

29 Apr 2016

**Board of Directors:**

Michael Fry  
(Non-executive Chairman)

Robert Willes  
(Managing Director)

William Bloking  
(Non-executive Director)

**Issued capital:**

384,793,851 fully paid  
ordinary shares (ASX: CEL)

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

57,000,000 unlisted options  
and rights

**Substantial holders:**

LQ Super 11.28%

W&M Brown 7.56%

**Registered office:**

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VICTORIA 3000  
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## QUARTERLY ACTIVITIES REPORT FOR THE PERIOD ENDING 31 MARCH 2016

### HIGHLIGHTS

- **Positive industry engagement with government on key legislation – progress on MPRDA Amendment Bill and licence application process anticipated soon.**
- **Minister of Mineral Resources, Mosebenzi Zwane, addresses community gathering in the Karoo, states that “...government, based on the balance of available scientific evidence, took a decision to proceed with the development of shale gas in the Karoo formation of South Africa”**
- **Minister of Finance, Pravin Gordhan, states in February 2016 Budget speech that “Building on the success of our Renewable Energy initiatives, the Independent Power Producers Programme will be extended to include coal and gas power projects over the period ahead. “**
- **Power tariff to rise by 9.4% for 2016/17 after regulator allows state power utility Eskom a partial claw back of R22.8 billion of costs it applied for (primarily related to diesel consumption and reduced revenue).**
- **South African media reports that the regulator expects to make its recommendations to the Minister of Mineral Resources on the first two shale gas exploration rights applications, including Bundu’s, by early May.**
- **Capital raise completed to raise \$900,000 before associated costs.**

### **Legislative Framework**

As previously reported, the petroleum industry (via the industry associations, the Offshore Petroleum Association of South Africa (“OPASA”) and the Onshore Petroleum Association of South Africa (“ONPASA”) have engaged with government 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), these 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. The expectation is that the legislative process to reconsider the 2013 MPRDA Amendment Bill will be finalised in the near future.

The South African Shadow Minister of Mineral Resources, James Lorimer, who represents his party on the parliamentary portfolio committee on mineral resources, has referred to this matter in recent South African media reporting. Mr Lorimer comments on his expectations of the outcomes of revision of the MPRDA for South Africa’s oil and gas industry, including the nascent shale gas sector.

He is reported as saying that the bill is likely to re-emerge on the parliamentary agenda and that the concerns of the oil and gas industry have been largely addressed in the new version, with agreement on the wording of the paragraphs that will govern state participation. He is quoted as saying:

*"The 20% free carried interest will go, for example and there will still be a state interest but it will be a more subdued formulation" and*

*"Exploration and production costs will be covered before the state starts taking its 20% share in profits. This is much more regular across the world and more acceptable."*

### **Role of gas in South Africa’s energy mix**

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.

In his Budget Speech on 24 February 2016, Finance Minister Pravin Gordhan commented that

*“Building on the success of our Renewable Energy initiatives, the Independent Power Producers Programme will be extended to include coal and gas power projects over the period ahead. “*

and

*“About ZAR17.6 billion will be spent on the Integrated National Electrification Programme between 2016/17 and 2018/19 to provide 840 000 households with access to on-grid electricity,..”*

### **South African Economy**

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

Then Finance Minister Nhlanhla Nene presented his medium-term budget policy statement speech in October 2015, 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. The Treasury reduced its growth expectations for 2015 and 2016 with Nene saying that this was the result of electricity supply constraints, falling commodity prices and lower confidence levels.

Finance Minister Pravin Gordhan quoted Nene in his February 2016 Budget Speech, noting the need for greater certainty in respect of policies that affect investment decisions. He listed policy uncertainty, electricity supply constraints and regulatory barriers to investment as being reflected in the low economic growth outlook stating that

*“We are responding to appeals from the business sector for greater certainty in respect of policies that affect investment decisions.” and “Regulatory challenges that affect mining investment and employment are being addressed.”*

The financial pressure on state power utility Eskom has also continued. Following public hearings, the National Energy Regulator of South Africa (NERSA) announced on 1 March 2016 that it has granted Eskom an additional electricity tariff increase to claw back approximately R11.2 billion of the approximately R22.8-billion of costs it had sought to recoup (including diesel expenses and a revenue variance owing to lower than anticipated demand during the period).

NERSA has decided that the average tariff for standard tariff customers will be increased by 9.4% for the 2016/17 financial year. This follows a prior grant to Eskom that was reported to have resulted in an increase of 12.69% in 2015/16. NERSA also instructed Eskom to make a new multiyear price determination (MYPD4) application within three months, based on revised assumptions and forecasts that reflect the recent circumstances.

