

28th October 2014

Board of Directors:

Michael Fry
(Non-executive Chairman)

Robert Willes
(Managing Director)

William Bloking
(Non-executive Director)

**Issued capital
(as at 30 September, 2014):**

329,482,541 fully paid
ordinary shares (ASX: CEL)

65,896,502 listed options
(ASX: CELO)

41,500,000 unlisted options
and rights

Substantial holders:

LQ Super 12.61%

W & M Brown 5.24%

Registered office:

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QUARTERLY ACTIVITIES REPORT FOR THE PERIOD ENDING SEPTEMBER 30 2014

HIGHLIGHTS

South Africa

- **Momentum grows towards approval of applications for shale gas exploration rights in South Africa**
 - **Significant milestone – government to proceed with processing exploration right application**
 - **Minister of Mineral Resources plans to consult stakeholders prior to finalising Technical Regulations**
 - **Minister makes recommendations on MPRDA Bill to President Zuma – announcement expected soon**
 - **Calls for commission of inquiry into energy crisis as new Eskom bail-out is announced**
- **Farm-out discussions continue pending grant of exploration right**

Corporate

- **Challenger continues to build its corporate profile and relationships in South Africa, and with the Australian Government**

South Africa

Momentum continues to build towards the determination of applications for shale gas exploration.

Post the reporting period, Bundu Gas and Oil Exploration Pty Ltd (Bundu) has been advised by the Petroleum Agency SA (PASA) that a decision has been taken to proceed with processing Bundu's application for a shale gas Exploration Right in South Africa's Karoo Basin.

Significant time has elapsed since the application was submitted in 2010, and it is important that the documentation is up to date. PASA has requested that Bundu review and augment its Environmental Management Programme (EMPr) where necessary. In accordance with the Mineral and Petroleum Resources Development Act 2002, Bundu is required to notify and consult with affected communities and parties in respect of any such revisions. Bundu has been requested to complete this process by 27 February 2015.

Challenger considers this to be very significant and positive news. The applications for shale gas exploration rights have been on hold since 2011, so the decision to proceed with the processing of Bundu's application represents a major milestone and signals that the South African Government is ready to move forward with the exploration and appraisal of this potentially vital national resource. Challenger is greatly encouraged by this development, and looks forward to engaging with local communities and stakeholders.

The Minister of Mineral Resources, Ngoako Ramatlhodi, has indicated in public presentations at conferences and in media reports that progress is being made on both the Technical Regulations and the MPRDA Bill.

The government is to consult interested and affected stakeholders before finalising the Technical Regulations. These are expected soon.

"Operation Phakisa" (or "Hurry Up") is a Government initiative launched in July and managed by McKinsey over a period of six weeks. The Operation Phakisa process was conceived as a way to "kick start" the ocean economy in South Africa, focused on four key sectors, including oil and gas. The Offshore Petroleum Association of South Africa (OPASA) participated as a major stakeholder in the offshore oil and gas sector. One of the major issues addressed was the legislative uncertainty created by the Mineral and Petroleum Resources Development Amendment Bill. The results were announced in Durban in October. Several of the recommendations coming out of this process relate to the provisions of the MPRDA. Government has advised that the Onshore Petroleum Association of South Africa (ONPASA) will be consulted in the implementation of this process. We understand that the Minister has now made his recommendations to the President regarding the MPRDA Bill, and an announcement on this is expected shortly. It is possible that the MPRDA may be referred back to Parliament, and the indications are that this will be positive for the oil and gas industry.

Challenger Managing Director, Robert Willes, participated as part of an expert panel on shale gas at the Jo'burg Mining Indaba in October. The keynote address from Minister

Ramathlodi referred to the MPRDA, stating that “the amendment of the Minerals Bill is sitting with the President as we speak and resolutions are expected soon”.

ANC Secretary General Gwede Mantashe also spoke at the Indaba and commented regarding shale gas that “we can’t afford to talk about this for 10 years” and “we need to get on with it”.

In the meantime, South Africa’s energy dilemma continues to deepen with calls for a commission of inquiry into the worst crisis in this arena for 40 years. In September it was announced that Eskom is to receive further government support, including a capital injection.

In the meantime, Challenger and Bundu continue to stay close to the evolving situation in South Africa, and continue to progress discussions on a potential farm-in with interested parties.

