Challenger Energy Ltd

ASX:CEL
ASX:CELO
www.challengerenergy.com.au

30th Oct 2015

Board of Directors:

Michael Fry
(Non-executive Chairman

Robert Willes
(Managing Director)

William Bloking
(Non-executive Director)

Issued capital (as at 30 September, 2015):

352,025,933 fully paid ordinary shares (ASX: CEL)

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

26,00,000 unlisted options and rights

Substantial holders:

LQ Super	11.72%
W&M Brown	7.32%

Registered office:

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QUARTERLY ACTIVITIES REPORT FOR THE PERIOD ENDING 30 SEPTEMBER 2015

HIGHLIGHTS

- **Positive industry engagement with government on key legislation - MPRDA Amendment Bill anticipated to go to Parliament soon.**
- **President Zuma states *"We will soon be issuing licences for the exploration of shale gas drilling through hydraulic fracturing."***
- **McKinsey report identifies natural gas as one of the "Big Five" opportunities that can reignite South Africa's progress.**
- **Energy Minister Tina Joemat-Pettersson highlights importance of gas in South Africa's future energy mix at inaugural South Africa Gas Options Conference, stating that gas will be a cornerstone of base load power generation.**
- **ANC National General Council identifies ongoing power crisis as one of the "specific domestic weaknesses" in the economy undermining growth, investment and confidence, emphasises role of gas and affirms role of Independent Power Producers ("IPPs") to be expanded beyond renewables to include gas.**
- **Mid-term budget highlights pressure from deteriorating economic outlook, growth forecasts downgraded due to electricity supply constraints, lower commodity prices and lower confidence levels.**
- **Farm-out discussions continue pending grant of exploration right.**

South Africa

As previously reported, the petroleum industry has continued to engage with Government throughout the year to deliver constructive solutions for the legislative framework (the Mineral and Petroleum Resources Development Act, 28 of 2002 - "MPRDA"). Linked to Operation Phakisa (a government programme aimed at fast-tracking the implementation of solutions on critical development issues, particularly oil and gas) the Minister of Mineral Resources established a bilateral process between the Department of Mineral Resources ("DMR") and the industry associations, the Offshore Petroleum Association of South Africa ("OPASA") and the Onshore Petroleum Association of South Africa ("ONPASA"). These bilateral engagements took into account the frontier nature of South Africa's petroleum industry, along with the imperative to achieve the national development goals as outlined in the National Development Plan and related government policies. The engagements have been constructive and productive, with convergence on key principles and a clear desire on the part of government to move the process forward. Consequently we anticipate that a mutually acceptable revision to the MPRDA will be proposed to Parliament soon – potentially in late 2015 or early 2016.

Also as previously reported, Bundu updated its application to reflect the amended work programme. At the request of the regulator (Petroleum Agency SA – "PASA"), Bundu has excluded protected areas, revising the application area to approximately 870,449 acres.

In August, President Zuma stated at the presentation of credentials by new Heads of Mission accredited to South Africa that

> *"We will soon be issuing licences for the exploration of shale gas drilling through hydraulic fracturing..."*

On 22 September, President Zuma announced a cabinet reshuffle, moving Mineral Resources Minister Ngoako Ramatlhodi to the Public Service and Administration portfolio and appointing Mosebenzi Zwane to Mineral Resources. OPASA has had a positive meeting with the new minister, and at the time of writing ONPASA is also seeking a meeting. Our interface with the regulator indicates that the processing of the exploration rights applications is continuing. We understand that this is moving forward and expect that these should be determined either in late 2015 or early 2016.

In September, the McKinsey Global Institute report *"South Africa's Big Five: Bold Priorities for Inclusive Growth"* was released, identifying the *"five bold opportunities that can reignite South Africa's progress"* and which could increase GDP growth by 1.1 percentage points per year, adding one trillion rand ($87 billion) to annual GDP by 2030 and creating 3.4 million new jobs. McKinsey cites natural gas amongst the big five, stating;

> *"South Africa's electricity shortage has constrained growth, and despite new capacity, another shortfall is projected between 2025 and 2030. Natural gas plants - which are fast to build, entail low capital costs, and have a low carbon footprint - can provide an alternative to diversify the power supply. With the necessary regulatory certainty, we estimate that South Africa could install up to 20GW of gas-fired power plants to diversify base-load capacity by 2030. Gas can be provided through imports, local shale gas resources (if proven), or both."*

In late September the inaugural South Africa Gas Options Conference was held in Cape Town, attracting significant interest and widely reported commentary from Energy Minister Tina Joemat-Pettersson with regard to the importance of gas in South Africa's future energy mix.

Minister Joemat-Pettersson reportedly likened South Africa to a *"junkie"* addicted to coal and diesel, and stressed that gas will be the cornerstone of the country's base load power.

> *"Our coal and diesel dependence has to decrease,"* and *"I need base load electricity, and gas will be a cornerstone of base load,"*

South Africa has already benefitted from a successful renewable energy IPP programme, with approximately 3.9 GW contracted and around 1.8 GW capacity connected to the national grid by 31 March 2015. The Department of Energy ("DOE") is preparing to release the request for proposals for 3.13 GW of gas-fired generation capacity between 2019 and 2025 before the end of the year. The minister stated that it was vital for South Africa to change its energy mix, noting that the target for gas-fired power generation from 2019 to 2025 to widen South Africa's electricity base could be increased. A total of 150 companies submitted responses under the DOE's request for information for the design of its gas-to-power programme, which closed on 20 July. The ministry had a "number of very good proposals", she said.

> *"I'm not obsessed with nuclear energy, it is only one source of base load. I am obsessed with gas, by the way. For base load and/or mid-merit energy generation, capacity needed from gas-fired power generation is there and is necessary to contribute towards energy security,"* and *"Our key challenge is how to bring [about] the benefits of natural gas as an energy source as early as possible,"*

The government would play a significant role in developing timely, reliable and affordable electricity, while investment was encouraged in exploration and the development of natural gas resources, the minister said.

> *"The opportunities from the successful development of gas resources are large in scale, but our long-term challenge is to successfully move towards that potential, while also addressing the short-term necessities of our country."*

Minister Joematt-Pettersson said Operation Phakisa would help to speed up the process.

> *"This inaugural conference for gas options is strategically important, because it comes at a time when we are updating our National Development Plan. We are defining the energy mix for South Africa and the Southern African power pool."*

Post the reporting period, in October the governing African National Congress ("ANC") held its National General Council ("NGC"). Held midway between party conferences, the NGC is convened to discuss and debate the "strategic organisational and political issues facing the movement."

Delegates to the NGC were reported to have agreed that priority should be given to making clear decisions on future base load power investments, so as to avoid economically debilitating supply instability medium- to long-term. The ongoing power crisis was stated to be one of the "specific domestic weaknesses" in the economy undermining growth, investment and confidence.

The expanded role of IPPs was affirmed, together with the desirability of extending the success of the renewables procurement programme to technologies such as coal and gas.

The ANC also emphasised the role of gas in South Africa's future energy mix, arguing gas, including shale gas, could be a "game changer" for the South African economy.

These positive developments take place against a background of continuing economic pressure.

On 21 October, Finance Minister Nhlanhla Nene presented his medium-term budget policy statement speech making the point that without economic growth, there is no revenue growth, and without revenue growth, expenditure cannot increase and the nation cannot develop and succeed. Meantime the economic outlook has deteriorated such that the Treasury now expects growth of just 1.5% for this year and 1.7% for the next as compared to February's economic growth expectations of 2% for 2015 and 2.4% for 2016.

Electricity supply constraints, falling commodity prices and lower confidence levels have resulted in South Africa's growth forecasts being revised lower, Nene said.