### **Exploration Rights Application**

In January 2016, Minister of Mineral Resources Mosebenzi Zwane gave an address at a community Imbizo (or gathering) on shale gas development at Cradock in the Karoo. He stated that

*“The government, based on the balance of available scientific evidence, took a decision to proceed with the development of shale gas in the Karoo formation of South Africa”*

and

*“Currently South Africa is a net importer of energy sources such as crude oil, refined petroleum products and natural gas. It is estimated that the Karoo shale gas resources would mean South Africa has the 5th largest reserves, estimated at 485 trillion cubic feet (Tcf). We however take a conservative view of a 30 Tcf economically recoverable resource, which is equivalent to 30 times the size of the Mossgas plants.”*

*“Ladies and gentlemen, the other potential economic benefits of shale gas include business development within communities, including establishment of black industrialists, employment, specialised skills development and youth development. “*

*“It is my firm belief that the excitement we have about the discovery of this resource needs to be shared and also enjoyed by communities. In this regard my department has devised a promotional programme through which the public and especially communities that are close to the proposed development are educated and informed about these developments. This will ensure that communities are kept up to date about the exploration method and benefits that can be realised from the exploitation of shale gas and informed about the mechanisms and instruments that seek to augment existing laws for the protection of water resources and for the protection of the environment.”*

Post the reporting period, during his address to the National Assembly on the occasion of the Budget Vote (on 19 April), the Minister further stated that

*“We are delighted with the state of South Africa’s petroleum exploration potential with frontier basins both onshore and offshore. This potential includes oil and gas. We have also noted the concerns of some members of the community on the potential impact of shale gas extraction on both the environment and water. We have accordingly taken measures to mitigate the risks inherent in the future.”*

Challenger also notes recent reports in the South African media indicating that the regulator, Petroleum Agency SA (“PASA”), expects to make its recommendations to the Minister of Mineral Resources on the first two of five shale gas exploration license applications by early May.

The acting chief executive of PASA, Lindiwe Mekwe, is reported to have told Reuters that the two license applications the agency was making recommendations on were those submitted by Falcon Oil and Gas and Bundu Gas and Oil Exploration (Challenger’s South African subsidiary and applicant for the exploration right).

Challenger understands that the final decision on granting exploration rights will be made by the Minister of Mineral Resources once PASA has made its recommendations.

In the meantime, Challenger continues to seek to progress farm-in arrangements and we will continue to keep shareholders updated and informed as and when there is material progress.

### **Mountain Zebra and Camdeboo Protected Environment**

As previously reported, the South African Department of Environmental Affairs (“DEA”) published notices in December 2014 inviting comment on proposals to incorporate additional land into the Mountain Zebra National Park and to declare portions of land as the Mountain Zebra and Camdeboo Protected Environment. Some of these proposed additional portions fall within Bundu’s application area. Bundu accordingly lodged a submission requesting that the Minister for Mineral Resources be consulted in the manner required by the National Environmental Management: Protected Areas Act. The DEA has recently confirmed that it has consulted the Department of Mineral Resources, and that the final regulations to be published in respect of the Mountain Zebra and Camdeboo Protected Environment have been amended by deleting the references to restriction of Mining Activities and Hydraulic Fracturing. The DEA advises that it will now proceed with the declaration of the Mountain Zebra and Camdeboo Protected Environment. The portions falling inside Bundu’s application area total approximately 70,800 hectares, representing some 20% of Bundu’s revised application area. Bundu understands that development will therefore not be precluded within the Protected Area or the buffer zone of 5km that will surround each protected area, but the declaration may have the effect of lowering thresholds of activity for permitting purposes (ie a lower level of a given activity may trigger the need for a permit). Bundu’s updated Environmental Management Programme as submitted to the regulator in February 2015 is available via a link on the Company’s website and contains maps showing the location of existing protected areas, together with those portions of land that are proposed for inclusion in the new Protected Environment. These maps show that the majority of the protected areas and buffer zone that would result from such a declaration are covered by existing Critical Biodiversity Areas<sup>1</sup> where lower permitting thresholds may already apply.

Additional land units were incorporated into the Mountain Zebra National Park during 2015. These land units represent approximately 1% of Bundu’s application area. Bundu will be precluded from conducting any operations within this area.

### **Corporate**

In March, the Company raised \$900,000 before associated costs via a private placement to sophisticated investors, the majority of whom are existing shareholders of the Company. This raising will fund the progression of the licence application process in South Africa, working capital and the cost of the offer. It is a further strong vote of confidence in Challenger and the shale gas potential within its Karoo Basin acreage application.

