STERLING RESOURCES

TSX:SLG
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MESSAGE TO SHAREHOLDERS

Second Quarter 2011

During the second quarter the Company continued to focus on activities around its core assets. The four-well drilling campaign at Cladhan in the Northern UK North Sea was completed, actions were taken to preserve rights and ultimately to achieve success in Romania, and subsequent to the end of the quarter we were pleased to receive regulatory approval for the development of Breagh in the Southern UK North Sea, as well as signing the project financing facility agreement with a group of banks.

The completion of the four-well appraisal drilling campaign at Cladhan during the second quarter has successfully increased the vertical height of the oil column in the northern core area from 798 feet to a minimum of 1,228 feet as an oil water contact was not seen, and has improved definition of the northern core area. This enables us to proceed with development planning for Cladhan which, at this stage, is primarily focused on a subsea tie-back of the main northern area to nearby third-party facilities. From this northern hub, other areas could be developed such as the South Cladhan area and the prospective areas to the east. Definition of other adjacent resources will be conducted during our next drilling campaign. Pipeline route and environmental survey work has commenced at Cladhan with a target for first oil in 2014. The recent well results are being integrated with an ongoing seismic re-processing exercise to provide new resource estimates to be released late September 2011.

During mid July we announced the signing of a loan facility agreement with a group of banks for a £105 million senior secured loan for the Phase 1 development of the Breagh gas field by its wholly-owned subsidiary, Sterling Resources (UK) Ltd. The signing of this facility was the culmination of many months of close collaboration with our bank group. The discussions took considerable time due to the nature of the two phased development and the impact of the successful 42/13a-6 well drilled earlier this year. The loan amount provided under the facility is composed of a main tranche of £95 million and a cost-overrun tranche of £10 million, and the loan has a maximum life of 6.5 years. Closing and first drawdown is expected in the very near future. The facility also has a step-up amount of up to £50 million for the Phase 2 development on an uncommitted basis.

Shortly after finalizing the loan facility we were pleased to announce the approval by the UK Department of Energy and Climate Change ("DECC") of the Field Development Program ("FDP") for Phase 1 development of the Breagh gas field. The procurement of the loan facility and approval by DECC are major milestones in enabling Sterling's evolution from exploration company to a full-cycle exploration, development and production company. Sterling has been at the forefront of the project as operator of the licenses containing the field awarded in 2004 and 2005, culminating in a very successful appraisal drilling campaign in 2007 and 2008.

Phase 1 of the Breagh development comprises a platform on the western side of the field from which 10 wells are planned to be drilled, a 100 kilometer 20-inch gas export pipeline to Teesside together with an associated smaller service pipeline and cable, an onshore pipeline and modifications to the Teesside Gas Processing Plant. Fabrication of both the jacket and topsides for the Breagh Alpha platform is progressing towards tow-out and installation, which is currently scheduled for early September 2011. Pipelay operations are also progressing well with both the 20-inch production pipeline and the three-inch methanol line having been laid. The current capital expenditure budget for Phase 1, assuming Phase 2 follows on, remains at around £420 million (for 100 percent of the field) although there remains some scope for minor variances in the final level of expenditures. The FDP capital expenditure budget for Phase 1 without a second platform is £485 million, which includes approximately £65 million for drilling three additional long reach wells out to the east

of the field from Breagh Alpha platform. First production from Phase 1 is expected in mid-2012 and peak proved plus probable (2P) production is expected in 2015 at 167 million cubic feet of sales gas per day (MMcf/d) (100 percent) as estimated by the Company's independent reserves evaluator RPS Energy.

Phase 2 of the Breagh development is currently under consideration and is likely to comprise a second platform with further wells on the eastern side of the field, drilled from a Breagh Bravo platform tied back to Alpha. Assuming this goes ahead, incremental production from Phase 2 could commence in 2013 with peak full field 2P sales gas production in 2016 at 186 MMcf/d (100 percent), as estimated by RPS Energy. The Breagh field is one of the largest natural gas discoveries to be developed in the UK Southern North Sea in recent years. The gas field is a conventional Carboniferous reservoir and will be the first large scale production for Sterling.

On July 5, 2011, Sterling announced increased Company interest reserves numbers for the Breagh field as a result of the successful drilling of the 42/13a-6 well earlier in 2011. Proved reserves (1P) have risen from 23.6 million barrels of oil equivalent ("MMboe") at year end 2010, as evaluated by RPS Energy, to 28.2 MMboe, an increase of approximately 19 percent. Similarly, an increase in the 2P reserves has been realized rising from 31.6 MMboe as at December 31, 2010 to 35.3 MMboe as at May 31, 2011, an increase of 12 percent. Finally, proved plus probable plus possible (3P) reserves have risen from 39.0 MMboe as at December 31, 2010 to 44.1 MMboe as at May 31, 2011, an increase of 13 percent.

During the quarter Sterling initiated three separate, but related, actions to defend its rights with the intent of removing the roadblocks impeding progress offshore Romania. In late April the Company declared Force Majeure on its Midia and Pelican Blocks in the Black Sea after the Company had been unable to undertake petroleum operations for reasons outside of its control. In early May a Notice of Default was filed with the National Agency of Mineral Resources ("NAMR") as a result of NAMR's failure to grant license assignments to Sterling's farm in partners for a cumulative 35 percent license holding on its offshore blocks. Finally, in late June Sterling filed a Notice of Dispute with the State of Romania under the Treaty for the Promotion and Reciprocal Protection of Investments between Romania and Canada. The Notice of Dispute was filed as a result of deliberate and discriminatory actions taken against the Company's investments on its offshore blocks. The Notice of Dispute allows for a six-month period of negotiations in which to resolve the issues amicably. If Sterling is unable to obtain satisfactory resolution on all the issues within this period, the Company can then submit the matter to arbitration, if it so desires. Under the arbitration process, Sterling would claim monetary damages that reflect the entire and significant ultimate value of its offshore assets.

Despite this unfortunate situation, we continue our dialogue with NAMR and other Romanian authorities to find a resolution that will allow the Company to fulfill its obligations, preserve its rights and ultimately achieve success for the Company and the people of Romania. Assuming a satisfactory resolution can be achieved through this dialogue, we are hopeful that we can advance our plans to undertake further exploration on these very prospective blocks and bring Ana and Doina to production within three years. This will bring significant benefits to Romania in terms of greater energy self-sufficiency, the possible award of construction and oil service contracts to local companies, and encouragement to a wide range of companies to explore offshore Romania.

Offshore the Netherlands, in the fourth quarter of this year the Company intends to drill and potentially to test a well on an existing discovery in block F17. Pre-planning has been conducted and subsequent to the end of the quarter, a suitable rig has been selected to spud the well in November 2011.

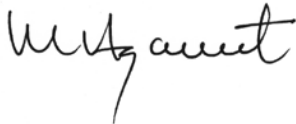
In the Paris Basin of France, Sterling as operator is still awaiting final confirmation of the award of 9.5 blocks. The French government has recently passed legislation governing the drilling technologies to be employed to unlock the oil potential of the Lias shale in the region. This has delayed the final award of the blocks but there have been recent developments that should enable a resolution during the fourth quarter. No drilling is planned by Sterling until 2012 in the Paris Basin, although a multi-well drilling program is planned for later in 2011 on an adjacent third-party license and its outcome will assist us in developing our own drilling plans going forward.

On July 26, 2011, the Company entered into a bought deal financing agreement with a syndicate of underwriters to issue 32,143,000 common shares at a price of $1.40 per share. The offering closed on August 16, 2011. Total gross proceeds from the issue were

$45,000,000 and total net proceeds after deducting the underwriters' fee and other expenses were $42,600,000. Net proceeds will be used towards: (1) meeting the liquidity threshold set under the recently signed £105 million senior secured loan facility to finance development of Phase 1 of the Breagh gas field along with any potential cost overruns; (2) an accelerated incremental appraisal/ development well on the Crosgan discovery in the UK North Sea; and (3) a potential production test of the appraisal well planned on block F17 offshore the Netherlands later this year.

In spite of the many challenges we faced during the quarter, Sterling remains well positioned with an attractive asset base, a continuing appraisal program with drilling in the Netherlands later this year, a strong, focused management team and Board, and significant production from the middle of 2012 commencing with the Breagh gas field. We have now secured sufficient funds to cover the first phase of the Breagh development and meet the minimum cash requirements under the loan facility, which is very reassuring given the recent further upheavals in international financial markets. In the current market with depressed share prices we all feel frustrated that the value of our enviable asset base is not realized at the moment. However, the fundamentals are still intact and in time we will reap the rewards of our focused perseverance. We thank you our shareholders for your support in these challenging times.

On Behalf of the Board of Directors,



Mike Azancot
President and Chief Executive Officer
August 23, 2011

MANAGEMENT'S DISCUSSION AND ANALYSIS

This management's discussion and analysis (MD&A) of the operating results and financial condition of Sterling Resources Ltd. ("Sterling" or the "Company") for the three and six month periods ended June 30, is dated August 23, 2011 and should be read in conjunction with Sterling's unaudited condensed interim consolidated financial statements and accompanying notes as at and for the three months ended March 31, 2011 and those for the three and six month periods ended June 30, 2011 ("the Financial Statements") both prepared in accordance with *IAS 34 Interim Financial Reporting*, representing generally accepted accounting principles for publicly accountable enterprises in Canada, as well as the audited consolidated financial statements for the year ended December 31, 2010, prepared in accordance with Canadian Generally Accepted Accounting Principles at that time ("previous GAAP"). All comparative figures have been restated using IFRS.

The same accounting policies and methods of computation were followed in the preparation of these Financial Statements for the three and six month periods ended June 30, 2011 as were followed in the preparation of the Financial Statements for the three month period ended March 31, 2011. In addition, the Financial Statements for the three month period ended March 31, 2011 contain certain incremental annual IFRS disclosures not included in the annual financial statements for the year ended December 31, 2010 prepared in accordance with previous GAAP.

