LODESTONE ENERGY LIMITED
ABN 20 075 877 075

HALF-YEAR REPORT – 31 DECEMBER 2010

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This interim financial report does not include all the notes of the type normally included in an annual financial report. Accordingly, this report is to be read in conjunction with the annual report for the year ended 30 June 2010 and any public announcements made by Lodestone Energy Limited during the interim reporting period in accordance with the continuous disclosure requirements of the Corporations Act 2001.

DIRECTORS' REPORT

Your directors present their report on Lodestone Energy Limited consolidated group (the Group) consisting of Lodestone Energy Limited and the entities it controlled at the end of, or during, the half-year ended 31 December 2010.

Directors
The following persons were directors of Lodestone Energy Limited during the whole of the half-year and up to the date of this report:

G A J Baynton
W R Stubbs
L R Grimstone
G Baker

M Ackland was a director from the beginning of the half-year until his resignation on 8 November 2010.

R Clarke was appointed a director on 2 September 2010 and continues in office at the date of this report.

Review of operations
The loss after income tax of the Group for the half-year was $632,105 (2009: loss $707,061). The loss reflects the nature of the Group's principal activity, being coal, coal seam gas (CSG) and mineral exploration.

The Company completed its merger transaction with Tambo Coal & Gas Pty Limited and Moreton Energy Pty Limited in July 2010, resulting in 100% ownership of each of the Company's coal and gas exploration projects by Lodestone Energy Limited.

During the half-year, an additional ten Exploration Permits for Coal (EPCs) were granted, bringing the total to twenty seven in the Tambo Project area, all of which contain one or more coal targets of interest.

In addition the rights to EPC 2056 (Chinchilla East coal project) were acquired for no consideration from interests associated with Lodestone Director Greg Baynton.

Drilling continued during the December quarter with an initial scout drilling program within EPC 1786 being completed. The programme confirmed strata in this area contained coal seams but were above the main Walloon targets in the Juandah and Taroom Coal Measures.

Ongoing rain, flooding and resulting poor access conditions in the Maranoa region interrupted operations several times and prevented material drilling progress during 2010. The company used this time to conduct further desktop analysis and identification of both coal and petroleum targets within its EPCs and ATP 1020 for upcoming drilling programs.

In September 2010, via its wholly-owned subsidiary, Surat Gas Pty Ltd, Lodestone applied for new ATPs for petroleum exploration pursuant to the Queensland Government's 2010 Petroleum Land Release competitive tender process which closed in September 2010.

Following the Queensland Government's assessment process, Surat Gas was appointed preferred tenderer for three new petroleum tenements (ATPs) 1072, 1095 and 1098 in the Surat/Eromanga Basin. Each of the new ATP areas is either unexplored (or significantly underexplored) for petroleum and gas and all are contiguous with each other and/or Lodestone's existing tenement footprint. These three new ATPs will result in a 310% increase in the Company's petroleum and gas acreage footprint in the Surat/Eromanga Basin. This would result in the Company's acreage portfolio in this region representing one of the largest holdings in the Surat/Eromanga/Galilee region, including approximately 20,500 square kilometres.

The Company also continues to hold its interests in the Chillagoe and Mount Morgan minerals projects. Situated 130km north of the Chillagoe township in North Queensland, the Chillagoe district project is believed to have structural and lithological settings similar to the Mungana and Red Dome gold-copper deposits near Chillagoe. A 10 hole drilling program was conducted during the September quarter, however further assays results and completion of microscope examination of samples are being completed before deciding on future work. Given its focus on energy projects, the Company did not undertake further in-field exploration activities at its Mount Morgan project. Lodestone is considering funding and farm-out options for both of its minerals projects.

Following acquisition of Tambo Coal and Gas Pty Limited and Moreton Energy Pty Limited in July 2010 and the appointment as preferred tenderer for three new petroleum tenements (ATPs) 1072, 1095 and 1098 in the Surat/Eromanga/Galilee Basin, Lodestone is exploring commercial arrangements for future joint ventures, farm-outs, spin-offs and project funding options.

Auditor's independence declaration
The auditor's independence declaration under Section 307C of the Corporations Act 2001 is set out on page 3 of for the half year ended 31 December 2010.