This capital raising was undertaken via the placement of 30 million new fully paid ordinary shares at an issue price of 3 cents (\$0.03) per share with an unlisted attaching option

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<sup>1</sup> *Critical Biodiversity Areas (“CBAs”) are not legislated but are planning instruments developed to guide decision-making. The Department of Economic Development and Environment Affairs together with the Department of Water Affairs have collaborated to draw up the Eastern Cape Biodiversity Conservation Plan (ECBCP). The ECBCP addresses the need to identify and map CBAs and priorities for conservation in the Province.*

for each share subscribed for, exercisable at a price of 5 cents (\$0.05) each on or before June 30, 2020.

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

### **Background**

The Karoo Basin, which extends across 600,000 km<sup>2</sup>, 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 on 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.

# 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 March 2016

### Consolidated statement of cash flows

Cash flows related to operating activities	Current quarter \$A'000	Year to date (9 months) \$A'000
1.1 Receipts from product sales and related debtors	-	-
1.2 Payments for (a) exploration & evaluation	-	(103)
(b) development	-	-
(c) production	-	-
(d) administration	(37)	(392)
1.3 Dividends received	-	-
1.4 Interest and other items of a similar nature received	1	4
1.5 Interest and other costs of finance paid	-	-
1.6 Income taxes paid	-	-
1.7 Other – VAT refund	-	28
<b>Net Operating Cash Flows</b>	<b>(36)</b>	<b>(463)</b>
<b>Cash flows related to investing activities</b>		
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	-	-
<b>Net investing cash flows</b>	<b>-</b>	<b>-</b>
1.13 Total operating and investing cash flows (carried forward)	<b>(36)</b>	<b>(463)</b>

+ 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)	(36)	(463)
	<b>Cash flows related to financing activities</b>		
1.14	Proceeds from issues of shares, options, etc.	900	900
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)
	<b>Net financing cash flows</b>	900	898
	<b>Net increase (decrease) in cash held</b>	864	435
1.20	Cash at beginning of quarter/year to date	283	714
1.21	Exchange rate adjustments to item 1.20	(1)	(3)
1.22	<b>Cash at end of quarter</b>	1,146	1,146

### 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

2,767,918 shares and 1,000,000 options were issued in settlement of \$96,927 in fees, services and associated accruals.

- 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	
4.2 Development	
4.3 Production	
4.4 Administration	320
<b>Total</b>	<b>320</b>

### 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	1,146	283
5.2 Deposits at call		
5.3 Bank overdraft		
5.4 Other (provide details)		
<b>Total: cash at end of quarter (item 1.22)</b>	<b>1,146</b>	<b>283</b>

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+ 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	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	<b>Preference securities</b> (description)			
7.2	Changes during quarter (a) Increases through issues (b) Decreases through returns of capital, buy-backs, redemptions			
7.3	<b>+Ordinary securities</b>	384,793,851	384,793,851	
7.4	Changes during quarter (a) Increases through issues  (b) Decreases through returns of capital, buy-backs	2,767,918 30,000,000	2,767,918 30,000,000	3.5 3.0
7.5	<b>+Convertible debt securities</b> (description)			

+ 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	<b>Options</b> (description and conversion factor)	7,500,000 65,896,502 31,000,000	- 65,896,502 -	<i>Exercise price</i> 15 cents 20 cents 5 cents	<i>Expiry date</i> 20/11/2016 30/06/2016 30/06/2020
	<b>Performance Rights</b>	2,500,000 4,000,000 8,000,000 4,000,000	- - - -	<i>Exercise price</i> Nil Nil Nil Nil	<i>Expiry date</i> 30/06/2016 07/04/2016 07/04/2018 07/04/2020
7.8	Issued during quarter - Options	31,000,000	-	5 cents	30/06/2020
7.9	Exercised during quarter				
7.10	Options expired during quarter				
7.11	<b>Debentures</b> (totals only)				
7.12	<b>Unsecured notes</b> (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: 29 April 2016

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 31 MARCH 2016**

*Cranemere Project (South Africa)*

<i>Location</i>	<i>Gross Acreage</i>	<i>Working Interest</i>	<i>Status</i>
<b>Karoo Basin</b>	<b>870,449</b>	<b>95%</b>	<b>Application</b>
Final area is subject to granting of the application.			

*Mercury Stetson (United States)*

<i>Location</i>	<i>Gross Acreage</i>	<i>Working Interest</i>	<i>Status</i>
<b>Grayson County</b>	<b>1729</b>	<b>15%</b>	<b>15% earned to date with the ability to earn up to 50%</b>

~258 acres expired during the quarter.