Corporate Overview and Strategy

Sterling is a publicly-traded, international energy company engaged in the acquisition of petroleum and natural gas rights, and the exploration for, and the development and production of, crude oil and natural gas. The Company operates primarily in the United Kingdom, Romania, the Netherlands and France, and is headquartered in Calgary, Alberta.

The Company's primary strategy for achieving growth is to source and initiate international projects with the potential to yield large, low-cost reserves. It concentrates on accumulating, exploring and exploiting licenses and prospects in selected core areas of the world. Sterling's strategy also targets blocks with high initial working interests where possible. Financial exposure and technical risk are managed by obtaining partner participation through farm-out and other arrangements. Under these arrangements, a portion of the Company's interest is given up in exchange for the partner paying a share of the costs of exploration, appraisal or development of the license. A secondary strategy is to acquire interests in discoveries where the Company believes that its technical and operational expertise can accelerate development, especially where there are multiple development candidates or significant exploration prospectivity nearby.

Forward-Looking Statements and Business Risks

Certain statements contained in this MD&A are forward-looking statements. These statements relate to future events or the Company's future performance. All statements other than statements of historical fact may be forward-looking statements. In some cases, forward-looking statements can be identified by terminology such as "may", "will", "would", "should", "expect", "plan", "anticipate", "believe", "estimate", "predict", "potential", "continue", "intend", or the negative of these terms or other comparable terminology. In addition, statements relating to reserves or resources are deemed to be forward-looking statements as they involve the implied assessment, based on certain estimates and assumptions that the reserves and resources described can be profitably produced in future.

Forward-looking statements in this MD&A include, but are not limited to, statements with respect to:

- Development activities in the greater Breagh area;
- Expectations regarding the Company's cost structure;
- Factors upon which the Company will decide whether or not to undertake a specific course of action;
- The quantity and timing of hydrocarbon production from the Company's development projects;
- The sale, farming-in, farming-out or development of certain exploration properties using third party resources;
- The realization of anticipated benefits of acquisitions and dispositions;
- The possible impact of changes in government policy with respect to onshore and offshore drilling;
- The Company's ability to obtain certain government and regulatory approvals;
- The Company's cash requirements and funding for the next year;
- The Company's expectations regarding its ability to raise additional financing;
- The Company's drilling plans and plans for completion and installation of production platforms or other infrastructure;
- The Company's tax horizon;
- The Company's strategies, the criteria to be considered in connection therewith and the benefits to be derived therefrom;
- The Company's expectations regarding government policies with respect to concerns about climate change and the protection of the environment; and
- The Company's plans and expectations that are described on page 14 under "2011 Plans".

These statements are only predictions. Actual events or results may differ materially. In addition, this MD&A may contain forward-looking statements attributed to third-party industry sources, which sources are not endorsed or adopted by Sterling expressly or implicitly.

Undue reliance should not be placed on these forward-looking statements, as there can be no assurance that the plans, intentions or expectations upon which they are based will occur. By its nature, forward-looking information involves numerous assumptions, known and unknown risks and uncertainties, general and specific, that contribute to the possibility that the predictions, forecasts, projections and other forward-looking statements will prove inaccurate. Certain of these risks are beyond the Company's control, including: political instability in the countries in which it operates, the impact of general economic conditions in the areas in which it operates, civil unrest, industry conditions, changes in laws and regulations including the adoption of new environmental laws and regulations and changes in how they are interpreted and enforced, increased competition, the lack of availability of qualified personnel or management, fluctuations in commodity prices, foreign exchange or interest rates, stock market volatility and obtaining required approvals of regulatory authorities. In addition there are risks and uncertainties associated with oil and natural gas operations. Readers should also carefully consider the matters discussed under the heading "Risk Factors" beginning on page 17 of the Company's Annual Information Form.

With respect to forward-looking statements in this MD&A the Company has assumed, among other things, that the Company:

- Will have access to the funds described under note 18 of the June 30, 2011 interim condensed consolidated financial statements;
- Is able to satisfy the undertakings and conditions under the Breagh loan facility agreement;
- Will produce hydrocarbons and receive cash flows in connection therewith which are consistent with the production and cash flows as estimated in the reserves report prepared by RPS Energy evaluating the reserves of the Breagh field as at May 31, 2011;
- Operates in an environment of fiscal and political stability;
- Operates in an environment of increasing competition;
- Is able to obtain additional financing or farm-out additional interests on satisfactory terms;
- Is able to continue to attract and retain qualified personnel; and
- Is able to obtain necessary approvals from partners for a particular course of action.

Although the Company believes that the expectations reflected in the forward-looking statements are reasonable, there can be no assurance that such expectations will prove to be correct. The Company cannot guarantee future results, levels of activity, performance, or achievements. Moreover it does not assume any obligation to update forward–looking statements except as required by law.

Actual results and future plans could differ materially from those anticipated in similar forward-looking statements in this MD&A as a result of the risks described above. These statements speak only as of the date of this MD&A.

The forward-looking statements contained in this MD&A are expressly qualified by the foregoing cautionary statement. Financial outlook information contained in this MD&A about prospective results of operations, financial position or cash flows is based on assumptions about future events, including economic conditions and proposed courses of action, based on management's assessment of the relevant information currently available. Readers are cautioned that such financial outlook information contained in this MD&A should not be used for purposes other than for which it is disclosed herein.

Transition to International Financial Reporting Standards (IFRS)

The Company's Financial Statements for the three and six month periods ended June 30, 2011 have been prepared in accordance with *IAS 34, Interim Financial Reporting.* The same accounting policies and methods of computation were followed in the preparation of these Financial Statements as were followed in the preparation of the Financial Statements for the three month period ended March 31, 2011. In addition, the Financial Statements for the three month period ended March 31, 2011 contain certain incremental annual IFRS disclosures not included in the annual financial statements for the year ended December 31, 2010 prepared in accordance with previous GAAP. Accordingly, these Financial Statements should be read together with the annual financial statements for the year ended December 31, 2010 prepared in accordance with previous GAAP, as well as the Financial Statements for the three month period ended March 31, 2011.

The following is a summary of the impact on shareholders' equity of the key adjustments resulting from the application of IFRS for the second quarter of 2010:

	Note	As at June 30, 2010
(Unaudited)		$000's
Total equity under previous GAAP		199,862
Adjustments:		
Dry hole costs	(a)	(10,844)
Pre-license costs and other costs expensed under IFRS	(b)	(35,893)
Foreign currency impact of change in functional currencies	(c)	(7,218)
Capitalized share-based compensation expensed under IFRS	(d)	(2,044)
Total equity under IFRS		143,863

a. Exploration and Evaluation Assets

The Company previously followed the full cost method of accounting for oil and gas assets. Under this method, all expenditures incurred in connection with the acquisition, exploration, appraisal and development of oil and gas assets were capitalized in cost centres on a country-by-country basis. As permitted under IFRS the Company has changed its policy to a successful efforts based accounting policy on a retroactive basis. Under this policy the costs of unsuccessful exploration wells are expensed as dry hole costs in the income statement in the period in which they are determined to be unsuccessful. Successful exploration wells remain capitalized, as do subsequent appraisal and development costs as they help to define the prospect. All assets are subsequently reviewed on a quarterly basis for impairment indicators.

b. Pre-License Acquisition Costs and Indirect Overhead Charges

Under previous GAAP all costs associated with property acquisition, exploration and development activities were capitalized within a cost centre, including costs incurred prior to the acquisition of a mineral right. In addition all administrative and general overhead costs were capitalized to cost centres.

IFRS 6 only applies to activities undertaken after the acquisition of the legal rights to explore and therefore does not apply to pre-exploration costs. As these costs do not meet the definition of an asset they are expensed. In addition only directly attributable general and overhead costs have been capitalized to exploration and evaluation assets.

c. Functional Currency and Foreign Operations

IFRS requires that the functional currency of each entity of the Company be determined separately in accordance with *IAS 21 – Foreign exchange,* and should be measured using the currency of the primary economic environment in which they operate ("the functional currency"). IFRS provides IFRS indicators that are used to assist in assessing the functional currency of the entity. Under previous GAAP, foreign currency translation was determined based upon the relationship between the parent company and the respective operating division – i.e. if they are financially or operationally interdependent with the reporting entity. Based upon this, the UK pound ("GBP") was determined to be the functional currency for all entities under previous GAAP.

Using the IFRS indicators, a change of functional currency to the Canadian dollar for Sterling Resources Ltd. and the U.S. dollar for its Romanian operations was determined necessary.

d. Share-Based Compensation

Under previous GAAP the proportion of share-based compensation attributable to exploration and evaluation activities was capitalized within a cost centre. With the adoption of a successful efforts approach under IFRS, much of the share-based compensation previously capitalized would not be permitted as it relates to pre-license activity or unsuccessful wells.

A number of new standards and amendments to standards and interpretations are not yet effective for the year ended December 31, 2011 and have not been applied in preparing these Financial Statements. The following pronouncements from the International Accounting Standards Board ("IASB") are applicable to Sterling and will become effective for future reporting periods, but have not yet been adopted:

- *IFRS 9 Financial Instruments* – IFRS 9 deals with the classification and measurement of financial assets. In October 2010, the IASB updated IFRS 9 by incorporating requirements for the accounting for financial liabilities;
- *IFRS 10 Consolidated Financial Statements* – establishes the accounting principles for consolidated financial statements when one entity controls other entities. This standard establishes a new control model that applies to all entities and replaces *IAS 27 Consolidated and Separate Financial Statements* and the related provisions of *SIC-12 Consolidation – Special Purpose Entities.*
- *IFRS 11 Joint Arrangements* – establishes the accounting principles for parties to a joint arrangement and replaces *IAS 31 Interest in Joint Ventures* and *SIC-13 Jointly Controlled Entities: Non-Monetary Contributions by Venturers*. This standard requires a party to assess its rights and obligations from the arrangement in order to determine the type of joint arrangement. The choice of proportionate consolidation accounting is now prohibited for joint ventures as equity accounting is required;
- *IFRS 12 Disclosure of Interests in Other Entities* – establishes comprehensive disclosure requirements for subsidiaries, joint arrangements, associates, and unconsolidated structured entities and replaces existing disclosures in related standards;
- *IFRS 13 Fair Value Measurement* – establishes a single framework for fair value measurement and disclosures when fair value is required or permitted under IFRS;
- *IAS 27 Separate Financial Statements* – establishes the accounting and disclosure requirements for investments in subsidiaries, joint ventures, and associates when an entity prepares separate financial statements. The standard replaces the current *IAS 27 Consolidated and Separate Financial Statements;*
- *IAS 28 Investments in Associates and Joint Ventures* – establishes the accounting for investments in associates and defines how the equity method is applied.

