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QUARTERLY ACTIVITIES REPORT QUARTER ENDED 30 SEPTEMBER 2012

This recent quarter was eventful and positive for Metgasco, with the NSW Government issuing a range of new regulations, renewing numerous exploration licences and approving our first production licence to support, Metgasco's Casino Gas Project / Richmond Valley Power Station project. In doing so, the NSW Government gave the green light to the CSG industry. The announcements end a prolonged period of uncertainty and little field activity.

The highlights of the quarter were:

- the NSW Government's announcement of new regulations and codes of practice;
- the renewal of Metgasco's PEL 13 and PEL 16 exploration licences;
- the approval of Metgasco's first production lease, PPLA 9 (actual numbering/title still to be confirmed);
- Metgasco has been offered a new exploration licence, PEL 130, immediately adjacent to PEL 13;
- continued progress with local sales gas initiatives, with Pacific Intermodal and companies proposing compressed natural gas distribution and sales options;
- submission of a revised water management plan for Metgasco's exploration activities;
- further preparation for the planned drilling program, with Metgasco's new Drilling and Production Manager commencing work in August; and
- the placement of new shares to raise \$10.2m to fund the ongoing program and the initiation of a share purchase plan to allow pre-placement shareholders to participate under the same terms.

The market for natural gas remains very strong, with open recognition that NSW's contracted gas supplies expire in the 2014 to 2017 period. The NSW Infrastructure report referred to development of NSW's CSG industry as vital and CSG as a "game changer" for the state. The Queensland Gas Market Review forecast gas prices to be in the range of \$6.50 to \$10/GJ by 2015 and \$7 to \$12/GJ by 2020.

With its established CSG reserves and conventional potential, strong market and support from the NSW Government, Metgasco is well positioned.

Review of Exploration and Development Activities

Conventional Exploration and Appraisal Program

Regional work on the hydrocarbon potential and aquifer properties of the strata within the Clarence-Moreton Basin continued with a paper presented by Metgasco in September at the Eastern Australian Basin Symposium in Brisbane summarising some of this work. Metgasco's geoscience team received the best full paper award at the symposium.

Metgasco was offered an additional exploration licence, PEL 130, a block that is immediately adjacent to PEL 13. Metgasco applied for the licence about two years ago and has accepted the offer, subject to a refinement to the work program. This refinement should be clarified before year end.

Work continued on preparations for drilling of Rosella-1 on the Greater Mackellar structure. Weather conditions have improved significantly and the planned seismic will be acquired as soon as the seismic acquisition equipment can be mobilised, which is expected to be in the next two months. The timing of drilling is subject to the availability of the results of the seismic but is planned to be in the second quarter of calendar 2013, possibly using the same drilling rig as the rig to be mobilised for the CSG lateral well program.

Discussions are ongoing with several parties interested in farming into the conventional opportunities by funding drilling.

Proposed Kangaroo Creek Sandstone Test in MSC06

The proposed test of the Kangaroo Creek sandstone will be firmed up with the benefit of information obtained from a well planned by a competitor in an adjacent block, which Metgasco understands has been scheduled for year end.

Certified Reserves

The Company recognises the following gas reserves and resources in its tenement areas.

Independently certified gas reserves – Petajoules (PJ) All reserves are 100% owned by Metgasco			
Reserve Category	PEL 13	PEL 16	Total
1P (Proven)		2.7	2.7
2P (Proven + Probable)	31	397	428
3P (Proven + Probable + Possible)	303	2,239	2,542
2C Contingent Resource	1,334	1,177	2,511

The estimates of gas reserves have been prepared by Mr Tim Hower, and staff under his supervision, of MHA Petroleum Consultants (Denver). Mr Hower is chairman of MHA and has over 25 years of petroleum engineering

experience and is a qualified person as defined under the ASX listing rule 5.11. Reserves have been developed within the guidelines of the SPE. MHA has consented to the use of this information.

