



Q3
REPORT



For the nine months ended September 30, 2005



Diaz Resources Ltd.

Corporate Profile

Diaz Resources Ltd. is an oil and gas exploration and development company with land holdings and production in Canada and the United States. The Company's principal business is the exploration for and marketing of natural gas with the majority of the Company's revenue being generated from gas production in Alberta and Texas.

The Company currently focuses its exploration activities on shallow gas reservoirs in southern Alberta, a multi-zone oil and gas prospect at Harmattan in central Alberta and a deep Wilcox gas play in Texas. Southern Alberta combines low cost drilling and low risk exploration opportunities with an excellent natural gas infrastructure while Texas and Harmattan provide significant upside potential for reserves and production.

Corporate Summary

(Thousands, except per share amounts)

	Nine Months Ended September 30	
	2005	2004
Financial		
Total revenue	\$ 12,274	\$ 10,551
Cash flow from operations	\$ 7,859	\$ 6,717
per share, diluted	\$ 0.13	\$ 0.12
Earnings for the period	\$ 2,322	\$ 976
per share, diluted	\$ 0.04	\$ 0.02
Capital additions	\$ 7,014	\$ 7,596
Dispositions	\$ 725	\$ 219
Net debt	\$ 7,651	\$ 7,622
Total assets	\$ 50,197	\$ 43,789
Operations		
Production		
Gas (MMcfd)	6.0	6.3
Oil (Bopd)	165	105
BOEd (6Mcf = 1Bbl)	1,161	1,162
Product Prices		
Gas (\$/Mcf)	\$ 7.61	\$ 6.76
Oil (\$/Bbl)	\$ 60.74	\$ 46.92
Total shares outstanding, at period end	59,815	58,296

To the Shareholders



Financial and operating results for the nine months ended September 30, 2005 were improved over the same period in 2004, primarily due to higher commodity prices. However, exploration and development successes throughout the year, primarily in the Company's natural gas properties in Texas, have set the stage for significant production and cash flow growth in the fourth quarter of 2005.

Strategic Review Process

Diaz advises that due to the Company's recent successes in its U.S. exploration program, together with high commodity prices, the Board of Directors has terminated the formal strategic review process relating to the sale of assets, or the Company, at this time. Although Diaz continues to explore all avenues relative to increasing shareholder value, the focus for the near future will be to increase its U.S. exploration and drilling activities.

Exploration and Development

UNITED STATES – TEXAS

ALLEN RANCH – DIAZ WORKING INTEREST 20%

In Q1 2005, Diaz completed the drilling of the Hancock #1 well on the Allen Ranch prospect. The well encountered four prospective Wilcox sands. After completion and stimulation, the initial sand flowed gas at 1.4 MMcfd at 4,300 psi and was temporarily suspended. The second sand initially flowed gas at 3.8 MMcfd at 6,500 psi and after production testing flowed at a rate of 1.8 MMcfd before being temporarily suspended. The third sand is currently flowing at a stabilized rate of 5.8 MMcfd at a flowing pressure of 5,000 psi. The operator plans to complete and test the fourth zone in this well bore in the future and commingle production from the four zones.

Subsequent to the end of the quarter, a second well on the prospect has commenced drilling. This well will target a deeper Wilcox sand identified on seismic and the upper four sands identified in the initial well. The well should reach total depth in December 2005.

HOUND DOG – DIAZ WORKING INTEREST 28.1%

The R. Dickson #1 well, drilled in Q1 2004, encountered nine prospective sands. Most of the deeper Wilcox sands are off-structure and although the well flowed gas from these sands, after lengthy completion operations, the rates were not economic.

The well was finally completed in the Wilcox No. 8 sand and is currently producing at a rate of 4.0 MMcfd at a flowing pressure of 2,000 psi. In October, Diaz purchased an additional 5.6% working interest in this well for a consideration of \$450,000 U.S. to increase its interest to 28.1%.

CANADA – ALBERTA

RETLAW – DIAZ WORKING INTEREST 50%

Diaz participated in the drilling of a gas well at Retlaw 15-29-12-19 W4. The well was completed with an initial production rate of 2.0 MMcfd, and is anticipated to be on stream by early December 2005.

Diaz has drilled an additional well on this prospect, which was cased as a gas well subsequent to the reporting period.

Financial

Revenue for the nine months ended September 30, 2005 totaled \$12.3 million compared with \$10.6 million one year earlier.

Cash flow for the period increased by 17% to \$7.9 million, or \$0.13 per share compared with \$6.7 million, or \$0.12 per share in 2004. The rapid growth in U.S. production revenue resulted in Diaz's cash flow being negatively impacted by \$575,000 of current taxes. The Company plans to rapidly increase its U.S. capital budget, which will defer some of the current taxes payable.

Diaz reported earnings for the nine months ended September 30, 2005 of \$2.3 million, or \$0.04 per share compared with \$1.0 million, or \$0.02 per share reported in 2004.

Capital expenditures for the nine months ended September 30, 2005 totaled \$7.0 million compared with \$7.6 million in 2004 and were wholly financed from cash flow. Diaz completed the third quarter of 2005 with net

debt of \$7.7 million and debt repayability, annualized, from cash flow from operations was approximately 0.7 times.