Except as noted above, all of the above pronouncements are effective for annual periods beginning on or after January 1, 2013 with earlier adoption permitted. Sterling is currently assessing the impact of adopting these pronouncements.

Significant Estimates

Management is required to make judgments, assumptions and estimates in the application of IFRS that have a significant impact on the financial results of the Company. Significant estimates in the financial statements include amounts recorded for the provision for future decommissioning obligations, share-based compensation expense and capital expenditure accruals. In addition, the Company uses estimates for numerous variables in the assessment of its assets for impairment purposes, including oil and natural gas prices, exchange rates, cost estimates and production profiles. By their nature, all of these estimates are subject to measurement uncertainty and the effect on future consolidated financial statements from changes in such estimates could be significant.

Operating Highlights

	Three Months Ended June 30		Six Months Ended June 30	
	2011	2010	**2011**	2010
$000's except per share information				
Operating loss	**13,615**	6,183	**36,015**	7,368
Net financing (income) expense	**(32)**	(85)	**(40)**	276
Net loss for the period	**13,583**	6,098	**35,975**	7,644
Per common share – basic and diluted	**0.07**	0.05	**0.19**	0.06
Exploration and evaluation asset additions	**58,807**	4,695	**105,624**	6,566

	As at June 30, 2011	As At December 31, 2010
$000's except share information and acreage		
Net working capital	**3,473**	138,410
Total assets, end of period	**278,794**	270,316
Share capital, end of period	**295,081**	290,444
Net license acreage (000's of acres)	**2,577**	2,618
Common shares outstanding 000's – basic, end of period	**190,451**	188,944
Common share options 000's outstanding – end of period	**14,387**	11,949

For the three months ended June 30, 2011, the Company recorded a net loss of $13,583,000 ($0.07 per share) compared with a net loss of $6,098,000 ($0.05 per share) for the three months ended June 30, 2010. The increase in the loss is comprised of the following key elements:

Bad Debt Expense

During the second quarter of 2011, the Company made a full provision of $6,792,000 against recovery of overdue amounts receivable from a co-venturer in the unsuccessful Grian well on Block 48/28b in the UK Southern North Sea.

Dry Hole Expense

There were no dry hole costs incurred in the second quarter of 2011. During the second quarter of 2010, the Company expensed dry hole costs of $2,386,000 relating to the unsuccessful Macanta exploration well in the UK Southern North Sea.

For the six months ended June 30, 2011, the Company expensed dry hole costs of $9,733,000 relating to the unsuccessful Grian exploration well on Block 48/28b (Sterling 57%) in the UK Southern North Sea. In the same period of 2010, dry hole costs of $4,076,000 related to the unsuccessful Airidh and Macanta exploration wells in Quad 42 of the UK Southern North Sea.

Pre-License and Other Exploration Costs

For the second quarter of 2011 pre-license and other exploration costs of $2,237,000 were comparable to the $2,480,000 in the same period of the prior year.

For the six month period ended June 30, 2011, pre-license and other exploration costs of $7,151,000 increased by $2,763,000 over the same period in 2010. Most of this increase was attributable to initial costs and purchase of seismic data associated with the start-up of operations in the Netherlands in the first quarter of 2011. The Company is currently in negotiations to drill a well on its acreage in the Netherlands in the fourth quarter of 2011.

Employee Expenses

Employee expenses of $3,398,000 for the second quarter of 2011 has increased by $2,051,000 over the quarter ended June 30, 2010. $522,000 of this increase is attributable to the increase in non-cash share-based compensation expense due to share options issued to the new management team as well as options issued to other employees as part of the annual award program. The remaining increase is due to expansion of the management team and hiring of other new employees as the Company's role as an operator in the UK North Sea and internationally expands.

For the six months ended June 30, 2011, employee expenses of $6,122,000 has increased by $3,566,000 over the same period in 2010. $1,435,000 of this is due to non-cash share-based compensation as described in the previous paragraph, and similarly, the remainder of the increase of $2,131,000 is due to expansion activities as described for the second quarter.

Foreign Exchange

The Company's cash balances are maintained in the currencies in which they are expected to be utilized. Exchange gains and losses reflected in the income statement are then largely offset by corresponding reductions or increases in underlying capital and other expenditures. Foreign exchange losses of $478,000 for the second quarter of 2011 and $4,926,000 for the six months ended June 30, 2011 arose mainly in the first quarter on translation of US dollar cash balances into the respective functional currencies of the operations holding the funds. During the first quarter, the US dollar weakened from par with the Canadian dollar to US$1.00=C$0.9725, and from US$1.00=£0.6465 to US$1.00=£0.6237.

The foreign exchange gains of $383,000 in the second quarter of 2010 and $4,595,000 for the six months ended June 30, 2010 arose similarly on translation of funds into functional currency. During the first quarter when most of these gains were incurred, the US dollar strengthened from US$1.00=C$0.9532 to US$1.00=C$0.9815 against the Canadian dollar and against the UK pound from US$1.00=£0.6279 to US$1.00=£0.6637.

General and Administrative Expense

General and administrative expense of $645,000 for the second quarter of 2011 has increased from $314,000 in the same quarter of 2010, due to expansion of UK operations and the opening of a new office in the Netherlands. For the six months ended June 30, 2011, general and administrative expense of $1,199,000 increased by $314,000 over the same period in 2010 for the same reasons.

Financing Costs

Financing costs include interest expense, amortization of debt issue costs and accretion of the discount on decommissioning obligations. Following the final repayment of the Company's secured note facility in April of 2010, financing costs have been comprised only of accretion of the discount on decommissioning obligations. Reductions in financing costs of $73,000 between the second quarter of 2011 and 2010, as well as $517,000 for the corresponding six month periods are substantially due to the repayment of the notes.

Income Taxes

The Company has not recognized the tax benefit of losses incurred to June 30, 2011 as at that time it had neither significant current production nor regulatory approval for the development of the Breagh or Cladhan fields offshore UK, or for the Doina/Ana field in the Black Sea offshore Romania. In addition, uncertainty exists as to the final price the Company will receive from its share of production from the fields and the final operating and capital costs needed to bring the fields on to production. Consequently there is no assurance the tax benefit will be realized. However, as the Breagh platform nears completion and installation, and the Company enters into arrangements to hedge the price of Breagh gas, the likelihood of recovery will change and recoverability of loss carry-forwards will remain under continuous review.

As at June 30, 2011, the Company had estimated UK tax losses carried forward of approximately £177,000,000 and other capital allowances of $44,898,000 available to shield future taxable income in Canada, Romania and other international jurisdictions. These losses are not subject to expiry. In addition, the Company has approximately $26,386,000 of Canadian and other international non-capital allowances which are subject to expiry over the next 20 years.

The Company is also required to incur eligible expenditures of approximately £57,000,000 as defined under present UK tax law within a period of three years in order to qualify for exemption from UK capital gains taxes associated with the gain on the disposition of a part interest in the greater Breagh area in August 2009. Of this amount approximately £50,000,000 of eligible expenditures have been incurred to June 30, 2011, and it is anticipated that with ongoing planned development expenditures for 2011 and 2012, total expenditures will be sufficient to ensure the Company qualifies for the full exemption.

Overview and Summary of Results for the Eight Most Recently Completed Quarters

The Company had only minor commercial production during the first half of 2011. Any other minor pre-commercial production revenues during earlier quarters have been netted against related expenses, and the net amount capitalized as test production. Up to June 30, 2011 Sterling's results from operations were not affected by seasonal considerations. The following table summarizes the Company's income statements for the eight most recently completed quarters ended June 30, 2011. Quarters previous to the Company's Transition Date to IFRS of January 1, 2010 are reported under previous GAAP.

	IFRS						Previous GAAP	
	2011		2010				2009	
Quarter ended	Jun-30	Mar-31	Dec-31	Sep-30	Jun-30	Mar-31	Dec-31	Sep-30
$000's except per share information								
Net (loss) income								
Canada	**(2,072)**	(2,955)	926	(1,694)	(857)	(1,690)	(1,619)	(438)
United Kingdom	**(9,249)**	(13,875)	(4,859)	(6,804)	(2,956)	1,367	818	70,773
Romania	**(1,732)**	(2,994)	(974)	(873)	(1,809)	(1,203)	251	(581)
Other International	**(530)**	(2,568)	(1,020)	(865)	(476)	(20)	(1)	4
Net (loss) income	**(13,583)**	(22,392)	(5,927)	(10,236)	(6,098)	(1,546)	(551)	69,758
Net (loss) income per share								
Basic	(**0.07**)	(0.12)	(0.04)	(0.07)	(0.05)	(0.01)	–	0.53
Diluted	(**0.07**)	(0.12)	(0.04)	(0.07)	(0.05)	(0.01)	–	0.53

Under the Company's successful efforts accounting policy for exploration and appraisal activity, the Company's results from quarter to quarter are significantly impacted by the level and success of its drilling program.

Exploration and Evaluation Activity

During the six months ended June 30, 2011 key operational activity and expenditures included the following:

- Ongoing construction work totaling $72,924,000 on the Breagh platform jacket, topsides, pipeline sections and onshore facilities;
- The East Breagh appraisal well 42/13a-6 costing $5,732,000. The success of the well means that a second phase of Breagh development involving a second platform is now very likely.
- The four-well Cladhan drilling program costing $26,968,000 . Pre-development work on the field commenced with the objective of working towards project sanction in 2013 and first production in 2014; and
- The operated Grian 48/28b-2 exploration well, costing a total of $9,733,000.