Background

The Karoo Basin, which extends across 600,000 km² is located in central and southern South Africa and contains organic rich shales of Permian age with combined thickness up to 5000 feet. The focus for shale gas exploration is in the southern portion of the basin where the shales are at sufficient depth and where five wells, all pre-1970, intersected the shales with significant gas shows. One well, the Cranemere CR 1/68 well, flowed more than 8 MMcf/day of natural gas from the Fort Brown shale during testing over a 158 feet interval in 1968. The production was judged to be from fractures and secondary porosity in the shales. As first mover, Bundu selected its application area of approximately 1 million acres to be centred around this well.

The US Energy Information Administration (EIA) updated its 2011 report on World Shale Gas Resources in June 2013. The EIA estimates that the Lower Permian Ecca Group shales in the Karoo Basin contain 1,559 Tcf of risked shale gas in-place, with 370 Tcf as the risked, technically recoverable shale gas resource.

To demonstrate the scale of the estimated resource, according to the US Department of Energy, 1 Tcf of natural gas is enough to heat 15 million homes for one year, generate 100 billion kilowatt hours of electricity, or fuel 12 million natural gas-fired vehicles for one year. Significantly, the current EIA estimate excludes the thicker Upper Ecca shales on the basis that they have a lower reported total organic carbon content. These Upper Ecca shales include the Fort Brown shale, from which gas flowed at the Cranemere CR 1/68 well.

The Karoo Basin has become the focus of intense interest in the past few years, following the initial application to explore for shale gas in the basin by Bundu (acquired by CEL in April 2010) in February 2009. A number of major international companies, including Shell, Chevron and Falcon Oil & Gas, are also pursuing exploration rights in the region.

Furthermore, the low economic growth rates and power crisis in South Africa have strongly motivated the government to pursue potential shale gas resources as a catalyst to transform the economy.

As previously noted, Chevron Business Development South Africa Limited (Chevron) has announced an Agreement with Falcon Oil and Gas Ltd to jointly co-operate on unconventional gas opportunities in the Karoo Basin, with the result that Challenger – through its subsidiary, Bundu – is the only junior company with interests in the basin, alongside Shell and Chevron.

Mercury Stetson

The Company is assessing next steps following completion of plugging and abandonment of the well drilled in the permit during 1Q13.

Corporate

Challenger continues to build its corporate profile and relationships in South Africa, and with the Australian Government. Highlights include:

- Attendance at a private dinner with the Australian Minister for Foreign Affairs, Julie Bishop, in Johannesburg, along with key business and community leaders.
- Presentation to the Africa Down Under conference in Perth in September.
- Media interviews, resulting in coverage in both Australia and South Africa.
- Introducing Challenger to the investor community in South Africa via one-on-one meetings and an investor breakfast briefing.
- Participation in the expert panel discussion on shale gas at the Jo'burg Indaba in October.
- Participation in the Coega Shale Gas Forum and the Shell 'Building Petroleum Capability for SA' workshop in Cape Town. The Shale Gas Forum is a regular series of meetings with representatives of development agencies, working together to address capacity issues and to achieve maximum benefit for the region.

- Sponsorship of the “Celebrating Twenty Years of Democracy: Australia’s Contribution to the New South Africa” photographic exhibition, a collaboration between the Australian High Commission and the University of Pretoria.

Post the reporting period, Challenger presented at Proactive Investors investor luncheons in Melbourne and Sydney.

The Annual Report was released to the ASX on 26 September, and the Company’s Annual General Meeting has been announced for 19 November 2015.

Yours faithfully



Robert Willes
Managing Director

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CHALLENGER ENERGY (ASX code: CEL, CELO) is focused on the fast-emerging, world-scale shale gas province in South Africa’s Karoo Basin. The Karoo is strategic, and central to the South African Government’s agenda, given the country’s power crisis and need for economic growth, jobs and infrastructure development. Through its South African subsidiary, Bundu Gas and Oil Exploration Pty Ltd, Challenger was first to recognise this opportunity and to apply for exploration rights in the Karoo - and has since been followed by Shell and Falcon Oil and Gas, which has brought Chevron in as a joint venture partner.

Petroleum Agency SA (<http://www.petroleumagency.com>) promotes exploration for onshore and offshore oil and gas resources and their optimal development on behalf of government. The Agency regulates exploration and production activities, and acts as the custodian of the national petroleum exploration and production database.