Production

Natural gas production for the nine months ended September 30, 2005 averaged 6.0 MMcfd compared with 6.3 MMcfd for the same period in 2004. Oil production averaged 165 Bopd for the period compared with 105 Bopd in 2004 and total production averaged 1,161 BOEd in 2005 compared with 1,162 BOEd for the same period in 2004.

Production growth in Canada continued to be impaired by the premature decline of one of the Company's wells in the Enchant area. The Company's plans to increase production were further impacted by wet conditions, which delayed drilling, pipelining and completion operations.

At September 30, 2005, Diaz had over 500 BOEd temporarily restricted or behind pipe, 270 BOEd of which was on stream in October 2005. However, based on identified reserves currently behind pipe, which the Company plans to connect in Q4 2005 and Q1 2006, Diaz believes that it will exit the year at 1,600 BOEd and be producing at over 2,000 BOEd in Q1 2006.

Non-Core Asset Disposition

During the third quarter, Diaz sold its 12.5% working interest in a non-core oil property located in southern Alberta. The property was providing approximately 21 BOEd before the sale and was sold for \$657,000.

Share Capital Reorganization

At its shareholders' meeting on June 9, 2005, the Company's shareholders approved the amendment to the Articles of the Company to convert Subordinate Voting Shares and Multiple Voting Shares into one class of Common Shares, on a one-for-one basis. As a result, the Company now has only one class of shares outstanding.

Business Outlook

The Company is optimistic regarding the outlook for the balance of 2005 and 2006.

Recent results from the Company's deep Wilcox gas exploration program, especially the multi-zone success of the Allen Ranch prospect, has been encouraging. As a result, Diaz anticipates production and reserve increases in the United States during 2006. In addition, exploration and development work in southern and central Alberta should provide production and reserve increases in Canada during 2006.

Increased production from the Texas Wilcox trend and the development of the new discoveries in the Harmattan and Retlaw areas, together with high energy prices, should provide the Company with increased cash flow, which will finance an increased capital budget.

On behalf of the Board,

"Signed"

R.W. Lamond
President

November 10, 2005



Management's Discussion and Analysis

Prepared as of November 10, 2005

The following discussion and analysis is management's assessment of Diaz's historical, financial and operating results, together with future prospects, and should be read in conjunction with the unaudited consolidated financial statements of the Company for the nine months ended September 30, 2005 and the audited financial statements at December 31, 2004. The reader should be aware that historical results are not necessarily indicative of future performance.

Basis of Presentation

The financial data presented herein has been prepared in accordance with accounting principles generally accepted in Canada. All dollar amounts are in Canadian dollars unless otherwise indicated.

Non-GAAP Measurements – The Management's Discussion and Analysis contains the term cash flow from operations, which should not be considered an alternative to, or more meaningful as an indicator of the Company's performance than, cash flow from operating activities, as determined in accordance with accounting principles generally accepted in Canada. Diaz's determination of cash flow from operations may not be particularly comparable to that reported by other companies especially those in other industries. The reconciliation between net earnings and cash flow from operations can be found in the consolidated statements of cash flows in the unaudited interim consolidated financial statements and the audited consolidated financial statements. The Company also presents cash flow from operations per share. Per share amounts are calculated using weighted average shares outstanding consistent with the calculation of earnings per share.

BOE Presentation – The term barrels of oil equivalent (BOE) may be misleading, particularly if used in isolation. A BOE conversion ratio of 6 Mcf : 1 Bbl is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. All BOE conversions in this report are derived by converting gas to oil in the ratio of six Mcf of gas to one Bbl of oil.

This discussion and the Company's third quarter interim report contain forward-looking statements that involve risk and uncertainties. Such information, although considered reasonable by management at the time of preparation, may prove to be incorrect and actual results may differ materially from those anticipated in the statements made.

Oil & Gas Production

Diaz is primarily a natural gas producer with 84% of its production in Q3 2005 coming from natural gas wells. Diaz owns interests in producing properties in Canada: Alberta and Saskatchewan, and in the United States, almost exclusively in Texas. Significant increases in gas production from the Wilcox play in Texas have increased the Company's U.S. production to 36% of production in Q3 2005 from 24% in Q3 2004. Higher production rates at Hound Dog and Allen Ranch have increased the Company's production from the U.S. wells by an additional 240 BOEd in October 2005, further increasing the impact of U.S. production on the Company's results.

Production averaged 1,161 BOEd for the nine months ended September 30, 2005, unchanged from 1,162 BOEd in 2004. Oil and NGL production for the period increased to average 165 BOEd, compared with 105 BOEd in 2004. Increased production from the Company's discovery well at Harmattan offset declines and the sale of non-core assets during the period.

Natural gas production declined to average 6.0 MMcfd during the first nine months of 2005 from 6.3 MMcfd in 2004. U.S. gas production increased to average 2.1 MMcfd compared with 1.7 MMcfd in 2004. In spite of the fact that the Hound Dog and Allen Ranch wells were produced at half of their capacity during much of Q3 due to completion operations being carried out on the wells, the U.S. production for Q3 2005 was 2.4 MMcfd compared with 1.6 MMcfd for the same quarter in 2004. In October this production rate increased by 1.4 MMcfd due to increased production from both the Allen Ranch and Hound Dog wells.

Canadian natural gas production decreased by 18% due to the faster than anticipated decline in a well at Enchant and the Company's drilling, completion and pipeline operations being hampered by unseasonably wet weather. At Q3 2005, the Company had approximately 1.6 MMcfd of its Canadian natural gas production behind pipe, most of which should be on stream in December 2005.

Oil & Gas Production	Three Months Ended September 30		Nine Months Ended September 30	
	2005	2004	2005	2004
Gas – Canada				
Enchant	1,165	1,981	1,406	1,733
Retlaw/Little Bow	694	1,111	800	1,059
Carmangay	385	450	483	429
Therien	252	233	227	237
Harmattan	284	–	141	–
Jaslan	76	242	131	267
Provost	84	182	127	203
Iron Springs	94	147	98	154
Edward	10	117	71	155
Other	332	400	312	390
Gas – Canada (Mcf)	3,376	4,863	3,796	4,627
Oil & Liquids – Canada				
Harmattan	103	–	72	–
Parkman	31	37	30	36
Neutral Hills	–	18	14	20
Red Earth	12	14	12	13
Other	29	22	21	21
Oil & Liquids – Canada (Bopd)	175	91	149	90
BOEd – Canada (6Mcf = 1Bbl)	737	902	782	861

Oil & Gas Production (continued)	Three Months Ended September 30		Nine Months Ended September 30	
	2005	2004	2005	2004
Gas – U.S.				
Provident City	1,443	1,554	1,566	1,598
Allen Ranch	336	–	297	–
Hound Dog	558	–	239	–
Mustang Creek	61	67	68	99
Other	8	26	12	16
Gas – U.S. (Mcf)	2,406	1,647	2,182	1,713
Oil & Liquids – U.S.				
Provident City	13	14	16	15
Other	–	1	–	–
Oil & Liquids – U.S. (Bopd)	13	15	16	15
BOEd – U.S. (6Mcf = 1Bbl)	415	290	379	301
Gas – Company (Mcf)	5,782	6,510	5,978	6,340
Oil and Liquids – Company (Bopd)	188	106	165	105
BOEd – Company	1,152	1,191	1,161	1,162

Average commodity prices for the nine months ended September 30, 2005 were approximately 16% higher than prices for the same period in 2004 and the outlook remains positive for gas prices to remain at these levels. For the nine months ended September 30, 2005, Canadian gas prices averaged \$7.12 per Mcf, 9.9% higher than the \$6.48 reported in 2004. Oil prices were 30.4% higher than the comparable period, at \$60.28 per barrel from \$46.23 in 2004. In the U.S., both gas and oil prices increased by 12.8% and 27.3%, respectively.

Product Prices	Three Months Ended September 30		Nine Months Ended September 30	
	2005	2004	2005	2004
Canada				
Gas (\$/Mcf)	\$ 7.74	\$ 6.31	\$ 7.12	\$ 6.48
Oil & Liquids (\$/Bbl)	\$ 66.65	\$ 50.61	\$ 60.28	\$ 46.23
\$/BOE	\$ 51.24	\$ 39.14	\$ 46.06	\$ 39.66
U.S.				
Gas (\$/Mcf)	\$ 9.42	\$ 7.58	\$ 8.47	\$ 7.51
Oil & Liquids (\$/Bbl)	\$ 79.97	\$ 56.20	\$ 65.04	\$ 51.08
\$/BOE	\$ 57.30	\$ 46.03	\$ 51.39	\$ 45.38
\$/BOE – Company	\$ 53.42	\$ 40.81	\$ 47.80	\$ 41.14

Diaz believes oil prices will remain high throughout 2005 due to a strong global demand for oil, and gas prices will be held up by the trend to follow crude oil pricing. To this end, the Company has sold forward approximately 2.0 MMcf of natural gas production in Canada for the month of October 2005, with a floor price of \$6.86 per Mcf and a ceiling price of \$7.86 per Mcf, and 2.0 MMcf for the five months ending March 31, 2006 at a price of \$10.71 per Mcf.

Revenue from Oil and Gas Production (Thousands)	Three Months Ended September 30		Nine Months Ended September 30	
	2005	2004	2005	2004
Canada				
Natural gas	\$ 2,405	\$ 2,822	\$ 7,376	\$ 8,217
Oil and natural gas liquids	1,070	424	2,453	1,145
Other	54	6	72	20
Total Revenue	\$ 3,529	\$ 3,252	\$ 9,901	\$ 9,382
U.S.				
Natural gas	\$ 2,086	\$ 1,149	\$ 5,044	\$ 3,525
Oil and natural gas liquids	99	75	278	214
Other	2	–	2	1
Total Revenue	\$ 2,187	\$ 1,224	\$ 5,324	\$ 3,740
Total Revenue – Company	\$ 5,716	\$ 4,476	\$ 15,225	\$ 13,122

Diaz's increasing focus on U.S. exploration is reflected in growing U.S. gas production, with revenue from U.S. production accounting for 35% of the Company's revenue during Q3 2005, up from 28.5% in 2004.

