

The Business Environment

The benchmark WTI crude oil price averaged US\$41.40/bbl in 2004, up from US\$30.99 in 2003 and US\$26.15 in 2002.

Despite current price levels, world oil demand increased by an estimated 2.7 mmbbls/d in 2004, reaching a record high 82 mmbbls/d average for the year. OECD countries only accounted for about one-quarter of the growth, with the majority coming from emerging market economies, in particular China and India.

Non-OPEC production increased by about one mmbbls/d, most of which came from the former Soviet Union and the remainder was supplied by OPEC. As a result, OPEC is running at close to maximum capacity. The lack of surplus crude, combined with political uncertainty in the Middle East and elsewhere, has kept prices at high levels.

NYMEX natural gas prices averaged US\$6.09/mmbtu in 2004, compared to US\$5.44 in 2003 and US\$3.25 in 2002.

Current natural gas prices reflect the inability of US natural gas producers to increase production in recent years. Some estimates show that US natural gas production has fallen by over 5% over the past three years, causing prices to rise to a point where they are rationing demand. US natural gas demand has also fallen by 5%, with most of the decrease occurring in the electrical generation and industrial sectors. In 2004, Canadian natural gas production increased by an estimated 2%.

Talisman netbacks averaged \$24.45/boe in 2004, up from \$22.99 in 2003.

The Canadian dollar strengthened against the US dollar in 2004, gaining approximately 7%. This had the effect of lowering Talisman's reported netbacks, which are shown in Canadian dollars. Most of Talisman's liquids and natural gas sales are priced off US\$ denominated benchmarks.

Unit operating costs were up 4% overall. Increases in Canada and the North Sea were partly offset by the addition of lower cost production elsewhere.

Hedging losses increased to \$3.02/boe in 2004. The Company hedged approximately 22% of its 2004 production volumes. However, only 2% of 2005 production is currently hedged.

Royalty rates were unchanged at 16%.

Detailed information on Talisman's netbacks can be found in Talisman's Annual Report Financial Review.

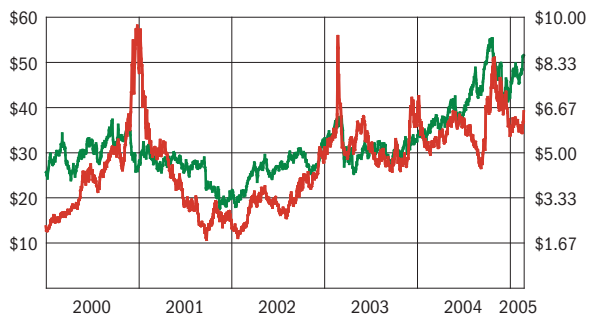
Netbacks

(boe)	2004	2003	2002	2001	2000
Sales price (before hedging)	42.75	38.51	32.89	32.90	34.74
Hedging (gain) loss	3.02	1.34	(0.46)	(0.06)	2.53
Royalty	7.04	6.18	5.74	6.47	6.29
Transportation	1.20	1.26	1.20	—	—
Opex	7.04	6.74	6.06	5.79	5.19
Netback	24.45	22.99	20.35	20.70	20.73

Excludes synthetic

WTI Crude Oil (US\$/bbl)

NYMEX Natural Gas (US\$/mmbtu)



The Bleo Holm FPSO at the Ross/Blake fields.

Financial and Operating Performance



Talisman-operated Edson Gas Plant.

Talisman generated \$2.9 billion in cash flow in 2004

Cash flow totaled \$2.9 billion in 2004 (\$7.65/share) versus \$2.7 billion (\$7.07/share) a year earlier. Gross sales were \$6.9 billion, up \$1.3 billion compared to 2003 on higher volumes and prices. Higher sales revenues were partially offset by higher royalties, operating costs, hedging losses and current taxes. Cash flow is a non-GAAP measure. Please refer to the advisories on the inside back cover.

Net income for 2004 was \$663 million (\$1.77/share), compared to \$1,012 million (\$2.56/share) in 2003. Talisman also calculates net income in accordance with US GAAP. On this basis, earnings were \$694 million in 2004 (\$1.81/share) compared to \$922 million (\$2.39/share) in 2003.

Earnings from operations up 15%

Talisman's earnings from operations in 2004 were \$773 million (\$2.02/share) compared to \$673 million (\$1.74/share) the previous year. Earnings from operations are calculated to help investors understand the Company's core operating performance on a consistent, comparable basis. For example, the sale of Talisman's assets in Sudan and adjustments to tax rates had a significant positive impact on 2003 earnings.

Earnings from operations in 2004 were up, due largely to higher volumes and prices. Offsetting this was higher depreciation, depletion and amortization expense, as well as higher dry hole and exploration costs.