This report is made in accordance with a resolution of the Board of directors and is signed for and on behalf of the directors by:

R Clarke
Chairman

8 March 2011

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DECLARATION OF INDEPENDENCE BY CHRIS SKELTON TO THE DIRECTORS OF LODESTONE ENERGY LIMITED

As lead auditor for the review of Lodestone Energy Limited for the half-year ended 31 December 2010, I declare that to the best of my knowledge and belief, there have been:

- no contraventions of the auditor independence requirements of the Corporations Act 2001 in relation to the review; and
- no contraventions of any applicable code of professional conduct in relation to the review.

This declaration is in respect of Lodestone Energy Limited and the entities it controlled during the period.

BDO Audit (QLD) Pty Ltd

CJ Skelton

Director

Brisbane: 8 March 2011

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CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
FOR THE HALF-YEAR ENDED 31 DECEMBER 2010

	Half-year 2010 $	Half-year 2009 $
Revenue	57,235	36,344
Professional services expenses	(123,452)	(163,072)
Tenement expenditure written off	(37,697)	(19,207)
Impairment of assets	(11,595)	-
Corporate overhead expenses	(376,586)	(294,296)
Depreciation expenses	(5,393)	(5,719)
Directors' remuneration	(128,051)	(128,982)
Share based payments expense	(6,566)	(132,129)
Loss before income tax	(632,105)	(707,061)
Income tax expense	-	-
Net loss for the half-year	(632,105)	(707,061)
Other comprehensive income		
Other comprehensive income for the period, net of tax	-	-
Total comprehensive income / (loss) attributable to the owners of Lodestone Energy Limited	(632,105)	(707,061)

	Cents	Cents
Loss per share for loss attributable to Lodestone Energy Limited:		
Basic earnings per share	(0.1)	(0.4)
Diluted earnings per share	(0.1)	(0.4)

The above consolidated statement of comprehensive income should be read in conjunction with the accompanying notes.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION
AS AT 31 DECEMBER 2010

	Notes	31 December 2010 $	30 June 2010 $
ASSETS			
Current assets			
Cash and cash equivalents		2,206,976	774,058
Receivables		221,566	45,076
Total current assets		2,428,542	819,134
Non-current assets			
Plant and equipment		15,322	22,465
Exploration and evaluation expenditure		43,537,050	41,800,748
Other assets		160,797	123,400
Total non-current assets		43,713,169	41,946,613
Total assets		46,141,711	42,765,747
LIABILITIES			
Current liabilities			
Trade and other payables		181,399	265,896
Total current liabilities		181,399	265,896
Non-current liabilities			
Other financial liabilities	4	3,000,000	3,000,000
Total non-current liabilities		3,000,000	3,000,000
Total liabilities		3,181,399	3,265,896
Net assets		42,960,312	39,499,851
EQUITY			
Issued capital	5	53,111,857	49,025,857
Reserves		822,352	815,786
Accumulated losses		(10,973,897)	(10,341,792)
Total equity		42,960,312	39,499,851

The above consolidated statement of financial position should be read in conjunction with the accompanying notes.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE HALF-YEAR ENDED 31 DECEMBER 2010

	Issued capital $	Accumulated losses $	Share based payments reserve $	Total $
Balance at 1 July 2009	10,425,961	(7,531,803)	549,555	3,443,713
Loss for the period	-	(707,061)	-	(707,061)
Total other comprehensive income	-	-	-	-
Total comprehensive income	-	(707,061)	-	(707,061)
Transactions with owners in their capacity as owners:				
Issue of share capital	1,943,445	-	-	1,943,445
Non-cash share based payments	-	-	132,129	132,129
Sub total	1,943,445	-	132,129	2,075,574
Balance at 31 December 2009	12,369,406	(8,238,864)	681,684	4,812,226
Balance at 1 July 2010	49,025,857	(10,341,792)	815,786	39,499,851
Loss for the period	-	(632,105)	-	(632,105)
Total other comprehensive income	-	-	-	-
Total comprehensive income	-	(632,105)	-	(632,105)
Transactions with owners in their capacity as owners:				
Issue of share capital	4,086,000	-	-	4,086,000
Non-cash share based payments	-	-	6,566	6,566
Sub total	4,086,000	-	6,566	4,092,566
Balance at 31 December 2010	53,111,857	(10,973,897)	822,352	42,960,312

The above consolidated statement of changes in equity should be read in conjunction with the accompanying notes.

CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE HALF-YEAR ENDED 31 DECEMBER 2010

	Half-year	
	2010	**2009**
	$	**$**
Cash flows from operating activities		
Receipts in the course of operations (inclusive of goods and services tax)	140,447	95,288
Payments to suppliers (inclusive of goods and services tax)	(1,009,802)	(821,423)
Interest received	55,118	30,997
Net cash outflow from operating activities	(814,237)	(695,138)
Cash flows from investing activities		
Payments for exploration expenditure	(1,808,948)	(1,817,472)
Payments for plant and equipment	-	(19,884)
Proceeds on sale of plant and equipment	5,000	-
Payment for security deposit	(35,577)	(24,720)
Refund of security deposit	680	-
Net cash outflow from investing activities	(1,838,845)	(1,862,076)
Cash flows from financing activities		
Proceeds from share issue	4,086,000	1,957,000
Payment of share issue costs	-	(13,555)
Proceeds from financial liability	-	2,249,019
Net cash inflow from financing activities	4,086,000	4,192,464
Net increase / (decrease) in cash and cash equivalents	1,432,918	1,635,250
Cash and cash equivalents at the beginning of the half-year	774,058	3,355,688
Cash and cash equivalents at the end of the half-year	2,206,976	4,990,938

The above consolidated statement of cash flows should be read in conjunction with the accompanying notes.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE HALF-YEAR ENDED 31 DECEMBER 2010

Note 1 Summary of significant accounting policies

This general purpose interim financial report for the half-year reporting period ended 31 December 2010 has been prepared in accordance with Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Act 2001*.

The historical cost basis has been used, except for financial instruments which have been measured at fair value.

This interim financial report does not include all the notes of the type normally included in an annual financial report and therefore cannot be expected to provide as full an understanding of the financial performance, financial position and financing and investing activities of the consolidated entity as the full financial statements. Accordingly, this report is to be read in conjunction with the annual report for the year ended 30 June 2010 and any public announcements made by Lodestone Energy Limited during the interim reporting period in accordance with the continuous disclosure requirements of the *Corporations Act 2001*.

The accounting policies and methods of computation adopted are consistent with those of the previous financial year and corresponding interim reporting period.

Critical judgements in applying accounting policies
The accounting policies include the capitalisation of exploration and evaluation expenditure which as at 31 December 2010 amounts to $43,537,050 (30 June 2010: $41,800,748). This represents a significant asset of the Group. Given exploration activities have not yet reached a stage which permits a reasonable assessment of the existence or otherwise of recoverable resources and the difficulty in forecasting cash flows to assess the fair value of this expenditure there is uncertainty as to the recovery of the carrying value of exploration and evaluation expenditure. The ultimate recovery of the carrying value is dependent upon the successful development and commercial exploitation or, alternatively, sale of the interest in the tenements.

Basis of preparation and going concern basis
The financial statements have been prepared on the going concern basis, which contemplates continuity of normal business activities and the realization of assets and liabilities in the normal course of business.

As disclosed in the financial statements, the Group recorded an operating loss of $632,105 (2009: $707,061) and had net cash outflows from operating activities of $814,237 (2009: $695,138) for the half-year ended 31 December 2010.

The group also has expenditure commitments in the next 12 months of $16,357,694 as detailed in Note 6.

The Directors acknowledge that, as in the prior year, to continue the exploration and development of the Group's exploration projects, the budgeted cash flows from operating and investing activities for the future will necessitate further capital raising. In the event that the Group is unable to raise future funding requirements, they may be required to realise their assets at amounts different to those currently recognized, settle liabilities other than in the ordinary course of business and make provisions for costs which may arise as a result of cessation or curtailment of normal business operations.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE HALF-YEAR ENDED 31 DECEMBER 2010

Note 2 Segment information

Identification of reportable segments
The Group has identified its operating segments based on the internal reports that are reviewed and used by the Board of Directors in assessing performance and determining the allocation of resources.

The Group is managed primarily on the basis of product category having different risk profiles and performance assessment criteria. Operating segments are therefore determined on this basis.

Description of segments
The Group has identified its reportable operating segments based on its internal reports that are reviewed and used by the board of directors in assessing performance and in determining the location of resources. It's reporting on an operating basis into the following segments.

Tambo
Exploration for coal, oil and gas.

Moreton
Exploration for coal.

Minerals
Exploration for base metals.