Higher product prices and increased U.S. production increased revenue from U.S. wells to \$5.3 million for the nine months ended September 30, 2005 from \$3.7 million reported in 2004. Lower gas production volumes in Canada, due to production declines, were offset by higher gas prices and total revenue increased by 5.5%, to \$9.9 million for the year, to date.

As a result of increased production at Allen Ranch and Hound Dog in the U.S. and behind pipe production of 265 BOEd in Canada, combined with continued high oil and gas prices, Diaz is confident that revenues will continue to grow throughout the winter.

Royalties (Thousands, except per BOE and percentage amounts)	Three Months Ended September 30		Nine Months Ended September 30	
	2005	2004	2005	2004
Canada				
Crown	\$ 342	\$ 397	\$ 891	\$ 1,112
Freehold	167	173	559	583
Alberta Royalty Tax Credit (ARTC)	(73)	(79)	(178)	(223)
Royalties, net of ARTC	\$ 436	\$ 491	\$ 1,272	\$ 1,472
per BOE	\$ 6.43	\$ 5.92	\$ 5.96	\$ 6.24
Royalty as a percentage of revenue	12.4%	15.1%	12.8%	15.7%
U.S.				
Royalties	\$ 694	\$ 364	\$ 1,679	\$ 1,099
per BOE	\$ 18.20	\$ 13.69	\$ 16.21	\$ 13.34
Royalty as a percentage of revenue	31.7%	29.7%	31.5%	29.4%
Total Royalties – Company	\$ 1,203	\$ 934	\$ 3,129	\$ 2,794
per BOE	\$ 11.35	\$ 8.53	\$ 9.87	\$ 8.77

Canadian royalty rates declined to average 12.4%, after ARTC, for Q3 2005. This reflects the royalty free period for the first year of the Harmattan oil production.

Operating and Transportation Expense	Three Months Ended September 30		Nine Months Ended September 30	
	2005	2004	2005	2004
<i>(Thousands, except per BOE amounts)</i>				
Canada	\$ 701	\$ 985	\$ 2,186	\$ 2,598
per BOE	\$ 10.34	\$ 11.88	\$ 10.24	\$ 11.01
U.S.	\$ 57	\$ 28	\$ 144	\$ 79
per BOE	\$ 1.49	\$ 1.05	\$ 1.39	\$ 0.96
Total Expense – Company	\$ 758	\$ 1,013	\$ 2,330	\$ 2,677
per BOE	\$ 7.15	\$ 9.25	\$ 7.35	\$ 8.41

During the first nine months of 2005, operating costs in Canada decreased by 7.5%, to \$10.24 per BOE. In the U.S., operating costs increased to \$1.39 per BOE. As a result, overall operating costs decreased to average \$7.35 per BOE from \$8.41 per BOE in 2004. This decrease resulted from a higher percentage of the Company's production coming from high impact, low cost production in the U.S.

General & Administrative Expense	Three Months Ended September 30		Nine Months Ended September 30	
	2005	2004	2005	2004
<i>(Thousands, except per BOE amounts)</i>				
Cash compensation costs	\$ 246	\$ 208	\$ 731	\$ 648
Stock based compensation costs	102	13	527	89
Other overhead costs	252	215	763	636
Recovered from third parties	(75)	(108)	(230)	(297)
Capitalized	(45)	(49)	(126)	(150)
Net General & Administrative Expense	\$ 480	\$ 279	\$ 1,665	\$ 926
per BOE	\$ 4.53	\$ 2.55	\$ 5.25	\$ 2.91

Overhead costs increased to \$1.7 million during the nine months ended September 30, 2005 primarily as a result of stock based compensation costs, which is a non-cash expense relating to the issue of employee stock options.

Interest Expense	Three Months Ended September 30		Nine Months Ended September 30	
	2005	2004	2005	2004
<i>(Thousands, except per BOE and percentage amounts)</i>				
Average bank debt	\$ 8,484	\$ 7,635	\$ 8,780	\$ 7,495
Interest expense	\$ 131	\$ 99	\$ 372	\$ 276
per BOE	\$ 1.24	\$ 0.90	\$ 1.17	\$ 0.87
Average interest rate	5.1%	4.6%	5.0%	4.7%

Total interest expense increased to \$372,000 during the nine months ended September 30, 2005 from \$276,000 reported one year earlier. This was due to the larger loan amount during the current period.

The Company's bank debt levels increased to \$9.0 million in 2005 and interest rates have increased due to tightening fiscal policies, which will likely increase Diaz's interest expense.

