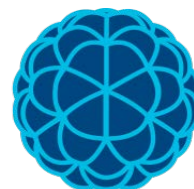




QUARTERLY REPORT

FOR THE PERIOD ENDED
30 JUNE 2016



carbon**energy**

CARBON ENERGY LIMITED

QUARTERLY ACTIVITIES REPORT FOR THE PERIOD ENDED 30 JUNE 2016

ABN 56 057 552 137

ASX Code: CNX OTCQX Code: CNXAY

KEY EVENTS FOR THE QUARTER

- The Company raised \$3.48 million before costs through a renounceable rights issue which closed on 4 April 2016.
- On 18 April 2016 the Queensland government introduced a ban on underground coal gasification (UCG) in Queensland.
- CEO, Morné Engelbrecht, advised the Company that he will not be renewing his contract which expired 17 June 2016. Mr Engelbrecht agreed to extend his contract under the same terms and conditions up until 12 August 2016 to ensure an orderly leadership transition.
- The China University for Mining and Technology International Research Centre for UCG (the Centre) was officially opened on 24 April 2016, with Carbon Energy's Dr Cliff Mallett appointed as Director of the Centre. The Centre has been established to develop the highest standards for China's growing UCG industry.
- A key milestone was announced on 17 June 2016, being the formal registration of the Chinese Joint Venture Company, the Beijing JinHong New Energy Development Joint Venture (JV) by the Chinese corporate registry. Under the JV Agreement, JinHong will contribute US\$30 million towards developing a commercial demonstration project upon the JV meeting certain milestones.
- On 23 June 2016, a Memorandum of Understanding was signed with Photon Energy NV (Photon Energy) to evaluate the development of a large scale solar power generation plant with up to 20 MW capacity at the Company's Bloodwood Creek facility in Queensland. Under the MOU, feasibility of an innovative power storage system on the Bloodwood site will also be assessed.
- On 6 May 2016, the United States District Court for the Northern District of California dismissed the complaint brought against the Company by Summa Resource Holdings LLC without the need for a hearing.
- Grant Thornton Australia have been appointed Company auditors from 28 June 2016, replacing Deloitte Touche Tohmatsu.

SUBSEQUENT TO QUARTER END

- Following 8 years of persistence, hard work and over \$150 million investment in our technology, on 25 July 2016 the Company announced it had received confirmation from the Queensland government Chief Scientist, Dr Geoff Garrett that Carbon Energy has satisfactorily completed the recommendations of the Government appointed Independent Scientific Panel (ISP). This achievement has been our most important priority since we began trials at Bloodwood Creek. Carbon Energy is the only Company to receive this acknowledgement and the ISP process has now been successfully concluded.
- Further to the close of the renounceable rights issue on 4 April 2016, under its Rights Issue Shortfall allocation, on 4 July 2016, the Company issued a further 30,769,232 shares raising \$400,000 before costs.
- Entered into a sub-lease for part of its corporate office premises in Brisbane, which will reduce operating costs going forward.

COMPANY UPDATE

CHINA

JinHong Joint Venture (JV)

During the period the Company laid the foundation for strong growth in China by registering the Beijing JinHong New Energy Development JV .

The registration triggers the initial US\$10 million contribution to the Joint Venture from our Chinese partner, JinHong, of which payment is now due. In addition, JinHong will contribute a further US\$20 million towards developing a commercial Demonstration Project upon the JV meeting certain milestones.

Carbon Energy will provide technical and design services support, supervision and training for all JV projects under the Technical Services Agreement. The achievement of registration in June 2016 triggered the formal signing of Technology Licensing and Technical Services Agreements. The Technology Licencing Agreement was signed in July 2016, with the Technical Services Agreement still to be finalised and signed.

The JV will have a non-exclusive license to use Carbon Energy's keyseam technology up until the successful commissioning of the Demonstration Project but can sub-license keyseam technology in China during the non-exclusive period. The license will become exclusive (within the People's Republic of China) after the successful commissioning of the Demonstration Project.