Appendix 5B

Mining exploration entity and oil and gas exploration entity quarterly report

Introduced 01/07/96 Origin Appendix 8 Amended 01/07/97, 01/07/98, 30/09/01, 01/06/10, 17/12/10, 01/05/2013

Name of entity

Challenger Energy Limited

ABN

45 123 591 382

Quarter ended ("current quarter")

30 September 2014

Consolidated statement of cash flows

Cash flows related to operating activities	Current quarter \$A'000	Year to date (3 months) \$A'000
1.1 Receipts from product sales and related debtors	-	-
1.2 Payments for (a) exploration & evaluation (b) development (c) production (d) administration	(17) - - (279)	(17) - - (279)
1.3 Dividends received	-	-
1.4 Interest and other items of a similar nature received	4	4
1.5 Interest and other costs of finance paid	-	-
1.6 Income taxes paid	-	-
1.7 Other - rental income	32	32
Net Operating Cash Flows	(260)	(260)
Cash flows related to investing activities		
1.8 Payment for purchases of: (a) prospects (b) equity investments (c) other fixed assets	- - -	- - -
1.9 Proceeds from sale of: (a) prospects (b) equity investments (c) other fixed assets	- - -	- - -
1.10 Loans to other entities	-	-
1.11 Loans repaid by other entities	-	-
1.12 Other (provide details if material)	-	-
Net investing cash flows	-	-
1.13 Total operating and investing cash flows (carried forward)	(260)	(260)

+ See chapter 19 for defined terms.

Appendix 5B

Mining exploration entity and oil and gas exploration entity quarterly report

1.13	Total operating and investing cash flows (brought forward)	(260)	(260)
	Cash flows related to financing activities		
1.14	Proceeds from issues of shares, options, etc.	-	-
1.15	Proceeds from sale of forfeited shares	-	-
1.16	Proceeds from borrowings (refer 2.1 below)	-	-
1.17	Repayment of borrowings	-	-
1.18	Dividends paid	-	-
1.19	Other – costs of equity issues	(18)	(18)
	Net financing cash flows	(18)	(18)
	Net increase (decrease) in cash held	(278)	(278)
1.20	Cash at beginning of quarter/year to date	761	761
1.21	Exchange rate adjustments to item 1.20	2	2
1.22	Cash at end of quarter	485	485

Payments to directors of the entity, associates of the directors, related entities of the entity and associates of the related entities

	Current quarter \$A'000	
1.23	Aggregate amount of payments to the parties included in item 1.2	119
1.24	Aggregate amount of loans to the parties included in item 1.10	-
1.25	Explanation necessary for an understanding of the transactions	
	Directors' fees paid during the quarter.	

Non-cash financing and investing activities

- 2.1 Details of financing and investing transactions which have had a material effect on consolidated assets and liabilities but did not involve cash flows

None.

- 2.2 Details of outlays made by other entities to establish or increase their share in projects in which the reporting entity has an interest

None.

+ See chapter 19 for defined terms.

Financing facilities available

Add notes as necessary for an understanding of the position.

	Amount available \$A'000	Amount used \$A'000
3.1 Loan facilities	-	-
3.2 Credit standby arrangements	-	-

Estimated cash outflows for next quarter

	\$A'000
4.1 Exploration and evaluation	75
4.2 Development	
4.3 Production	
4.4 Administration	250
Total	325

The Company will rely on its existing cash resources and future capital raising to funds its current activities.

The Company will consider raising further funds from the placement of equity securities, including the utilisation of the equity available under Chapter 7 of ASX Listing Rules. The Company will also consider other fund raising alternatives if so required.

In light of the above factors, the Company believes that it will have sufficient cash to fund its activities. The Company expects to have negative cashflows from operations of approximately \$325,000 for the forthcoming quarter. The Company's Board and Management is focused on meeting its current objectives and confirm that it is in compliance with ASX Listing Rules, in particular, Listing Rule 3.1;

Reconciliation of cash

Reconciliation of cash at the end of the quarter (as shown in the consolidated statement of cash flows) to the related items in the accounts is as follows.	Current quarter \$A'000	Previous quarter \$A'000
5.1 Cash on hand and at bank	485	761
5.2 Deposits at call		
5.3 Bank overdraft		
5.4 Other (provide details)		
Total: cash at end of quarter (item 1.22)	485	761

+ See chapter 19 for defined terms.