Depletion, Depreciation & Accretion <i>(Thousands, except per BOE amounts)</i>	Three Months Ended September 30		Nine Months Ended September 30	
	2005	2004	2005	2004
Canada				
Depletion and depreciation	\$ 1,238	\$ 1,531	\$ 3,785	\$ 3,970
Asset retirement obligation accretion	50	54	150	130
Net depletion, depreciation & accretion	\$ 1,288	\$ 1,585	\$ 3,935	\$ 4,100
per BOE	\$ 19.00	\$ 19.11	\$ 18.44	\$ 17.37
U.S.				
Depletion and depreciation	\$ 358	\$ 218	\$ 940	\$ 584
Asset retirement obligation accretion	–	–	1	1
Amortization of deferred credit	–	–	–	(15)
Net depletion, depreciation & accretion	\$ 358	\$ 218	\$ 941	\$ 570
per BOE	\$ 9.37	\$ 8.20	\$ 9.09	\$ 6.92
Total – Company	\$ 1,646	\$ 1,803	\$ 4,876	\$ 4,670
per BOE	\$ 15.53	\$ 16.46	\$ 15.38	\$ 14.67

Diaz's overall corporate depletion rate has increased to \$15.38 per BOE. This reflects a Canadian depletion rate of \$18.44 per BOE and a U.S. depletion rate of \$9.09 per BOE. Diaz anticipates its depletion rate will be reduced in 2005 as the Company completes wells and increases its proved reserves and as the lower cost U.S. production becomes a larger percentage of the Company's production base.

Quarterly Financial Information

	Three Months Ended							
	2005	2005	2005	2004	2004	2003	2003	2003
	Sept. 30	June 30	Mar. 31	Dec. 31	Sept. 30	June 30	Mar. 31	Dec. 31
<i>(Thousands, except per share amounts)</i>					(Restated) ⁽¹⁾	(Restated) ⁽¹⁾	(Restated) ⁽¹⁾	(Restated) ⁽¹⁾
Total revenue	\$ 4,585	\$ 4,253	\$ 3,436	\$ 3,730	\$ 3,621	\$ 3,818	\$ 3,112	\$ 2,713
Earnings	\$ 1,101	\$ 831	\$ 390	\$ 568	\$ 26	\$ 360	\$ 590	\$ 191
per share	\$ 0.02	\$ 0.01	\$ 0.01	\$ 0.01	\$ –	\$ 0.01	\$ 0.01	\$ 0.01
Cash flow from operations	\$ 3,299	\$ 2,492	\$ 2,068	\$ 2,068	\$ 2,204	\$ 2,540	\$ 1,973	\$ 1,395
per share	\$ 0.05	\$ 0.05	\$ 0.03	\$ 0.04	\$ 0.04	\$ 0.04	\$ 0.03	\$ 0.02
Fixed asset additions (net)	\$ 1,261	\$ 2,717	\$ 2,260	\$ 4,562	\$ 2,117	\$ 2,348	\$ 2,912	\$ 3,822
Total assets	\$ 50,197	\$ 48,563	\$ 46,455	\$ 46,675	\$ 43,789	\$ 43,251	\$ 39,805	\$ 39,636
Net debt	\$ 7,651	\$ 9,604	\$ 9,211	\$ 9,095	\$ 7,622	\$ 7,882	\$ 7,992	\$ 7,100

⁽¹⁾Transportation costs have been restated as operating expense rather than deducting them from revenue.

Liquidity and Capital Resources

Diaz completed the nine months ended September 30, 2005 with a net debt of \$7.7 million compared with \$7.9 million in 2004. The Company has a credit facility of \$10.8 million, which is reviewed annually in May.

The Company's capital expenditure budget for 2005 will be funded primarily from cash flow.

Income Taxes <i>(Thousands)</i>	Three Months Ended September 30		Nine Months Ended September 30	
	2005	2004	2005	2004
Canada				
Current tax	\$ 6	\$ 15	\$ 20	\$ 20
Future tax	394	359	(166)	453
Total – Canada	\$ 400	\$ 374	\$ (146)	\$ 473
U.S.				
Current tax	\$ 13	\$ 24	\$ 555	\$ 24
Future tax	14	(55)	252	489
Total – U.S.	\$ 27	\$ (31)	\$ 807	\$ 513
Total – Company	\$ 427	\$ 343	\$ 661	\$ 986

For the nine months ended September 30, 2005, Diaz's income tax expense was \$661,000 consisting of current taxes payable of \$575,000 and future tax liability of \$86,000. The majority of the current tax liability reflects the tax payable in the U.S., as Diaz's capital expenditures did not keep pace with the Company's rapidly growing U.S. revenues.

The Company's plans include a significantly increased U.S. capital budget, both in Q4 2005 and 2006.

Normal Course Issuer Bid

During the nine months ended September 30, 2005, Diaz repurchased 9,000 Subordinate Voting Shares, no Multiple Voting Shares and 10,000 Common Shares and at an average price of \$0.66 per share.

Diaz was authorized to repurchase up to 2,968,500 Common Shares through the facilities of the Toronto Stock Exchange pursuant to a normal course issuer bid, which expires on September 5, 2006. Shares repurchased pursuant to the bid are cancelled.

Business Risk

The Company is engaged in the exploration, development, production and acquisition of crude oil and natural gas. Diaz's business is inherently risky and there is no assurance that hydrocarbon reserves will be discovered and economically produced.

Financial risks associated with the petroleum industry include fluctuations in commodity prices, interest rates and currency exchange rates. Operational risks include competition, environmental factors, reservoir performance uncertainties, a complex regulatory environment and safety concerns.

The Company minimizes its business risks by focusing on a select group of properties. This enables Diaz to have more control over the timing, direction and costs related to exploration and development opportunities. The geological focus is on areas in which the prospects are well understood by management. Technological tools are regularly used to reduce risk and increase the probability of success. The Company closely follows all government regulations and has an up-to-date emergency response plan that has been communicated to all field operations by management. Diaz also carries insurance coverage to protect itself against potential losses.

