

During the year, transactions with directors in respect of share options were as follows:

	Share Options Issued	Issue Price	Share Options Exercised	Exercise Price
J. Teeling	500,000	€0.0769	1,000,000	€0.0127
D. Horgan	200,000	€0.0769	1,000,000	€0.0127
G. Delbes *	—	—	—	—
J. Finn (Secretary)	200,000	€0.0769	300,000	€0.0127

* In addition, the 100,000 share option at €0.1537 previously granted to G. Delbes were cancelled and re-issued at €0.0769 each.

Report of the Directors (Continued)

SUBSTANTIAL SHAREHOLDINGS

The share register records that, in addition to the directors, the following shareholders held 3% or more of the issued share capital as at 30 April 2003:

	Number of Ordinary Shares	%
Bank of Ireland Nominees	3,250,000	6.39%
BNY (OCS) Nominees Limited	2,800,000	5.51%
BNY Gil Client Account (Nominees) Limited	1,960,000	3.86%
Scoti Company Limited C06150	1,765,000	3.47%
Vidacos Nominees Limited	1,540,000	3.03%
Yewpole Limited	1,986,694	3.91%

HEALTH AND SAFETY

The well-being of employees is safeguarded through strict adherence to health and safety standards and compliance with the requirements of the Safety, Health and Welfare at Work Act, 1989.

GOING CONCERN

The directors, having made the necessary enquiries, have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. The directors therefore propose the continued preparation of the financial statements on a going concern basis.

SUBSIDIARY

Details of the company's subsidiary are set out in Note 6 to the financial statements.

AUDITORS

Deloitte & Touche, Chartered Accountants, will continue in office as auditors in accordance with Section 160(2) of the Companies Act 1963.

Signed on behalf of the Board :

John Teeling
David Horgan } Directors

June 27, 2003

Directors' Responsibilities

Irish company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period.

In preparing those financial statements, the directors are required to

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper books of account which disclose with reasonable accuracy at any time the financial position of the company and to enable them to ensure that the financial statements are prepared in accordance with accounting standards generally accepted in Ireland and comply with Irish statute comprising the Companies Acts, 1963 to 2001 and the European Communities (Companies : Group Accounts) Regulations 1992. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Independent Auditors’ Report

We have audited the financial statements Petrel Resources Plc for the year ended December 31, 2002 which comprise the Consolidated Profit and Loss Account, the Consolidated and Company Balance Sheets, the Consolidated Cash Flow Statement, the Statement of Accounting Policies and the related notes 1 to 18. These financial statements have been prepared under the accounting policies set out in the Statement of Accounting Policies.

This report is made solely to the company's members, as a body, in accordance with Section 193 the Companies Act, 1990. Our audit work has been undertaken so that we might state to the company’s members those matters we are required to state to them in an auditors’ report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company’s members as a body, for our audit work, for this report, or for the opinions we have formed.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The directors are responsible for preparing the Annual Report, including as set out in the Statement of Directors’ Responsibilities, the preparation of the financial statements in accordance with applicable Irish law and accounting standards. Our responsibilities, as independent auditors, are established in Ireland by statute, Auditing Standards as promulgated by the Auditing Practices Board in Ireland and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with Irish statute comprising the Companies Acts, 1963 to 2001 and the European Communities (Companies: Group Accounts) Regulations, 1992. We also report to you whether in our opinion: proper books of account have been kept by the company; whether, at the balance sheet date, there exists a financial situation requiring the convening of an extraordinary general meeting of the company; and whether the information given in the directors' report is consistent with the financial statements. In addition, we state whether we have obtained all information and explanations necessary for the purposes of our audit and whether the company's balance sheet is in agreement with the books of account.

We also report to you if, in our opinion, any information specified by law regarding directors' remuneration and directors' transactions is not given and, where practicable, include such information in our report.

Independent Auditors’ Report (Continued)

We read the Directors’ Report and consider the implications for our report if we become aware of any apparent misstatement within it. Our responsibilities do not extend to other information.

BASIS OF AUDIT OPINION

We conducted our audit in accordance with the auditing standards issued by the Auditing Practices Board and generally accepted in Ireland. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements and of whether the accounting policies are appropriate to the circumstances of the company, and the group, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we evaluated the overall adequacy of the presentation of information in the financial statements.

INTANGIBLE FIXED ASSETS

In forming our opinion we have considered the adequacy of the disclosures made in the financial statements concerning the valuation of intangible fixed assets. The realisation of the intangible fixed assets of €1,081,085 included in the consolidated and company balance sheets, is dependent on the successful development of economic reserves. We draw attention to further details given in Note 5. Our opinion is not qualified in this respect.