To date, Carbon Energy and JV partner, JinHong have made progress in advancing the JV. Key priorities remain:

- securing a suitable coal field – more than ten coal fields reviewed to date;
- engaging the in-country engineering, procurement and construction management contractor;
- contracting an in-country drilling company; and
- commencing pre-engineering works once the coal field and engineering, procurement and construction contractor is appointed and a suitable coal field secured by the JV.

The JV remains committed to ensuring the initial project commences as soon as possible.

China UCG Research Centre

The China University for Mining and Technology International Research Centre for UCG (the Centre) was officially opened on 24 April 2016, with Carbon Energy's Dr Cliff Mallett appointed as Director of the Centre. The Centre has been established to encourage the development of UCG technology by industry and Government groups alike, as the environmentally acceptable utilisation method for coal. The Centre will seek to simplify the regulatory process by establishing national and international standards of operation for UCG and formally seek recognition by Government.

The establishment of the Centre is an important step forward in the advancement of Carbon Energy's expansion plans in China. Whilst the Centre is still being established it is currently determining the Centre's physical location on campus, the outline of the research program and conducting assessment of a number of projects suitable for initial trials.

Business Development

Carbon Energy is currently pursuing a number of business development opportunities in Asia, South America, and Australia.

QUEENSLAND

MOU for a large-scale solar energy plant and storage facility at Bloodwood Creek

On 23 June 2016, Carbon Energy announced a MOU with Photon Energy to evaluate the development of a large scale solar power generation plant, up to 20MW as well as investigate the use of the site's existing underground infrastructure to store energy for use during peak energy periods.

This is a positive step for the Bloodwood Creek site and will enable the Company to realise some of the site's potential, while contributing to Queensland and Australia's growing renewable energy needs.

Confirmation of successful completion of the ISP process in QLD

On 25 July 2016 the Company announced that it had received confirmation from the Queensland government Chief Scientist, Dr Geoff Garrett that Carbon Energy has satisfactorily completed the key recommendations of the Government appointed Independent Scientific Panel (ISP) into underground coal gasification (UCG).

Dr Garrett, who led the formal peer review process of the ISP, expressly acknowledges Carbon Energy as the only company to meet the recommendations of the ISP. He also recognises that the Company's successful and innovative keyseam technology is different from that of other technologies employed, stating "it is clear that Carbon Energy has contributed to the collective understanding of UCG and the conditions under which the operation is likely to be both safe and successful."

This acknowledgment from such a senior and well respected Government source is likely to pave the way for expedited commercialisation of the Company's technology in other jurisdictions.

Dr Garrett further confirms that the ISP report and its key recommendations were accepted by the Queensland Department of Natural Resources & Mines (DNRM). Dr Garrett also confirms the Company's actions demonstrating safe and effective decommissioning and completing a plan for rehabilitation were independently reviewed by experts appointed by the Department of Environment and Heritage Protection (DEHP).

The acknowledgement comes after 8 years of trials and over a \$150 million investment, having been the primary aim of Company.

Since the Queensland government announced its decision not to allow UCG projects to proceed in Queensland on the 18 April 2016 the Company has held several meetings with the Government including the Minister of Natural Mines and Resources as well as other senior government officials. Despite acknowledgement of the work Carbon Energy has done to date there have been no changes proposed in regards to the proposed legislation of the ban.

Carbon Energy has done everything in its power to seek amendments to the Government's proposed ban. This has included seeking legal advice from Senior Queens Counsel on the legal options available to the Company.

Environmental sampling of groundwater and measurement of other environmental metrics continues at Bloodwood Creek, following delivery of the Decommissioning Report and Rehabilitation Plan to the Queensland government in FY15.

The Queensland government's letter, issued by the Chief Scientist, is significant for the Company as it officially recognise the success of Carbon Energy's keyseam technology in meeting the rigorous assessment parameters set out by the Queensland Government.