Employing a highly motivated and experienced staff of petroleum and natural gas professionals further minimizes the business risk.

The Company is exposed to commodity price and market risk for its principal products of petroleum and natural gas. Commodity prices are influenced by a wide variety of factors of which most are beyond the control of Diaz. To manage this risk, the Company has entered into a number of forward sales contracts in relation to gas prices.

Outlook

Diaz believes energy prices will remain near current levels throughout 2005. These high prices combined with higher production levels in both Canada and the United States should result in higher cash flow.

Higher cash flow will allow the Company to increase its capital budget and provide continued growth in 2005.

Strategic Review Process

Diaz advises that due to the Company's recent successes in its U.S. exploration program, together with high commodity prices, the Board of Directors has terminated the formal strategic review process relating to the sale of assets, or the Company, at this time. Although Diaz continues to explore all avenues relative to increasing shareholder value, the focus for the near future will be to increase its U.S. exploration and drilling activities.

Consolidated Balance Sheet

(unaudited)

(Thousands)

As at	September 30 2005	December 31 2004
ASSETS		
Current Assets		
Cash	\$ 1,723	\$ 762
Accounts receivable	5,791	5,006
Prepaid expense	323	213
	7,837	5,981
Property, plant and equipment	68,331	61,939
Accumulated depletion and depreciation	(25,971)	(21,245)
	42,360	40,694
Total Assets	\$ 50,197	\$ 46,675
LIABILITIES		
Current Liabilities		
Accounts payable and accrued liabilities	\$ 6,220	\$ 7,569
Income tax payable	378	–
Bank debt (Note 3)	8,890	7,507
	15,488	15,076
Other Liabilities		
Future income tax liability	5,493	5,432
Asset retirement obligation (Note 6)	2,469	2,338
Total Other Liabilities	7,962	7,770
	23,450	22,846
SHAREHOLDERS' EQUITY		
Share capital (Note 4)	16,235	16,165
Contributed surplus (Note 4)	828	300
Retained earnings	9,684	7,364
	26,747	23,829
Total Liabilities and Shareholders' Equity	\$ 50,197	\$ 46,675

Approved by the Board:

"Signed"

R.W. Lamond
Director

"Signed"

C.A. Teare
Director

Consolidated Statement of Operations & Retained Earnings

(unaudited)

(Thousands, except per share amounts)

	Three Months Ended September 30		Nine Months Ended September 30	
	2005	2004	2005	2004
Revenue				
Production	\$ 5,642	\$ 4,471	\$ 15,151	\$ 13,101
Royalties – net of ARTC	(1,131)	(855)	(2,951)	(2,571)
Interest and other income	74	5	74	21
	4,585	3,621	12,274	10,551
Expenses				
Operating and transportation	758	1,013	2,330	2,677
General and administration	480	279	1,665	926
Interest expense	131	99	372	276
Foreign exchange loss	42	58	48	40
Depletion, depreciation and accretion	1,646	1,803	4,876	4,670
	3,057	3,252	9,291	8,589
Earnings before income tax	1,528	369	2,983	1,962
Income tax				
Current	19	39	575	44
Future	408	304	86	942
Total income tax	427	343	661	986
Net earnings for the period	1,101	26	2,322	976
Excess of cost over paid up capital on share repurchases	(1)	(49)	(2)	(111)
Retained earnings, beginning of period	8,584	6,984	7,364	6,067
Change in accounting policy (Note 2)	–	(21)	–	8
Retained earnings, end of period	\$ 9,684	\$ 6,940	\$ 9,684	\$ 6,940
Earnings per share, basic and diluted	\$ 0.02	\$ 0.00	\$ 0.04	\$ 0.02

Consolidated Statement of Cash Flows

(unaudited)

(Thousands)

	Three Months Ended September 30		Nine Months Ended September 30	
	2005	2004	2005	2004
Cash provided by (used for):				
Operating Activities				
Earnings for the period	\$ 1,101	\$ 26	\$ 2,322	\$ 976
Non-cash items:				
Depreciation, depletion and accretion	1,646	1,803	4,876	4,670
Non-cash compensation	102	13	527	89
Future taxes	408	304	86	942
Foreign exchange loss	42	58	48	40
Cash flow from operations	3,299	2,204	7,859	6,717
Abandonments	(15)	(19)	(122)	(169)
Change in non-cash working capital	(559)	1,499	(762)	383
	2,725	3,684	6,975	6,931
Investing Activities				
Property, plant & equipment – additions	(1,936)	(2,319)	(7,014)	(7,596)
Property, plant & equipment – dispositions	675	202	725	219
Change in non-cash working capital	(804)	(2,505)	(1,179)	(2,180)
	(2,065)	(4,622)	(7,468)	(9,557)
Financing Activities				
Increase (decrease) in bank debt	(66)	(114)	1,384	3,123
Common Shares				
Issued for cash on exercise of options	6	–	6	–
Repurchased for cancellation	–	–	(6)	–
Class A Subordinate Voting Shares				
Issued for cash on exercise of options	–	373	76	450
Repurchased for cancellation	–	(99)	(6)	(119)
Class B Multiple Voting Shares				
Repurchased for cancellation	–	(16)	–	(124)
Offering cost	–	–	–	(2)
	(60)	144	1,454	3,328
Increase (decrease) in cash	600	(794)	961	702
Cash, beginning of period	1,123	1,620	762	124
Cash, end of period	\$ 1,723	\$ 826	\$ 1,723	\$ 826
Supplementary information regarding cash payments:				
Interest paid during the period	\$ 131	\$ 99	\$ 372	\$ 276
Taxes paid during the period	\$ 51	\$ 39	\$ 153	\$ 44