Whilst it is difficult to provide precise guidance on the timing of the application determination process, momentum continues to build, as does the economic and political pressure to resolve the power crisis and grow the economy. The potential of natural gas to address these issues is increasingly appreciated and promoted, and the foundations for gas in South Africa's future energy mix are clearly being laid. As described above, Challenger anticipates that there will soon be positive developments with regard to key legislation and progression of the application process in either late 2015 or early 2016.

In the meantime, 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.

Corporate

Whilst working to progress the licence application, management continues to focus on cost reduction, and this is reflected in the reduced burn rate forecast for the coming quarter.

Background

The Karoo Basin, which extends across 600,000 km^2 is located in central and southern South Africa and contains organic rich shales of Permian age with combined thickness up to 5,000 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 CR1/68 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 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.

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.petroleumagencysa.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.*

Rule 5.5

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	Quarter ended ("current quarter")
45 123 591 382	30 September 2015

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	(103)	(103)
	(b) development	-	-
	(c) production	-	-
	(d) administration	(227)	(227)
1.3	Dividends received	-	-
1.4	Interest and other items of a similar nature received	2	2
1.5	Interest and other costs of finance paid	-	-
1.6	Income taxes paid	-	-
1.7	Other – VAT refund	16	16
	Net Operating Cash Flows	(312)	(312)
	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	-	-
	Net investing cash flows	-	-
1.13	Total operating and investing cash flows (carried forward)	(312)	(312)

+ See chapter 19 for defined terms.

1.13	Total operating and investing cash flows (brought forward)	(312)	(312)
	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	(2)	(2)
	Net financing cash flows	(2)	(2)
	Net increase (decrease) in cash held	(314)	(314)
1.20	Cash at beginning of quarter/year to date	714	714
1.21	Exchange rate adjustments to item 1.20	1	1
1.22	**Cash at end of quarter**	401	401

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	-
1.24	Aggregate amount of loans to the parties included in item 1.10	-

1.25 Explanation necessary for an understanding of the transactions

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

Shares were issued in lieu of a cash payment of $18,881 for consultancy services provided by WES Capital Pte Ltd.

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.

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	80
4.2	Development	
4.3	Production	
4.4	Administration	110
	Total	**190**

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	401	715
5.2	Deposits at call		
5.3	Bank overdraft		
5.4	Other (provide details)		
	Total: cash at end of quarter (item 1.22)	401	715

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		Refer to the attached schedule on page 7.		
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** *(description)*				
7.2	Changes during quarter (a) Increases through issues (b) Decreases through returns of capital, buy-backs, redemptions				
7.3	**+Ordinary securities**	352,025,933	352,025,933		
7.4	Changes during quarter (a) Increases through issues (b) Decreases through returns of capital, buy-backs	330,570	330,570	5.7	5.7
7.5	**+Convertible debt securities** *(description)*				

7.6	Changes during quarter (a) Increases through issues (b) Decreases through securities matured, converted				
7.7	**Options** *(description and conversion factor)*	 7,500,000 65,896,502	 - 65,896,502	*Exercise price* 15 cents 20 cents	*Expiry date* 20/11/2016 30/06/2016
	Performance Rights	 2,500,000 4,000,000 8,000,000 4,000,000	 - - - -	*Exercise price* Nil Nil Nil Nil	*Expiry date* 30/06/2016 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				
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: Date: 30 October 2015
Managing Director

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 2015

Cranemere Project (South Africa)

Location	*Gross Acreage*	*Working Interest*	*Status*
Karoo Basin	**870,449**	**95%**	**Application**

Final area is subject to granting of the application. Application amended at the regulator's request from 1,040,000 acres to exclude protected areas.

Mercury Stetson (United States)

Location	*Gross Acreage*	*Working Interest*	*Status*
Grayson County	**~3,152**	**15%**	**15% earned to date with the ability to earn up to 50%**

A total of 3,018.37 acres expired during the quarter (opening balance of ~6,170 acres).
A further 778.12 acres have expired as at the date of this report.

+ See chapter 19 for defined terms.