During the six months ended June 30, 2011 the Company relinquished its interest in Blocks 42/2b, 42/3 and 42/4 containing the Darach prospect in the UK Southern North Sea, following the Operator's decision not to proceed with future work after the evaluation of seismic data acquired in 2010.

In the first half of 2010, petroleum and natural gas expenditures totaled $6,566,000 comprised mostly of Breagh development costs. Pre-license and dry hole cost totalling $8,464,000 were expensed.

Financing Activities

During the six months ended June 30, 2011, the Company's only cash financing activity was the issue of 1,507,000 common shares as a result of share options exercised by employees and directors under the Company's share option plan. The weighted average exercise price of the underlying options was $2.21 and aggregate proceeds were $3,334,000.

Subsequent to the end of the quarter, on July 19, 2011 the Company signed a loan facility agreement (the "Facility") with a group of banks for a £105 million senior secured loan for the Phase 1 development of the Breagh gas field. The loan amount provided under the Facility comprises a main tranche of £95 million and a cost-overrun tranche of £10 million, and the loan has a life of 6.5 years. The Facility also has a step-up amount of up to £50 million for the Phase 2 development on an uncommitted basis.

Also subsequent to the end of the quarter, on July 26, 2011 Sterling entered into a bought deal financing arrangement with a syndicate of underwriters to issue 32,143,000 common shares at a price of $1.40 per common share for net proceeds of $42,600,000 after fees and expenses. The offering closed on August 16, 2011. The net proceeds will be used to fund incremental appraisal and development activities on the UK Crosgan discovery and a potential production test on the Netherlands F17 well. In addition, approximately $30 million of the net proceeds is being raised with a view to ensuring that the Company maintains sufficient cash to meet the liquidity threshold set under the Breagh Facility through the end of 2012.

In August 2011, the Company hedged a portion of its Breagh proved reserves (P90) gas production for winter 2012 through to summer 2014 as required by the Facility. This was done by buying put options at a price above the lending banks' price assumptions but below the forward curve.

During the six months ended June 30, 2010, the Company received proceeds of $1,384,000 from the exercise of 908,000 options at a weighted average price of $1.52, and additional proceeds of $1,159,000 from the exercise of 1,380,000 warrants. Other financing activity for the six months ended June 30, 2010 included the final scheduled repayments of the outstanding bridging facility of $7,437,000.

Financing, Liquidity and Solvency

Net Working Capital

$000's	**June 30, 2011**	December 31, 2010
Cash and cash equivalents	**39,799**	142,624
Restricted cash	**8,704**	963
Trade and other receivables	**5,222**	4,095
Prepaid expenses	**195**	62
Trade and other payables	**(49,269)**	(7,434)
Provisions	**(1,178)**	(1,900)
	3,473	138,410

Net working capital of $3,473,000 at June 30, 2011 has decreased substantially from year-end 2010 levels mainly due to the increase in operational activity at Breagh, Cladhan and Grian in the UK North Sea.

Cash and cash equivalents at June 30, 2011 include term deposits of $35,220,000 (December 31, 2010 – $139,238,000). Certain of these term deposits have maturities greater than 30 days from inception, but have cashable options and are therefore considered cash equivalents by management.

Restricted cash of $8,704,000 at June 30, 2011 ($963,000 as at December 31, 2010) comprised cash held in escrow which was available only for payment of expenditures included in trade payables relating to the ongoing drilling programs, primarily at Cladhan.

As at June 30, 2010, other than the partner receivable referred to above, and which has been fully provided for, only minor trade receivables are greater than 90 days.

Trade and other payables of $49,269,000 at June 30, 2011 comprised mainly of accrued expenditures related to the Breagh development project. The increase over the $7,434,000 as at December 31, 2010 is indicative of the ramping up of activity during the quarter.

Provisions of $1,178,000 at June 30, 2011 have been reduced from $1,900,000 at December 31, 2010. This provision was set up in 2010 to provide for an underpayment of employment taxes, associated interest and possible penalties relating to the Company's share option plan for UK employees. In the first quarter of 2011, certain affected individuals were determined to be non-resident, and therefore unaffected by the UK regulations, and the provision was reduced accordingly.

Commitments and Contingencies

Excluding amounts held in escrow and shown as restricted cash for the Cladhan drilling program, as at June 30, 2011 commitments for the remainder of 2011 and years up to 2015 comprised the following:

$000's	2011	2012	2013	2014	2015	**Total**
Oil and gas drilling	–	8,781	14,343	–	–	**23,124**
Seismic	319	2,391	–	–	–	**2,710**
License fees	1,537	2,961	4,354	5,747	7,140	**21,739**
Other operating	44	44	44	33	1,721	**1,886**
Office and other leases	390	75	43	–	–	**508**
	2,290	14,252	18,784	5,780	8,861	**49,967**

In addition to these commitments, the Company will also be required to incur eligible expenditures of approximately £57,000,000 as defined under present UK tax law within a period of three years in order to qualify for exemption from UK capital gains taxes associated with the gain on the disposition of a part interest in the greater Breagh area in 2009. Of this amount approximately £50,000,000 of eligible expenditures have been incurred to June 30, 2011, and it is anticipated that with other planned development and exploration expenditures for 2011 and 2012, total expenditures will be sufficient to ensure the Company qualifies for the full exemption.

On April 28, 2011 the Company invoked the force majeure provisions of its concession agreement for the Midia and Pelican Blocks in the Black Sea on the premise that it was unable to undertake petroleum operations for reasons outside of its control. One impact of the force majeure provisions will be to extend the duration of the concession agreement. On May 2, 2011 the Company filed a Notice of Default with the Romanian National Agency of Mineral Resources for failure to grant license assignments to its partners. Failure to resolve this problem would put the parties into a dispute resolution procedure which could ultimately result in international arbitration.

On June 20, 2011 the Company filed a Notice of Dispute with the Government of Romania under the bi-lateral Treaty for the Promotion and Reciprocal Protection of Investments between Romania and Canada. As recent specific measures launched by the Company including the declaration of force majeure and the issuance of a Notice of Default have not resolved the issues preventing the Company from continuing its offshore activities, the Company had no choice but to take this action to promote dialogue for a resolution of the impasse over the next 6 months and, if necessary, to resort to international arbitration under the Treaty after 6 months has elapsed from the date of filing the Notice of Dispute. The Company remains confident in its legal position with respect to these proceedings and accordingly has made no provision for impairment as at June 30, 2011.

Decommissioning Obligations

The Company's decommissioning obligation results from net ownership interests in petroleum and natural gas exploration stage activity. The provision is the discounted present value of the estimated cost, using existing technology at current prices. The Company estimates the total undiscounted amount of cash flows required to settle its asset retirement obligations to be approximately $3,792,000

which will be incurred between 2015 and 2032. Risk free interest rates based on UK long-term government bond rates varying from 3.25% to 4.75% and an inflation rate of 4 percent were used to calculate the fair value of asset retirement obligations. Revisions to estimates relate primarily to the extension of anticipated field lives as a result of the respective drilling programs.

$000's	**Six Months Ended June 30, 2011**	Year Ended December 31, 2010
At beginning of period	**1,814**	2,199
Arising during period	**187**	–
Revisions to estimates	**52**	(337)
Foreign exchange differences	**58**	(209)
Accretion of discount	**160**	161
At end of period	**2,271**	1,814

Liquidity and Solvency

As at June 30, 2011, the Company's net working capital totaled $3,473,000. Together with the recently approved reserves based loan facility, and the new equity issue, this is considered sufficient to cover its obligations and commitments for the next year. However, additional funding would be required for Phase 2 of the Breagh development, for the development of Cladhan and Doina/Ana subject to the relevant approvals and for any other additional exploration and appraisal activity.

During the second quarter of 2011 the Company became cash generating through its Kirkleatham onshore UK development, though revenues from the field are small.

2011 Plans

The Company outlined its plans for 2011 in the annual report for the year ended December 31, 2010. Several of the specific plans have been completed:

- Four appraisal wells were drilled on the Cladhan discovery, consistent with the previously announced intention to drill at least two such wells;
- An exploration well was drilled on Block 48/28b in the UK Southern North Sea (Grian); and
- Kirkleatham was brought on-stream.

Several plans in the 2010 annual report are unchanged:

- Progress the Breagh development towards achieving first gas in 2012;
- Continue geological and geophysical work on exploration prospects and discoveries on all its licenses; and
- Continue farming out a portion of Company licenses in order to manage risks and reduce costs.

Other plans have been revised:

- Drilling operations on the Breagh development will not commence until December 2011 owing to third party rig commitments, and will commence with tie-back operations on two existing wells. The drilling of new development wells will follow in the first quarter of 2012;
- Two exploration wells offshore Romania are now unlikely to be drilled in 2011. Various permits and approvals have not yet been received so the earliest offshore operations can resume is likely to be 2012; and
- An exploration well on the Craiova block onshore Romania has been postponed into 2012, in order first to acquire further seismic data.

New plans not previously disclosed are as follows:

- Work with the operator to define Phase 2 of the Breagh development and to submit an addendum to the current Field Development Program to the government;
- Pursue a resolution to matters in Romania which will allow the development of the Ana/Doina field to move forward;
- Drill and potentially test an appraisal well on an existing oil discovery in Block F17 offshore the Netherlands; and
- Drill an appraisal/development well on the Crosgan discovery, which is likely to be tied-back to the Breagh facilities.

These plans remain contingent on partner approval, upon availability of suitable financing and (if appropriate) farm-out partners.

Corporately, the last annual report referred to plans regarding the senior debt facility and a listing on the main board of the London Stock Exchange. The senior debt facility for Phase 1 of the Breagh development has been signed. The timing of the London listing is dependent on several factors: finalization of appraisal and development plans for Cladhan, the ability to progress operations offshore Romania and wider equity market conditions. Management remains of the view that a London listing is appropriate for the Company and hopes to progress these plans in 2012.

Additional Information

Additional information about Sterling Resources Ltd. and its business activities, including Sterling's Annual Information Form, is available via SEDAR at www.sedar.com.