Notes to the Interim Consolidated Financial Statements

For the Nine Months Ended September 30, 2005

1. Accounting Policies

The interim consolidated financial statements of Diaz Resources Ltd. ("Diaz") have been prepared in accordance with accounting principles generally accepted in Canada. Management has made the necessary estimates and assumptions regarding certain types of assets, liabilities, revenues and expenses in the preparation of the financial statements. Accordingly, actual results may differ from estimated amounts but management does not believe such differences will materially affect Diaz's financial position or results of operations. Certain information and disclosures normally required to be included in the notes to the annual consolidated financial statements have been condensed or omitted. The reader should refer to the annual consolidated financial statements of Diaz at December 31, 2004.

2. Change in Accounting Policies

ASSET RETIREMENT OBLIGATIONS

As at January 1, 2004, the Company has retroactively adopted the Canadian Institute of Chartered Accountants ("CICA" guideline for accounting for asset retirement obligation – "ARO"). Under this standard, the Company must recognize the fair value of an ARO as a liability in the period in which it is incurred if a reasonable estimate of fair value can be made. The present value of the estimated ARO is capitalized as part of the net capitalized asset base and the depletion of the capitalized asset retirement cost is determined on a basis consistent with depletion of the Company's other assets. With time accretion will increase the carrying amount of the obligation. Accretion will be expensed.

Previously, the Company provided for estimated future abandonment and site restoration costs for its oil and gas properties using the unit-of-production method.

STOCK BASED COMPENSATION

At January 1, 2004, the Company adopted the fair value method for accounting of stock based compensation. The change was accounted for retroactively without restatement of prior period numbers. Using the fair value method, compensation costs of stock based compensation are estimated and charged to earnings in the period of the option grant.

Previously, the Company used the intrinsic value method and no compensation expense was recognized.

3. Bank Debt

All credit facilities that are revolving, in nature, must be disclosed as "current portion of long-term debt." Diaz utilizes a secured revolving production loan that is payable on demand and is subject to an annual review and, therefore, is considered "current," for disclosure purposes and has been disclosed under current liabilities

4. Share Capital

<i>(Thousands)</i>	No. of Shares	Amount
Common Shares		
Balance, December 31, 2004	–	\$ –
Issued on conversion of Subordinate Voting Shares ⁽¹⁾	53,839	14,449
Issued on conversion of Multiple Voting Shares ⁽¹⁾	5,963	1,780
Issued on conversion of options	13	6
Balance, September 30, 2005	59,815	\$ 16,235

4. Share Capital (continued)

<i>(Thousands)</i>	No. of Shares	Amount
Subordinate Voting Shares		
Balance, December 31, 2004	53,638	\$ 14,385
Purchased for cancellation	(19)	(12)
Issued on exercise of options	220	76
Converted to Common Shares ⁽¹⁾	(53,839)	(14,449)
Balance, September 30, 2005	–	\$ –
Multiple Voting Shares		
Balance, December 31, 2004	5,963	\$ 1,780
Converted to Common Shares ⁽¹⁾	(5,963)	(1,780)
Balance, September 30, 2005	–	\$ –
Total Shares Outstanding, September 30, 2005	59,815	\$ 16,235
Contributed Surplus		\$ 828

⁽¹⁾ SHARE CAPITAL REORGANIZATION

On June 9, 2005, the shareholders approved the amendment to the Articles of the Company to convert all of the Subordinate Voting Shares and Multiple Voting Shares into Common Shares on a one-for-one basis.

STOCK OPTION PLAN

As at September 30, 2005, there are a total of 3,558,333 outstanding under the stock option plan with a weighted average exercise price of \$0.53 per share. A total of 2,228,233 options with a weighted average exercise price of \$0.43 are exercisable at the end of the period.

The Company accounts for its stock based compensation plan using the fair value method, whereby compensation costs are charged to earnings in the period in which they are incurred.

The fair value of each option granted is estimated on the date of grant using the Black-Scholes option-pricing model with assumptions as follows:

	Risk Free Interest Rate (%)	Expected Life (Years)	Expected Volatility	Dividends per Share
2004	3.00	4.0	0.90	n/a
2005	3.23	4.0	0.90	n/a

5. Financial Instruments

The Company is exposed to fluctuations in commodity prices, interest rates and Canada/U.S. dollar exchange rates. The Company, when appropriate, utilizes financial instruments to manage its exposure to these risks.

