Petsec Energy Ltd

Results for announcement to market
For the twelve months ended 31 December 2019

Key Points

- Net loss after tax of US$24.2 million for the twelve months to 31 December 2019 after the recognition of dry hole and impairment expense of US$13.8 million, financial expense of US$3.7 million, and DD&A expense of US$2.6 million.
- Net oil and gas revenues of US$1.1 million generated from production of 368 MMcfe at an average gas equivalent sales price of US$2.96/Mcfe.
- Appointment of Mr. Syed Bokhari, a highly experienced production operations engineer and E&P leader, as Managing Director of Petsec Energy Ltd, effective 1 May 2019.
- USA: Main Pass Blocks 270/273/274, Hummer Project: The Main Pass Block 273 B-2 appraisal/development well was drilled to a final depth of 15,990 feet TVD /17,570 feet MD and did not encounter commercial hydrocarbons.
- YEMEN: Damis (Block S-1): Efforts toward a restart of oil production operations at the An Nagyah Oilfield continued following meetings with the Yemen Minister of Oil & Minerals, his encouragement to secure joint venture partners to co-invest in the development of Block S-1, the Company's subsequent field inspection to determine the state of the oilfield infrastructure and preparation of a final restart plan.
- Petsec responded to a claim and release of funds in January 2020 that were held in support of the Letter of Credit for Block 7 in Yemen. Legal options for recovery are being evaluated.
- Independently estimated net proven and probable (2P) oil and gas reserves of 8.4 MMboe at 1 January 2020 with an estimated net present value (NPV_{10}) of US$177.3 million, representing net 2P reserves in the USA of 2.8 MMboe (NPV_{10}: US$21.9 million, 1 January 2020) and An Nagyah (Yemen) net 2P reserves of 5.6 MMbbl (NPV_{10}: US$155.4 million, 1 January 2016).
- At 31 December 2019, Petsec Energy held total cash deposits of US$0.7 million (including US$0.1 million of restricted deposits).

Key data – Twelve months ended 31 December 2019 compared to the twelve months ended 31 December 2018

	Twelve Months to 31 December 2019	Twelve Months to 31 December 2018	% Increase/ (Decrease)
Key Operating/Financial Data			
Net production (MMcfe [1])	**368**	796	(54%)
Net revenues after royalties (US$m)	**1.1**	3.1	(65%)
Net loss after tax (US$m)	**(24.2)**	(10.1)	n/a
Add: Depreciation, depletion & amortisation and reclamation expense (US$m)	**2.6**	1.8	44%
Add: Change in rehabilitation provision (US$m)	**0.5**	-	n/a
Add: Dry hole and impairment expense (US$m)	**13.8**	0.5	2,660%
Add: Net financial expense (US$m)	**3.7**	4.9	(24%)
EBITDAX (US$m) [2]	**(3.6)**	(2.9)	n/a
Key Performance Indicators			
Average net sales price/Mcfe [3] (US$)	**2.96**	3.93	(25%)
Add: Other revenue/(expense)/Mcfe (US$)	**(0.48)**	0.04	n/a
Less: Operating costs/Mcfe (US$) [4]	**(12.36)**	(7.66)	n/a
EBITDAX/Mcfe (US$)	**(9.88)**	(3.69)	n/a
Gross margin [5]	**n/a**	n/a	n/a
DD&A/Mcfe (US$)	**7.05**	2.27	210%
Other Financial Data			
Acquisition, exploration and development expenditure (US$m)	**2.6**	4.2	(38%)
USD/AUD average exchange rate	**0.6967**	0.7476	(7%)

1 MMcfe = million cubic feet of gas equivalent (conversion ratio: 1 barrel of oil = 6 Mcf of gas).
2 Earnings before interest (financial income and expense), income tax, depreciation, depletion, and amortisation and exploration (including dry hole and impairment expense). EBITDAX is a non-IFRS number and is unaudited.
3 Mcfe = thousand cubic feet of gas equivalent.
4 Operating costs comprise lease operating expense plus geological, geophysical and administration expenses.
5 Gross margin is EBITDAX as a percentage of sales.

Commentary on results

General

The Appendix 4E results and the accompanying consolidated final financial statements are prepared in accordance with Australian Accounting Standards (AASBs) and International Financial Reporting Standards (IFRS) and are presented in United States dollars.

Current period: Twelve months ended 31 December 2019; Previous corresponding period: Twelve months ended 31 December 2018.

Key Operating/Financial Data

- Petsec Energy reported net production of 332 MMcf of gas and 5,945 barrels of oil/condensate (equivalent to 368 MMcfe) for the current period. This was 54% lower than the net production of 796 MMcfe in the previous corresponding period due to production decline in the Hummer and Mystic Bayou Fields.
- Net oil and gas revenues (after royalties) derived for the current period were US$1.1 million. This was 65% lower than the previous corresponding period of US$3.1 million due to the lower production volumes coupled with a lower average natural gas equivalent sales price received for the current period.
- The Group recorded negative EBITDAX of US$3.6 million (previous corresponding period: negative EBITDAX of US$2.9 million).
- The Group incurred a net loss after tax of US$24.2 million (previous corresponding period: US$10.1 million) after the recognition of dry hole and impairment expense of US$13.8 million, net financial expense of US$3.7 million, and depreciation, depletion and amortisation ("DD&A") expense of US$2.6 million.

  Dry hole and impairment expense of US$13.8 million mainly comprised the dry hole cost of the Main Pass Block 273 B-2 well (US$6.4 million) and the recognition of an impairment expense of US$7.3 million against the Hummer Gas/Oil Field primarily due to a reduction in reserves, based on the results of the B-2 well.

  Financial expense of US$3.7 million comprised expenses incurred in connection with the convertible note facility – facility fees, interest expense and movements in the fair value of the financial derivative component of the convertible note liability.

Key Performance Indicators

- The Group realised an average net gas equivalent sales price of US$2.96/Mcfe in the current period. This was 25% lower than the US$3.93/Mcfe realised for the previous corresponding period, reflecting the lower commodity price environment. The Group received average sales prices of US$2.22/Mcf of gas and US$58.87/bbl for its natural gas and oil/condensate production, respectively. This compares to US$3.12/Mcf and US$65.89/bbl in the previous corresponding period.
- After unit operating costs of US$12.36/Mcfe (previous corresponding period: US$7.66/Mcfe) the EBITDAX margin was negative US$9.88/Mcfe (previous corresponding period: US$3.69/Mcfe).
- Unit DD&A expense was US$7.05/Mcfe for the current period (previous corresponding period: US$2.27/Mcfe).

Other Financial Data

- Acquisition, exploration and development expenditures for the current period of US$2.6 million primarily related to drilling costs associated with the Main Pass Block 273 B-2 well on the Hummer Gas/Oil Field in the shallow waters in the Gulf of Mexico, USA.

Dividend

Petsec Energy Ltd does not propose the payment of a dividend in respect of the twelve months ended 31 December 2019.

Net Tangible Asset Backing

The Group's net tangible asset backing per ordinary security for the current period was negative US$0.05 (previous corresponding period: nil).

Petsec Energy

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Petsec Energy Ltd

ABN 92 000 602 700

The Company is listed on the Australian Stock Exchange (symbol: PSA) and traded over the counter in the USA as American Depositary Receipts (ADRs) (symbol: PSJEY). Its corporate office is in Sydney, Australia, its USA operations office is in Houston, Texas, and its Middle East and North Africa (MENA) operations office are in Dubai, United Arab Emirates (UAE) and Sana'a, Yemen.

Annual General Meeting

To be held at: 11 a.m. (AEST) on Thursday, 7 May 2020, at the Governor Macquarie Tower, Level 15 Bligh Room, 1 Farrer Place, Sydney, NSW Australia.

Capital Structure

At 20 February 2020

Australia

Exchange	ASX
Ticker	PSA
Shares on issue	398.6 million
Share price	A$0.044
Market capitalisation	A$17.5 million

USA

Exchange	OTC Pink Sheets
Ticker	PSJEY

Annual Report
For the year ended 31 December 2019

Corporate Objective and Strategy

Petsec Energy's corporate objective is to increase shareholder value by increasing the net asset value of the Company through successful oil and gas exploration, development, and production, thereby building Petsec Energy into a significant mid-tier oil and gas exploration and production company, respected in the industry for its technical skills, timely and cost effective delivery of projects, and the integrity with which it conducts its business.

The Company's strategy to meet the above objective is to maximise the value of its current reserves, pursue participation in high quality, high impact exploration drilling opportunities, and to acquire leases with undeveloped or producing oil and gas reserves, which also hold significant development and exploration potential.

Prior to 2014 the strategic and geographical focus of the Company was predominately in Louisiana, USA. This focus shifted in 2014 to include oil reserve acquisitions in the MENA region. In the Republic of Yemen, the Company holds two leases: one with undeveloped oil resources and substantial exploration potential; and the second a production licence over five sizeable oil and gas discoveries, one of which is developed (An Nagyah) and was in production until late in February 2014. The Company will continue to identify and pursue additional developed and undeveloped reserves within both the MENA and US regions.

Company Profile and History

Petsec Energy Ltd is an independent oil and gas exploration and production company listed on the Australian Stock Exchange (symbol: PSA) and traded over the counter in the USA in the form of American Depositary Receipts (symbol: PSJEY).

The Company was established on 7th December 1967 and its registered Australian Company Number is: 000 602 700.

The Company through its wholly owned subsidiary companies Petsec Energy Inc. and Petsec Exploration and Production LLC has operations in the shallow waters of the Gulf of Mexico and onshore Louisiana, USA. The Company also owns interests onshore in the Republic of Yemen through its wholly owned subsidiary Petsec Energy (Middle Eastern) Limited.

The Company has been active in the USA since 1989 and has explored offshore in the Gulf of Mexico and onshore in Louisiana, and Texas. The Company has drilled over 100 wells in the USA and has enjoyed a success rate of 74%.

From 2002 to 2011, the Company was active in the Beibu Gulf, China, participating in the drilling of 7 exploration wells resulting in 3 oil fields being discovered. The fields were sold in 2011.

In 2014, the Company determined that it wished to pursue both an exploration and an oil reserves acquisitions strategy. Following a strategic review, the Company identified the Middle East & North African (MENA) region as a growth area for the Company where licences with producing oil reserves or near development reserves, with associated high exploration potential, can be acquired at lower prices than those in the USA.

In 2015, a non-operated interest in a large licence (Block 7) area was acquired in Yemen. Two wells previously drilled on the Block indicate the potential for a substantial resource coupled with a number of drill prospects which have been identified with 2D and 3D seismic. In 2016 thru 2018, the Company completed several transactions that resulted in securing Block 7 operatorship and potentially increase the Company's interest in Block 7 to 100% subject to customary approvals from the Yemen Government.

In early 2016, the Company acquired a 100% working interest in Damis (Block S-1) in Yemen, which holds five oil and gas fields of which one field, the An Nagyah Oilfield, had been developed and was producing until political unrest in 2014 caused it to be shut-in.

The Company's corporate office is in Sydney, Australia and the Company's operational offices are located in Houston, Texas, in the USA, and in Dubai, UAE, and Sana'a, Yemen in the MENA region.

Petsec Energy

Annual Report

For the year ended 31 December 2019

2019 Year in Review

Corporate

- Appointment of Mr Syed Bokhari as Managing Director of Petsec Energy Ltd, effective 1 May 2019.
- Variation of the terms of the Convertible Note Facility making US$5 million available to support the Company's restart of production from the An Nagyah Oilfield, Block S-1 Yemen.
- Closure of the Lafayette office in the USA.
- Relocation of corporate registered office to Level 7, BMA House, 135 Macquarie Street, Sydney NSW Australia.

Operations

USA:

Production

- The Company holds an interest in three producing fields – the Jeanerette and Mystic Bayou Fields, onshore Louisiana, and the Hummer Gas/Oil Field offshore Louisiana, Gulf of Mexico, USA.
- Production for the year of 368 MMcfe was derived from the Hummer Gas/Oil Field (299 MMcfe) and the Mystic Bayou Field (69 MMcfe).
- USA net 2P oil and gas reserves as of 1 January 2020 were 11.0 Bcf of gas and 977.8 Mbbl of oil (equivalent to 2.8 MMboe) with an NPV_{10} value of US$21.9 million (Cawley, Gillespie & Associates).

Development

- The Main Pass Block 273 B-2 appraisal/development well, the second well to be drilled on the Hummer Gas/Oil field, was drilled to a final depth of 15,990 feet TVD/17,570 feet MD and did not encounter commercial hydrocarbons.

MENA

Damis (Block S-1) Production Licence, Yemen
Petsec: 100% working interest (82.5% participating interest)

- The block of 1,152 square kilometres (284,665 acres), located in the Marib Oil Basin, was acquired by the Company in early 2016.
- The block contains five sizeable oil and gas discoveries with target resources in excess of 54 million barrels of oil and 550 Bcf of natural gas including the developed/productive An Nagyah Oilfield (> 19.8 MMbbls remaining) complete with surface facilities to process and transport 20,000 bopd. The An Nagyah Oilfield commenced production in 2005 with an estimated 50 MMbbls of recoverable oil of which half remains. The field has been shut-in since 2014 due to the political situation in the country.
- The An Nagyah Oilfield was estimated by DeGolyer and McNaughton, reserve engineers, to hold 19.8 million barrels of remaining recoverable oil using 1 January 2016 forward oil prices.
- The block also contains significant additional resource potential in the four undeveloped fields (Osaylan, An Naeem, Wadi Bayhan and Harmel fields) which have been defined by nine wells and 3D seismic and hold target resources of 34 MMbbl of oil and 550 Bcf of gas.
- The internationally recognised Yemen Government led by President Hadi had requested in late 2016, that oil producers in Southern Yemen restart production as soon as possible, using the Yemen Government's facilities in the Shabwah and Masila areas until such times as the Marib Pipeline is permitted to be operational. To meet this request by the Hadi Government, the Company started making preparations and field operational changes to restart production from the An Nagyah Oilfield.

2019 Year in Review (continued)

MENA (continued)

Damis (Block S-1) Production Licence, Yemen (continued)
Petsec: 100% working interest (82.5% participating interest)

- The Company had been seeking, since early 2017, the necessary government support and formal approvals for a trucking operation to access government oil export facilities in order to restart oil production at the An Nagyah Oilfield until such times as the Ras Isa oil export terminal at the Port of Hodeidah and the Marib pipeline resumes operations. Delays have been due to limited and changing Yemen administration capabilities, political changes, security conditions, Petsec Energy as a new entrant to operations in Yemen, and consideration of the Company's technical and financial capacity.
- Construction of a 16 inch oil transport pipeline connecting Block 5 (to which Block S-1 is connected) to the oil export pipeline of Block 4, was completed in late 2019. Pre-startup testing is currently underway. The Yemen Oil Ministry expects it to be operational by March 2020. This pipeline will connect Block S-1 to the Rudum Terminal in Bir Ali on the southern coast making it possible for crude to flow from Block 4 to the Rudum terminal for further shipment. This route is in a more politically stable environment.
- During 2019, operations at the Company's An Nagyah Oilfield in Block S-1 remained shut-in while the Company continued its efforts to secure government approvals to transport oil and to access Yemen Government owned facilities in neighbouring Block 4.
- The Company completed a field visit in June/July 2019 to inspect the Block S-1 Production Facility and gather data to use in the planning and timing for the restart of production. The condition of the facilities and information gathered was very encouraging and supported the Company's target of being able to commence production within 3 months of returning to the field full time.
- The Shabwah Governate, in which Petsec's Blocks S-1 and 7 are located, is under the control of the internationally recognised Yemen Government with support from Saudi and local forces. The security position is generally good and OMV has been producing since 2018. OMV is trucking oil 20 kilometres to Block 4, and then flowing through the 204 kilometre pipeline to Bir Ali export terminal.
- During fourth quarter 2019, the government owned Safer Exploration Production Oil Company (SEPOC) started production of 5,000 bopd from Block 18 and is trucking it South all the way to the Rudum Terminal at Bir Ali. This is a significant development as Block 18 is a major oil producer for the country, producing on average 35,000 bopd prior to rebel control of the Marib Export Pipeline.

Block 7, Al Barqa Permit, Yemen
Petsec: 75% working interest (63.75% participating interest)

- The Company has operatorship and holds a 75% working interest in Block 7 (63.75% participating interest) in the Al Barqa (Block 7) Joint Venture. In September 2016, the Company entered into an agreement with Kufpec to acquire their 25% working interest in Block 7 by meeting their share of Block 7 costs. The Kufpec transaction was subject to customary approvals from the Government of Yemen which had not been obtained at balance date.
- The block of 5,000 square kilometres (1,235,527 acres) contains the Al Meashar prospect on which two wells were drilled in 2010 that encountered oil. The two wells flowed oil to surface on a limited production test which indicates the potential of a substantial resource.
- The block also contains an inventory of leads and prospects, which were identified by 2D and 3D seismic surveys.

2019 Year in Review (continued)

Financial

- Net production: 368 MMcfe, down 54%.
- Gas equivalent average sales price realised: US$2.96/Mcfe, down 25%.
- Net oil and gas revenues (after royalties): US$1.1 million, down 65%.
- EBITDAX: negative US$3.6 million (previous corresponding period: negative US$2.9 million).
- Impairment, abandonment, and exploration expense: US$13.8 million (previous corresponding period: US$0.5 million).
- Depreciation, depletion and amortisation (DD&A) expense: US$2.6 million (US$7.05/Mcfe), up 44%.
- Unit operating costs: US$12.36/Mcfe (previous corresponding period: US$7.66/Mcfe).
- Net loss after tax: US$24.2 million (previous corresponding period: US$10.1 million).
- Acquisition, exploration and development expenditures: US$2.6 million, down 38%.
- Cash (including restricted cash) at 31 December 2018: US$0.7 million, down 85%.
- US$15 million convertible note facility: US$1.5 million available at 31 December 2019.

Chairman's Report

Dear Shareholder,

Petsec faced several challenges during 2019. We were unable to deliver the growth that was anticipated from the drilling of the second well on the Hummer Gas/Oil Field, in the Gulf of Mexico, USA, and while there were promising developments in Yemen, the restart of oil production from the Company's An Nagyah Oilfield in Damis (Block S-1) continues to be delayed.

The Main Pass Block 273 B-2 appraisal/development well, which was drilled from the Main Pass Block 270 "B" Production Platform in the shallow waters of the Gulf of Mexico reached a final depth of 15,990 feet TVD/17,570 feet MD in March 2019, some seven months after it had been spud in August 2018. The Company was disappointed with not only the results of the well but also the significant amount of time delays and cost overruns that were incurred over the course of this drilling project. The total cost incurred in drilling the B-2 well was US$6.4 million, net to Petsec Energy.

The outcome of the B-2 well contributed to a 17% reduction in the Company's estimated remaining US net proved and probable (2P) reserves at 1 January 2020, which were estimated by the independent reserve auditors Cawley, Gillespie & Associates to be 11 billion cubic feet of gas ("Bcf") and 977.8 thousand barrels of oil ("Mbo") – which equates to 2.8 million barrels of oil equivalent ("MMboe").

The net present value of those USA reserves was estimated to be US$21.9 million at an annual discount rate of 10% (NPV_{10}) calculated using the forward swap prices in effect on 31 December 2019. Notwithstanding that the natural gas forward swap prices were up to 16% lower than the prices utilised in the previous year estimates, this NPV_{10} value equates to approximately 8 cents per Petsec Energy share.

In Yemen, operations at the Company's An Nagyah Oilfield in Block S-1 continued to be shut-in throughout 2019 while awaiting Yemen Government consents for access to pipeline, storage and export facilities that are required to support the restart of production. The Company had been hopeful that access would be forthcoming in 2019, following Petsec's engagement with the Yemen Minister of Oil & Minerals, His Excellency Aws Al-Aud ("Minister") and his department, the restart of oil production by other operators in the region, and the beginnings of a UN sponsored peace process with the rebels.

In May 2019, the Company appointed Mr. Syed Bokhari, a highly experienced production operations petroleum engineer, as Managing Director of Petsec Energy Ltd. Mr. Bokhari has significant experience in the MENA region and his appointment was seen by the Board as an important step in the Company's strategy to secure access to Government owned facilities and for preparation for the restart of production from the An Nagyah Oilfield.

Immediately following his appointment, Mr. Bokhari and I met with the Minister to share the Company's restart plans for the An Nagyah Oilfield and provide support for Petsec's technical and financial capabilities. The Minister showed considerable interest in the restart plan and expressed a desire to have the field in production within six months to coincide with the expected completion of a 16-inch oil pipeline connecting Block 5 (to which Block S-1 is connected) to the Block 4 export pipeline. He also encouraged Petsec to seek joint venture partners to co-invest in the development of Block S-1, which holds four undeveloped fields in addition to the developed An Nagyah Oilfield.

Subsequent to the meeting with the Minister, in June 2019 Petsec Energy sent a technical team to Block S-1 to evaluate the condition of the An Nagyah production facilities and prepare start-up plans. The evaluation team consisted of an international production facilities expert, four Yemeni oil field professionals, Petsec Energy staff, and a representative of the Yemen Ministry of Oil & Minerals.

The team found the facilities to be in good condition which will allow for an efficient commencement of production once on location permanently. Local staff and contractors also expressed a desire to see an early restart of production.

Final plans are being prepared for the production start-up that include all technical work, equipment/services required, contract support, manpower ramp up, transport and access to export facilities, and export sales agreements. Plans are also being prepared for Operating Committee Meetings (OCMs) to be held and restart budgets to be agreed with the government representatives. It is anticipated that the plan can be concluded within a month of receipt of the Yemen Government consents which will allow for an immediate deployment of personnel to the site to begin start-up operations. It is expected that oil production can commence within 3 months of the Company's occupation of Block S-1.

Chairman’s Report (continued)

The Company’s engineers estimate initial rates of 5,000 bopd of oil production within 3 months of being on site increasing to 10,000 bopd within 6 to 12 months from the time of receipt of Yemen Government consents to access Block 4 oil export facilities.

In response to the Minister’s encouragement that Petsec Energy seek investors in the development of Yemen’s oil resources, Petsec has engaged with several E&P companies interested in a joint venture partnership over Block S-1. These discussions are ongoing.

During the fourth quarter of 2019, the government run Safer Exploration Production Oil Company (SEPOC) started production of 5,000 bopd from Block 18 and is trucking it south to the Rudum Terminal at Bir Ali. This is a significant development as Block 18 is a major oil producer for the country, producing on average 35,000 bopd prior to rebel control of the Marib Export Pipeline. SEPOC’s Block 18 and Petsec’s Block S-1 are connected by pipeline to Block 5 which will soon be connected to Block 4 following the completion of an 80-kilometre, 16-inch pipeline.

Completion of this pipeline, restart of production from Block 18, and the recent declaration by the Yemen Oil Minister that Blocks 5 and S-1 will be in production in early 2020, demonstrates the government’s desire to bring all fields in the Shabwah region back into production.

Fraudulent claim against US$4.2 million Letter of Credit supporting Block 7 exploration obligations

In late November 2019, we became aware that an illegal and fraudulent claim was being made by the rebel Houthi controlled Ministry of Oil and Minerals in Sana’a to Arab Bank, Sana’a, which held a US$4.2 million Letter of Credit (LoC) that supports the Block 7 JV exploration obligations. Arab Bank Sana’a in turn issued a claim to Qatar National Bank in Sana’a which held US$1.68 million of the Company’s funds in support of the Block 7 LoC, and to the National Bank of Kuwait which held US$1.05 million in support of KUFPEC’s 25% interest share of the Block 7 LoC.

In our opinion the claims by the Ministry of Oil and Minerals and subsequently by Arab Bank were illegal and fraudulent, not only under the terms of the LoC but also because the rebel Houthis are a recognised terrorist group sanctioned by the UN, USA, and Europe.

Upon learning of the claim, Petsec contacted its joint venture partners to alert them that the claims being made were fraudulent and illegal. We also immediately contacted Arab Bank, Sydney, Sana’a and Jordan, and Qatar National Bank, Sana’a to alert the banks that the claims were fraudulent and illegal. AWE/Mitsui, which has US$1.05 million on deposit in support of the Block 7 LoC, was provided with evidence that they could use to inform their bank, Commonwealth Bank of Australia, Sydney (CBA), to alert them of the fraudulent claims including the consequent instructions to the counterparty banks. We provided copies of instructions from the legitimate, UN supported government of Yemen forbidding any financial dealings with the Houthis and the Ministry in Sana’a, evidence of the block being in Force Majeure, and a copy of the LoC which states clearly that no claim can be made while the block is in Force Majeure. In addition, a copy of the instruction to QNB from Arab Bank was provided which directed QNB to convert Petsec’s US$1.68 million into Euros and transfer the funds to Raiffeisen Bank in Sofia, Bulgaria. These instructions from Arab Bank to QNB were inconsistent with the fraudulent claim by MoM to Arab Bank which required the LoC funds to be remitted in US dollars. In early January 2020, Petsec received a copy of a letter addressed to Arab Bank, Sana’a and Jordan from the legitimate Minister of Oil and Minerals in Aden, stating that there was no claim on the LoC. This letter was also provided to AWE/Mitsui.

Despite concerted efforts by Petsec to prevent any action on the claims, QNB without notice nor informing us for 6 weeks, released Petsec’s funds on the 8 January 2020. We understand the US$1.68 million was converted to Euros and instructions were given for the funds to be transferred to Raiffeisen Bank. We are seeking legal advice as to the best way to recover those funds and expect to commence legal actions against Arab Bank and QNB to recover the US$1.68 million that was in our opinion fraudulently obtained.

In early January 2020, AWE/Mitsui informed us that the CBA had received a claim on the 23 December 2019 and paid out US$1.05 million to, we understand, Arab Bank, Sana’a on the 8 January 2020. Mitsui is seeking to recover these funds from Petsec and the Company is seeking and has been seeking since mid-January, further information from AWE/Mitsui and the CBA regarding the payment details in respect of the illegal claim. Mitsui were given due notice that the claim was illegal, and stated to Petsec that all the evidence of the illegal claim had been delivered to the CBA. The Company will vigorously defend any action by Mitsui to recover the funds and are seeking legal advice in respect of possible cross claims.

Chairman's Report (continued)

Funding

During 2019, there continued to be significant demands placed upon the Company's working capital, primarily due to the substantial cost overruns that were incurred in the drilling of the Hummer B-2 well and resultant loss of expected cash flows from that well, coupled with the continued delay in obtaining Yemen Government consents to restart production from the An Nagyah Oilfield. As a consequence, the Company has drawn further against the US$15 million convertible note facility, and also modified the terms of the facility including an extension to the date of redemption.

In order to conserve capital, the Company implemented further cost cutting initiatives during the year aimed at rationalising operations and minimising general and administrative costs, across all geographical segments – Sydney, USA and MENA. This resulted in the closure of the Company's Lafayette office in September 2019, with the Houston office being retained as a regional operational office in the USA, and the relocation of the corporate registered office in Sydney to smaller premises in November 2019. Further cost-cutting measures are expected to be undertaken during the 2020 year.

The An Nagyah Oilfield is the Company's largest asset and holds significant value for the Company. The restart of oil production from the field will allow for positive cashflow generation and which would provide the opportunity to access more flexible funding to strengthen the Company's balance sheet.

Outlook 2020

In 2020, no further exploration or development is anticipated by the Company in the USA. The Company will continue to evaluate its U.S. business strategy and look for alternatives for the U.S. assets.

In Yemen, the final restart plan for the An Nagyah Oilfield will be completed to enable the immediate restart on receipt of the requisite Yemen administrative consents to transport and export oil via Block 4 to Ruduum Terminal at Bir Ali.

We will continue engagement with interested potential joint venture partners in Damis (Block S-1), but also look to rationalise the MENA operations while maintaining preparations for a restart, and minimising general and administrative costs until such time as government consents are obtained.

In closing, the Board and I would like to thank you, our shareholders, for your ongoing support, throughout what has been a difficult and challenging year.

I look forward to providing further details on our progress at the AGM to be held in May 2020.

TN Fern

Chairman

Directors' Report
For the year ended 31 December 2019

The directors present their report together with the Financial Report of Petsec Energy Ltd ("the Group"), being Petsec Energy Ltd (the Company) and its subsidiaries, for the financial year ended 31 December 2019 and the independent auditor's report thereon.

1. Directors

The names and particulars of the qualifications and experience of each director during or since the end of the financial year are:

Terrence N Fern
Executive Chairman

Mr Fern has been a director since 1987 and has over 45 years of extensive international experience in petroleum and minerals exploration, development and financing. He holds a Bachelor of Science degree from the University of Sydney and has followed careers in both exploration geophysics and natural resource investment. Mr Fern was formerly a director of TSX and ASX listed company OceanaGold Corporation from 2006 until June 2011.

Syed W Bokhari
Managing Director

Mr Bokhari joined the Company in 2019 as Managing Director of Petsec Energy Ltd. Mr. Bokhari is a highly experienced production operations petroleum engineer and a senior oil and gas executive, having served as the CEO and Managing Director of Pakistan Petroleum Limited (the Pakistan National Oil Company) and prior to that as a Regional Manager for Kuwait Foreign Petroleum Exploration Co. (KUFPEC – a subsidiary of Kuwait National Oil Company).

Mr Bokhari has over 35 years of experience, mostly with major E & P companies, including, Atlantic Richfield Company (ARCO), ENI (AGIP & Lasmo), KUFPEC and Pakistan Petroleum Limited (PPL). He has a proven track record of leading, developing and managing E&P organizations and has managed operations in the USA (onshore and offshore), Canada, Australia, UK North Sea, China, Ecuador, Peru, Nigeria, Pakistan, Iraq, Kuwait and Yemen.

Mr Bokhari is based in Dubai UAE. Mr Bokhari holds a BSc and MSc in Petroleum Engineering, from the University of Texas in Austin, Texas.

David A Mortimer AO, FAICD
Non-executive Director
Chairman of the Audit Committee and the Nomination and Remuneration Committee

Mr Mortimer was appointed to the Board in 1985 and has over 40 years of corporate finance and management experience. He was a senior executive of TNT Limited Group from 1973, serving as Finance Director and then as Chief Executive Officer until his resignation in October 1997. He is presently Chairman of Opera Australia, Buildcorp Advisory Board, IRAA, and is Chairman of the Senate Investment Committee of The University of Sydney. Mr Mortimer is a member of the Advisory Committee of CEDA.

Mr Mortimer holds a Bachelor of Economics degree (First Class Honours) from the University of Sydney and was a Fellow of the University of Sydney Senate from 2010 to December 2017. He is a fellow of the Australian Institute of Company Directors. Mr Mortimer's other roles include Governor of the Australia Israel Chamber of Commerce, Chairman of the Sydney University Football Club Foundation and Chairman of the Australian Schoolboys Rugby Foundation.

Mr Mortimer was formerly a director and Chairman of ASX listed company Leighton Holdings Limited from 1997 until August 2011 and Chairman of Australia Post from 2006 to 2012. He was a foundation shareholder and Chairman of Crescent Capital Partners until 31 December 2017 and was a member of the Grant Samuel Advisory Board until December 2017. He has held many directorships and has chaired listed and unlisted companies as well as written three major reports for Governments.

1. Directors (continued)

Alan P Baden

Non-executive Director

Member of the Audit Committee and the Nomination and Remuneration Committee

Mr Baden was appointed to the Board in May 2013 and is a U.S. citizen, resident in Houston, Texas. He is Of Counsel with the legal firm of Thompson & Knight and has over 40 years of experience in the U.S. oil and gas industry, with a focus on mergers and acquisitions, public and private financings, and U.S. capital market activities, representing U.S. and foreign E&P companies, master limited partnerships and other energy companies. He has been recognised by his peers to be a leading lawyer in oil and gas transactions and in securities and corporate finance.

Mr Baden holds a Juris Doctor Degree from Case Western Reserve University, and a Bachelor of Science (Economics) Degree from the Wharton School of the University of Pennsylvania.

2. Executive Officers

Ross A Keogh

President of PEI and Group Chief Financial Officer

Mr Keogh joined the Company in 1989 and has over 35 years of experience in the oil and gas industry. Between 1979 and 1989, Mr Keogh worked in the financial accounting and budgeting divisions of Total Oil Company and as Joint Venture Administrator for Bridge Oil Limited in Australia. Mr Keogh holds a Bachelor of Economics degree, with a major in Accounting, from Macquarie University in Sydney. Mr Keogh was appointed Chief Financial Officer in November 1998 until April 2002, and appointed President of PEI in April 2002. Mr Keogh took on the extended role of Group Chief Financial Officer in February 2012, in addition to his current role of President of PEI.

Paul Gahdmar

Company Secretary and Group Financial Controller

Mr Gahdmar joined the Company in 1999 as the Financial Accountant of the Petsec Energy Ltd group and has since held a number of management positions within the Company. Mr Gahdmar was appointed as the Company Secretary of Petsec Energy Ltd in 2008 and has over 25 years of experience in corporate accounting and finance in listed companies within the mining and resources industry. Mr Gahdmar holds a Master of Business and Technology degree from The University of New South Wales and a Diploma in Investor Relations from the Australasian Investor Relations Association. Mr Gahdmar is a Fellow of the Institute of Public Accountants and a Member of the Australian Institute of Company Directors.

3. Directors' meetings

The Board has a formally constituted Audit Committee and a Nomination and Remuneration Committee, of which Mr Mortimer and Mr Baden (non-executive directors) are members. Mr Mortimer chairs both committees.

The number of directors' meetings (including meetings of committees of directors) and number of meetings attended by each of the directors of the Company during the financial year are:

	Regular Board Meetings	Additional Board Meetings	Audit Committee Meetings	Nomination & Remuneration Committee Meetings
Total number held during the year	***8***	***6***	***4***	***3***
T N Fern [1]	8	6	4	3
S W Bokhari [1, 2]	5	-	3	1
D A Mortimer	8	6	4	3
A P Baden	8	6	4	3

[1] *Mr Fern and Mr Bokhari attended the Audit and Nomination & Remuneration Committee meetings as invitees.*
[2] *Mr Bokhari was appointed as Managing Director of Petsec Energy Ltd on 1 May 2019.*

4. Remuneration report

The Remuneration Report is set out on pages 24 to 32 and forms part of the Directors' Report for the financial year ended 31 December 2019.

5. Principal activities

The principal activities of the Group during the course of the year were oil and gas development and production onshore and coastal waters of the Louisiana Gulf Coast region, and the shallow waters of the Gulf of Mexico, USA and in the MENA region.

There have been no significant changes in the nature of these activities during the year.

During the year, the Group relocated its corporate registered office in Sydney, Australia and closed its Lafayette office in Louisiana, USA as part of cost cutting initiatives aimed at rationalising operations and minimising general and administrative costs. The Houston office has been retained as the Group's operational office in the USA.

6. Financial review

The Group incurred a net loss after tax of US$24.2 million for the twelve months ended 31 December 2019 (previous corresponding period: net loss after tax of US$10.1 million) after the recognition of dry hole and impairment expense of US$13.8 million, net financial expense of US$3.7 million, and depreciation, depletion and amortisation ("DD&A") expense of US$2.6 million.

Dry hole and impairment expense of US$13.8 million mainly comprised the dry hole cost of the Main Pass Block 273 B-2 well (US$6.4 million) and the recognition of an impairment expense of US$7.3 million against the Hummer Gas/Oil Field due to a reduction in reserves, based on the results of the B-2 well.

Financial expense of US$3.7 million comprised expenses incurred in connection with the convertible note facility – facility fees, interest expense and movements in the fair value of the financial derivative component of the convertible note liability.

Net oil and gas revenues of US$1.1 million were derived for the current period, from production of 368 MMcfe at an average natural gas equivalent sales price of US$2.96/Mcfe. This was 65% lower than the net oil and gas revenues generated in the previous corresponding period of US$3.1 million due to lower production volumes coupled with the lower average natural gas equivalent sales price received.

Net production of 368 MMcfe in the current period was derived from the Main Pass Block 270 B-1 well on the Hummer Gas/Oil Field in the shallow waters in the Gulf of Mexico, USA, and the Williams No. 2 well on the Mystic Bayou Field, onshore Louisiana, USA. This was 54% lower than the previous corresponding period primarily due to production decline in both fields.

The Group realised an average net gas equivalent sales price of US$2.96/Mcfe in the current period. This was 25% lower than the US$3.93/Mcfe achieved for the previous corresponding period. The Group received average sales prices of US$2.22/Mcf and US$58.87/bbl for its natural gas and oil/condensation production, respectively. This compares to US$3.12/Mcf and US$65.89/bbl received respectively, in the previous corresponding period.

Operating expenses (i.e. (lease operating and geological, geophysical and administrative expense) of US$4.5 million (previous corresponding period: US$6.1 million) were lower in the current period, mainly reflecting the ongoing effort to reduce GG&A costs across the Group's geographical segments.

The Group recorded negative earnings before interest, income tax, depreciation, depletion and amortisation, and exploration expense ("EBITDAX") of US$3.6 million for the current period (previous corresponding period: negative EBITDAX of US$2.9 million).

Depreciation, depletion and amortisation ("DD&A") expense was US$2.6 million in the current period (previous corresponding period: US$1.8 million).

Financial position

At 31 December 2019, the Group's cash deposits were US$0.7 million (31 December 2018: US$4.5 million). The cash deposits are predominantly held in US dollars and include restricted cash amounts of US$0.1 million (US$1.9 million restricted cash at 30 December 2018).

As at 31 December 2019, the Consolidated Entity has a cash balance (excluding restricted deposits of US$46,000) of US$645,000 (31 December 2018: US$2.6 million) and current net liabilities of US$647,000 (31 December 2018: current net assets US$0.5 million).

Financial position (continued)

As at 31 December 2019, the Group had drawn down US$13.5 million under its US$15 million Convertible Note Facility Agreement.

7. Operations review

Petsec Energy Ltd (the "Company") is an independent oil and gas exploration and production company listed on the Australian Stock Exchange (ASX Ticker: PSA) and is traded over the counter in the USA in the form of American Depositary Receipts (symbol: PSJEY). The Company has operations in the shallow waters of the Gulf of Mexico and onshore Louisiana, USA and in the Republic of Yemen.

USA

Production

Petsec Energy holds interests in three production fields in the USA – the Jeanerette and Mystic Bayou Fields, onshore Louisiana, and the Hummer Gas/Oil Field offshore Gulf of Mexico. The Company produced 368 MMcfe in the twelve months to 31 December 2019, from the Main Pass Block 270 B-1 well on the Hummer Field and the Mystic Bayou Field, onshore Louisiana USA.

Main Pass Block 270 B-1 well – Hummer Gas/Oil Field (Main Pass 270/273/274)
Petsec: 12.5% working interest (10.7431% net revenue interest)

The Main Pass Block 270 B-1 well on the Hummer exploration prospect in 215 feet of water, offshore Louisiana (federal waters) was drilled during the second half of 2015 and brought into production on 21 November 2017.

The well contributed 299 MMcfe to production for the year.

Williams No.2 well – Mystic Bayou Field
Petsec: 25% working interest (18.5% net revenue interest)

The Williams No.2 gas/condensate discovery well on the Mystic Bayou Field in St. Martin Parish, Louisiana was drilled and brought into production on 31 August 2015.

The well contributed 69 MMcfe to production for the year.

Adeline Sugar Factory No. 4 Well – Jeanerette Field
Petsec: 12.5% working interest (9.2% net revenue interest)

The Adeline Sugar Factory ("ASF") No. 4 well located in St. Mary Parish, Louisiana was drilled and brought into production in June 2014. The well was shut-in in mid-November 2015 due to high water production and a restriction in the tubing due to salt build-up. The well has produced on an intermittent basis since that time, and it's the operator's intention to continue with intermittent production for the near-term.

7. Operations review (continued)

Development

Main Pass Block 270 B-1 well – Hummer Gas/Oil Field (Main Pass 270/273/274)

Petsec: 12.5% working interest (10.26354% net revenue interest and 0.441% overriding royalty interest)

The Hummer Gas/Oil Field encompasses Main Pass Blocks 270,273 and 274, in the Gulf of Mexico, offshore Louisiana, USA. The Hummer Field structure extends over a strike of five miles within the Main Pass Block 270, 273 and 274 leases which cover 15,000 acres, in some 200 feet of water.

The Hummer Gas/Oil Field was discovered in late 2015, the Main Pass 270 "B" production platform and export pipelines were set in late 2017, and first production from the B-1 discovery well commenced in November 2017.

With a view to further development of the Hummer Gas/Oil Field, the Main Pass 270 "B" platform was built with three well slots and sufficient space available on the deck to expand production capacity and accommodate increased production from additional wells expected to be drilled from the "B" platform and any proximal well head platforms.

On 19 August 2018, the Main Pass Block 273 B-2 appraisal/development well was spud and drilled from the Main Pass Block 270 "B" Production Platform. The B-2 well had a bottom-hole location some 6,000 feet to the east of the B-1 discovery well, a significant step-out from the Main Pass 270 B-1 discovery well. The primary objectives of the well were two sand reservoirs that were encountered in the B-1 well, one of which was completed and produces in the B-1, and the other identified as proven undeveloped by Cawley, Gillespie & Associates, the Company's independent reserve engineers.

The B-2 well was drilled to a final depth of 15,990 feet TVD/17,570 feet MD in March 2019 and did not encounter commercial hydrocarbons. While the B-2 wellbore encountered numerous thin and stratigraphic oil and gas pay zones, the two primary objectives of the well were non-reservoir quality or absent at the well location.

The joint venture deemed the primary objectives in the deeper section of the well to be uneconomic for production, and therefore it was decided to permanently plug and abandon the open hole portion in the bottom of the well. In the shallower section, where pipe had already been set, certain pay zones may potentially be commercial subject to commodity prices. In order to maintain the option to complete and produce in the future, the B-2 well was temporarily abandoned and the rig moved off location.

Petsec Energy's share of the drilling costs of the B-2 well of US$6.4 million has been expensed.

MENA

Yemen

The Company holds rights in two blocks in Yemen, 80 kilometres apart in the Marib Basin - Damis Block S-1 Production Licence and Al Barqa, Block 7 Exploration Licence.

Damis (Block S-1) is located approximately 80 kilometres to the southwest of Block 7 and holds five sizeable oil and gas discoveries. The developed An Nagyah Oilfield has produced around 25 million barrels of oil since start of production in 2004 out of the original recoverable reserves of 50 million barrels of oil. An Nagyah Oilfield was productive until it was suspended in 2014. The other four undeveloped oil and gas fields are Osaylan, An Naeem, Wadi Bayhan, and Harmel. The Damis Block S-1 contains has target resources in excess of 54 million barrels of oil and 550 Bcf of natural gas. The An Nagyah Oilfield is developed with 32 wells and has associated production facilities capable of producing 20,000 bopd, connected by an 80,000 bopd pipeline to the Marib Pipeline which terminates at the Ras Isa Oil Export Terminal on the Red Sea to the West. The Marib Pipeline and Ras Isa Oil Export Terminal have been shut since March 2015 due to the conflict between Houthi rebels and the legitimate Federal Government.

Al Barqa, Block 7 is a 5,000 square kilometre (1,235,527 acres) area on which two exploration wells were drilled in 2010 to test the Al Meashar prospect. The two wells encountered oil and on a limited production test flowed oil to surface which indicates the potential of a substantial resource.

Damis (Block S-1), Republic of Yemen

Operations at the Company's An Nagyah Oilfield in Block S-1 continue to be shut-in while the Company seeks to secure government approvals to allow the Company to transport oil and access Yemen Government owned pipeline, storage and oil export shipping facilities in neighbouring Block 4.

7. Operations review (continued)

Damis (Block S-1), Republic of Yemen (continued)

The operating environment in the Shabwah Governorate, within which both Block S-1 and Block 7 are located, continues to improve. In April 2018, Austrian oil company OMV, became the first foreign oil company to restart production in Yemen since the industry wide shut-in of March 2015.

OMV has maintained oil production of the order of 16,000 bopd in the neighbouring Block S-2 from its Habban Oilfield (350 million barrels), 70 kilometres North East of An Nagyah Oilfield and 14 kilometres West of the Al Meashar oil discovery in Block 7. Habban oil is transported by truck South to the Main Oil Pumping Station (MOPS) near the West Ayad Oilfield at the head of the Block 4 export pipeline, then piped some 200 kilometres South to the Rudum Oil Terminal located at Bir Ali on the coast of the Gulf of Aden. Shipments of some 600,000 barrels of oil is made every 6 to 7 weeks.

Construction of a 16-inch oil transport pipeline connecting Block 5 (to which Block S-1 is connected) to the oil export pipeline of Block 4 at MOPS, is nearly complete and pre-startup testing is currently underway. The Yemen Oil Ministry expects it to be operational by end March 2020. This pipeline will connect Block S-1 to the Rudum Terminal in Bir Ali on the southern coast making it possible for crude to flow from Block S-1 to the Rudum terminal for further shipment. This route is in a more politically stable environment. The Company plans to pump oil 27 kilometres NW to Block 5 through the existing Block S-1 10-inch pipeline and then to the Main Oil Pumping Station (MOPS) in Block 4 through the newly constructed 80 km, 16-inch pipeline. From MOPS, oil will be pumped 204 kilometres South to Rudum Terminal at Bir Ali.

The Company has been seeking, since early 2017, the necessary government support and formal approvals to transport oil market. Initial request was to transport crude by truck to Petro Masila's Block 10 and then pipe to terminal at Mukalla, then in the past year the request was revised to truck crude to Block 4, and now the plan is to transport crude entirely through the pipeline system through Block 5 and Block 4 to the Rudum oil export terminal at Bir Ali.

Access to these facilities are part of the Contractor's rights contained within the Block S-1 Production Sharing Agreement. Delays have been due to limited and changing Yemen administration capabilities, political changes, and security conditions.

We have engaged with the Oil Minister, His Excellency Aws Al-Awd, since his appointment in January 2018, seeking his support for the restart of production at the An Nagyah Oilfield. Documentation supporting the Company's technical and financial capabilities to restart production at the An Nagyah Oilfield was supplied to the Minister of Oil and Minerals during the September 2018 quarter for his review and approval.

Petsec Energy's Chairman, Terrence Fern and Managing Director, Syed Bokhari, met with the Yemen Minister of Oil & Minerals, Aws Al Awd, in May 2019 to share the Company's restart plans for the An Nagyah Oilfield with supporting technical and financial capabilities. The Minister showed considerable interest in the restart plan, expressing a desire to have the field in production within 6 months to coincide with the expected completion of a 16-inch oil pipeline connecting Block 5 (to which Block S-1 is already connected) to the Block 4 export pipeline. He also encouraged Petsec to seek joint venture partners to co-invest in the development of Block S-1 which holds four undeveloped fields in addition to the developed An Nagyah Oilfield.

Subsequent to the meeting with the Minister, Petsec sent a team of oil field production experts in June 2019 to the An Nagyah Oilfield in the Shabwah Province of Yemen to evaluate the condition of the facilities and prepare final production start-up plans. The evaluation team consisted of an international production facilities expert, four Yemeni oil field professionals, Petsec Energy staff, and a representative of the Yemen Ministry of Oil & Minerals.

The team found the facilities to be in good condition allowing for an early production start-up. Local staff and contractors were keen to see an early restart of production. Final plans are nearly complete for the production start-up that include all technical work, equipment/services required, contract support, manpower ramp up, oil transport and access to export facilities. It is expected this plan will be concluded within a month of receipt of the Yemen governments consents allowing for an immediate restart of onsite operations. It is expected that oil production can commence within 3 months of the Company's occupation of Block S-1. The Company's engineers estimate the cost to restart oil production at An Nagyah will be under US$5 million, and would take between 6 and 12 months to reach a peak rate of 10,000 bopd from the time of receipt of Yemen Government approvals to access Block 4 oil export facilities.

In response to the Minister's wish that Petsec Energy seeks further investors in the development of Yemen oil resources, Petsec has engaged with several E&P companies interested in a joint venture partnership with Petsec Energy in Block S-1 which includes the An Nagyah Oilfield. These discussions are ongoing.

7. Operations review (continued)

Damis (Block S-1) (continued)

Post 30 September 2019, the government run Safer Exploration Production Oil Company (SEPOC) has started production of 5,000 bopd from Block 18 and is trucking it South all the way to Rudum Terminal at Bir Ali. This is a significant development as Block 18 is a major oil producer for the country, producing on average 35,000 bopd prior to rebel control of the Marib Export Pipeline. SEPOC's Block 18 and Petsec's Block S-1 are connected by pipeline to Block 5 which will soon be connected to Block 4 following completion of the 80-kilometre, 16-inch pipeline.

Completion of this pipeline, restart of production from Block 18, and the recent declaration by the Yemen Oil Minister that Blocks 5 and S-1 will be in production in early 2020, demonstrates the government's desire to bring all fields in the Shabwah region back into production.

Block 7, Al Barqa Permit, Republic of Yemen

Petsec: 75% working interest (63.75% participating interest)

Petsec Energy acquired its interest over the period 2014-2017.

Block 7 is an onshore exploration permit covering an area of 5,000 square kilometres (1,235,527 acres) located approximately 340 kilometres east of Sana'a. The block contains two wells that were drilled on the Al Meashar prospect as well as an inventory of leads and prospects identified by 2D and 3D seismic surveys with significant oil potential.

The Company has operatorship and holds a 75% working interest (63.75% participating interest) in the Al Barqa (Block 7) Joint Venture. It also had an agreement with KUFPEC to acquire their 25% working interest in Block 7 to potentially bring the Company's interest in the block to 100% pending customary approvals from the Government. The Government approvals had not been received as of balance date, and the agreement with KUFPEC expired.

Block 7 contains two suspended discovery wells that were drilled on the Al Meashar oil prospect and is located 14 kilometres East of OMV's Habban Oilfield which holds ultimate reserves of 350 million barrels of oil, in the same reservoir rocks as Al Meashar. In 2010-11, limited production tests of the two Al Meashar wells flowed oil to surface which indicates a potential substantial resource.

Oil and Gas Reserves

Petsec Energy Group Net Reserves as of 1 January 2020

Oil Equivalent (Mboe [1])	Net Proved Reserves [3]	Net Probable Reserves [3]	Net Proved and Probable Reserves [3]
USA Reserves [2]			
Reserves as of 1 January 2019	2,729.4	739.7	3,469.1
Additions/(revisions)	(592.4)	(0.1)	(592.5)
Production	(61.6)	-	(61.6)
USA reserves as of 1 January 2020	2,075.4	739.6	2,815.0
Developed	*180.2*	*-*	*180.2*
Undeveloped	*1,895.2*	*739.6*	*2,634.8*
Yemen Reserves [2]			
Reserves as of 1 January 2019	4,540.0	1,108.0	5,648.0
Additions/(revisions)	-	-	-
Yemen reserves as of 1 January 2020	4,540.0	1,108.0	5,648.0
Developed	*4,540.0*	*1,108.0*	*5,648.0*
Undeveloped	*-*	*-*	*-*
Total Petsec Group Reserves			
Total Petsec Group Reserves as of 1 January 2020	**6,615.4**	**1,847.6**	**8,463.0**
Developed	***4,720.2***	***1,108.0***	***5,828.2***
Undeveloped	***1,895.2***	***739.6***	***2,634.8***

Footnotes

1. *Mboe = One thousand barrels of oil equivalent (using a ratio of approximately six thousand cubic feet of natural gas to one barrel of oil).*
2. *The USA and Yemen reserve assessments presented in the table above and throughout this report are consistent with the announcement released to the ASX on 24 February 2020. The Company confirms that it is not aware of any new information or data that materially affects the information included in these announcements, and that all the material assumptions and technical parameters underpinning the estimates therein continue to apply and have not materially changed.*

   The U.S. reserves are stated for the Jeanerette, Mystic Bayou and Main Pass Block 270/273 fields. U.S. 2P reserves were 10.4 Bcf of gas and 981 Mbbl of oil. The Yemen reserves are stated only for oil in the An Nagyah Oilfield and are unchanged from the assessment announced to the ASX on 15 March 2016 using a Brent price of US$30/bbl and 5,000 bopd trucked 580 kilometres to PetroMasila's Block-14 truck unloading facilities.
3. *Net reserves mean those reserves representing the Company's net revenue interest (or net economic interest) which is the Company's working interest less royalties payable in the USA, and after all costs - operational, government taxes and government participation in Yemen, according to the terms of the Participating Agreement with the Yemen government.*

To ensure accuracy and compliance of reserves estimations, the Company has put in place a robust process that incorporates the following governance arrangements and internal controls:

- At least once a year, as part of the year-end reporting procedures, the Company's producing oil and gas reserves are to be reviewed by an external, independent expert. The independent verified reserves are to be used as the basis for depreciation, depletion and amortisation calculations.
- All releases or reports containing statements of reserves are to be in accordance with ASX listing rules, requiring sign-off for content and context by an appropriately qualified person and in accordance with the Company's Reserves Policy.

8. Objectives, strategy and future performance

It is the Group's objective to increase the value of the Company and thus shareholder value through successful oil and gas exploration, development, and production, and through acquisitions. The Group's strategy to meet the above objective is to produce its current reserves, pursue participation in high quality, high impact exploration drilling opportunities in the Gulf Coast onshore Louisiana and offshore Gulf of Mexico, USA. The Group also intends to explore opportunities to acquire onshore producing oil and gas reserves in MENA which hold significant development, exploitation potential.

The Group's strategy takes into account the expected operating and market conditions, together with general economic conditions, which are inherently uncertain. The Group has in place, structured and proactive risk management and internal control systems to manage material risks. Certain of those risks are inherent to the Group's business, such as drilling for, producing and marketing oil and gas. Although the Group is committed to minimising its risk exposure, many risks are largely beyond the control of the Group and its directors. Moreover, other more general risks associated with the vicissitudes of commercial life, political change, and cyclical economic conditions are risks that the Group cannot control. The following are those risks which management and the Board consider to be material business risks that could adversely affect the achievement of the financial prospects of the Company discussed above:

Drilling and Production Risks

Drilling for oil and natural gas is subject to numerous risks. Paramount is the risk that drilling operations will not result in the discovery of commercially productive oil or natural gas reservoirs. Also, projects are subject to economic risks. Before beginning a drilling project, the Company can only estimate the cost of drilling and completing wells as many indeterminable factors can affect the total cost. For example, oil and natural gas drilling and production activities may be extended, shortened, delayed or cancelled as a result of a variety of factors, many of which are beyond the Company's control. These risks may negatively impact the economics of drilling projects. In part, these factors include:

- Unexpected drilling conditions including abnormal geological pressure or irregularities in formations;
- Equipment failures or accidents;
- Weather conditions, including hurricanes and other tropical weather disturbances;
- Shortages in experienced labour;
- Shortages, delays in the delivery, or high cost of drilling rigs and equipment;
- Constraints on access to transportation systems (pipelines) delaying sale of oil and natural gas;
- Reduction or losses of resources or reserves;
- Acquiring and maintaining title to its interests;
- Unresolved landowner or regulatory issues; and
- Inability of third-party joint venture partners to participate in or fund their share of drilling and production activities.

Operating Risks

The exploration for and development and production of oil and natural gas involves a variety of industry operating risks. If any of these industry-operating risks occur, the Company could have substantial losses. Substantial losses could include injury or loss of life, severe damage to or destruction of property, natural resources and equipment, pollution or other environmental damage, clean-up responsibilities, regulatory investigation and penalties and suspension of operations. These risks include:

- Fire, explosions, blow-outs and surface cratering;
- Lost or damaged oilfield drilling pipe and service tools;
- Casing or cement failures;
- Environmental hazards caused by oil spills, natural gas leaks, pipeline ruptures or discharges of toxic gases; and
- Hazards of marine operations such as capsizing, collision and adverse weather and sea conditions.

8. Objectives, strategy and future performance Marketing and Sales Risks (continued)

Pricing Risks

The marketing and sale of oil and natural gas is subject to the risk of adverse commodity price fluctuations that impact cash flow. Some factors that affect commodity prices include:

- Relatively minor changes in the supply of and demand for oil and natural gas;
- Market uncertainty;
- The level of consumer product demand;
- Weather conditions;
- Domestic and foreign governmental regulations;
- The price and availability of alternative fuels;
- Technological advances affecting oil and natural gas consumption;
- Political and economic conditions in oil producing countries, particularly those in the Middle East;
- Policies of the Australian, U.S. and Yemen governments;
- The foreign supply of oil and natural gas;
- The price of oil and natural gas imports; and
- General economic conditions.

To reduce the impact of price fluctuations, from time to time, the Company has used derivative financial instruments, such as natural gas swaps, puts and costless collars, on a portion of its future production. However, such hedging activities may not be sufficient to protect the Company against the risk of price declines and may limit income and liquidity if prices rise.

- Hedging activities that are intended to reduce the risk of downward price fluctuations on a portion of our future production may limit the Company's potential income if oil and gas prices rise above a level established by its hedge instruments.
- Hedging counterparties require collateral when the mark-to-market value of our hedge instruments is in the counterparties' favour and exceeds the Company's credit limits with such counterparties. As a result, the Company may be required to provide substantial security to the counterparties when commodity prices change significantly. The security provided may be in the form of cash or letters of credit, and thus, could have a significant impact on the Company's liquidity.

Exchange Rate Risks

Adverse exchange rate variations between the U.S. dollar and the Australian dollar may impact upon cash balances held in Australian dollars. Since most of the Company's operations are conducted in U.S. dollars, the Company generally maintains a substantial portion of its cash balances in U.S. dollar accounts. Occasionally, however, it may have some cash deposits in Australian dollar accounts. Until these funds are converted into U.S. dollars, the U.S. dollar value of the deposits will change as the exchange rate between the two currencies fluctuates.

Other Risks

Other factors can impact the environment in which the Company operates and thus can affect its ability to perform as desired. Such factors include:

- Changes in legislation and Government regulation both in the USA and in other countries in which the Company operates.
- Political and societal risks from wars, social and ethnic unrest, changes in government and insurgencies in the districts, regions and countries in which the Company operates;
- Environmental risks from existing and new regulations and standards being applied in the jurisdictions in which the Company operates;
- General economic conditions in the countries in which the Company operates;
- Stock market conditions in Australia;
- Fluctuations in asset values; and
- Availability of and access to capital.

9. Dividends

Directors do not recommend the payment of a dividend for the financial year ended 31 December 2019. No dividends were paid during the financial year.

10. Significant changes in state of affairs

There were no significant changes to the state of affairs of Petsec Energy during the financial year, other than those detailed in the "Financial review" and "Operations review" sections of this report.

11. Environmental regulation

The Group's oil and gas exploration and production activities are subject to significant environmental regulation under U.S. Federal and State legislation and Republic of Yemen legislation.

The Group is committed to achieving a high standard of environmental performance and compliance with all lease conditions. Directors are not aware of any breach of environmental compliance requirements relating to the Group's activities during the year.

12. Likely developments

The Group's focus in 2020 will be:

USA:

- No exploration or development work is anticipated.
- Continuing evaluation of its strategy and alternatives for its assets in the U.S.

MENA:

- Completion of the final restart plan for the An Nagyah Oilfield to enable immediate return to the field and restart of operations on receipt of the requisite Yemen administrative consents.
- Continuing engagement with interested potential joint venture partners in Block S-1.
- Continued engagement with Government agencies to obtain the required consents to transport oil via Block 4 to Rudum Terminal at Bir Ali.
- Rationalisation of MENA operations in preparation for restart, and minimising GG&A costs until such time as government consents are obtained.

13. Directors' interests

The relevant interest of each director in the shares or options over such instruments issued by the Company, as notified by the directors to the Australian Securities Exchange in accordance with S205G (1) of the Corporations Act 2001, at the date of this report is as follows:

Director	Ordinary Shares	Options over Ordinary Shares
T N Fern	37,876,361	Nil
D A Mortimer	12,241,098	Nil
S W Bokhari	Nil	Nil
A P Baden	Nil	Nil

14. Share options

Options granted to directors and officers of the Company

As at 31 December 2019, there were 8,200,000 options over ordinary shares (pursuant to Employee Option Plan) in Petsec Energy Ltd on issue.

During or since the end of the financial year:

- No options over ordinary shares were granted under the Employee Option Plan to key management personnel of the Company as part of their remuneration.
- 5,000,000 share options were forfeited under the Employee Share Plan by key management personnel.

The Company will issue 5,000,000 options to Mr Bokhari, Managing Director of Petsec Energy Ltd, as part of his remuneration, subject to obtaining shareholder approval at its next General Meeting, currently scheduled in May 2020. The options will be issued at 20 cents each under the Employee Option Plan

During or since the end of the financial year, no ordinary shares have been issued by the Company as result of the exercise of options.

15. Indemnification and insurance of officers

During the year ended 31 December 2019, the Company maintained policies of insurance in respect of directors and officers liability. The policies insure persons who are directors or officers of the Company and its controlled entities against certain costs and expenses which may be incurred by them in defending proceedings and against other liabilities which may arise from their positions. The insured directors and officers are the directors, executive officers and secretaries of the Company and the directors, executive officers and secretaries of controlled entities.

The insurance contracts prohibit the disclosure of particulars of the premiums and the nature of the liabilities insured.

The Company has entered into Deeds of Indemnity and Access with directors on the terms approved by shareholders. The agreements stipulate that the Company will meet the full amount of any liabilities to another person that might arise from their position (except where the liability arises out of conduct involving a lack of good faith).

The Company has made during or since the end of the financial year no payments in relation to indemnification. The Company provides the normal indemnities to directors and officers in relation to the work carried out on behalf of or at the request of the Company.

16. Non-audit services

The Company's auditor, KPMG, may perform certain other services in addition to their statutory duties.

The Board considers the non-audit services provided during the year by the auditor and in accordance with advice provided by resolution of the audit committee, is satisfied that the provision of those non-audit services during the year by the auditor is compatible with, and did not compromise, the auditor independence requirements of the Corporation Act 2001 for the following reasons:

- All non-audit services were subject to the corporate governance procedures adopted by the Company and have been reviewed by the audit committee to ensure they do not impact the integrity and objectivity of the auditor; and
- The non-audit services provided do not undermine the general principles relating to auditor independence as set out in APES 110 *Code of Ethics for Professional Accountants*, as they did not involve reviewing or auditing the auditor's own work, acting in a management or decision-making capacity for the Company, acting as an advocate for the Company or jointly sharing risks and rewards.

Details of the amounts paid to the auditor of the Company, KPMG, and its related practices for audit and non-audit services provided during the year are set out in note 7 of the accompanying Financial Statements.

17. Lead auditor's independence declaration

The Lead Auditor's Independence Declaration is set out on page 35 and forms part of the Directors' Report for the financial year ended 31 December 2019.

18. Rounding off

The Company is of a kind referred to in ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191 dated 24 March 2016 and in accordance with that Class Order, amounts in the Financial Report and Directors' Report have been rounded off to the nearest one thousand dollars, unless otherwise stated.

19. Events subsequent to balance date

As announced to the ASX on 19 February 2020, a claim was made on the Letter of Credit issued under the Production Sharing Agreement on Block 7. In Petsec's opinion, the claim is fraudulent and was made by the illegitimate rebel Houthi Minister for Oil and Minerals. Despite concerted efforts by Petsec to prevent any action on the claim, the Qatar National Bank released the US$1.68 million of restricted cash that was on deposit as collateral to support the Group's Letter of Credit. Other banks also responded to the fraudulent claim and the Company is working with its legal advisors to pursue all options it has to recover the funds.

The Company was also advised by Mitsui that the Commonwealth Bank Australia had also released US$1.05 million of AWE/Mitsui's funds in response to a similar claim. Mitsui is seeking to recover these funds from Petsec and the Company is seeking further information from AWE/Mitsui and will defend any action to recover the funds.

Other than the matter disclosed above, there has not arisen in the interval between the end of the financial year and the date of this report any item, transaction or event of a material and unusual nature likely, in the opinion of the directors of the Company, to affect significantly the operations of the Group, the results of those operations, or the state of affairs of the Group, in future years.

This report is made with a resolution of the directors:

T N Fern
Director

Sydney, 28 February 2020

20. Remuneration Report – Audited

20.1 Introduction

This Remuneration Report forms part of the Directors' Report. It outlines the overall remuneration strategy, framework and practices adopted by the Company and the Group ("Petsec Energy Group") for the year ended 31 December 2019 and has been prepared in accordance with Section 300A of the *Corporations Act 2001* and its regulations.

In accordance with the *Corporations Act 2001*, remuneration details are disclosed for the Petsec Energy Group's Key Management Personnel.

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Petsec Energy Group. Key management personnel comprise the directors of the Company and senior executives of the Petsec Energy Group, whose names appear in the tables in section 20.5 of this report.

20.2 Executive summary

The Board's remuneration policy is to provide fair and market competitive levels of remuneration for all employees, including directors and key management personnel in order for the Company and the Petsec Energy Group to benefit by attracting and retaining a high-quality team.

The Company has a Nomination and Remuneration Committee to assist the Board in the implementation and administration of the remuneration policy – refer to *section 20.3,* below.

The key developments during the year in the implementation and administration of the remuneration policy included:

- The annual review of key management personnel performance.
- Annual review of the Nomination & Remuneration Committee Charter.

20.3 Nomination and Remuneration Committee

The Nomination and Remuneration Committee oversees the appointment and induction process for directors and committee members, and the selection, appointment and succession planning process of the Company's Chief Executive Officer. The Committee makes recommendations to the Board on the appropriate skill mix, personal qualities, expertise and diversity of each position. When a vacancy exists or there is a need for particular skills, the Committee in consultation with the Board determines the selection criteria based on the skills deemed necessary.

The Committee reviews and makes recommendations to the Board on compensation packages and policies applicable to the executive officers and directors of the Petsec Energy Group. It is also responsible for oversight of diversity, employee share and option schemes, incentive performance packages, superannuation entitlements, retirement and termination entitlements, fringe benefits policies, deeds of access and indemnity, and professional indemnity and liability insurance policies.

Executive compensation and other terms of employment are reviewed annually by the Nomination and Remuneration Committee having regard to performance against goals set at the start of the year, relevant corporate information and where appropriate independent expert advice.

The Nomination and Remuneration Committee comprised the following members during the year:

- D A Mortimer (Chairman) – Independent Non-executive Director
- A P Baden – Independent Non-executive Director

The Board policy is that the Nomination and Remuneration Committee will comprise a majority of non-executive directors and a non-executive chairman.

20. Remuneration Report – Audited (continued)

20.3 Nomination and Remuneration Committee (continued)

The Nomination and Remuneration Committee meets at least twice a year and as required. The Committee met three times during the year and the Committee members' attendance record is disclosed in the table of directors' meetings.

The Nomination and Remuneration Committee's Charter is available on the Company's website www.petsec.com.au.

20.4 Principles of compensation

Compensation levels for key management personnel are competitively set to attract and retain appropriately qualified and experienced directors and senior executives. The Nomination and Remuneration Committee obtains peer comparisons and/or independent advice on the appropriateness of compensation packages of the Petsec Energy Group, given trends in comparative companies both locally and internationally and the objectives of the Company's compensation strategy.

The compensation structures explained below are designed to attract suitably qualified candidates, reward the achievement of the Company's objectives, and achieve the broader outcome of creation of value for shareholders.

The compensation structures take into account:

- The capability and experience of the key management personnel; and
- The ability of key management personnel to control the relevant performance of their segment of operation.

Compensation packages include a mix of fixed compensation and performance-based incentives, including equity-based incentives as set out below.

In addition to their salaries, the Petsec Energy Group also provides non-cash benefits to its key management personnel as set out below, and contributes to several post-employment defined contribution superannuation plans in Australia and also matches contributions made by U.S. based key management personnel to a voluntary savings plan under Section 401(k) of the U.S. tax code.

Fixed compensation

Fixed compensation consists of base compensation (which is calculated on a total cost basis and includes any FBT charges related to employee benefits), as well as employer contributions to superannuation funds in Australia and employer matching contributions to voluntary savings plans under Section 401(k) of the U.S. tax code. Non-cash benefits comprise employer payments towards U.S. health, dental and vision plans, as well as life and salary continuance insurance benefits.

The Nomination and Remuneration Committee reviews compensation levels and other terms of employment annually through a process that considers individual, segment and overall performance of the Company against goals set at the start of the year. In addition, where necessary, external consultants provide analysis and advice to ensure the directors' and senior executives' compensation is competitive in the market place.

Performance-linked compensation

Performance-linked compensation includes both short-term and long-term incentives and is designed to reward key management personnel for meeting or exceeding the Company's financial objectives and agreed individual objectives. The short-term incentive (STI) is an "at risk" bonus provided in the form of cash or ordinary shares in the Company, while the long-term incentive (LTI) is provided as either shares or options over ordinary shares of the Company under the rules of the Employee Share and Option Plans approved by shareholders at the Annual General Meeting held on 17 May 2018 (see note 17(b) to financial statements). The maximum number of securities in aggregate that may be issued under the Employee Share and Option Plans is 21,033,215.

20. Remuneration Report – Audited (continued)

20.4 Principles of compensation (continued)

Short-term incentive

Short-term incentives are provided to key management personnel through discretionary bonuses as determined and granted by the Company's Nomination and Remuneration Committee. Factors considered by the Committee when granting discretionary bonuses include personal performance, the achievement of strategic objectives, and the retention and motivation of employees.

No short-term incentives were awarded to key management personnel during the year.

Long-term incentive

Certain key management personnel are also provided with long-term incentives through participation in the Company's Employee Share and Option Plans, subject to the approval of the Committee. Key management personnel are typically offered options on an annual basis with the exercise price of the shares or options based on the weighted average market price of the Company's ordinary shares for the five trading days preceding the date of issue, subject to a minimum exercise price of 20 cents.

During the year, no shares or options over ordinary shares were issued to key management personnel as long-term incentive compensation under the Employee Share and Option Plans (previous corresponding period: 10,200,000 options).

Consequences of performance on shareholder wealth

In considering the Group's performance and benefits for shareholder wealth, the remuneration committee have regard to the following indices in respect of the current financial year and the previous four financial years.

	2019	2018	2017	2016	2015
Profit/(loss) attributable to owners of the company	(US$24,241,000)	(US$10,050,000)	(US$11,964,000)	(US$13,024,000)	(US$10,065,000)
Dividend paid	-	-	-	-	-
Closing share price as at 31 December	A$0.056	A$0.105	A$0.105	A$0.17	A$0.078
Change in share price	(A$0.049)	-	(A$0.065)	A$0.092	(A$0.037)

Net loss amounts for 2015 to 2019 have been calculated in accordance with Australian Accounting Standards (AASBs).

Service and employment agreements

Remuneration and other terms of engagement of executive employees are formalised in service agreements that are unlimited in term but capable of termination by varying periods of notice or by payment of an amount in lieu of notice. The service agreements generally outline the components of compensation paid, but do not prescribe how compensation levels are modified from year-to-year. Compensation levels are reviewed each year in light of cost-of-living changes, performance and changes in the scope of the role performed by the executive and changes required to meet the principles of the compensation policy.

20. Remuneration Report – Audited (continued)

20.4 Principles of compensation (continued)

The Executive Chairman, Mr Fern, is engaged via a company of which Mr Fern is a director. The Company may terminate this agreement without cause by giving not less than twelve months' notice, or pay an amount equal to the fees for twelve months in lieu of notice. Mr Fern may terminate the agreement with not less than six months' notice. In the event of a breach of the agreement by the Company, Mr Fern may terminate the agreement by giving one month's notice and would be entitled to a payment equal to fees for a twelve-month period.

The Managing Director, Mr Bokhari, has an employment agreement for an initial 12-month term. On achievement of certain performance hurdles, the agreement may be extended by an additional 12 to 24 months. The agreement may be terminated by either the Company or Mr Bokhari by giving a notice period of three months after the expiration of the initial 12-month period and the additional 12 to 24-month extension which may follow.

The Group Chief Financial Officer and President of Petsec Energy Inc., Mr Keogh has an employment agreement that is capable of termination without cause by the company by a lump sum payment equal to one times his annual Base Salary. Mr Keogh may terminate the agreement without cause by giving the company at least 120 days' notice in writing. In the event of a breach of the agreement by the Company, Mr Keogh may terminate his agreement by giving 30 days' notice and would be entitled to receive a lump sum payment equal to one times their annual base salary at that time.

Non-executive directors

Directors' fees are set having regard to periodic advice from external remuneration consultants, market surveys and the level of fees paid relative to those of other comparable companies. Directors' fees for the 2019 year were unchanged from the 2018 year and comprise base fees, plus statutory superannuation for Australian directors. Directors are also entitled to reasonable travel, accommodation and other expenses incurred in attending meetings or while engaged on Company business.

Non-executive directors do not receive performance-related compensation. Directors' fees cover all main Board activities and membership of committees and are subject to the aggregate limit of A$300,000 approved by shareholders at the 1996 Annual General Meeting.

Non-executive directors appointed prior to 2003 are entitled to receive a retirement benefit equivalent to the remuneration received in the three years prior to retirement. Incoming non-executive directors are not entitled to retirement benefits.

Petsec Energy

Directors' Report

For the year ended 31 December 2019

20. Remuneration Report – Audited (continued)

20.5 Directors' and Executive Officers' Remuneration Report

Details of the nature and amount of remuneration for the key management personnel consisting of each director and executive officer of the Company and the Group are:

			Short-term benefits				Post-employment benefits		Share-based payment			
			Salary & fees US$	Short-term incentive/ retention cash bonus US$	Other benefits US$	Service agreements US$	Super-annuation/ 401K benefits US$	Termination benefits US$	Accounting fair value US$	Total US$	Proportion of remuneration performance related %	Accounting fair value as proportion of remuneration %
Directors [1]												
Executive												
T N Fern [1]	Executive Chairman	**2019**	**-**	**-**	**29,694**	**359,962**	**-**	**-**	**-**	**389,656**	**-**	**-**
(Note 1)		2018	-	-	36,795	456,036	-	-	-	492,831	-	-
S W Bokhari	Managing Director	**2019**	**233,333**	**-**	**20,549**	**-**	**8,458**	**-**	**-**	**262,340**	**-**	**-**
(Note 2)		2018	-	-	-	-	-	-	-	-	-	-
Non-executive												
D A Mortimer [1]	Director	**2019**	**45,286**	**-**	**-**	**-**	**4,302**	**-**	**-**	**49,588**	**-**	**-**
		2018	48,594	-	-	-	4,616	-	-	53,210	-	-
A P Baden	Director	**2019**	**50,000**	**-**	**-**	**-**	**-**	**-**	**-**	**50,000**	**-**	**-**
		2018	50,000	-	-	-	-	-	-	50,000	-	-
Total directors remuneration		**2019**	**328,619**	**-**	**50,243**	**359,962**	**12,760**	**-**	**-**	**751,584**	**-**	**-**
		2018	98,594	-	36,795	456,036	4,616	-	-	596,041	-	-

[1] *Australian-based directors' remuneration amounts are actually paid in Australian dollars and presented in US dollars at the following average FX rates i) 2019 – 0.6967 ii) 2018 – 0.7476.*

20. Remuneration Report – Audited (continued)

20.5 Directors' and Executive Officers' Remuneration Report (continued)

Details of the nature and amount of remuneration for the key management personnel consisting of each director of the Company and executive officer of the Company and the Group are:

			Short-term benefits				Post-employment benefits		Share-based payment			
			Salary & fees US$ *Note 4*	Short-term incentive/ retention cash bonus US$ *Note 5*	Other benefits US$ *Note 6*	Service agreements US$	Super-annuation /401K benefits US$	Term-ination benefits US$	Accounting fair value US$ *Note 7*	Total US$	Proportion of remuneration performance related %	Accounting fair value as proportion of remuneration %
Executives												
R A Keogh	President, PEI and Group Chief Financial Officer	**2019**	**245,833**	**-**	**31,180**	**-**	**12,292**	**-**	**6,980**	**296,285**		**2.4**
		2018	295,000	-	36,455	-	14,750	-	18,331	364,536	-	5.0
M Petkovski [1] *(Note 3)*	Chief Executive Officer of Petsec Energy (Middle Eastern) Limited *(resigned 30 April 2019)*	**2019**	**-**	**-**	**1,141**	**73,345**	**-**	**243,845**	**44,466**	**362,797**	**-**	**12.3**
		2018	-	-	28,402	261,660	-	-	72,068	362,130	-	19.9
P Gahdmar [1]	Company Secretary, Group Financial Controller	**2019**	**119,012**	**-**	**5,675**	**-**	**11,306**	**-**	**20,235**	**156,228**		**13.0**
		2018	143,744	-	13,510	-	13,231	-	34,327	204,812	-	16.8
Total executive remuneration		**2019**	**364,845**	**-**	**37,996**	**73,345**	**23,598**	**243,845**	**71,681**	**815,310**		**8.8**
		2018	438,744	-	78,367	261,660	27,981	-	124,726	931,478	-	13.4
Total directors and executive officer remuneration		**2019**	**693,464**	**-**	**88,239**	**433,307**	**36,358**	**243,845**	**71,681**	**1,566,894**		**4.6**
		2018	537,338	-	115,162	717,696	32,597	-	124,726	1,527,519	-	8.2

[1] *Australian-based executive officers' remuneration amounts are actually paid in Australian dollars and presented in US dollars at the following average FX rates i) 2019 – 0.6967 ii) 2018 – 0.7476.*

20. Remuneration Report – Audited (continued)

20.5 Directors' and Executive Officers' Remuneration Report (continued)

Notes

1) Included in service agreements above is an amount of US$359,962 (2018: US$456,036) which was paid or is payable to, a company of which Mr Fern is a director.

   During the year, a company of which Mr Fern is a director provided management services to the Company and its controlled entities. The dealings were in the ordinary course of business and on normal terms and conditions.
2) Mr. Bokhari was appointed as Managing Director of Petsec Energy Ltd effective 1 May 2019.
3) Included in service agreements above is an amount of US$73,345 (2018: US$261,660) which was paid, or is payable to a company of which Mr. Fern is a director and through which Mr. Petkovski provided services.
4) Salary and fees for certain specified executives includes the movement during the reporting period of accruals for annual leave and long service leave.
5) Short-term incentive/retention cash bonuses represent discretionary bonus amounts granted based on a number of factors including personal performance, the achievement of strategic objectives, retention and motivation of employees.
6) Other benefits represent amounts paid on behalf of the Managing Director and Executive Officers in respect of insurance, car parking, fringe benefits and sign-on bonuses.
7) The fair value of options and shares is calculated at the date of the grant using the Black-Scholes model and allocated to each reporting period over the period from grant date to vesting date.

During the year, termination payments of US$243,845 were paid to key management personnel (2018: nil).

The following table sets out the factors and assumptions used in determining the fair value of the shares or options issued to key management personnel.

Grant date	Expiry date	Average fair value per option	Exercise price	Price of shares on grant date	Weighted Average estimated volatility	Risk-free interest rate	Dividend yield
2/02/18 [1]	16/02/23	A$0.01	A$0.20	A$0.11	69.4%	2.165%	-
2/02/18 [2]	23/02/23	A$0.01	A$0.20	A$0.11	70.1%	2.165%	-
9/02/18 [3]	23/02/23	A$0.02	A$0.20	A$0.10	103.6%	2.165%	-

1 Issued to R. Keogh. Options vest between 1 March 2018 and 1 March 2020 at a minimum share price of A$0.20.
2 Issued to P. Gahdmar. Options vest between 1 March 2018 and 1 March 2020 at a minimum share price of A$0.20.
3 Issued to P. Gahdmar. Options vest between 1 March 2019 and 1 March 2021 at a minimum share price of A$0.20.

20.6 Analysis of short-term incentive/retention cash bonuses included in remuneration

Amounts included in remuneration for the financial year, within the table included in note 20.5 of this Directors' