



2003
Annual Report

CORPORATE PROFILE

Canoro Resources Ltd. is an international oil and gas company whose focus is India and Russia. Canoro currently operates in India with the development of the AA-ON/7 exploratory and Amguri production blocks. The Corporation also has mature business development activities ongoing in both India and Russia.

Canoro trades on the TSX Venture Exchange under the symbol "CNS".

ANNUAL MEETING

Shareholders are invited to attend the Company's Annual General Meeting on Tuesday, September 16, 2003 at 2:30 p.m., 5th Floor, 715 - 5th Avenue S.W., Calgary, Alberta.

Table of Contents

Message to the Shareholders	Page 1
Principal Properties	3
Management's Discussion and Analysis	5
Management's Report	7
Auditors' Report to the Shareholders	8
Consolidated Financial Statements	9
Notes to Consolidated Financial Statements	12
Corporate Information	IBC

MESSAGE TO THE SHAREHOLDERS

On behalf of the Board of Directors of Canoro Resources Ltd. we are pleased to present our Annual Report for the fiscal year ended March 31, 2003.

This fiscal year may best be described as a continuation of the turnaround that was initiated by B. Vaughan Armstrong in the fall of calendar 2001, and achievement of financial and operational milestones by the new management team.

Canoro has focused its efforts on the Indian market and plans to continue to concentrate on both the AA-ON/7 exploration block and the Amguri production block. In addition, Canoro is searching for additional 'high impact' type projects in both the Indian and Russian markets.

India, a net importer of both oil and natural gas is an excellent market for many reasons, not the least of which is the fact that only 6 of its 22 sedimentary basins have been significantly explored. The potential size of hydrocarbon discoveries in India is on a world class scale as evidenced by recent discoveries off India's East Coast. For this reason alone it is worth continuing to participate in and expand Canoro's interests in this market.

Upon joining Canoro in August 2002 management set priorities to resolve the ownership and control issues which had been a major obstacle to the advancement of Canoro's interests in India, and to raise capital to fund Canoro's programs and initiatives. Both these objectives were met.

Canoro raised \$ 3.3 million of capital during its fiscal year ended March 31, 2003 to fund its planned activity through December 2003, including:

- ◆ A \$2 million financing through a public offering which closed on February 20, 2003
- ◆ A \$1 million private placement financing which closed on November 11, 2002
- ◆ The balance of a \$1 million debenture financing which was completed on November 4, 2002

We wish to thank everyone who participated in these financings. Each of the three financings was over-subscribed.

The goal now is to put Canoro into positive cash flow by finalizing negotiations on the Amguri Block Mining Lease Agreement which would then enable us to work over the existing oil wells and restart production. Simultaneously we will continue our efforts to explore and evaluate the AA-ON/7 block with a view to drilling Canoro's first exploratory well.


Canoro is now well positioned to take advantage of its opportunities. As a debt free company with operatorship and a majority working interest position in both blocks in India, we are in a position to seek the most efficient and beneficial ways for Canoro to grow and reward its shareholders.

Canoro is committed to communicating effectively with its shareholders. During the fiscal year we improved how we distribute our news releases so they are more readily available at the major financial portals on the Internet. Also, Canoro's PowerPoint investor presentation is now available at our upgraded website www.canoro.com.

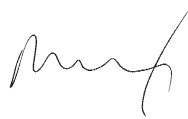
Canoro's management and directors appreciate your patience and continued support. To paraphrase one successful oil and gas exploration and production operator in India: *"In India it takes a long time to get things done... but it is worth the wait"*.

We truly believe that Canoro is now on the path to realizing its goal of maximizing shareholder value.

On Behalf of the Board of Directors



L. B. Kondratoff
President and Chief Executive Officer



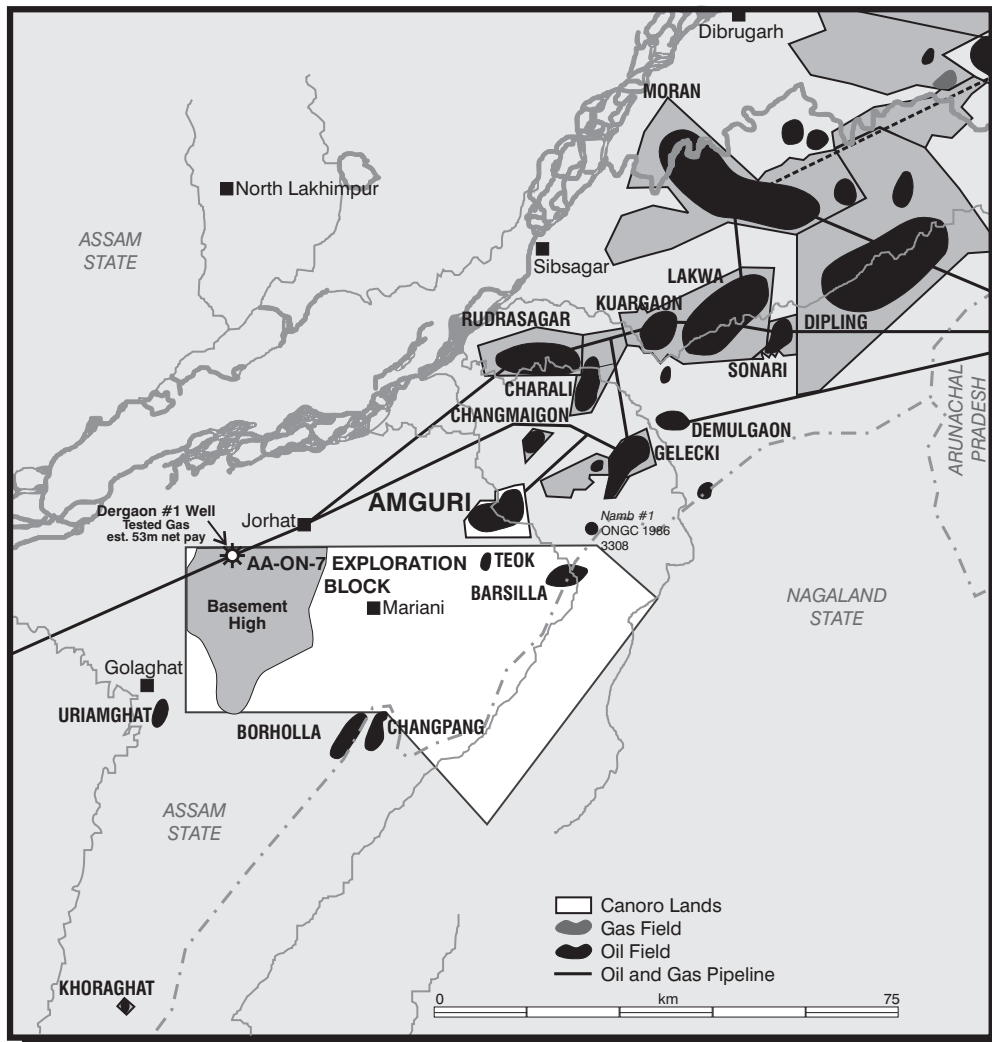
B. Vaughan Armstrong
Chairman of the Board

August 20, 2003

PRINCIPAL PROPERTIES

AA-ON/7 Exploratory Block

The AA-ON/7 exploratory block covers an area of 1,934 square kilometers in both the Assam and Nagaland states in North East India. Only five wells have been drilled in this entire block. One well (Dergaon #1) had evidence of multiple zone hydrocarbon potential. This well is slated for a long-term production test during the fourth quarter of calendar 2003. This block also contains more than 1,000 line kilometers of existing 2-D seismic which is available to Canoro and its partner for reprocessing.



Canoro entered into the AA-ON/7 Production Sharing Contract (PSC) as part of a consortium in partnership with Centurion Energy International Inc. Part of Canoro's turnaround strategy was to take over Centurion's interest and to assume the role of the Operator on the block after Centurion elected to focus on its more

advanced international operations outside India. On February 13, 2003 Canoro announced that the Government of India had approved the assignment of a 30% interest and of operatorship in the AA-ON/7 block to Canoro. This increased Canoro's working interest in the block to 65% from 35%.

Canoro has also recently received approval from the Government of India for an 18-month extension to its Phase I obligations on the AA-ON/7 Block. This extension will lapse on September 26, 2004, and provides an adequate amount of time to perform the reprocessing and seismic acquisition on the block, along with the Dergaon well test mentioned above.

The AA-ON/7 PSC has three stages. The first stage calls for the reprocessing of a minimum of 100 line kilometers of 2-D seismic and the acquisition of 50 line kilometers of 2-D seismic. Canoro is presently reprocessing 200 line kilometers of seismic and intends to acquire between 50 to 150 line kilometers of seismic during the dry season that runs from November to March. Based on the result of our seismic reinterpretation and acquisition and a preliminary production test on certain of the zones in the Dergaon well, Canoro will determine the best place to drill an exploratory well subject to approval by its partners and the Government of India (a stage two commitment). The third stage is the declaration of commerciality based on a discovery in stage two, or an optional second exploratory well.

AMGURI Production Block

The Amguri Production Block is a 52.75 square kilometer block that contains nine wells of which four are expected to be productive after well workovers. One of these four wells (well #8A) is currently producing gas after a workover last December.

Canoro purchased a 35% working interest in the Amguri Block in 1998 from the Assam Tea Company and on July 3, 2003 announced the purchase of an additional 25% interest in the Amguri Block and project operatorship from Joshi Technologies International Inc. (subject to Government of India approval).

The Mining Lease was released by the Assam State on April 29, 2003. The next step is the final negotiation and signing of the Petroleum Mining Lease Agreement. Following this approval, the partners will realize cash flow from the existing producing gas well; Canoro will then determine a Development Plan for Amguri subject to approval by its partners and the Government of India. It is Canoro's desire to begin workover operations on the existing wells on the Amguri Production Block during the dry season referred to above.

INDIAN AND RUSSIAN BUSINESS DEVELOPMENT

Canoro is evaluating additional business opportunities in both Russia and India. This is where Canoro's core expertise lies and these are also two areas that have enormous hydrocarbon potential.

The Corporation is looking at prospective blocks being offered in the Government of India's fourth round of projects offered under its New Exploration Licensing Policy (NELP IV) amongst other opportunities that may arise in India in the future.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Canoro is engaged in early stage acquisition, exploration, and development of petroleum and natural gas in India and Russia. During the fiscal year ended March 31, 2003 Canoro continued to focus on consolidating and expanding its interests in the Amguri Production Block and the AA-ON/7 Exploratory Block in Assam State, India.

Following its announced acquisition in July 2003 of a further 25% interest in the 52.75 square kilometer Amguri production block, Canoro will have operatorship and a 60% working interest in the block, subject to Government of India approvals and final closing.

Canoro was designated operator of the AA-ON/7 Exploration Block in Assam State, India, following consolidation of Canoro's 65% interest in September 2002. Recently Canoro obtained an 18-month extension on the Phase I seismic work program to September 26, 2004 on this block.

Results of Operations

During the year Canoro generated only a modest amount of net revenue from its Canadian oil and gas property due to operational difficulties, and returned the property to the vendor in exchange for cancelling all the outstanding debt on the property. As a result, the Corporation had a net loss of \$1.1 million or (\$0.06) per share in the fiscal year ended March 31, 2003 compared to a net loss of \$0.8 million or (\$0.05) per share in the prior year. Cash flow used in operations was (\$0.6) million or (\$0.03) per share in 2003 compared to (\$0.6) million or (\$0.04) per share in 2002. The primary reasons for change in results from the prior year were non-cash items: stock-based compensation for management services rendered, an allowance for stock-based compensation calculated on stock options granted to consultants and financial institutions, an allowance for discount on convertible debentures, and foreign exchange loss on bank guarantee funding held in U.S. dollars since the prior year.

Corporate

Administrative costs increased in 2003 to \$814,000 compared to \$794,000 in 2002. Management fees were \$257,000 (\$64,000 of this related to fiscal year 2002), up from \$33,600 booked in 2002. This increase was due to the value of shares issued to the Chairman in his then role as President and CEO and to another director for management and corporate reorganization services. Office costs increased to \$160,000 in 2003 from \$117,000 in 2002 due to computer network and central filing system setup in Calgary, and Russia personnel and business development costs. Legal, business promotion and termination costs decreased in 2003 from 2002. Salaries and benefits accounted for 18% (2002 - 24%) of general and administrative expenses.

Interest and finance costs increased to \$78,000 in 2003 from \$58,000 in 2002 due to the issuance of further convertible debentures. \$70,000 of these costs were paid by issuance of common shares to debenture holders in lieu of cash.

Capital Expenditures

Cash capital expenditures totaled \$395,000 in 2003 compared to \$440,000 in 2002. In 2003 \$105,000 in issuance of common share performance bonuses were capitalized (2002 - \$60,000). All of the 2003 expenditures were dedicated to the India projects, while in 2002 \$250,000 was spent on the India projects and \$190,000 was spent on a Canadian property. In 2003 \$112,000 was placed in restricted refundable investments as security for contract performance guarantees in India (2002 - \$339,000).

On July 3, 2003 the Corporation entered into an agreement to purchase a 25% interest in an oil and gas property in India. To date the Corporation has paid U.S.\$175,000 towards the purchase. If all approvals are not received by a certain date agreed upon by the Corporation and vendor, then the agreement may be terminated and the lesser of U.S.\$40,000 or 15% of payments made to the vendor is non-refundable. Further payments are due upon receiving certain approvals from the Government of India and completion and filing of necessary documents and permits in India.

Liquidity and Capital Resources

The Corporation has met its funding needs through a combination of equity issues and a convertible debenture. During 2003 net funds of \$2.75 million were raised through issuance of common shares (2002 - \$nil), and \$0.3 million (2002 - \$0.7 million) was raised through issuance of convertible debentures. The debentures, maturing February 13, 2004, bear interest at 10% per annum. During the year \$900,000 in debentures were converted into common shares (2002 - \$nil) at \$0.35 per share and the remaining \$100,000 are convertible at the rate of one common share for each \$0.60 of principal until maturity.

The Corporation had working capital of \$1.875 million at March 31, 2003 compared to a working capital deficit of \$168,000 at the prior year-end.

The AA-ON/7 Production Sharing Contract commits the Corporation to acquire 50 line kilometers of seismic and reprocess 100 line kilometers on the property before September 26, 2004 at an estimated cost to the Corporation of \$1.5 million and, if seismic data identifies a drilling target, to drill one exploratory well on the property before March 31, 2006 at an estimated dry hole cost to the Corporation of \$1.5 million.

Acquisition of Private Company

On August 28, 2002 the Corporation finalized an agreement resulting in the acquisition of all of the issued and outstanding shares of a private Alberta company for consideration of approximately \$280,000, consisting of 800,000 shares of the Corporation at an ascribed value of \$0.35 per share. The assets of the acquired company consisted of various contracts under negotiation for potential acquisition of interests in oil and gas properties in Russia. The transaction is accounted for on the balance sheet as goodwill.

MANAGEMENT'S REPORT


All information in this Annual Report is the responsibility of Management. The financial statements necessarily include amounts that are based on estimates, which have been objectively developed by Management using all relevant information. The financial information contained elsewhere in this report has been reviewed to ensure consistency with the financial statements.

Management maintains a system of internal accounting controls designed to provide reasonable assurance that assets are safeguarded, transactions are properly authorized and financial records are properly maintained to provide reliable information for the preparation of financial statements.

The Audit Committee of the Board of Directors, comprised of non-management directors, has reviewed the financial statements with Management and KPMG. The financial statements have been approved by the Board of Directors on the recommendation of the Audit Committee.



L. B. Kondratoff
President and Chief Executive Officer



Brian M. Hearst
Chief Financial Officer

AUDITORS' REPORT TO THE SHAREHOLDERS

We have audited the consolidated balance sheets of Canoro Resources Ltd. as at March 31, 2003 and 2002 and the consolidated statements of operations and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Corporation as at March 31, 2003 and 2002 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP

Chartered Accountants

Calgary, Canada
July 30, 2003

CONSOLIDATED BALANCE SHEETS

March 31, 2003 and 2002

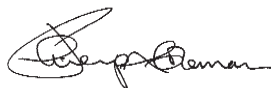
	<u>2003</u>	<u>2002</u>
Assets		
Current assets:		
Cash and cash equivalents	\$ 2,316,535	\$ 238,890
Accounts receivable	20,481	54,517
Prepaid expenses	18,244	31,079
	<u>2,355,260</u>	324,486
Restricted investments (note 4)	450,583	338,776
Deferred financing costs (note 7)	-	26,250
Capital assets (note 5)	2,504,617	2,168,683
Goodwill (note 12)	280,000	-
	<u>\$ 5,590,460</u>	<u>\$ 2,858,195</u>
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 394,589	\$ 327,497
Current portion of convertible debentures (note 7)	87,543	-
Promissory note payable (note 6)	-	164,999
	<u>482,132</u>	492,496
Convertible debentures (note 7)	-	539,805
Provision for future site restoration	-	1,500
Shareholders' equity:		
Share capital (note 8)	11,801,896	7,237,471
Convertible debentures (note 7)	23,449	185,035
Deficit	<u>(6,717,017)</u>	<u>(5,598,112)</u>
	5,108,328	1,824,394
Future operations (note 1)		
Commitments (notes 5 and 11)		
Contingencies (note 14)		
Subsequent event (note 15)		
	<u>\$ 5,590,460</u>	<u>\$ 2,858,195</u>

See accompanying notes to consolidated financial statements.

Approved by the Board:



Director



Director

CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT

Years ended March 31, 2003 and 2002

	<u>2003</u>	<u>2002</u>
Revenues:		
Oil and gas sales	\$ 12,277	\$ 140,119
Interest	-	13,457
	<u>12,277</u>	<u>153,576</u>
Expenses:		
General and administrative	814,341	793,632
Annual accretion of discount on convertible debentures (note 7)	103,569	24,840
Stock-based compensation (note 8)	82,000	-
Interest and financing	77,946	57,515
Amortization of deferred financing costs (note 7)	32,375	1,750
Depletion, depreciation and site restoration	21,758	47,697
Foreign exchange loss	20,033	-
Operating	3,160	23,511
	<u>1,155,182</u>	<u>948,945</u>
Loss before other item	(1,142,905)	(795,369)
Other item:		
Gain on disposal of capital assets (note 6)	24,000	-
Net loss	(1,118,905)	(795,369)
Deficit, beginning of year	(5,598,112)	(4,802,743)
Deficit, end of year	<u>\$ (6,717,017)</u>	<u>\$ (5,598,112)</u>
Net loss per share – basic and diluted (note 8(e))	<u>\$ (0.06)</u>	<u>\$ (0.05)</u>

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended March 31, 2003 and 2002

	<u>2003</u>	<u>2002</u>
Cash provided by (used in):		
Operations:		
Net loss	\$ (1,118,905)	\$ (795,369)
Add items not affecting cash:		
Common shares issued for services performed	256,500	64,000
Annual accretion of discount on convertible debentures	103,569	24,840
Stock-based compensation	82,000	–
Common shares issued for interest	71,572	–
Amortization of deferred financing costs	32,375	1,750
Gain on disposal of capital assets	(24,000)	–
Depletion, depreciation and site restoration	21,758	47,697
Common shares issued on settlement of debt	–	66,000
Funds utilized in operations	(575,131)	(591,082)
Net change in non-cash working capital (note 10)	153,963	217,463
	<u>(421,168)</u>	<u>(373,619)</u>
Financing:		
Issuance of common shares and special warrants for cash	2,999,900	–
Issuance of convertible debentures	300,000	700,000
Share issue costs	(254,089)	–
Repayment of share purchase loans	–	47,596
	<u>3,045,811</u>	<u>747,596</u>
Investments:		
Capital asset additions	(395,191)	(440,023)
Restricted investments	(111,807)	(338,776)
Net change in non-cash working capital (note 10)	(40,000)	–
	<u>(546,998)</u>	<u>(778,799)</u>
Increase (decrease) in cash and cash equivalents	2,077,645	(404,822)
Cash and cash equivalents, beginning of year	238,890	643,712
Cash and cash equivalents, end of year	<u>\$ 2,316,535</u>	<u>\$ 238,890</u>

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Years ended March 31, 2003 and 2002

General:

Canoro Resources Ltd. (the "Corporation") was continued under the Business Corporations Act (Alberta) and is engaged in the acquisition, development and exploration for and production and marketing, of petroleum and natural gas in India and Russia.

1. Future operations:

These financial statements have been prepared by management on the basis of accounting principles applicable to a going concern, which assumes that the Corporation will continue in operation for the foreseeable future and will be able to realize its assets and discharge its obligations in the normal course of operations.

As at March 31, 2003, the Corporation had working capital of \$1,873,128 (2002 - a deficiency of \$168,010) and had incurred a net loss of \$1,118,905 (2002 - \$795,369), and utilized funds from operations totaling \$575,131 (2002 - \$591,082) for the year then ended. The application of the going concern concept is dependent upon the Corporation's ability to generate future profitable operations and obtain the necessary financing to do so. During the year ended March 31, 2003, the Corporation issued common shares for cash totaling approximately \$3,000,000 (see note 8). While these funds will be used to continue the Corporation's development of its petroleum and natural gas properties in India, additional funds will still be required to be generated in fiscal 2004 to continue the Corporation's development of its petroleum and natural gas properties in India (see note 5).

Management believes the going concern assumption to be appropriate for these financial statements. If the going concern assumption were not appropriate for these financial statements, adjustments might be necessary to the carrying values of assets and liabilities, reported revenues and expenses and the balance sheet classifications used.

2. Significant accounting policies:

(a) Basis of presentation:

These consolidated financial statements include the accounts of the Corporation and its subsidiaries, all of which are wholly-owned. Certain of the comparative figures have been reclassified to conform to the current year's financial statement presentation.

(b) Petroleum and natural gas properties:

(i) Capitalized costs:

The Corporation follows the full cost method of accounting for its petroleum and natural gas properties. Under this method all costs related to the exploration for and development of petroleum and natural gas reserves are capitalized in cost centers on a country-by-country basis. Costs include lease acquisition costs, geological and geophysical expenses, overhead directly related to exploration and development activities and costs of drilling both productive and non-productive wells. Proceeds from the sale of properties are applied against capitalized costs, without any gain or loss being realized, unless such sale would significantly alter the rate of depletion and depreciation by 20% or more.

2. Significant accounting policies (continued):

- (ii) Depletion and depreciation:

Depletion of petroleum and natural gas properties and depreciation of production equipment is provided using the unit-of-production method based upon estimated proven petroleum and natural gas reserves, before royalties, on a cost center basis. The costs of significant unevaluated properties are excluded from costs subject to depletion. For depletion and depreciation purposes, relative volumes of petroleum and natural gas production and reserves are converted at the energy equivalent conversion rate of six thousand cubic feet of natural gas to one barrel of crude oil.
- (iii) Ceiling tests:

In applying the full cost method, the Corporation calculates a ceiling test for each cost center whereby the carrying value of petroleum and natural gas properties and production equipment, net of recorded future income taxes and the accumulated provision for site restoration costs, is compared annually to an estimate of future net cash flow from the production of proven reserves for the individual cost centres. Net cash flow is estimated using period end prices; less estimated future site restoration, general and administrative expenses, financing costs and income taxes. In addition, the net capitalized costs of all cost centers, less related future income taxes, are limited to the estimated future net revenues from all cost centers plus the net cost of major development projects and unproved properties less future removal and site restoration costs, administrative expenses, financing costs and income taxes. Should these comparisons indicate an excess carrying value, the excess is charged against earnings as additional depletion and depreciation.
- (iv) Joint venture activities:

The Corporation conducts substantially all of its oil and gas exploration and production activities on a joint venture basis. These financial statements reflect only the Corporation's proportionate interest in such activities.
- (c) Site restoration:

Estimated future site restoration costs for each cost center are provided for over the life of the proven reserves on a unit-of-production basis. Costs for each cost center are estimated by management based on current regulations, costs, technology and industry standards. The annual charge is included in the provision for depletion and depreciation and actual site restoration expenditures are charged against the accumulated provision account as incurred.
- (d) Office furniture and equipment:

Depreciation of office furniture and equipment is based on estimates of useful lives and is calculated using the declining balance method at rates ranging from 20% to 100% per annum.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

Years ended March 31, 2003 and 2002

2. Significant accounting policies (continued):

(e) Foreign currency translation:

The financial statements are stated in Canadian dollars. Foreign currency denominated assets and liabilities are translated at the exchange rate prevailing at the balance sheet date for monetary items and at the transaction date for non-monetary items. Revenues and expenses, except depletion and depreciation, are translated at average exchange rates for the year. Depletion and depreciation are translated at the same rate as the related assets. Gains or losses on translation are included in net income for the year except for those relating to long-term monetary items, which are deferred and amortized over the remaining terms of the related items.

(f) Convertible debentures and deferred financing costs:

Convertible debentures are recorded as the amount of proceeds received less the amount attributed to the conversion feature which is included as part of shareholders' equity. The difference between the recorded amount and the face value of the convertible debentures is charged to income and included in annual accretion of discount of convertible debentures on an effective yield basis.

Financing costs associated with the issue of convertible debentures are deferred and amortized over the term of the debentures.

(g) Revenue recognition:

Revenues associated with the sale of crude oil and natural gas are recorded when title passes to the customer. Revenues from crude oil and natural gas production from properties from which the Corporation has an interest with other producers are recognized on the basis of the Corporation's net working interest.

(h) Income taxes:

The Corporation follows the liability method of accounting for income taxes. Under this method, temporary differences arising from the difference between the tax basis of an asset or liability and its carrying amount on the balance sheet are used to calculate future income tax liabilities or assets. Future income tax liabilities or assets are calculated using substantively enacted tax rates anticipated to apply in the periods that the temporary differences are expected to reverse.

(i) Per share data:

Basic net loss per common share is computed by dividing net loss from operations by the weighted average number of common shares outstanding for the period. Diluted per share amounts reflect the potential dilution that could occur if securities or other contracts to issue common shares were exercised or converted to common shares. The treasury stock method is used to determine the dilutive effect of stock options and other dilutive instruments. Under the treasury stock method, only options for which the exercise price is less than the market value impact the dilution calculations.

2. Significant accounting policies (continued):

(j) Cash equivalents:
Cash equivalents are comprised of term deposits and other highly liquid investments with a remaining maturity of three months or less at the time of purchase and, as such, are classified with cash.

(k) Stock-based compensation:
The Corporation has a stock option plan as described in note 8.

Effective April 1, 2002, the Corporation adopted the new Canadian accounting standard relating to stock-based compensation and other payments. The new standard is applied prospectively to all stock based payments to non-employees, and to employee awards that are direct awards of stock, call for settlement in cash or other assets, or are stock appreciation rights that call for settlement by the issuance of equity instruments, granted on or after April 1, 2002, except for grants outstanding at April 1, 2002, that call for settlement in cash or other assets or stock appreciation rights that call for settlement in equity instruments. For such grants, the new standard is applied retroactively, without restatement. As the Corporation has no such grants, there was no retroactive impact of applying the standard.

The Corporation has chosen not to use the fair value method to account for stock-based employee compensation plans and therefore, the Corporation records no compensation expense when options are issued to employees. Any consideration paid by employees on the exercise of options is credited to share capital. The Corporation discloses the pro forma effect of accounting for these awards under the fair value based method (see note 8).

(l) Goodwill:
Goodwill represents the excess of the purchase price over the value attributed to the net tangible and intangible assets acquired. Goodwill is not subject to amortization but is subject to an annual review for impairment (or more frequently if events or changes in circumstances indicate that goodwill is impaired) which consists of a comparison of fair value of the assets to their carrying value. The net carrying value of goodwill would be written down if the value is permanently impaired.

(m) Use of estimates:
The preparation of the financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates. The most significant estimates relate to determining the cost recoverability of the Corporation's capital assets and the provisions for depletion, depreciation and site restoration, which are based upon such estimates as proven reserves and future development costs.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

Years ended March 31, 2003 and 2002

3. Related party transactions:

(a) Share purchase loans:

At March 31, 2001, the Corporation had share purchase loans outstanding totaling \$73,950 due from officers, directors and employees. These loans were unsecured, non-interest bearing with no fixed terms of repayment. During the year ended March 31, 2002, \$47,596 of the share purchase loans were repaid and with respect to the remaining balance, totaling \$26,354, 75,000 common shares were returned to the Corporation and cancelled in settlement of the loans (see note 8).

(b) Issuance of common shares:

During the year ended March 31, 2003 the Corporation issued 200,000 common shares with an ascribed value of \$0.32 per share and 1,050,000 common shares with an ascribed value of \$0.35 per share for consideration totaling in aggregate \$431,500 (see note 8). Of this amount, \$70,000 related to and was recorded as share issue costs, \$105,000 related to direct overhead costs associated with the Corporation's exploration and development activities in India and was recorded as a capital asset and the balance totaling \$256,500 related to general and administrative expenses.

4. Restricted investments:

Restricted investments are represented by guaranteed investment certificates amounting to U.S.\$303,000 bearing interest at rates ranging from 0.50% to 0.745% per annum, and maturing on dates ranging from April 11, 2003 to June 2, 2003.

The guaranteed investment certificates have been provided as a guarantee, which has been issued to the government of India pursuant to the terms of a production-sharing contract for the performance of certain seismic activities expected to be completed by September 30, 2004. As such, the guaranteed investment certificates are restricted until the completion of the seismic activities to the satisfaction of the government of India.

5. Capital assets:

	Cost	Accumulated depletion and depreciation	Net book value
2003			
Petroleum and natural gas properties:			
India	\$ 2,454,266	\$ -	\$ 2,454,266
Canada	-	-	-
	<u>2,454,266</u>	<u>-</u>	<u>2,454,266</u>
Office furniture and equipment	99,485	49,134	50,351
	<u>\$ 2,553,751</u>	<u>\$ 49,134</u>	<u>\$ 2,504,617</u>
2002			
Petroleum and natural gas properties:			
India	\$ 1,981,573	\$ -	\$ 1,981,573
Canada	189,999	38,000	151,999
	<u>2,171,572</u>	<u>38,000</u>	<u>2,133,572</u>
Office furniture and equipment	76,462	41,351	35,111
	<u>\$ 2,248,034</u>	<u>\$ 79,351</u>	<u>\$ 2,168,683</u>

5. Capital assets (continued):

(i) Activities in India:

Depletion, depreciation and site restoration has not been recorded with respect to the petroleum and natural gas properties in India as production has not yet commenced. During the year ended March 31, 2003, direct overhead costs totaling approximately \$300,000 (2002 - approximately \$200,000) were capitalized relating to the Corporation's exploration, development and property acquisition programs in India.

Effective May 25, 1998, the Corporation acquired an interest in an oil and gas field in India for approximately \$300,000. As part of the acquisition agreement, the Corporation is committed to fund certain seismic costs by October 31, 2004 totaling approximately \$1,500,000. In addition, the Corporation is committed to drill an exploratory well by March 31, 2006, which is expected to cost approximately \$1,500,000. To date the Corporation has not incurred any costs with respect to the commitment to fund the seismic costs or to drill the exploratory well.

(ii) Activities in Russia:

During the year ended March 31, 2003 the Corporation incurred approximately \$40,000 (2002 - \$nil) relating to establishing its exploration and development activities in Russia. This amount was expensed and is included as part of general and administrative expenses.

(iii) Activities in Canada:

During the year ended March 31, 2003 the Corporation disposed of its only remaining petroleum and natural gas property in Canada resulting in a gain of \$24,000 (see note 6).

6. Promissory note payable:

During the year ended March 31, 2002, the Corporation issued a promissory note in the amount of \$164,999 as consideration on the acquisition of a petroleum and natural gas property. The note bore interest at a rate of 0.8% per month payable monthly, and was unsecured. During the year ended March 31, 2003, the Corporation returned the property to the vendor in exchange for cancellation of the note payable resulting in a gain on disposal of the capital asset of \$24,000.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

Years ended March 31, 2003 and 2002

7. Convertible debentures:

	2003	2002
Convertible debentures:		
Balance, beginning of year	\$ 539,805	\$ -
Issued during the year	300,000	700,000
Less: equity component	(70,346)	(185,035)
	769,459	514,965
Add: accretion of discount on conversion feature	103,569	24,840
Less: amount converted to share capital	(785,485)	-
	87,543	539,805
Less: classified as current	87,543	-
Balance, end of the year	\$ -	\$ 539,805
Deferred financing costs:		
Deferred financing costs	\$ 34,125	\$ 28,000
Less accumulated amortization	(34,125)	(1,750)
	\$ -	\$ 26,250

At March 31, 2003, convertible debentures with a principal balance of \$100,000 (March 31, 2002 - \$700,000) were outstanding. These debentures bear interest at the rate of 10% per annum payable annually, are repayable in full on February 11, 2004, and are secured by a floating charge and general security interest on all of the Corporation's assets. In addition, the debentures are convertible, at the option of the holder, at a conversion price of \$0.35 per common share until February 2003, and \$0.60 per common share until February 11, 2004.

During the year ended March 31, 2003, the debenture holders converted debentures with a principal balance of \$900,000 into 2,571,434 common shares (see note 8) at \$0.35 per common share, leaving a principal balance outstanding of \$100,000. As such, both the liability component totaling \$785,485 and the equity component totaling \$231,932 of the convertible debentures, which were converted, have been reclassified to share capital.

During the year ended March 31, 2003 the Corporation issued 17,500 common shares at an ascribed value of \$0.35 per share relating to the cost of issuing the convertible debentures with a principal balance of \$300,000. During the year ended March 31, 2002 the Corporation issued 70,000 common shares at an ascribed value of \$0.40 per share relating to the cost of issuing the convertible debentures with a principal balance of \$700,000.

8. Share capital:

- (a) Authorized:
Unlimited voting common shares, without nominal or par value; and
Unlimited non-voting preferred shares without nominal or par value.
- (b) Common shares issued or to be issued:

	2003		2002	
	Number	Amount	Number	Amount
Common shares:				
Balance, beginning of year	15,268,275	\$ 7,237,471	14,953,275	\$ 7,105,825
Issued for cash	8,571,143	2,999,900	–	–
Issued on conversion of convertible debenture (note 7)	2,571,434	1,017,417	–	–
Issued for services performed (note 3)	1,050,000	361,500	200,000	64,000
Issued for interest expense	204,494	71,572	–	–
Issued for share issue costs (note 3)	200,000	70,000	–	–
Issued on settlement of debt	–	–	120,000	66,000
Issued on convertible debenture financing (note 7)	17,500	6,125	70,000	28,000
Issued on acquisition of private company (note 12)	800,000	280,000	–	–
Cancelled	–	–	(75,000)	(26,354)
	28,682,846	12,043,985	15,268,275	7,237,471
Share issue costs	–	(393,089)	–	–
Stock-based compensation	–	151,000	–	–
Balance, at end of year	28,682,846	\$ 11,801,896	15,268,275	\$ 7,237,471

- (c) Stock options:
The Corporation has a stock options plan whereby officers, directors, employees and consultants may be granted options to purchase common shares of the Corporation. At March 31, 2003, options have been granted to purchase 1,933,500 (2002 - 1,198,500) common shares at prices ranging from \$0.35 to \$0.77 until expiry on dates ranging from May 18, 2003 to February 13, 2008.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

Years ended March 31, 2003 and 2002

8. Share capital (continued):

(c) Stock options (continued):

Details of the options outstanding under the stock option plan are as follows:

	2003		2002	
	Number	Weighted average exercise price	Number	Weighted average exercise price
Outstanding options, beginning of year	1,198,500	\$ 0.44	1,262,500	\$ 0.66
Granted	1,300,000	0.35	788,500	0.35
Exercised	-	-	-	-
Expired / cancelled	(565,000)	0.40	(852,500)	0.60
Outstanding options end of year	1,933,500	\$ 0.39	1,198,500	\$ 0.44
Options exercisable, end of year	1,066,834	\$ 0.43	410,000	\$ 0.61
	Outstanding at March 31, 2003	Weighted Average Remaining Contractual Life	Exercisable at March 31, 2003	Weighted Average Remaining Contractual Life
Options Range of Exercise Price				
\$ 0.35	1,723,500	4.2 years	856,834	4.2 years
\$ 0.72 - \$0.77	210,000	0.4 years	210,000	0.4 years
	1,933,500	3.8 years	1,066,834	3.8 years

In addition, the Corporation also granted 571,400 agent's options exercisable at \$0.35 per common share to certain financial institutions in conjunction with share issues which occurred during the year ended March 31, 2003. These options expire on February 20, 2005 and were exercisable when granted.

(d) Stock-based compensation:

Effective April 1, 2002, the Corporation prospectively adopted the new Canadian accounting standard relating to stock based compensation. Under this standard the Corporation accounts for stock options granted to non-employees using the fair value based method. Under this method, compensation cost is measured at fair value at grant date and recognized over the vesting period. For stock options granted to employees, the proceeds on the issue of shares upon exercise of the options is included in share capital.

The Corporation recognized compensation expense of \$82,000 for stock options granted to consultants and non-employees as general and administrative expense for the year ended March 31, 2003. In addition, the Corporation recognized \$69,000 of share issue costs representing the fair value of the agent's options (see note 8(c)) granted during the year ended March 31, 2003.