OPINION

In our opinion the financial statements give a true and fair view of the state of the affairs of the company and the group as at December 31, 2002 and of the loss of the group for the year then ended and have been properly prepared in accordance with the Companies Acts, 1963 to 2001 and the European Communities (Companies: Group Accounts) Regulations, 1992.

We have obtained all the information and explanations we considered necessary for the purpose of our audit. In our opinion proper books of account have been kept by the company. The company’s balance sheet is in agreement with the books of account.

Independent Auditors' Report (Continued)

In our opinion the information given in the directors' report is consistent with the financial statements.

The net assets of the company, as stated in the balance sheet of the company are more than half the amount of its called-up share capital and, in our opinion, on that basis there did not exist at December 31, 2002 a financial situation which, under Section 40(1) of the Companies (Amendment) Act, 1983, would require the convening of an extraordinary general meeting of the company.

Deloitte & Touche
Chartered Accountants and Registered Auditors
Deloitte & Touche House
Earlsfort Terrace
Dublin 2

June 27, 2003

Statement of Accounting Policies

The significant accounting policies adopted by the company are as follows:

BASIS OF PREPARATION

The financial statements are prepared in accordance with the historical cost convention, the relevant Statements of Recognised Practice for the oil and gas industry, other applicable accounting standards generally accepted in Ireland and Irish statute comprising the Companies Acts, 1963 to 2001 and the European Communities (Companies: Group Accounts) Regulations, 1992.

CONSOLIDATION POLICY

The consolidated financial statements include the financial statements of the parent company and its subsidiary made up to the end of the financial year.

DEFERRED DEVELOPMENT EXPENDITURE

Exploration costs are capitalised until the results of the projects, which are based in geographic areas, are known. Exploration costs include an allocation of administration and salary costs as determined by management. If the project is successful, when the related exploration costs are written off over the life of the estimated ore reserve on a unit of production basis. Where a project is terminated, the related exploration costs are written off immediately.

TANGIBLE FIXED ASSETS

Depreciation is provided to write-off the cost less the estimated residual value of tangible assets by equal instalments over their useful economic lives as follows:

Office Equipment 5 years

FOREIGN CURRENCY

Monetary assets and liabilities denominated in foreign currencies are translated into Euro at the rate of exchange prevailing at the balance sheet date. Transactions in foreign currencies are recorded at the rate of exchange prevailing at the date of the transactions.

DEFERRED TAXATION

Deferred taxation is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date.

Deferred tax assets are only recognised to the extent that they are regarded as recoverable. They are regarded as recoverable to the extent that, on the basis of all available evidence, it can be regarded as more likely that not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Condsolidated Profit and Loss Account

For the Year Ended December 31, 2002

	Notes	2002 €	2001 €
Administrative expenses		(238,080)	(284,338)
LOSS ON ORDINARY ACTIVITIES BEFORE INTEREST		(238,080)	(284,338)
Interest income		—	7,517
LOSS FOR THE YEAR BEFORE TAXATION	1	(238,080)	(276,821)
Taxation	2	—	—
LOSS FOR THE YEAR AFTER TAXATION		(238,080)	(276,821)
Profit and loss account : opening - (deficit)		(1,618,344)	(1,341,523)
Profit and loss account : closing - (deficit)		(1,856,424)	(1,618,344)
Loss per share - basic	3	(0.54c)	(0.71c)
Loss per share – fully diluted	3	(0.54c)	(0.71c)

All gains and losses are dealt with through the profit and loss account. Results derive from continuing operations.

The financial statements were approved by the Board of Directors on June 27, 2003 and signed on its behalf by:

John Teeling
David Horgan
Directors

Condolidated & Company Balance Sheets

For the Year Ended December 31, 2002

	Notes	Group 2002 €	Company 2002 €	Group 2001 €	Company 2001 €
FIXED ASSETS					
Tangible assets	4	5,426	5,426	6,576	6,576
Intangible assets	5	1,081,085	1,081,085	912,812	912,812
Financial assets	6	—	3	—	3
		1,086,511	1,086,514	919,388	919,391
CURRENT ASSETS					
Debtors	7	27,260	27,260	4,952	4,952
Cash at bank		6,645	6,645	13,762	13,762
		33,905	33,905	18,714	18,714
CREDITORS : (Amounts falling due within one year)	8	(152,826)	(152,829)	(301,664)	(301,667)
NET CURRENT LIABILIATIES		(118,921)	(118,924)	(282,950)	(282,953)
TOTAL ASSETS LESS CURRENT LIABILITIES		967,590	967,590	636,438	636,438
CAPITAL AND RESERVES					
Called-up share capital	9	601,055	601,055	487,305	487,305
Capital conversion reserve fund	10	7,694	7,694	7,694	7,694
Share premium	11	2,215,265	2,215,265	1,759,783	1,759,783
Profit and loss account - (deficit)		(1,856,424)	(1,856,424)	(1,618,344)	(1,618,344)
EQUITY SHAREHOLDERS' FUNDS	12	967,590	967,590	636,438	636,438

The financial statements were approved by the Board of Directors on June 27, 2003 and signed on its behalf by:

John Teeling
David Horgan } Directors

Consolidated Cash Flow Statement

For the Year Ended December 31, 2002

	Notes	2002 €	2001 €
NET CASH OUTFLOW FROM OPERATING ACTIVITIES	14(a)	(406,812)	(238,363)
RETURNS ON INVESTMENT AND SERVICING OF FINANCE			
Interest received		—	7,517
NET CASH INFLOW FROM RETURNS ON INVESTMENTS AND SERVICING OF FINANCE		—	7,517
TAXATION			
Corporation tax paid		—	—
CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT			
Payments to acquire intangible fixed assets		(168,273)	(409,455)
Payment to acquire tangible fixed asset		(1,264)	(4,606)
NET CASH OUTFLOW BEFORE FINANCING		(576,349)	(644,907)
FINANCING			
Issue of ordinary share capital		569,232	—
NET CASH INFLOW FROM FINANCING		569,232	—
DECREASE IN CASH	14(b)	(7,117)	(644,907)

Notes to the Financial Statements

For the Year Ended December 31, 2002

1. LOSS BEFORE TAXATION

	2002	2001
	€	€
The loss before taxation is stated after charging the following items:		
Depreciation	2,414	2,162
Directors' remuneration		
– fees	32,400	31,740
– salary	40,500	28,142
Auditors' remuneration	7,000	4,200
Staff costs – salaries	20,351	35,166

The company had two employees during the year.

2. TAXATION

No charge to taxation arises in the current year as the company has availed of available loss relief. No deferred tax asset has been recognised on accumulated tax losses as the recoverability of any assets is not likely in the foreseeable future. At the year end deferred tax amounts totalling €73,142 (2001: €44,708) were not recognised.

3. LOSS PER SHARE

Basic earnings per share is computed by dividing the loss after taxation for the year available to ordinary shareholders by the sum of the weighted average number of ordinary shares in issue and ranking for dividend during the period. Diluted earnings per share is computed by dividing the loss after taxation for the year by the weighted average number of ordinary shares in issue, adjusted for the effect of all dilutive potential ordinary shares that were outstanding during the year.

The following table sets forth the computation for basic and diluted earnings per share (EPS):

	2002 €	2001 €
Numerator		
Numerator for basic EPS retained loss	(238,080)	(276,821)
Denominator		
Denominator for basic EPS	44,276,054	38,984,388
Effect of diluted securities – options	—	—
Denominator for diluted EPS	44,276,054	38,984,388
Basic EPS	(0.54c)	(0.71c)
Diluted EPS	(0.54c)	(0.71c)

Basic and diluted EPS are the same in respect of 2002 as the effect of outstanding options is anti-dilutive and therefore excluded.

4. TANGIBLE FIXED ASSETS

	2002 €
Group and Company	
Office equipment	
Cost :	
At January 1, 2002	10,810
Additions	1,264
At December 31, 2002	12,074
Accumulated Depreciation	
At January 1, 2002	4,234
Charge for year	2,414
At December 31, 2002	6,648
Net book value :	
At December 31, 2002	5,426
At December 31, 2001	6,576

5. INTANGIBLE ASSETS

	2002
	€
Group and Company	
Deferred development expenditure:	
Cost :	
At January 1, 2002	912,812
Additions	168,273
At December 31, 2002	1,081,085
Net book value :	
At December 31, 2002	1,081,085
At December 31, 2001	912,812

Intangible Assets
Deferred development expenditure at December 31, 2002 represents exploration and related expenditure in respect of projects in Iraq.

The realisation of this intangible asset is dependent on the development of economic reserves, including the ability to raise finance to develop the project. Should this prove unsuccessful the value included in the balance sheet would be written off.

The directors are aware that by its nature there is an inherent uncertainty in such development expenditure as to the value of the asset. In addition, the current and economic political situation in Iraq, is uncertain. Having reviewed the deferred development expenditure at December 31, 2002, the directors are satisfied that the value of the intangible asset is not less than net book value.