CORPORATE

CASH MANAGEMENT

Subsequent to the End of Financial Year on 4 July 2016, the Company raised a further \$400,000 from 30,769,232 new shares under the Rights Issue Shortfall. The Company's 2016 Income Tax Return has also been lodged with an estimated Research and Development (R&D) rebate of approximately \$1.38 million expected to be paid within the next 30 days.

The Company continues to manage its cash resources prudently as it pursues international and Australian business development opportunities while also progressing the Rehabilitation Plan as outlined in the work plan for the mineral development licence (MDL374), which includes the continuation of the Company's ground water monitoring program.

The Company managed its expenses during the period by:

- the appointment of Grant Thornton as auditor, following a competitive tender process. Ratification of the new auditor is subject to shareholder ratification at the Company's Annual General Meeting.
- Executing a contract to sublease surplus office space at Carbon Energy's Brisbane head office.

CHANGE OF AUDITORS

Carbon Energy appointed new auditors during the Quarter. The Company and Deloitte made a commercial decision that it would be more appropriately serviced by a mid-tier firm than a Big 4 firm. Following a competitive tender process the Board has appointed Grant Thornton Australia. The decision is subject to ratification by shareholders at the next Annual General Meeting.

LEGAL MATTERS - SUMMA SHARE SALE AGREEMENT

On 27 November 2015 the Company advised it had been served with proceedings filed by Summa Resource Holdings LLC (Summa) against it in the United States District Court for the Northern District of California (Complaint).

As announced to the ASX on 6 May 2016, the Court dismissed the Complaint without the need for a hearing.

The Court found that Carbon Energy had sufficiently demonstrated that permitting the action to proceed in the Northern District of California would be unnecessarily burdensome and that the factors considered by the Court weighed in favour of the matter being dismissed on the basis of forum non conveniens. Accordingly, the Court did not need to consider the merits of Carbon Energy's motions to dismiss and strike Summa's claim.

For and on behalf of the Board



Morné Engelbrecht
Managing Director & Chief Executive Officer
29 July 2016

TENEMENT STATUS AT 30 JUNE 2016

Tenement	Status	Area km ²
MDL 374	Granted*	28.68
MLa 50253	Application Pending**	13.43
PFL 6	Renewal Pending***	0.03

* Renewal granted in December 2015 through to 31 January 2018

** Application awaiting Environmental Impact Assessment prior to finalisation and assessment

*** Renewal submitted March 2015

Tenement	Status	Sub-Blocks	Area km ²
EPC 867	Renewal Pending [#]	167	509.35
EPC 868	Renewal Pending [#]	44	134.20
EPC 869	Granted	63	192.15
EPC 1132	Granted	23	70.15
Total Eastern Surat Basin Tenements		297	905.85

Renewal Submitted November 2014

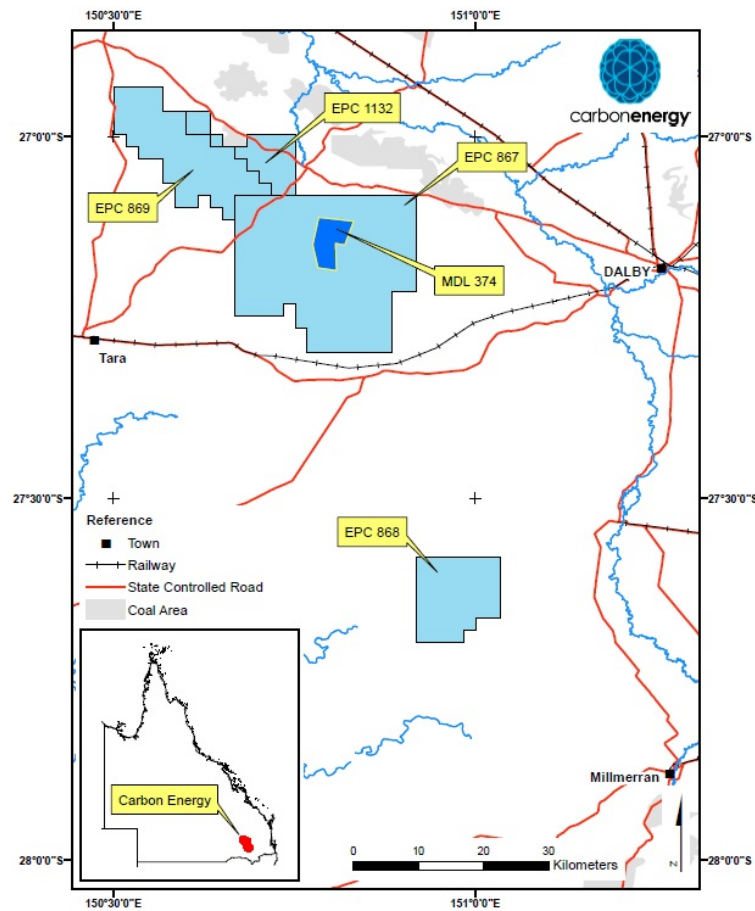


Figure 1 Carbon Energy Coal Tenure Surat Basin

APPENDIX 5B

MINING 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, 01/05/13

Name of entity

CARBON ENERGY LIMITED

ABN

Quarter ended ("current quarter")

56 057 552 137

30 June 2016

CONSOLIDATED STATEMENT OF CASH FLOWS

	Current Quarter	Year to date
	\$A'000	\$A'000
Cash flows related to operating activities		
1.1 Receipts from product sales and related debtors	-	69
1.2 Payments for		
(a) Exploration & Evaluation	(4)	(50)
(b) BWC Site Operating & Maintenance Costs & Technical Services & Rehabilitation Drilling	(408)	(1,973)
(c) Production	-	-
(d) Corporate, Commercial, New Business & Administration	(1,014)	(3,853)
1.3 Dividends received	-	-
1.4 Interest and other items of a similar nature received	6	75
1.5 Interest and other costs of finance paid	-	-
1.6 Income taxes paid	-	-
1.7 Other (provide details if material)	-	2,490
Government grants: Export Market Development Grant		
Net Operating Cash Flows	(1,420)	(3,242)

	Cash flows related to investing activities		
1.8	Payment for purchases of:		
	(a) prospects	-	-
	(b) equity investments	-	-
	(c) other fixed assets	(32)	(42)
1.9	Proceeds from sale of:		
	(a) prospects	-	-
	(b) equity investments	-	-
	(c) other fixed assets	3	3
1.10	Loans to other entities	-	-
1.11	Loans repaid by other entities	-	-
1.12	Other (provide details if material)	(45)	(126)
	Exploration & evaluation costs, trademarks		
	Net investing cash flows	(71)	(165)
1.13	Total operating and investing cash flows	(1,491)	(3,407)
	Cash flows related to financing activities		
1.14	Proceeds from issues of shares and options	3,483	5,406
1.15	Proceeds from sale of forfeited shares	-	-
1.16	Proceeds from short term loan facility	-	-
1.17	Repayment of short term loan facility	-	(1,166)
1.18	Term facility costs	-	(16)
1.19	Capital raising costs	(264)	(297)
	Net financing cash flows	3,219	3,927
	Net (decrease) / increase in cash held	1,725	519
1.20	Cash at beginning of quarter/year to date	483	1,689
1.21	Exchange rate adjustments to item 1.20		-
1.22	Cash at end of quarter	2,208	2,208

Subsequent to the end of the Quarter, the Company received \$0.4m (before expenses) being the Shortfall resulting from its renounceable rights issue which expired on 4 July 2016. Total available cash as at 29 July 2016, including the proceeds from the renounceable rights issue is \$2.4 million; with a further \$1.38 million due to be received for the R&D tax incentive.

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	192
1.24	Aggregate amount of loans to the parties included in item 1.10	-
1.25	Explanation necessary for an understanding of the transactions	
	Costs included in item 1.23 above relate to Directors' salaries, annual leave, fees and superannuation.	

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

Issue of 12,071,070 Ordinary Shares to cover the interest costs, payable 3 months in arrears, in relation to the Facility utilised under the \$10 million Pacific Road Convertible Note Facility Agreement. These shares are issued in accordance with ASX Listing Rule 7.

- 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

N/A

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 (Pac Road Convertible Note Facility)	10,000	10,000
3.2	Credit standby arrangements	344	240

The Pacific Road Convertible Note Facility is secured by a mortgage over the UCG technology and software transferred from CSIRO to Carbon Energy and 100% of the shares in Carbon Energy (Operations) Pty Limited, the subsidiary that owns the UCG technology and software transferred from the CSIRO. This entity also has the rights and obligations regarding the JinHong JV. The Pacific Road Convertible Note Facility is to be repaid on 18 January 2017, less than 12 months from the date of signing the Quarterly Report.

ESTIMATED CASH OUTFLOWS FOR NEXT QUARTER

		\$A'000
4.1	Exploration and evaluation	45
4.2	BWC Site Operating & Maintenance Costs & Technical Services & Rehabilitation Drilling	665
4.3	Production	-
4.4	Corporate, Commercial, New Business & Administration (including financing costs)	1,107
Total		1,817

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	Previous Quarter
		\$A'000	\$A'000
5.1	Cash on hand and at bank	258	332
5.2	Deposits at call	1,950	150
5.3	Bank overdraft	-	-
5.4	Other (provide details)	-	-
Total: cash at end of quarter (Item 1.22)		2,208	482

CHANGES IN INTERESTS IN MINING TENEMENTS

	Tenement reference	Nature of interest (note (2))	Interest at beginning of quarter	Interest at end of quarter
6.1	-	-	-	-
6.2	-	-	-	-

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	1,763,659,050	1,763,659,050		Fully paid
7.4 Changes during quarter				
(a) Increases through issues:	267,904,397	267,904,397	\$0.013	Fully paid
(b) Decreases through returns of capital, buy-backs	-	-	-	-
7.5 +Convertible debt securities (description)	Pacific Road Capital \$10 million Convertible Note Facility issued 5 January 2012 and repayable on 18 January 2017 with 5% interest payable quarterly in arrears in Company shares.			
7.6 Changes during quarter	-	-	-	-
(a) Increases through issues	-	-	-	-
(b) Decreases through securities matured, converted	-	-	-	-
7.7 Options			Exercise Price	Expiry Date
Listed Options \$0.0594	443,696,404	443,696,404	\$0.0594	31/07/2016
Unlisted Options \$0.026	7,081,738	-	\$0.026	15/10/2016
Unlisted Options \$0.1672	7,000,000	-	\$0.1672	18/01/2017
Unlisted Options \$0.1672	28,000,000	-	\$0.1672	25/02/2017
Unlisted Options \$0.0301	9,495,080	-	\$0.0301	25/08/2017
7.8 Issued during quarter	-	-	-	-
7.9 Exercised during quarter	-	-	-	-
7.10 Expired during quarter				
Unlisted Options \$0.0594	33,333,333	-	\$0.0594	30/06/2019
Unlisted Performance Rights	7,500,000	-	NIL	30/06/2019
7.11 Debentures (totals only)	-	-		
7.12 Unsecured notes (totals only)	-	-		

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.
- 2 This statement does give a true and fair view of the matters disclosed.

A handwritten signature in blue ink, appearing to read 'Catherine Costello', is positioned above the 'Sign here:' label.

Sign here:

Date: 29 July 2016

Name: Catherine Costello

Title: Chief Financial Officer & Company Secretary