2010	Tambo $	Moreton $	Minerals $	Consolidated $
Segment result				
Segment result	-	-	(20,297)	(20,297)
Corporate expenses				(611,808)
Loss for the year				(632,105)
Segment assets	38,082,091	5,179,411	408,981	43,670,483
Cash and cash equivalents				2,206,976
Trade and other receivables				221,566
Unallocated assets				42,686
Total assets				46,141,711
Segment liabilities	147,543	5,676	-	153,219
Other financial liabilities				3,000,000
Unallocated liabilities				28,180
Total liabilities				3,181,399

Note 2 Segment information (continued)

2009	Tambo $	Moreton $	Minerals $	Consolidated $
Segment result				
Segment result	-	-	-	-
Corporate expenses				(707,061)
Loss for the year				(707,061)
Segment assets	36,535,045	5,136,817	250,341	41,922,203
Cash and cash equivalents				774,058
Trade and other receivables				45,076
Unallocated assets				24,410
Total assets				42,765,747
Segment liabilities	189,746	-	-	189,746
Other financial liabilities				3,000,000
Unallocated liabilities				76,150
Total liabilities				3,265,896

Note 3 Loss for the half-year

	Half-year	
	2010 $	**2009 $**
Loss for the half-year includes the following items:		
Expenses		
Loss before income tax includes the following specific expenses:		
Tenement expenditure written off	37,697	19,207
Depreciation	5,393	5,719
Impairment of assets	11,595	-

Note 4 Non-current liabilities – Other financial liabilities

	31 December 2010 $	**30 June 2010 $**
Other financial liabilities	3,000,000	3,000,000

The Group has agreements with Oliver Lennox-King (Lennox-King), whereby Lennox-King has paid $3 million to Lodestone and in return Lodestone has agreed to pay Lennox-King a royalty equal to 1% of the gross value of coal sold and gas produced from the tenements currently held by Lodestone, in the areas of the Moreton Energy Coal Project in the Clarence-Moreton Basin and the Tambo Coal & Gas Project in the Upper Surat Basin.

The initial $3 million received and recorded as a liability was initially recognised at fair value. Post initial recognition, the $3 million received is accounted for in accordance with the Group policy for financial instruments set out in Note 1(a) of the 30 June 2010 Annual Report.

The royalty is only payable in the event of future production of coal and gas.

There has been no movement in the balance of the liability. The Group has assessed that the fair value at the time of the initial transaction, which was at arm's length, remains a reasonable assessment of the fair value at 31 December 2010 as no changes in the underlying circumstances have occurred since.

Note 5 Equity securities issued

	Half-year		Half-year	
	2010	**2009**	**2010**	**2009**
	Shares	**Shares**	**$**	**$**
Issues of ordinary shares during the half-year				
Shares issued in accordance with share sale and purchase agreement *	407,288,211	-	-	-
Shares issued to sophisticated investors	47,750,000	10,000,000	3,820,000	1,950,000
Shares issued on exercise of options	3,800,000	100,000	266,000	7,000
Shares issued on exercise of performance rights	8,250,000	-	-	-
Share issue expenses			-	(13,555)
Net increase in contributed equity	467,088,211	10,100,000	4,086,000	1,943,445

	Half-year	
	2010	**2009**
	Options	**Option**
Movement in options during the half-year		
Options exercised	(3,800,000)	(100,000)
	(3,800,000)	(100,000)

	Half-year	
	2010	**2009**
	Rights	**Rights**
Movement in performance rights during the half-year		
Performance rights exercised	(8,250,000)	-
Performance rights expired	(1,000,000)	-
	(9,250,000)	-

* No amount has been shown as an increase in the dollar amount of issued capital for the half-year ended 31 December 2010 as the increase was recorded in June 2010 as per note 15(h) of the June 2010 financial report.

Note 6 Commitments for expenditure

	31 December 2010 $	30 June 2010 $
Exploration commitments		
Commitments as at 31 December 2010 for payments under exploration permits for minerals in existence at the reporting date but not recognised as liabilities are payable as follows:		
Within one year	16,357,694	9,629,231
Later than one year but not later than 5 years	24,939,259	19,492,500
Later than 5 years	-	-
Commitments as at 31 December 2010 not recognised in the financial statements	41,296,953	29,121,731

To maintain current rights to tenure of various exploration tenements, the Group will be required to outlay amounts in respect of tenement exploration expenditure commitments. These outlays, which arise in relation to granted tenements are noted above. The outlays may be varied from time to time, subject to approval of the relevant government departments, and may be relieved if a tenement is relinquished.

Exploration commitments are calculated on the assumption that each of the tenements will be held for its full term. However, commitments may decrease materially as exploration advances and ground that is shown to be unprospective is progressively surrendered. Expenditure commitments on prospective ground will be met out of existing funds, joint ventures, farm-outs, and new capital raisings.

Note 7 Contingent liabilities

There have been no changes in contingent liabilities or contingent assets since the end of the previous annual reporting period.

Note 8 Events subsequent to reporting date

There have been no matters or circumstances that have arisen since the end of the half-year, that have significantly affected, or may significantly affect, the operations of the Group, the results of those operations or the state of affairs of the Group in future financial years.

DIRECTORS' DECLARATION

The directors declare that:

(a) The financial statements and notes set out on pages 4 to 12 are in accordance with the Corporations Act 2001 and:
  (i) comply with Accounting Standard AASB 134 Interim Financial Reporting and the Corporations Regulations 2001; and
  (ii) give a true and fair view of the consolidated entity's financial position as at 31 December 2010 and of its performance for the half-year ended on that date.

(b) In the directors' opinion there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.

This declaration is made in accordance with a resolution of the directors and is signed for and on behalf of the directors by:

R Clarke
Chairman

Brisbane
8 March 2011

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INDEPENDENT AUDITOR'S REVIEW REPORT

To the members of Lodestone Energy Limited

Report on the Half-Year Financial Report

We have reviewed the accompanying half-year financial report of Lodestone Energy Limited, which comprises the consolidated statement of financial position as at 31 December 2010, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the half-year ended on that date, notes comprising a summary of significant accounting policies and other explanatory information, and the directors' declaration of the consolidated entity comprising the disclosing entity and the entities it controlled at the half-year's end or from time to time during the half-year.

Directors' Responsibility for the Half-Year Financial Report

The directors of the disclosing entity are responsible for the preparation of the half-year financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such control as the directors determine is necessary to enable the preparation of the half-year financial report that is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express a conclusion on the half-year financial report based on our review. We conducted our review in accordance with Auditing Standard on Review Engagements ASRE 2410 *Review of a Financial Report Performed by the Independent Auditor of the Entity*, in order to state whether, on the basis of the procedures described, we have become aware of any matter that makes us believe that the financial report is not in accordance with the *Corporations Act 2001* including: giving a true and fair view of the consolidated entity's financial position as at 31 December 2010 and its performance for the half-year ended on that date; and complying with Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*. As the auditor of Lodestone Energy Limited, ASRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

A review of a half-year financial report consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Australian Auditing Standards and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Independence

In conducting our review, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of Lodestone Energy Limited, would be in the same terms if given to the directors as at the time of this auditor's report.

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BDO

Conclusion

Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the half-year financial report of Lodestone Energy Limited is not in accordance with the *Corporations Act 2001* including:

(a) giving a true and fair view of the consolidated entity's financial position as at 31 December 2010 and of its performance for the half-year ended on that date; and

(b) complying with Accounting Standard AASB 134 *Interim Financial Reporting* and *Corporations Regulations 2001*.

Emphasis of Matters

Without qualifying our conclusion, we draw attention to note 1 in the half-year financial report which details uncertainties regarding going concern and the recoupment of deferred exploration and evaluation costs.

As detailed in the note 1, the ability of the consolidated entity to maintain continuity of normal business activities and to pay its debts as and when they fall due is dependent upon the continued ability of the consolidated entity to raise capital and or to successfully explore and subsequently exploit the consolidated entity's tenements.

As set out in Note 1, the ultimate recoupment of costs carried forward for exploration and evaluation is dependent upon the successful development and commercial exploitation or sale of the respective areas of interest. Ultimate exploitation through the development of mines will depend on raising necessary funding.

No adjustments have been made to the financial report relating to the recoverability and classification of asset carrying amounts or the amounts and classification of liabilities that might be necessary should the company be unable to raise funding as and when required and not continue as a going concern and the exploitation of the areas of interest not be successful.

BDO Audit (QLD) Pty Ltd

BDO

C J Skelton

Director

Brisbane: 8 March 2011

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