CONSOLIDATED BALANCE SHEETS

(Unaudited)	June 30, 2011 $000's	December 31, 2010 $000's
ASSETS		
Current assets		
Cash and cash equivalents [note 4]	**39,799**	142,624
Restricted cash [note 5]	**8,704**	963
Trade and other receivables [note 6]	**5,222**	4,095
Prepaid expenses	**195**	62
	53,920	147,744
Non-current assets		
Exploration and evaluation assets [note 7]	**218,838**	122,359
Property, plant and equipment [note 8]	**6,036**	213
	224,874	122,572
	278,794	270,316
LIABILITIES AND EQUITY		
Current liabilities		
Trade and other payables	**49,269**	7,434
Provisions [note 9]	**1,178**	1,900
	50,447	9,334
Non-current liabilities		
Decommissioning obligations [note 9]	**2,271**	1,814
Commitments and contingencies [note 10]	**–**	–
Equity		
Share capital [note 11]	**295,081**	290,444
Contributed surplus	**10,854**	9,283
Accumulated other comprehensive loss	**(33,481)**	(30,156)
Deficit	**(46,378)**	(10,403)
	226,076	259,168
	278,794	270,316

The accompanying notes are an integral part of the interim condensed consolidated financial statements as at and for the three and six months ended June 30, 2011 and 2010 (“the Financial Statements”).

CONSOLIDATED INCOME STATEMENTS

(Unaudited)	Three Months Ended June 30 **2011** $000s except per share	2010 $000s except per share [note 19]	Six Months Ended June 30 **2011** $000s except per share	2010 $000s except per share [note 19]
Revenue	**329**	–	**329**	–
Expenses				
Bad debt expense [note 12]	**6,792**	–	**6,792**	–
Dry hole expense	**–**	2,386	**9,733**	4,076
Pre-license and other exploration expenditures	**2,237**	2,480	**7,151**	4,388
Employee expense [note 14]	**3,398**	1,347	**6,122**	2,556
General and administration	**645**	314	**1,199**	885
Foreign exchange loss (gain)	**478**	(383)	**4,926**	(4,595)
Depletion, depreciation and amortization	**394**	39	**421**	58
Total expenses	**13,944**	6,183	**36,344**	7,368
Operating loss	**13,615**	6,183	**36,015**	7,368
Financing income	**(110)**	(236)	**(200)**	(401)
Financing costs [note 15]	**78**	151	**160**	677
Net loss for the period	**13,583**	6,098	**35,975**	7,644
Net loss per common share [note 17]				
Basic	**0.07**	0.05	**0.19**	0.06
Diluted	**0.07**	0.05	**0.19**	0.06

The accompanying notes are an integral part of the Financial Statements.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

	Three Months Ended June 30		Six Months Ended June 30	
	2011	2010	**2011**	2010
(Unaudited)	**$000s**	$000s	**$000s**	$000s
		[note 19]		[note 19]
Net loss	**(13,583)**	(6,098)	**(35,975)**	(7,644)
Foreign currency translation adjustment	**(24,047)**	3,262	**(3,325)**	(8,916)
Comprehensive loss	**(37,630)**	(2,836)	**(39,300)**	(16,560)

The accompanying notes are an integral part of the Financial Statements.

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(Unaudited)	Share Capital $000's	Contributed Surplus $000's	Accumulated Other Comprehensive Loss $000's	Retained Earnings (Deficit) $000's	Total $000's
Balance at January 1, 2010	157,643	6,858	(20,708)	12,650	156,443
Exercise of stock options and warrants	2,543	–	–	–	2,543
Transferred from contributed surplus on exercise of options	539	(539)	–	–	–
Share-based compensation	–	1,437	–	–	1,437
Foreign currency translation into presentation currency	–	–	(8,916)	–	(8,916)
Loss for the period	–	–	–	(7,644)	(7,644)
Balance at June 30, 2010 [note 19]	160,725	7,756	(29,624)	5,006	143,863
Balance at January 1, 2011	290,444	9,283	(30,156)	(10,403)	**259,168**
Exercise of stock options	3,334	–	–	–	**3,334**
Share issue costs	2	–	–	–	**2**
Transferred from contributed surplus on exercise of options	1,301	(1,301)	–	–	**–**
Share-based compensation	–	2,872	–	–	**2,872**
Foreign currency translation into presentation currency	–	–	(3,325)	–	**(3,325)**
Loss for the period	–	–	–	(35,975)	**(35,975)**
Balance at June 30, 2011	**295,081**	**10,854**	**(33,481)**	**(46,378)**	**226,076**

The accompanying notes are an integral part of the Financial Statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three Months Ended June 30		Six Months Ended June 30	
	2011	2010	**2011**	2010
(Unaudited)	**$000s**	$000s	**$000s**	$000s
		[note 19]		[note 19]
Cash flows from operating activities				
Loss for the period	**(13,583)**	(6,098)	**(35,975)**	(7,644)
Adjustments to add (deduct) non-cash items				
Unrealized foreign exchange loss (gain)	**(569)**	1,792	**696**	78
Share-based compensation [note 14]	**1,390**	868	**2,872**	1,437
Accretion [note 15]	**78**	58	**160**	107
Depletion, depreciation and amortization	**394**	39	**421**	58
Amortization of debt issue costs [note 15]	**–**	62	**–**	358
Change in non-cash working capital	**303**	8	**(988)**	(142)
Net cash flows (used in) provided by operating activities	**(11,987)**	(3,271)	**(32,814)**	(5,748)
Cash flows from investing activities				
Decrease (increase) in restricted cash	**15,134**	73	**(7,741)**	(3,275)
Exploration and evaluation asset additions	**(58,807)**	(4,695)	**(105,624)**	(6,566)
Property, plant and equipment additions	**(556)**	(30)	**(679)**	(60)
Change in non-cash working capital	**(984)**	(4,256)	**40,841**	(4,280)
Net cash flows used in investing activities	**(45,213)**	(8,908)	**(73,203)**	(14,181)
Cash flows from financing activities				
Repayment of secured notes	**–**	(3,704)	**–**	(7,437)
Proceeds from exercise of share options	**68**	222	**3,334**	1,384
Proceeds from exercise of warrants	**–**	1,125	**–**	1,159
Net cash flows provided by (used in) financing activities	**68**	(2,357)	**3,334**	(4,894)
Effect of translation on foreign currency cash and cash equivalents	**(17)**	(312)	**(142)**	(5,991)
Decrease in cash and cash equivalents during the period	**(57,149)**	(14,848)	**(102,825)**	(30,814)
Cash and cash equivalents, beginning of period	**96,948**	65,833	**142,624**	81,799
Cash and cash equivalents, end of period	**39,799**	50,985	**39,799**	50,985

The accompanying notes are an integral part of the Financial Statements.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

For the Three and Six Months Ended June 30, 2011 and 2010

1. Corporate Information

Sterling Resources Ltd. (the "Company") is a publicly traded energy company incorporated and domiciled in Canada. The Company is engaged in the exploration, appraisal and development of crude oil and natural gas in the United Kingdom, Romania, the Netherlands and France. The registered office is located at Suite 1450, 736 Sixth Avenue S.W. Calgary, Alberta Canada.

The Company's Financial Statements comprise the financial statements of the Company and its 100% owned subsidiaries Sterling Resources (UK) Ltd. and Midia Resources SRL.

These unaudited interim condensed consolidated financial statements ("the Financial Statements") were approved for issue at a meeting of the Audit Committee on August 23, 2011.

2. Basis of Preparation

These Financial Statements for the three and six month periods ended June 30, 2011 were prepared in accordance with *IAS 34, Interim Financial Reporting and IFRS 1 First Time Adoption of International Financial Reporting Standards*. The same accounting policies and methods of computation were followed in the preparation of the Financial Statements as were followed in the preparation of the interim condensed consolidated financial statements for the three month period ended March 31, 2011. In addition, the interim condensed consolidated financial statements for the three month period ended March 31, 2011 contain certain incremental annual International Financial Reporting Standards ("IFRS") disclosures not included in the annual financial statements for the year ended December 31, 2010 prepared in accordance with former Canadian Generally Accepted Accounting Principles ("previous GAAP"). Accordingly, these Financial Statements for the three and six month periods ended June 30, 2011 should be read together with the annual consolidated financial statements for the year ended December 31, 2010 prepared in accordance with previous GAAP, as well as the interim condensed consolidated financial statements for the three month period ended March 31, 2011.

Exchanges of assets are measured at fair value unless the exchange transaction lacks commercial substance or the fair value of neither the asset received nor the asset given up is reliably measurable. The cost of the acquired asset is measured at the fair value of the asset given up, unless the fair value of the asset received is more clearly evident. Where fair value is not used, the cost of the acquired asset is measured at the carrying amount of the asset given up. The gain or loss arising is recognized in net income (loss).

3. New Accounting Standards and Interpretations Not Yet Adopted

The following pronouncements from the International Accounting Standards Board "IASB" are applicable to Sterling and will become effective for future reporting periods, but have not yet been adopted:

- *IFRS 9 Financial Instruments* – IFRS 9 deals with the classification and measurement of financial assets. In October 2010, the IASB updated IFRS 9 by incorporating requirements for the accounting for financial liabilities;
- *IFRS 10 Consolidated Financial Statements* – establishes the accounting principles for consolidated financial statements when one entity controls other entities. This standard establishes a new control model that applies to all entities and replaces *IAS 27 Consolidated and Separate Financial Statements* and the related provisions of *SIC-12 Consolidation – Special Purpose Entities.*
- *IFRS 11 Joint Arrangements* – establishes the accounting principles for parties to a joint arrangement and replaces *IAS 31 Interest in Joint Ventures* and *SIC-13 Jointly Controlled Entities: Non-Monetary Contributions by Venturers.* This standard requires a party to assess its rights and obligations from the arrangement in order to determine the type of joint arrangement. The choice of proportionate consolidation accounting is now prohibited for joint ventures as equity accounting is required;

- *IFRS 12 Disclosure of Interests in Other Entities* – establishes comprehensive disclosure requirements for subsidiaries, joint arrangements, associates, and unconsolidated structured entities and replaces existing disclosures in related standards;
- *IFRS 13 Fair Value Measurement* – establishes a single framework for fair value measurement and disclosures when fair value is required or permitted under IFRS;
- *IAS 27 Separate Financial Statements* – establishes the accounting and disclosure requirements for investments in subsidiaries, joint ventures, and associates when an entity prepares separate financial statements. The standard replaces the current *IAS 27 Consolidated and Separate Financial Statements;*
- *IAS 28 Investments in Associates and Joint Ventures* – establishes the accounting for investments in associates and defines how the equity method is applied.