6. FINANCIAL ASSETS

	2002 €	2001 €
Investment in subsidiary company		
Parent company		
Shares at cost - unlisted:		
Opening balance	3	3
Closing balance	3	3

The group consisted of the parent company and the following wholly owned subsidiary as at December 31, 2002:

Name Office	Registered Share	Group Business	Nature of
Petrel Industries Limited	162 Clontarf Road, Dublin 3.	100%	Dormant

7. DEBTORS

	Group and Company 2002 €	2001 €
Amounts falling due within one year:		
VAT refund due	5,889	756
Sundry	21,371	4,196
	27,260	4,952

8. CREDITORS : (Amounts falling due within one year)

	Group 2002 €	2001 €	Company 2002 €	2001 €
Accruals	152,826	301,664	152,826	301,664
Amount due to group company	—	—	3	3
	152,826	301,664	152,829	301,667

9. SHARE CAPITAL

	2002 €	2001 €
Authorised:		
200,000,000 ordinary shares of € 0.0125 (2001 : 200,000,000 ordinary shares of IR£0.0125 each)	2,500,000	2,500,000
Allotted, Called-Up and Fully Paid:		
Opening 38,984,388 shares of €0.0125 each (2001 : 38,984,388 shares of IR£0.01 each)	487,305	494,999
Issued:		
9,100,000 shares of €0.0125 each (2001 : Nil shares)	113,750	—
Transfer to capital conversion reserve fund	—	(7,674)
Closing 48,084,388 shares of €0.0125 each (2001 : 38,984,388 shares of €0.0125 each)	601,055	487,305

The total number of options outstanding at December 31, 2002, including to directors was €4,640,000 (2001: €5,990,000) shares. The options are exercisable at prices between €0.0127 and €0.15 in accordance with the option agreement.

During the year, 140,493 ordinary shares were issued at €0.0769 each in full settlement of outstanding fees in respect of development costs in Iraq.

10. REDENOMINATION AND RENOMINALISATION OF SHARE CAPITAL

Due to the introduction of the Euro each of the issued and unissued ordinary shares of IR£0.01 per share was redenominated into an ordinary share of €0.0126774 following a resolution passed at the Annual General Meeting held on 21 July 2001. Every such share was then renominalised to be an ordinary share of €0.0125. An amount equal to the reduction in the issued share capital resulting from this renominalisation was transferred to a capital conversion reserve fund (see below).

Capital Conversion Reserve Fund

	2002	2001
	€	€
Opening	7,694	—
Transfer from share capital	—	7,694
Closing	7,694	7,694

11. SHARE PREMIUM

	Group and Company	
	2002	2001
	€	€
Opening balance	1,759,783	1,759,783
Arising on shares issued during the year	455,482	—
Closing balance	2,215,265	1,759,783

12. RECONCILIATION OF MOVEMENT IN SHAREHOLDERS' FUNDS

	2002	2001
	€	€
Opening shareholders' funds	636,438	913,259
Loss for the year	(238,080)	(276,821)
Issue of shares:		
– at par	113,750	—
– share premium	455,482	—
Closing shareholders' funds	967,590	636,438

Notes to the Financial Statements (Continued)

For the Year Ended December 31, 2002

13. LOSS ATTRIBUTABLE TO PETREL RESOURCES PLC

The loss after taxation in the parent company amounted to €238,080 (2001 loss : €276,821).

A separate profit and loss account for Petrel Resources plc (the company) has not been prepared because the company has complied with the conditions laid down in Section 43(2) of the European Communities (Companies : Group Accounts) Regulations 1992.

14. CASH FLOW STATEMENT

(a) Reconciliation of operating profit to net cash outflow from operating activities

	2002 €	2001 €
Operating loss	(238,080)	(284,338)
(Decrease)/increase in creditors	(148,838)	32,210
(Increase)/decrease in debtors	(22,308)	11,603
Depreciation	2,414	2,162
Net cash outflow from operating activities	(406,812)	(238,363)

(b) Analysis of net funds

	At 1 January 2002	Cash flow	At 31 December 2002
Cash in bank and in hand	13,762	(7,117)	6,645

(c) Reconciliation of net cash flow to movement in net funds

	2002 €	2001 €
Decrease in cash in the year	(7,117)	(644,907)
Change in net funds resulting from cash flows	(7,117)	(644,907)
Movement in net funds in the year	(7,117)	(644,907)
Net funds at start of year	13,762	58,669
Net funds at end of year	6,645	13,762

15. RISK MANAGEMENT

The group's financial instruments comprise cash balances and various items such as trade debtors and trade creditors which arise directly from trading operations. The main purpose of these financial instruments is to provide working capital to finance group operations.

The group does not enter into any derivative transactions, and it is the group's policy that no trading in financial instruments shall be undertaken.

The main financial risk arising from the group's financial instruments is liquidity risk.

Interest Rate Risk

The group finances its operations through the issue of equity shares, and has no fixed interest rate agreements. The group has no significant exposures to interest rate risk.

Liquidity Risk

As regards liquidity, the group's exposure is confined to meeting obligations under short term trade creditor agreements. This exposure is not considered to be significant, and is fully financed from operating cashflow, or where this is insufficient during the development stage, through additional issues of ordinary equity shares.

Foreign Currency Risk

Although the group is based in the Republic of Ireland, amounts held as deferred development expenditure were originally expended in currencies other than Euro aligned currencies. However, this expenditure is not considered to be a monetary asset, and has been translated to the reporting currency at the rates of exchange ruling at the dates of the original transactions. The group at present does not hold significant foreign currency monetary assets or liabilities.

The group also has transactional currency exposures. Such exposures arise from expenses incurred by the group in currencies other than the functional currency. It is expected that almost all future revenue will arise in US dollars. The group seeks to minimise its exposure to currency risk by closely monitoring exchange rates, and restricting the buying and selling of currencies to predetermined exchange rates within specified bands.

The group does not presently utilise swaps or forward contracts to manage its currency exposures, although such facilities are considered and be may used where appropriate in the future.

16. RELATED PARTY TRANSACTIONS

During the year the company paid consultancy fees to Guy Delbes amounting to €23,644. Guy Delbes is a director of the company.

17. SUBSEQUENT EVENT

Subsequent to the balance sheet date the company raised Stg£144,375 through the issue of ordinary shares at Stg£0.0525 each.

18. NON-CASH TRANSACTIONS

Details of non-cash transactions during the year are set out in Note 9.

Notice of Meeting

Notice is hereby given that the annual general meeting of the members of Petrel Resources plc will be held on Friday, 25 July, 2003 in the Shelbourne Hotel, St. Stephens Green, Dublin 2 at 12 noon for the following purposes:

1. To receive the report of the directors and audited financial statements for the year ended December 31, 2002.

2. To re-appoint director: G. Delbes retires in accordance with article 95 and seeks re-election.

3. S. Borghi retires in accordance with article 101 and seeks election.

4. To authorise the directors to fix the remuneration of the auditors.

5. To transact any other ordinary business of an annual general meeting.

By order of the Board
James Finn
Secretary

June 27, 2003

Form of Proxy

I/We ....
(BLOCK LETTERS)

of...
being (an) ordinary shareholder(s) of Petrel Resources plc, hereby appoint the Chairman of the Meeting#

....

of...
as my / our proxy to vote for me / us and on my / our behalf at the Annual General Meeting of the Company to be held on Friday, 25 July, 2003 in the Shelbourne Hotel, St. Stephens Green, Dublin 2 at 12 noon and at any adjournment thereof.

I/We direct my / our proxy to vote on the resolutions set out in the Notice convening the Meeting as follows:

	For *	Against *
Reports and Accounts	☐	☐
Re-election of Director G. Delbes	☐	☐
Election of Director S. Borghi	☐	☐
Remuneration of Auditors	☐	☐

Signature..

Dated the ....day of...2003

If it is desire to appoint another person as proxy other than the Chairman of the Meeting the name and address of the proxy, who need not be a member of the Company, should be inserted, the words "the Chairman of the meeting" deleted and the alterations initialled.

* The manner in which the proxy is to vote should be indicated by inserting an "X" in the boxes provided. Proxies not marked as for or against will be regarded as giving the proxy authority to vote, or to abstain at his/her discretion.

NOTES

1. In the case of a corporation this proxy must be under its common seal or under the hand of an officer or attorney duly authorised in writing.

2. To be effective this proxy must reach the address on the reverse hereof not less than 48 hours before the time of the meeting.

3. In the case of joint holders, the vote of the senior who tenders a vote whether in person of by proxy, shall be accepted to the exclusion of the votes of the other joint holders and for this purpose seniority shall be determined by the order in which the names stand in the Register of member in respect of such holding.

FOLD 1

FOLD 2

FOLD 3
(then turn in)

The Secretary
Petrel Resources Plc
162 Clontarf Road
Dublin 3
Ireland