2012/2013 drilling program

Metgasco is planning a drilling program of three to four core wells, three lateral CSG wells and a conventional well (to test the Greater Mackellar structure). With the NSW Government's renewal of exploration licences, the timing of the drilling program will be driven by approval of specific well work programs by government, the re-approval of Metgasco's exploration water management plan and the availability of drilling rigs.

Metgasco is close to committing to a core rig and is confident that it can start the core well program shortly before year end and the CSG lateral and conventional program early in 2013.

Water handling

Metgasco submitted its revised exploration phase water management plan in the middle of August and is confident of approval shortly, facilitating the approval of its individual well submissions and approval to start re-testing Harrier P01. As part of the proposed program, Metgasco has already started to abandon and rehabilitate one of the ponds on Richmond Valley Council land.

Metgasco has received its second bioassay results of produced water from Aquatic Bioassay and Consulting Laboratories in California. The results indicate the absence of anything in the water that is toxic to the freshwater species tested. The higher salinity spent drilling fluid was required to be diluted to 10% to achieve satisfactory results while the produced water, which had a higher salinity than previously tested, required a dilution to around 25%. These are very positive results, indicating that with appropriate treatment, even potentially as simple as dilution, produced water can be managed safely.

Review of Commercial Developments

Gas commercialisation strategy

Metgasco continues to explore with several parties the potential for large interstate gas supplies and /or export opportunities, but our first priority is development of local sales.

Local sales opportunities

During the quarter, the NSW Government offered a production licence to underpin Metgasco's proposed Casino Gas Project / Richmond Valley Power station. This is the culmination of almost six years of work, with a Part 3A development approval received in June 2010 after a range of environmental submissions to government. The electricity market has changed significantly since the project's original inception. As a result, Metgasco is re-evaluating the optimal approach, varying from installation of smaller generating capacity initially through to joining with another company that is considering larger, peaking power generation in the area. We are also looking at different options that have the potential to reduce generating costs.

Metgasco continued discussions with industrial and agricultural consumers regarding potential natural gas, electricity and water sales in other areas of the Northern Rivers, including Lismore. Metgasco has agreed to work with a party that is keen to develop an industrial site in Casino, building on the advantages Casino has in terms of road and rail transport and workforce.

Metgasco also announced the appointment of technical consultants, CNC and OSD, to help prepare development plans and coordinate environmental studies and submissions to secure approval for a production lease ("West Casino Gas Project") capable of supplying up to 10 PJ/a to the Northern Rivers region. Metgasco also continues to negotiate with a company that proposes to operate a compressed natural gas operation, including distribution and marketing.

Interstate and export opportunities

Metgasco worked with the NSW government to convert the approval process for the Lion's Way Pipeline from the old Part 3A process to the government's new planning process, making sure that the completed environmental work can be used in the new process. The major outstanding work in NSW involves cultural heritage studies.

Concerns regarding the supply and pricing of gas into NSW from 2014 have continued. The NSW Government is promoting the rapid development of the state's CSG resources under the new regulatory regime. The price of gas is expected to increase significantly.

Review of Corporate Developments

Community and Government Engagement

NSW Government Gives Metgasco the Green Light

On 11 September 2012 the NSW Government announced a series of new regulations for the coal seam gas industry and the renewal of Metgasco's Petroleum Exploration Licences 13 and 16. At the same time, the Government granted a production lease to Metgasco, the first production lease granted by the new administration.

The announcement of the new regulations, a large number of exploration renewals and the grant of a production lease sent a clear message to the financial markets and general community that the NSW Government is strongly behind the development of the CSG industry in NSW.

The importance that the NSW Government has placed on the CSG industry to enhance the state's economy is apparent with the release of Infrastructure NSW's report entitled *The State Infrastructure Strategy 2012-2032* which states:

"Infrastructure NSW considers that the development of the Coal Seam Gas (CSG) industry will be game changing for NSW, providing a number of strategic benefits. It will help to address the security risk of declining reserves of conventional natural gas from interstate basins; meet the increasing demand for gas fired generation; and help to contain upward pressures on wholesale gas prices because of declining reserves and increased demand including for exports."