8. Share capital (continued):

(d) Stock-based compensation (continued):

Had the Corporation used the fair value method of accounting for options granted to employees officers and directors, the stock-based compensation costs, pro forma net income and pro forma net income per share would be as follows:

Increase to stock-based compensation expense	\$ 300,000
Net loss for the year:	
As reported	(1,118,905)
Pro forma	(1,418,905)
Net loss per share:	
Basic and diluted:	
As reported	(0.06)
Pro forma	(0.07)

The weighted-average fair value of stock options was estimated at \$0.26 per option using the Black-Scholes option-pricing model with the following assumptions:

Dividend yield	0%
Expected volatility (range)	97% to 170%
Risk free rate of return	5%
Expected option life (range)	2 - 5 years

(e) Per share amounts:

The weighted average number of common shares outstanding during the year ended March 31, 2003 was approximately 20,191,000 (2002 - approximately 15,163,000 shares).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

Years ended March 31, 2003 and 2002

9. Income taxes:

The provision for income taxes differs from the result, which would have been obtained by applying the combined federal and provincial income tax rates to the Corporation's loss before income taxes. This difference results from the following items:

	<u>2003</u>	<u>2002</u>
Combined federal and provincial income tax rate	42.12%	42.62%
Expected tax recovery	\$ (471,000)	\$ (339,000)
Increase (decrease) resulting from:		
Increase in valuation allowance	471,000	339,000
	<u>\$ -</u>	<u>\$ -</u>

The components comprising the future income taxes are as follows:

	<u>2003</u>	<u>2002</u>
Tax assets:		
Non-capital loss carry forwards	\$ 1,913,000	\$ 1,353,000
Share issue costs	302,000	108,000
Capital assets	1,492,000	1,023,000
	<u>3,707,000</u>	<u>2,484,000</u>
Less valuation allowance	(3,707,000)	(2,484,000)
Future income tax liability	<u>\$ -</u>	<u>\$ -</u>

At March 31, 2003, the Corporation had approximately \$4,500,000 (2002 - \$3,500,000) of losses available to reduce future taxable income expiring in the years 2004 to 2010. In addition, the Corporation has cumulative income tax deductions in excess of net book values totaling approximately \$3,500,000 (2002 - \$3,500,000), some of which may be restricted to operations in other countries. The related benefit of these losses and deductions has not been recognized in these financial statements.

10. Supplemental cash flow disclosure:

(a) Changes in non-cash working capital:

	<u>2003</u>	<u>2002</u>
Accounts receivable	\$ 34,036	\$ 3,583
Prepaid expenses	12,835	(15,510)
Accounts payable and accrued liabilities	<u>67,092</u>	<u>229,390</u>
	113,963	217,463
Less: changes in non-cash working capital related to investing	<u>(40,000)</u>	-
Changes in non-cash working capital related to operating activities	<u>\$ 153,963</u>	<u>\$ 217,463</u>

(b) Cash payments:

The following approximate cash payments were made:

	<u>2003</u>	<u>2002</u>
Interest	<u>\$ 2,000</u>	<u>\$ 44,000</u>

11. Commitment:

The Corporation is committed to making the following approximate payments for leased premises and equipment:

2004	\$ 62,000
2005	62,000
2006	62,000
2007	58,000
Thereafter	<u>10,000</u>

12. Business combination:

On August 28, 2002, the Corporation acquired all of the issued and outstanding shares of a private company for consideration consisting of 800,000 shares of the Corporation at an ascribed value of \$0.35 per share for consideration totaling \$280,000. The acquisition was accounted for by the purchase method whereby the assets and liabilities of the private company were recorded at fair market values, and the operating results were included in the Corporation's financial statements from August 28, 2002. As the private company had no assets or liabilities, all of the purchase price was allocated to goodwill.

In addition and pursuant to the acquisition agreement, the Corporation issued 1,000,000 common shares on August 28, 2002 at a price of \$0.35 per share for proceeds totaling \$350,000. Of this amount, \$100,000 was escrowed under an escrow agreement dated August 28, 2002 and released from escrow during the year ended March 31, 2003.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

Years ended March 31, 2003 and 2002

13. Financial instruments:

- (a) Interest rate risk:
As at March 31, 2003 and 2002, the Corporation was exposed to changes in interest rates with respect to its outstanding convertible debentures and its restricted investments.
- (b) Foreign currency exchange risk:
The Corporation is exposed to foreign currency fluctuations as crude oil and natural gas revenues as well as many of the Corporation's expenditures are referenced to the U.S. dollar.
- (c) Credit risk:
The Corporation's accounts receivable are primarily with customers in the oil and gas industry and government agencies and are subject to normal industry credit risks.
- (d) Fair value of financial instruments:
The carrying value of the Corporation's financial assets and liabilities approximated their fair values as at March 31, 2003 and 2002.

14. Contingencies:

The Corporation is subject to legal proceedings and actions arising in the normal course of business. Management believes that any assets or liabilities, which might arise pertaining to such matters, would not be expected to have a material effect on the Corporation's consolidated financial position.

15. Subsequent event:

On July 3, 2003 the Corporation entered into an agreement to purchase a 25% interest in an oil and gas property in India. To date the Corporation has paid U.S. \$175,000 towards the purchase. If all approvals are not received by a certain date agreed upon by the Corporation and vendor, then the agreement may be terminated and the lesser of U.S. \$40,000, or 15% of payments made to the vendor is non-refundable. Further payments are due upon receiving certain approvals from the government of India and completion and filing of necessary documents and permits in India.

CORPORATE INFORMATION

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P. Douglas McArthur, Q.C.⁽¹⁾⁽²⁾
Calgary, Alberta

Stephen B. Nerland⁽¹⁾⁽²⁾
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(2) Compensation and Corporate Governance Committees

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Geoffrey A. Carrington, Ph.D., P.Geoph.
Executive Vice-President

Brian M. Hearst, C.A.
Chief Financial Officer
and Corporate Secretary

Advisor

Subra V. Subramaniam

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Auditors

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Canada

Legal Counsel

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Registrar and Transfer Agent

Computershare Trust Company of Canada
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Stock Exchange Listing

TSX Venture Exchange
Symbol "CNS"

Printed in Canada

