

28 January 2015

Board of Directors:

Michael Fry
(Non-executive Chairman)

Robert Willes
(Managing Director)

William Bloking
(Non-executive Director)

**Issued capital
(as at 31 December, 2014):**

fully paid ordinary shares
(ASX: CEL)

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

11,500,000 unlisted options
and 18,500,000 performance
rights

Substantial holders:

LQ Super 11.76%

Mr & Mrs Brown 7.34%

Registered office:

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QUARTERLY ACTIVITIES REPORT FOR THE PERIOD ENDING DECEMBER 31 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**
 - **Bundu commences stakeholder consultation**
 - **Minister of Mineral Resources makes recommendations on MPRDA Bill to President Zuma – MPRDA referred back to National Assembly post the reporting period**
- **Farm-out discussions continue pending grant of exploration right**

Corporate

- **Capital raise completed to raise approximately \$1.2 million before associated costs.**

South Africa

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

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

This represents a major breakthrough for Challenger and Bundu, and the other companies pursuing acreage in the Karoo as the processing of applications for shale gas Exploration Rights in South Africa had been on hold since 2011.

It is a clear indication that the South African Government is ready to move ahead with the appraisal of the Karoo shales to see whether they offer a solution to the rapidly worsening energy crisis that continues to hinder the country's economic development.

As part of the procedure for progressing the application, PASA asked that Bundu review and update the Environmental Management Programme ("EMPr") submitted when its application was originally made in 2010 and also to engage in further stakeholder consultation. The EMPr update and the stakeholder consultation process are to be completed by 27 February 2015, and effectively set the regulatory machine in motion. Golder Associates, an independent environmental consultancy engaged by Bundu, has completed the update of the EMPr and has begun notifying and consulting with interested and affected parties in respect of the revised document.

The new EMPr describes a revised work programme that includes only seismic studies and drilling, the assessment of potential positive and negative impacts related to these activities and proposed mitigation measures to manage potential negative impacts. This is in line with the moratorium on further applications imposed in February this year. The moratorium excluded from its ambit existing Exploration Right applications, subject to the proviso that no hydraulic fracturing will be permitted until such time as the proposed Technical Regulations for Petroleum Exploration and Exploitation (the "Technical Regulations") have been published under the Mineral and Petroleum Resources Development Act, 28 of 2002 ("MPRDA"). This is a measured approach to shale gas exploration, which we fully endorse. We expect that the Technical Regulations will be finalised in the coming months.

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 Ramathodi 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".

We reported on “Operation Phakisa” (or “Hurry Up”) in the last Quarterly Report. This is a Government initiative 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 as predicted in the last Quarterly Report, it has been announced post the reporting period that the MPRDA has been referred back to the National Assembly. Our expectations are that this will be positive for the oil and gas industry.

The economic rationale for the South African Government to pursue the development of a shale gas industry continues to grow, with recent major electricity outages by state-owned utility Eskom. With the prospect of these continuing for some time, pressure on the economy is likely to increase and public concern to rise.

Against this backdrop, Challenger continues its discussions with prospective farm-in partners and we will continue to keep shareholders updated and informed as and when there is material progress.

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 390 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

The Company completed a private placement to raise approximately \$1.2 million before associated costs in late November. The placement comprised 20 million new fully paid ordinary shares issued at 6 cents (\$0.06) per share. The shares were placed with sophisticated investors, the majority of whom were existing shareholders in the company. This represents a strong vote of confidence in the Company, removes funding uncertainty and allows Challenger and Bundu to focus on moving forward with stakeholder consultation and the Exploration Right application process. The attached Appendix 5B reflects a higher run rate for the first quarter of 2015 as a result of activities connected with updating of the EMPr and the associated stakeholder consultation process.

Challenger continues to build its corporate profile and relationships in South Africa. Highlights include:

- 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.
- Presentation to the Investec Oil & Gas Conference in Cape Town in November.
- 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.

Challenger also presented at Proactive Investors investor luncheons in Melbourne and Sydney in October.

The Annual General Meeting was held on 19 November 2015. All resolutions were passed by the requisite majority.

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")

31 December 2014

Consolidated statement of cash flows

	Current quarter \$A'000	Year to date (6 months) \$A'000
Cash flows related to operating activities		
1.1 Receipts from product sales and related debtors	-	-
1.2 Payments for (a) exploration & evaluation (b) development (c) production (d) administration	(75) - - (266)	(92) - - (545)
1.3 Dividends received	-	-
1.4 Interest and other items of a similar nature received	2	6
1.5 Interest and other costs of finance paid	-	-
1.6 Income taxes paid	-	-
1.7 Other - rental income	26	58
Net Operating Cash Flows	(313)	(573)
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)	(313)	(573)

+ 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)	(313)	(573)
	Cash flows related to financing activities		
1.14	Proceeds from issues of shares, options, etc.	1,212	1,212
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	(73)	(91)
	Net financing cash flows	1,139	1,121
	Net increase (decrease) in cash held	826	548
1.20	Cash at beginning of quarter/year to date	485	761
1.21	Exchange rate adjustments to item 1.20	2	4
1.22	Cash at end of quarter	1,313	1,313

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	156
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 and short term incentive bonus 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	145
4.2 Development	
4.3 Production	
4.4 Administration	325
Total	470

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	1,313	485
5.2 Deposits at call		
5.3 Bank overdraft		
5.4 Other (provide details)		
Total: cash at end of quarter (item 1.22)	1,313	485

+ 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			
	<i>(description)</i>			
7.2	Changes during quarter			
	(a) Increases through issues			
	(b) Decreases through returns of capital, buy-backs, redemptions			
7.3	+Ordinary securities	350,643,655	350,643,655	
7.4	Changes during quarter			
	(a) Increases through issues	20,200,000	20,200,000	6.0
		666,667	666,667	nil
		294,447	294,447	7.5
	(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 (description and conversion factor)	2,000,000 2,000,000 7,500,000 65,896,502	- - - 65,896,502	<i>Exercise price</i> 35 cents 35 cents 15 cents 20 cents	<i>Expiry date</i> 01/02/2015 28/02/2015 20/11/2016 30/06/2016
	Performance Rights	2,500,000 4,000,000 8,000,000 4,000,000	- - - -	<i>Exercise price</i> Nil Nil Nil Nil	<i>Expiry date</i> 20/06/2015 07/04/2016 07/04/2018 07/04/2020
7.8	Issued during quarter				
7.9	Exercised during quarter				
7.10	Options expired during quarter	11,500,000	-	15 cents	20/11/2014
7.11	Debentures (totals only)				
7.12	Unsecured notes (totals only)				

+ 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 January 2015

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 Challenger Energy Limited's South African subsidiary, Bundu Gas and Oil Exploration (Pty) Ltd (Bundu) has been requested by the Petroleum Agency SA (PASA) to update the Environmental Management Programme (EMPr) previously submitted in October 2010 in support of its application for an exploration right in the Karoo. The updated EMPr is to be submitted to PASA on or before Friday, 27 February 2015. The "Estimated cash outflows for next quarter" reflects a higher run rate for the first quarter of 2015 as a result of activities connected with updating of the Environmental Management Programme (EMPr) and the associated stakeholder consultation process.
- 3 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.
- 4 **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.
- 5 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.

+ See chapter 19 for defined terms.

- 6 **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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