Earnings from operations is a non-GAAP measure. A reconciliation to net income has been provided on the inside back cover.

Liquidity and capital resources

Talisman's long-term debt at year end was \$2.5 billion, down from a total of \$2.6 billion (comprised of long-term debt of \$2.2 billion and preferred securities of \$431 million) at the end of 2003. During 2004, the Company generated \$3.1 billion of cash from operating activities and spent \$2.5 billion on exploration and development while spending \$242 million on acquisitions. Talisman also refinanced its preferred securities, paid dividends of \$114 million and repurchased almost nine million common shares for \$286 million. At year end, the Company had drawn \$328 million of its available \$1,335 million bank lines of credit.

Additional financial information can be found in Talisman's 2004 Annual Report Financial Review, available on our website or by contacting the Company.

Talisman sets production per share record

Production averaged 438,000 boe/d in 2004, an increase of 10%, setting a new record of 0.42 boe per share. The majority of the increase came from a full year of production at the PM-3 CAA project in Malaysia/Vietnam.

	2004	2003	2002
Production (daily average) ¹			
Oil and liquids (bbls/d)			
North America	57,392	59,578	62,676
North Sea	121,861	113,075	127,486
Southeast Asia	35,644	24,430	22,469
Algeria	13,537	6,594	—
Sudan	—	13,039	60,109
Total oil and liquids	228,434	216,716	272,740
Natural gas (mmcf/d)			
North America	885	864	820
North Sea	114	109	122
Southeast Asia	260	117	94
Total natural gas	1,259	1,090	1,036
Total mboe/d	438	398	445
Total mboe/d (net of royalties)	365	334	366

1 Production numbers are before royalties, unless otherwise indicated.



Marketing operations in Calgary.

Oil and liquids production increased by 5% with growth coming from the North Sea (up 8% due to North Tartan startup, Intrepid FCA acquisition and the Galley field acquisition), Southeast Asia (up 46% with a full year of production from PM-3 CAA) and Algeria (up 105% with a full year of production from the MLN field).

Talisman increased its natural gas production by 16%. Production in North America increased 2% with drilling success in the Foothills, west central Alberta and the Northeastern US. Production in Southeast Asia more than doubled. Gas sales in Indonesia averaged 141 mmcf/d (up 26%), reflecting new volumes to Singapore. Gas production from PM-3 CAA in Malaysia/Vietnam, averaged 119 mmcf/d, compared to 5 mmcf/d in 2003.

Talisman replaced 179% of production, a key indicator of future growth

Talisman replaced 179% of production from all sources in 2004 (proved reserves only) and 166% through drilling, including revisions. The Company added 265 mmboe of proved reserves through drilling and development (including net revisions) and 21 mmboe of proved reserves through net acquisitions.

Major contributors to the growth in reserves were 479 bcf of natural gas discoveries, additions and extensions in North America, 85 mmbbls of oil in the North Sea and 695 bcf of natural gas additions in Indonesia, primarily associated with the signing of a major new gas sales contract in August 2004.

As a result, Talisman increased its total proved reserves by 9%, to almost 1.5 billion boe. At year end, Talisman had a reserve life index of 9.3 years for proved reserves and 14 years based on proved and probable reserves. Talisman's net proved reserves increased by 11% to 1.2 billion boe.

Talisman Proved Reserves	Oil & NGLS¹ (mmbbls)	Natural Gas¹ (bcf)	BOE¹ (mm)	Net BOE² (mm)
Dec 31, 2003	579	4,695	1,362	1,086
Discoveries, additions and extensions	74	1,252	283	204
Net acquisitions	30	(50)	21	24
Revisions	17	(212)	(19)	22
Production	(82)	(462)	(159)	(129)
Total Proved Dec 31, 2004	618	5,223	1,488	1,207
Total Probable³ Dec 31, 2004	383	2,624	820	634

- 1 Talisman working interest reserves before royalties payable, plus royalty interests and net profit interests.
- 2 Talisman working interest net of royalties, plus royalty interests and net profit interests.
- 3 See "Reserves Data and Other Oil and Gas Information" on the inside back cover.

Approximately 42% of Talisman's proved reserves are high quality oil and liquids and 58% are natural gas. Proved reserves in North America account for 42% of the total, the North Sea 22% and Southeast Asia 30%. At year end, the Company had 820 mmboe of gross probable reserves, which comprise a large part of Talisman's development inventory.

Capital spending during 2004 totaled \$2,375 million for exploration and development, excluding Syncrude and mid-stream expenditures, and \$242 million for net acquisitions. Over the past three years, Talisman has added a total of 623 mmboe of proved reserves (including net acquisitions, but excluding the sale of Sudan assets) while spending \$7,461 million on exploration, development and net acquisitions.

Approximately 90% of Talisman's proved reserves have been independently evaluated over the past three years.