NATURAL GAS CONTRACTS

At September 30, 2005, the following contract was in effect:

Fixed Price

Volume	Fixed Price		Time Period for Contract
	(\$/Gj)	(\$/Mcf)	
2,000 Gj/d (1,900 Mcfd)	\$ 10.15	\$ 10.71	Nov. 1, 2005 to Mar. 31, 2006

Costless Collar

Volume	Floor Price		Ceiling Price		Time Period for Contract
	(\$/Gj)	(\$/Mcf)	(\$/Gj)	(\$/Mcf)	
2,000 Gj/d (1,900 Mcfd)	\$ 6.50	\$ 6.86	\$ 7.45	\$ 7.86	Oct. 1, 2005 to Oct. 31, 2005

6. Asset Retirement Obligation

The following table presents the reconciliation of the beginning and ending aggregate carrying amount of the obligation associated with the retirement of oil and gas properties:

	2005	2004
Asset Retirement Obligation, beginning of period	\$ 2,338	\$ 2,314
Liabilities incurred	135	281
Liabilities settled	(154)	(169)
Foreign exchange	–	2
Accretion expense	150	131
Asset Retirement Obligation, end of period	\$ 2,469	\$ 2,559

The total undiscounted amount of estimated cash flows required to settle the obligation is \$4,757,000, which has been discounted using a credit-adjusted risk free rate of 7 percent and an inflation rate of 2%. Most of these obligations are expected to be paid between 2005 and 2034.

7. Segmented Information

The Company's only industry segment is the exploration for and development and production of oil and natural gas. The following table sets forth the geographical segments of the Company's operations between Canada and the United States.

(Thousands)	Three Months Ended September 30		Nine Months Ended September 30	
	2005	2004	2005	2004
Revenue (net)				
Canada	\$ 3,091	\$ 2,761	\$ 8,628	\$ 7,910
United States	1,494	860	3,646	2,641
	\$ 4,585	\$ 3,621	\$ 12,274	\$ 10,551
Interest Expense				
Canada	\$ 131	\$ 99	\$ 372	\$ 276
United States	–	–	–	–
	\$ 131	\$ 99	\$ 372	\$ 276
Current Taxes				
Canada	\$ 6	\$ 15	\$ 20	\$ 20
United States	13	24	555	24
	\$ 19	\$ 39	\$ 575	\$ 44
Cash Flow from Operations				
Canada	\$ 1,923	\$ 1,400	\$ 4,962	\$ 4,207
United States	1,376	804	2,897	2,510
	\$ 3,299	\$ 2,204	\$ 7,859	\$ 6,717
Depletion, Depreciation & Accretion				
Canada	\$ 1,288	\$ 1,585	\$ 3,935	\$ 4,100
United States	358	218	941	570
	\$ 1,646	\$ 1,803	\$ 4,876	\$ 4,670
Net Earnings (Loss)				
Canada	\$ 140	\$ (559)	\$ 666	\$ (434)
United States	961	585	1,656	1,410
	\$ 1,101	\$ 26	\$ 2,322	\$ 976
Additions to Property, Plant & Equipment				
Canada	\$ 870	\$ 2,060	\$ 5,004	\$ 6,598
United States	400	(10)	1,388	889
	\$ 1,270	\$ 2,050	\$ 6,392	\$ 7,487
Identifiable Assets, Net				
Canada	\$ 42,369	\$ 39,765	\$ 42,369	\$ 39,765
United States	7,828	4,024	7,828	4,024
	\$ 50,197	\$ 43,789	\$ 50,197	\$ 43,789

Corporate Information

Directors

Robert W. Lamond
Calgary, Alberta

Charles A. Teare
Calgary, Alberta

Donald K. Clark
Calgary, Alberta

Clive M. Stockdale
Vancouver, British Columbia

Allan R. Twa
Calgary, Alberta

Raj Agrawal ⁽¹⁾
Calgary, Alberta

John G.F. McLeod ⁽¹⁾
Calgary, Alberta

Robert L. McPherson ⁽¹⁾
Calgary, Alberta

⁽¹⁾ Member of the Audit Committee

Legal Counsel

Burnet, Duckworth & Palmer LLP
Calgary, Alberta

Auditors

Pricewaterhouse Coopers LLP
Calgary, Alberta

Diaz Resources Ltd.

Suite 1800, 633 Sixth Avenue S.W.
Calgary, Alberta T2P 2Y5
Telephone: (403) 269-9889
Fax: (403) 269-9890
info@diazresources.com
www.diazresources.com

Officers

R.W. Lamond
President, Chairman of the Board & CEO

C.A. Teare
Executive Vice President & CFO

D.K. Clark
Vice President, Operations

C.S. Cohen
Corporate Secretary

R.D. Arsenault
Controller

Subsidiaries

Diaz Resources, Inc.

Orbit Oil & Gas Inc.

Registrar and Transfer Agent

Computershare Trust Company of Canada
Calgary, Alberta
Toronto, Ontario

Stock Exchange Listing

Toronto Stock Exchange
Trading Symbols: DZR



Diaz Resources Ltd.

Suite 1800, 633 Sixth Avenue S.W.

Calgary, Alberta T2P 2Y5

Telephone: (403) 269-9889

Fax: (403) 269-9890

info@diazresources.com

www.diazresources.com