Except as noted above, all of the above pronouncements are effective for annual periods beginning on or after January 1, 2013 with earlier adoption permitted. Sterling is currently assessing the impact of adopting these pronouncements.

4. Cash and Cash Equivalents

Cash and cash equivalents consist of the following:

	June 30, 2011	December 31, 2010
	$000's	$000's
Cash	**4,579**	3,386
Cash equivalents	**35,220**	139,238
	39,799	142,624
Balances held in:		
Canadian dollars	**4,712**	92,123
US dollars	**29,944**	35,994
UK pounds	**5,133**	14,445
Other	**10**	62
Cash and cash equivalents	**39,799**	142,624

As at June 30, 2011 cash equivalents carried interest rates between 0.02 percent and 1.0 percent (December 31, 2010 – 0.03 percent and 1.0 percent).

5. Restricted Cash

Restricted cash of $8,704,000 as at June 30, 2011 was comprised of cash held in escrow accounts which was available only for payment of expenditures relating to the 2011 drilling program. As at December 31, 2010, restricted cash of $963,000 was comprised of cash held in escrow accounts which was available only for payment of expenditures included in trade and other payables relating to certain drilling programs.

6. Financial Instruments

The Company is exposed to a number of different financial risks arising from normal course business exposures, as well as the Company's use of financial instruments. These risk factors include market risks relating to foreign exchange rate fluctuations and interest rate risk, as well as liquidity risk and credit risk.

Foreign Exchange Rate Risk

The Company's functional currencies for UK, Canadian and Romanian operations are the UK pound, Canadian dollar and US dollar respectively. Foreign exchange gains or losses can occur on translation of working capital denominated in currencies other than the functional currency of the jurisdiction which holds the working capital item. Excluding the impact of changes in the cross-rates, a one-percent fluctuation between translation rates would have the following impact on net income (loss), based on foreign currency balances held at June 30, 2011.

	C$000's
Canadian dollar vs. UK pound	(15)
Canadian dollar vs. US dollar	161
UK pound vs. US dollar	292

Interest Rate Risk

As at June 30, 2011, the Company had no "interest bearing" debt which exposed its cash flows to interest rate risk. However, from time to time the Company may have significant cash or cash equivalent balances invested at prevailing short-term interest rates. Accordingly cash flows are sensitive to changes in interest rates on these investments. Based on total cash and cash equivalents and restricted cash at June 30, 2011, a one percent change in average interest rates would increase or decrease net income (loss) by approximately $485,000 over a full year.

Liquidity Risk

Liquidity risk is the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities. As a result of the signing of a loan facility agreement and a bought deal financing subsequent to June 30, 2011 (refer to note 18) the Company has access to sufficient cash to settle its trade and other payables and meet its immediate joint venture commitments and license obligations. The Company monitors and manages its liquidity through comparisons of working capital with budgets and regular forecasts of cash requirements, and by adjusting discretionary expenditures where appropriate.

Credit Risk

Credit risk is the risk that a customer or counterparty will fail to perform an obligation or fail to pay amounts due causing a financial loss. The Company's trade and other receivables are primarily with governments for recoverable amounts of value added taxes (VAT) or joint venture partners in the oil and gas industry. Receivables from partners are secured by the partner's interest in the underlying oil and gas properties or if unsuccessful through gaining an equity portion in alternative assets. As at June 30, 2011 full provision of $6,792,000 has been made against a receivable due from a partner in the Grian well. Collection efforts are continuing, and there may still be partial recovery through assumption of certain of the partner's assets.

7. Exploration and Evaluation Assets

In accordance with the Company's impairment policy, exploration and evaluation assets were reviewed for indicators of impairment at the reporting dates. Based upon these reviews, management determined that no impairment test was needed.

	Six Months Ended June 30, 2011	Year Ended December 31, 2010
	$000's	$000's
Balance, beginning of period	**122,359**	85,799
Additions		
– Cash	**105,624**	40,295
– Non cash decomissioning costs	**187**	–
Transfers to producing oil and gas properties	**(5,549)**	–
Foreign exchange	**(3,783)**	(3,735)
Balance, end of period	**218,838**	122,359

8. Property, Plant and Equipment

	Six Months Ended June 30, 2011			Year Ended December 31, 2010		
	Producing Oil & Gas Properties	**Corporate and Other**	**Total**	Producing Oil & Gas Properties	Corporate and Other	Total
	$000's	**$000's**	**$000's**	$000's	$000's	$000's
Cost						
Balance, beginning of period	**–**	**615**	**615**	–	523	523
Additions	**435**	**244**	**679**	–	146	146
Transfers from exploration and evaluation	**5,549**	**–**	**5,549**	–	–	–
Foreign exchange differences	**15**	**2**	**17**	–	(54)	(54)
Balance, end of period	**5,999**	**861**	**6,860**	–	615	615
Accumulated depreciation and depletion						
Balance, beginning of period	**–**	**(402)**	**(402)**	–	(355)	(355)
Depreciation and depletion	**(364)**	**(57)**	**(421)**	–	(89)	(89)
Foreign exchange differences	**–**	**(1)**	**(1)**	–	42	42
Balance, end of period	**(364)**	**(460)**	**(824)**	–	(402)	(402)
Net book value						
Balance, beginning of period	**–**	**213**	**213**	–	168	168
Balance, end of period	**5,635**	**401**	**6,036**	–	213	213

9. Provisions

The following is a continuity of provisions:

	Six Months Ended June 30, 2011			Year Ended December 31, 2010		
	Decommissioning	**Other**	**Total**	Decommissioning	Other	Total
	$000's	**$000's**	**$000's**	$000's	$000's	$000's
At beginning of period	**1,814**	**1,900**	**3,714**	2,199	–	2,199
Arising during period	**187**	**–**	**187**	–	1,900	1,900
Revisions to estimates	**52**	**(653)**	**(601)**	(337)	–	(337)
Foreign exchange differences	**58**	**(69)**	**(11)**	(209)	–	(209)
Accretion of discount	**160**	**–**	**160**	161	–	161
At end of period	**2,271**	**1,178**	**3,449**	1,814	1,900	3,714

Decommissioning Obligations

The Company's decommissioning obligation results from net ownership interests in petroleum and natural gas exploration stage activity. The provision is the discounted present value of the estimated cost, using existing technology at current prices. The Company estimates the total undiscounted amount of cash flows required to settle its asset retirement obligations to be approximately $3,792,000 which will be incurred between 2015 and 2032. Risk free interest rates based on UK long-term Government bond rates varying from 3.25% to 4.75% and an inflation rate of 4 percent were used to calculate the decommissioning obligations.

Revisions to estimates relate primarily to the extension of anticipated field lives as a result of the respective drilling programs.

Other Provisions

Provisions of $1,178,000 at June 30, 2011 have been reduced from $1,900,000 at December 31, 2010. This provision was set up in 2010 to provide for an underpayment of employment taxes, associated interest and possible penalties relating to the Company's share option plan for UK employees. In the first quarter of 2011, certain affected individuals were determined to be non-resident, and therefore unaffected by the UK regulations, and the provision was reduced accordingly.

10. Commitments and Contingencies

Excluding amounts held in escrow, and shown as restricted cash, for the drilling programs, as at June 30, 2011, commitments for the remainder of 2011 and years up to 2015, are comprised of the following:

	2011	2012	2013	2014	2015	**Total**
	$000's	$000's	$000's	$000's	$000's	**$000's**
Oil and gas drilling	–	8,781	14,343	–	–	**23,124**
Seismic	319	2,391	–	–	–	**2,710**
License fees	1,537	2,961	4,354	5,747	7,140	**21,739**
Other operating	44	44	44	33	1,721	**1,886**
Office and other leases	390	75	43	–	–	**508**
	2,290	14,252	18,784	5,780	8,861	**49,967**

In addition to these commitments, the Company will also be required to incur eligible expenditures of approximately £57,000,000 as defined under present UK tax law within a period of three years in order to qualify for exemption from UK capital gains taxes associated with the gain on the disposition of a part interest in the greater Breagh area in 2009. Of this amount approximately £50,000,000 of eligible expenditures have been incurred to June 30, 2011, and it is anticipated that with other planned development and exploration expenditures for 2011 and 2012, total expenditures will be sufficient to ensure the Company qualifies for the full exemption.

On April 28, 2011 the Company invoked the force majeure provisions of its concession agreement for the Midia and Pelican Blocks in the Black Sea on the premise that it was unable to undertake petroleum operations for reasons outside of its control. One impact of the force majeure provisions will be to extend the duration of the concession agreement. On May 2, 2011 the Company filed a Notice of Default with the Romanian National Agency of Mineral Resources for failure to grant license assignments to its partners. Failure to resolve this problem would put the parties into a dispute resolution procedure which could ultimately result in international arbitration.

On June 20, 2011 the Company filed a Notice of Dispute with the Government of Romania under the bi-lateral Treaty for the Promotion and Reciprocal Protection of Investments between Romania and Canada. As recent specific measures launched by the Company including the declaration of force majeure and the issuance of a Notice of Default have not resolved the issues preventing the Company from continuing its offshore activities, the Company had no choice but to take this action to promote dialogue for a resolution of the impasse over the next 6 months and, if necessary, to resort to international arbitration under the Treaty after 6 months has elapsed from the date of filing the Notice of Dispute. The Company remains confident in its legal position with respect to these proceedings and accordingly has made no provision for impairment as of June 30, 2011.

11. Share Capital

Authorized share capital consists of an unlimited number of common shares without nominal or par value. The holders of common shares are entitled to one vote per share and are entitled to receive dividends as recommended by the Board of Directors.