An unfortunate effect of the NSW Government's delay in approving licences and determining a new regulatory regime was that support for the industry waned in the eyes of some in the

community. A recent poll conducted by the Australian Petroleum Production and Exploration Association showed that 66% of respondents had doubts about the CSG industry because of the NSW Government's delay in issuing licences. With the new regulations and support from key NSW Ministers, Metgasco is seeing evidence that community sentiment is changing. The Hon Chris Hartcher MP, Minister for Resources and Energy, was recently quoted as saying:

“Unlocking the wealth of our gas resources will kick-start a new economic boom, one that provides benefits for the entire State, whilst living in harmony with local communities.”

Consistent with the strong support from the NSW Government, Metgasco remains committed to our open community relations strategy. We continue to meet with local leaders and key community groups and have regularly participated in local media coverage.

Our community message remains unchanged – we represent an established, well regulated and safe industry with great potential to enhance and diversify the local economy. It is not just through direct employment that we see our role in the local economy. It is our belief that through local gas sales and the reduction in cost to energy dependent local businesses we will play an important role.

Meeting the energy demands of local business through the development of additional intrastate pipeline infrastructure was also highlighted as a key priority by *The State Infrastructure Strategy 2012-2032*. The Government's specific priority in this regard:

“Is to ensure that investment in gas infrastructure occurs in a timely manner and does not delay production or create supply bottlenecks.”

Obtaining exploration and production approvals in a timely manner is seen as very important to Metgasco's future success. With the announcement of a new regulatory regime, an obvious willingness of Government for the CSG industry to succeed and the Department of Resources recruiting additional officers, Metgasco believes that the approval process will be enhanced.

Personnel

Dr Simon Hann commenced work with Metgasco in late August as its Drilling and Production Manager. Dr Hann was the Drilling and Completions Manager for Santos/GLNG in Queensland and brings extensive drilling and coal seam gas experience to Metgasco. Given that drilling and production performance is one of the keys to Metgasco's success, this is a particularly important appointment. Metgasco is now recruiting other petroleum specialists and consultants to ensure that we have the appropriate resources to optimise our CSG well performance and evaluate our conventional gas potential.

Cash Position

The Company ended the quarter with a cash position of \$20 million, which included a placement of \$10.2 million, with shares issued at \$0.20. A Share Purchase Program, which provides pre-placement shareholders to contribute on the same terms as the placement is currently underway, with October 22 as the expiry date.

Shareholder Base

At 30 September Metgasco had 392 million shares on issue and 5.3 million options outstanding.

Outlook - Planned Forward Work Program Next Quarter

With the NSW Government's green light, Metgasco is ready to move ahead with further appraisal, development and commercialisation of its assets.

Metgasco's focus over the next quarter will be to:

- complete government approvals, allowing commencement of the core and lateral well program;
- continue environmental and development studies that are necessary to secure approval of the production licences required for local gas sales.;
- complete the seismic program, facilitating the drilling of the Rosella-1 conventional exploration prospect in 2013;
- further market development, both local and interstate / export LNG;
- continue discussions with potential farmin partners; and
- continue promoting the benefits and safety of the industry to the Northern Rivers Region.

Background on Metgasco

www.metgasco.com.au

Metgasco has a 100% interest in PEL 16, 13 and 426 in the Clarence Moreton Basin in NSW where it operates the largest acreage position in the basin. Metgasco currently has 2P gas reserves of 428 Petajoules and 3P gas reserves of 2,542 Petajoules. The Company is exploring for conventional and unconventional gas. Metgasco is currently progressing its gas commercialisation agenda which includes local NSW gas and electricity supply and gas supply to Queensland. With gas in place resources likely to exceed the domestic markets requirements and sufficient to supply export scale projects, Metgasco is also investigating LNG export options.

For further information contact:

Peter Henderson
Managing Director

Sean Hooper
Chief Financial Officer

Address
Level 9, 77 Pacific Highway
North Sydney NSW 2060

Tel: +61 2 9923 9100
Fax: +61 2 9923 9199