Appendix 5B

Mining exploration entity and oil and gas exploration entity quarterly report

Changes in interests in mining tenements and petroleum tenements

	Tenement reference and location	Nature of interest (note (2))	Interest at beginning of quarter	Interest at end of quarter
6.1	Interests in mining tenements and petroleum tenements relinquished, reduced or lapsed	-	-	-
6.2	Interests in mining tenements and petroleum tenements acquired or increased	-	-	-

Issued and quoted securities at end of current quarter

Description includes rate of interest and any redemption or conversion rights together with prices and dates.

	Total number	Number quoted	Issue price per security (see note 3) (cents)	Amount paid up per security (see note 3) (cents)
7.1	Preference securities			
7.2	<i>(description)</i> Changes during quarter (a) Increases through issues (b) Decreases through returns of capital, buy-backs, redemptions			
7.3	*Ordinary securities	329,482,541	329,482,541	
7.4	Changes during quarter (a) Increases through issues (b) Decreases through returns of capital, buy-backs			
7.5	*Convertible debt securities			
	<i>(description)</i>			

+ See chapter 19 for defined terms.

Appendix 5B

Mining exploration entity and oil and gas exploration entity quarterly report

7.6	Changes during quarter (a) Increases through issues (b) Decreases through securities matured, converted				
7.7	Options <i>(description and conversion factor)</i>	11,500,000	-	<i>Exercise price</i> 15 cents	<i>Expiry date</i> 20/11/2014
		2,000,000	-	35 cents	01/02/2015
		2,000,000	-	35 cents	28/02/2015
		7,500,000	-	15 cents	20/11/2016
		65,896,502	65,896,502	20 cents	30/06/2016
	Performance Rights			<i>Exercise price</i>	<i>Expiry date</i>
		2,500,000	-	Nil	20/06/2015
		4,000,000	-	Nil	07/04/2016
		8,000,000	-	Nil	07/04/2018
		4,000,000	-	Nil	07/04/2020
7.8	Issued during quarter				
7.9	Exercised during quarter				
7.10	Options expired during quarter				
7.11	Debentures <i>(totals only)</i>				
7.12	Unsecured notes <i>(totals only)</i>				

+ See chapter 19 for defined terms.

Compliance statement

- 1 This statement has been prepared under accounting policies which comply with accounting standards as defined in the Corporations Act or other standards acceptable to ASX (see note 5).
- 2 This statement does give a true and fair view of the matters disclosed.

Sign here:



Managing Director

Date: 28 October 2014

Print name: Robert Willes

Notes

- 1 The quarterly report provides a basis for informing the market how the entity's activities have been financed for the past quarter and the effect on its cash position. An entity wanting to disclose additional information is encouraged to do so, in a note or notes attached to this report.
- 2 The "Nature of interest" (items 6.1 and 6.2) includes options in respect of interests in mining tenements and petroleum tenements acquired, exercised or lapsed during the reporting period. If the entity is involved in a joint venture agreement and there are conditions precedent which will change its percentage interest in a mining tenement or petroleum tenement, it should disclose the change of percentage interest and conditions precedent in the list required for items 6.1 and 6.2.
- 3 **Issued and quoted securities** The issue price and amount paid up is not required in items 7.1 and 7.3 for fully paid securities.
- 4 The definitions in, and provisions of, *AASB 6: Exploration for and Evaluation of Mineral Resources* and *AASB 107: Statement of Cash Flows* apply to this report.
- 5 **Accounting Standards** ASX will accept, for example, the use of International Financial Reporting Standards for foreign entities. If the standards used do not address a topic, the Australian standard on that topic (if any) must be complied with.

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CHALLENGER ENERGY LIMITED
SCHEDULE OF OIL AND GAS INTERESTS
AS AT 30 SEPTEMBER 2014

Cranemere Project (South Africa)

<i>Location</i>	<i>Gross Acreage</i>	<i>Working Interest</i>	<i>Status</i>
Karoo Basin	1,040,000	95%	Application

Final area is subject to granting of the application.

There has been no change during the quarter. Subsequent to the reporting period, the South African Government advised that it had commenced processing the application.

Mercury Stetson (United States)

<i>Location</i>	<i>Gross Acreage</i>	<i>Working Interest</i>	<i>Status</i>
Grayson County	~8,000	15%	15% earned to date with the ability to earn up to 50%

During the quarter, there has been a reduction of **~18,000** acres due to expiry.