Share capital issued and outstanding is as follows:

	SIx Months Ended June 30, 2011		Year Ended December 31, 2010	
Continuity of common shares	**Shares 000's**	**Amount $000's**	Shares 000's	Amount $000's
Balance, beginning of period	**188,944**	**290,444**	132,175	157,126
Issued for cash:				
– public equity issuances	**–**	**–**	53,344	134,266
– exercise of stock options	**1,507**	**3,334**	2,045	3,325
– exercise of warrants	**–**	**–**	1,380	1,159
Share issue costs	**–**	**2**	–	(7,407)
Non-cash transfer from warrants	**–**	**–**	–	517
Transferred from contributed surplus on exercise of options	**–**	**1,301**	–	1,458
Balance, end of period	**190,451**	**295,081**	188,944	290,444
Continuity of warrants				
Balance, at beginning of period	**–**	**–**	1,380	517
Exercise of common share warrants	**–**	**–**	(1,380)	(517)
Balance, end of period	**–**	**–**	–	–
Share capital, end of period	**190,451**	**295,081**	188,944	290,444

On August 12, 2010, the Company completed a bought deal financing agreement with a syndicate of underwriters for the issue of 23,423,500 common shares at a price of $1.90 per share including an underwriters' over-allotment option of 2,368,500 common shares at the same price. The net proceeds of the issue were approximately $42,000,000, after fees and expenses.

On December 22, 2010, the Company completed a bought deal financing agreement with a syndicate of underwriters for the issue of 29,920,500 common shares at a price of $3.00 per share including an underwriters' over-allotment option of 3,250,500 common shares at the same price. The net proceeds of the issue were approximately $85,000,000, after fees and expenses.

12. Bad Debt Expense

During the second quarter of 2011, the Company made a full provision of $6,792,000 against recovery of overdue amounts receivable from a co-venturer in the unsuccessful Grian well on Block 48/28b in the UK Southern North Sea.

13. Segmented Information

There are four geographical reporting segments. Canada is the location of the head office. The United Kingdom, Romania and other international locations are involved in exploration and development operations. Other international comprises operations in France and Netherlands.

	Canada	United Kingdom	Romania	Other International	Consolidated
Segmented Results	$000's	$000's	$000's	$000's	$000's
Three months ended June 30, 2011					
Dry hole expense	**–**	**–**	**–**	**–**	**–**
Net loss	**(2,072)**	**(9,249)**	**(1,732)**	**(530)**	**(13,583)**
Six months ended June 30, 2011					
Dry hole expense	**–**	**(9,733)**	**–**	**–**	**(9,733)**
Net loss	**(5,117)**	**(23,083)**	**(4,677)**	**(3,098)**	**(35,975)**
Three months ended June 30, 2010					
Dry hole expense	–	(2,386)	–	–	(2,386)
Net loss	(857)	(2,956)	(1,809)	(476)	(6,098)
Six months ended June 30, 2010					
Dry hole expense	–	(4,076)	–	–	(4,076)
Net loss	(2,566)	(1,570)	(3,012)	(496)	(7,644)

	Canada	United Kingdom	Romania	Other International	Consolidated
Other Segmented Information	$000's	$000's	$000's	$000's	$000's
As at and for the six month period ended June 30, 2011					
Exploration and evaluation assets	**–**	**193,580**	**25,258**	**–**	**218,838**
Exploration and evaluation asset additions	**–**	**105,624**	**–**	**–**	**105,624**
Producing properties	**–**	**5,635**	**–**	**–**	**5,635**
Producing properties transfers and additions	**–**	**5,984**	**–**	**–**	**5,984**
As at and for the six month period ended June 30, 2010					
Exploration and evaluation assets	–	61,008	27,115	–	88,123
Exploration and evaluation asset additions	–	6,560	6	–	6,566
Producing properties	–	–	–	–	–
Producing properties transfers and additions	–	–	–	–	–

14. Share-Based Compensation

The Company has established a stock option plan whereby it may grant equity-settled options to its directors, officers, employees and consultants. On June 30, 2011 there were 19,040,000 (December 31, 2010 – 13,304,000) common shares reserved for issuance under the plan. The exercise price of each option equals the market price of the Company's shares on the date of the grant. The option's maximum term is five years, with the minimum vesting period to be 18 months. Stock options currently issued vest over the initial three years.

The following is a continuity of outstanding stock options:

	Six Months Ended June 30, 2011		Year Ended December 31, 2010	
Continuity of Common Share Options	**Options 000's**	**Weighted Average Exercise Price $**	Options 000's	Weighted Average Exercise Price $
Balance, beginning of period	**11,949**	**2.18**	8,627	1.90
Granted during the period	**4,155**	**2.00**	5,805	2.42
Exercised during the period	**(1,507)**	**2.21**	(2,045)	1.63
Expired during the period	**(210)**	**1.92**	(438)	2.45
Outstanding, end of period	**14,387**	**2.13**	11,949	2.18
Exercisable, end of period	**4,935**	**2.05**	3,390	2.09

The Black-Scholes option pricing model was used to calculate the fair value of the options granted during the period using the following weighted average assumptions:

	Six Months Ended June 30, 2011	Year Ended December 31, 2010
Weighted average share price	**$2.00**	$2.18
Weighted average exercise price	**$2.00**	$2.18
Risk-free interest rate	**2.06%**	2.21%
Expected hold period to exercise	**3.5 years**	3.5 years
Volatility in the price of the Company's shares	**78.0%**	83.9%
Expected annual dividend yield	**0%**	0%

The weighted average fair value of options granted during the six months ended June 30, 2011 was $1.10 per share (2010 – $1.32 per share). For the three months ended June 30, 2011, $1,390,000 of share-based compensation was expensed while $2,872,000 of share-based compensation was expensed during the six month period ended June 30, 2011. For the same periods in 2010 $868,000 and $1,437,000 respectively, was expensed.

The following stock options were outstanding at June 30, 2011:

Exercise Price		Options Outstanding			Options Exercisable		
From $	To $	Options 000's	Remaining Contract Life (Days)	Weighted Average Exercise Price $	Options 000's	Remaining Contract Life (Days)	Weighted Average Exercise Price $
1.00	**1.49**	**2,397**	**739**	**1.42**	**1,488**	**540**	**1.42**
1.50	**1.99**	**4,888**	**1,285**	**1.79**	**408**	**305**	**1.57**
2.00	**2.49**	**2,562**	**1,006**	**2.05**	**948**	**603**	**2.09**
2.50	**2.99**	**3,090**	**750**	**2.60**	**2,090**	**525**	**2.58**
3.00	**3.49**	**1,100**	**1,241**	**3.33**	**–**	**–**	**–**
3.50	**4.25**	**350**	**1,347**	**4.25**	**–**	**–**	**–**
1.00	**4.25**	**14,387**	**1,028**	**2.13**	**4,935**	**353**	**2.05**

15. Financing Costs

	Three Months Ended June 30		Six Months Ended June 30	
	2011	2010	**2011**	2010
	$000s	$000s	**$000s**	$000s
Interest expense	**–**	31	**–**	212
Amortization of debt issue costs	**–**	62	**–**	358
Accretion of discount [note 9]	**78**	58	**160**	107
Total financing costs	**78**	151	**160**	677

16. Income Taxes

Current Income Tax

No provision for current income tax is required due to availability of loss carry-forwards.

Deferred Tax

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts for income tax purposes. As at June 30, 2011, June 30, 2010 and December 31, 2010, the Company has not recognized a deferred income tax asset arising from tax pools in excess of the net book value of capital assets, share issue costs and non-capital losses.

17. Net Loss Per Share

The following reflects the loss and share data used in the basic and diluted earnings per share computations:

	Three Months Ended June 30		Six Months Ended June 30	
	2011	2010	**2011**	2010
	$000's except per share	$000's except per share	**$000's except per share**	$000's except per share
Weighted average shares outstanding	**190,451**	133,470	**190,207**	133,019
Net loss	**13,583**	6,098	**35,975**	7,644
Net loss per share				
– Basic	**0.07**	0.05	**0.19**	0.06
– Diluted	**0.07**	0.05	**0.19**	0.06

There have been no other transactions involving ordinary shares or potential ordinary shares between the reporting date and the release of these financial statements. In the period between the reporting date and the release of the financial statements 32,143,000 common shares were issued by way of a public issue (note 18), 705,000 options were issued to new employees and 50,000 options were exercised. As at June 30, 2011 and 2010, the dilutive effect of the Company's outstanding options was not included in diluted shares outstanding due to the net loss incurred during the periods.

18. Subsequent Events

On July 19, 2011 Sterling Resources (UK) Ltd. and its parent company Sterling Resources Ltd signed a loan facility agreement (the "Facility") with a group of banks for a £105 million senior secured loan for the Phase 1 development of the Breagh gas field. The loan amount provided under the Facility comprises a main tranche of £95 million and a cost-overrun tranche of £10 million, and the loan has a maximum life of 6.5 years. The Facility also has a step-up amount of up to £50 million for the Phase 2 development on an uncommitted basis.

The Field Development Program for Phase 1 of the Breagh Gas Field received approval of the UK Department of Energy and Climate Change on July 25, 2011.

On July 26, 2011 the Company entered into a bought deal financing arrangement with a syndicate of underwriters led by RBC Capital Markets to issue 32,143,000 common shares at a price of $1.40 per common share for net proceeds of $42,600,000, after fees and expenses. The offering closed on August 16, 2011. The net proceeds will be used to fund incremental appraisal and development activities on the UK Crosgan discovery and a potential production test on the Netherlands F17 well, in addition to allowing the Company to maintain sufficient cash to meet the liquidity threshold set under the Breagh loan facility through the end of 2012.

In August 2011, the Company hedged a portion of its Breagh proved reserves (P90) gas production for winter 2012 through to summer 2014 as required by the Facility. This was done by buying put options at a price above the lending banks' price assumptions but below the forward curve.

19. Transition to International Financial Reporting Standards

The accounting policies described in Note 3 of the March 31, 2011 interim condensed consolidated financial statements have been applied in preparing these Financial Statements for the three and six month periods ended June 30, 2011, and the comparative information for the three and six month periods ended June 30, 2010. For details of the Company's January 1, 2010 balance sheet (the date of transition) and the full year 2010 financial statements, please refer to the March 31, 2011 interim condensed consolidated financial statements.

This note explains the principal adjustments made by the Company in restating its previously published GAAP financial statements.

Restatement of Equity from Previous GAAP to IFRS

IFRS employs a conceptual framework that is similar to previous GAAP. However, significant differences exist in certain matters of recognition, measurement and disclosure. While adoption of IFRS has not changed the Company's actual cash flows, it has resulted in changes to the Company's reported balance sheet and income statement. In order to provide the users of the financial statements with an understanding of these changes, the Company's previous GAAP balance sheet as at June 30 2010 and the income statement and statement of comprehensive income (loss) for the three and six month periods ended June 30, 2010 have been reconciled to IFRS, with the resulting differences explained below.

a. Exploration and Evaluation Assets

The Company previously followed the full cost method of accounting for oil and gas assets. Under this method, all expenditures incurred in connection with the acquisition, exploration, appraisal and development of oil and gas assets were capitalized in cost centers on a country-by-country basis. As permitted under IFRS the Company has changed its policy to a successful efforts based accounting policy on a retroactive basis. Under this policy the costs of unsuccessful exploration wells are expensed in the income statement in the period in which they are determined to be unsuccessful.

Successful exploration wells remain capitalized, as do subsequent appraisal and development costs as they help define the prospect. All assets are subsequently reviewed on a quarterly basis for impairment indicators.

b. Pre-License Acquisition and Other Exploration Costs

Under previous GAAP all costs associated with property acquisition, exploration and development activities were capitalized within a cost centre, including costs incurred prior to the acquisition of a mineral right. In addition certain administrative and general overhead costs were capitalized to cost centers.

IFRS 6, Exploration of Mineral Resources, only applies to activities undertaken after the acquisition of the legal rights to explore and therefore does not apply to pre-license costs. As these costs do not meet the definition of an asset they are expensed. In addition, only directly attributable general and overhead costs have been capitalized to exploration and evaluation assets.

c. Functional Currency and Foreign Operations

IFRS requires that the functional currency of each entity of the Company be determined separately in accordance with *IAS 21 – Foreign exchange* and should be measured using the currency of the primary economic environment in which they operate ("the functional currency"). IFRS provides primary and secondary indicators that are used to assist in assessing the functional currency of the entity. Under previous GAAP, foreign currency translation was determined based upon the relationship between the parent company and the respective operating division – i.e. if they are financially or operationally interdependent with the reporting entity. Based upon this, the UK pound was determined to be the functional currency for all entities under previous GAAP.

Using the IFRS indicators, the functional currency for the entities differ from the functional currency determined under previous GAAP. When considering these indicators a change of functional currency to Canadian dollars for Sterling Resources Ltd. and U.S. dollars for its Romanian operations was determined necessary.

d. Presentation

IFRS presentation differs from the presentation in accordance with previous GAAP. In particular:

i. In accordance with *IFRS 6, Exploration of Mineral Resources,* E&E assets are classified as either intangible or tangible assets according to their nature. Under previous GAAP these costs were classified as tangible assets within property, plant and equipment. The Company will be classifying E&E assets as intangible assets.

ii. In accordance with *IAS 1, Presentation of Financial Statements*, certain line items on the previous GAAP income statement have been reclassified. In particular:

(a.) Exploration and Evaluation Assets

The Company previously followed the full cost method of accounting for oil and gas assets. Under this method, all expenditures incurred in connection with the acquisition, exploration, appraisal and development of oil and gas assets were capitalized in cost centres on a country-by-country basis. As permitted under IFRS the Company has changed its policy to a successful efforts based accounting policy on a retroactive basis. Under this policy the costs of unsuccessful wells are expensed as dry hole costs in the income statement in the period in which they are determined to be unsuccessful.

(b.) Pre-License Acquisition Costs and Indirect Overhead Charges

Under previous GAAP all costs associated with property acquisition, exploration and development activities were capitalized within a cost centre, including costs incurred prior to the acquisition of a mineral right. In addition all administrative and general overhead costs were capitalized to cost centres.

IFRS 6 only applies to activities undertaken after the acquisition of the legal rights to explore and therefore does not apply to pre-exploration costs. As these costs do not meet the definition of an asset they are expensed. In addition only directly attributable general and overhead costs have been capitalized to exploration and evaluation assets.

(c.) Functional Currency and Foreign Operations

IFRS requires that the functional currency of each entity of the Company be determined separately in accordance with IAS 21 – Foreign exchange, and should be measured using the currency of the primary economic environment in which they operate ("the functional currency"). IFRS provides IFRS indicators that are used to assist in assessing the functional currency of the entity. Under previous GAAP, foreign currency translation was determined based upon the relationship between the parent company and the respective operating division – i.e. if they are financially or

operationally interdependent with the reporting entity. Based upon this, the UK pound ("GBP") was determined to be the functional currency for all entities under previous GAAP.

Using the IFRS indicators, a change of functional currency to the Canadian dollar for Sterling Resources Ltd. and the U.S. dollar for its Romanian operations was determined necessary.

(d.) Share-Based Compensation
Under previous GAAP the proportion of share-based compensation attributable to exploration and evaluation activities was capitalized within a cost centre. With the adoption of a successful efforts approach under IFRS, much of the share-based compensation previously capitalized would not be permitted as it relates to pre-license activity or unsuccessful wells.

(e.) Under previous GAAP employee benefit costs were included with other general and administrative costs unless chargeable to capital projects. Under IFRS, employee benefit costs including share-based payments are required to be shown separately from other general and administrative expenses.

Reconciliation of Assets, Liabilities and Equity

		June 30, 2010		
	Note	Previous GAAP	Effect of Transition to IFRS	IFRS
(Unaudited)		$000's	$000's	$000's
ASSETS				
Current assets				
Cash and cash equivalents		50,985	–	50,985
Restricted cash		6,422	–	6,422
Trade and other receivables		1,918	–	1,918
Prepaid expenses		106	–	106
Assets held for sale	(a), (b), (c)	2,807	(2,253)	554
		62,238	(2,253)	59,985
Non-current assets				
Exploration and evaluation assets	(d)-i	–	88,123	88,123
Petroleum and natural gas properties and equipment	(a), (b), (c), (d)-i	141,863	(141,863)	–
Property, plant and equipment	(b)	189	(6)	183
		142,052	(53,746)	88,306
		204,290	(55,999)	148,291
LIABILITIES AND EQUITY				
Current liabilities				
Trade and other payables		2,190	–	2,190
Decommissioning obligations on assets held for sale		51	–	51
		2,241	–	2,241
Non-current liabilities				
Decommissioning obligations		2,187	–	2,187
Equity				
Share capital		160,725	–	160,725
Contributed surplus		7,756	–	7,756
Accumulated other comprehensive loss	(b)	(1,968)	(27,656)	(29,624)
Retained earnings	(a), (b), (c)	33,349	(28,343)	5,006
		199,862	(55,999)	143,863
		204,290	(55,999)	148,291

Reconciliation of Profit and Loss

		Three Months Ended June 30, 2010			Six Months Ended June 30, 2010		
	Note	Previous GAAP	Effect of Transition to IFRS	IFRS	Previous GAAP	Effect of Transition to IFRS	IFRS
(Unaudited)		$000's	$000's	$000's	$000's	$000's	$000's
Revenue		–	–	–	–	–	–
Expenses							
Dry hole expense	(a)	–	2,386	2,386	–	4,076	4,076
Pre-license and other exploration costs	(c)	–	2,480	2,480	–	4,388	4,388
General and administration	(b), (d)-ii	798	(484)	314	2,328	(1,443)	885
Employee expenses	(d)-ii	–	1,347	1,347	–	2,556	2,556
Foreign exchange (gain) loss	(b)	345	(728)	(383)	(3,150)	(1,445)	(4,595)
Share-based compensation	(b), (d)-ii	476	(476)	–	806	(806)	–
Accretion	(b), (d)-ii	58	(58)	–	110	(110)	–
Depreciation	(b)	20	19	39	40	18	58
Total expenses		1,697	4,486	6,183	134	7,234	7,368
Financing income	(d)-ii	–	(236)	(236)	–	(401)	(401)
Financing costs	(d)-ii	55	96	151	384	293	677
Net loss for the period		(1,752)	(4,346)	(6,098)	(518)	(7,126)	(7,644)

Reconciliation of Comprehensive Income (Loss)

		Three Months Ended June 30, 2010			Six Months Ended June 30, 2010		
	Note	Canadian GAAP	Effect of Transition to IFRS	IFRS	Canadian GAAP	Effect of Transition to IFRS	IFRS
(Unaudited)		$000's	$000's	$000's	$000's	$000's	$000's
Net loss for the period		(1,752)	(4,346)	(6,098)	(518)	(7,126)	(7,644)
Foreign currency translation into presentation currency	(b)	5,570	(2,308)	3,262	(11,732)	2,816	(8,916)
Comprehensive income (loss)		3,818	(6,654)	(2,836)	(12,250)	(4,310)	(16,560)

Reconciliation of Equity

	Note	As at June 30, 2010
(Unaudited)		$000's
Total equity under previous GAAP		199,862
Adjustments:		
Dry hole costs	(a)	(10,844)
Pre-license costs and other costs expensed under IFRS	(b)	(35,893)
Foreign currency impact of change in functional currencies	(c)	(7,218)
Capitalized share-based compensation expensed under IFRS	(d)	(2,044)
Total equity under IFRS		143,863

CORPORATE INFORMATION

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(2) Chair Reserves Committee
(3) Audit Committee
(4) Chair Audit Committee
(5) Governance and Compensation Committee
(6) Chair Governance and Compensation Committee

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ROBIN M. CLARKSON
Head of Legal and General Counsel

SHERRY L. CREMER
Treasurer and Corporate Secretary

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Group Financial Controller

GEORGE KESTEVEN
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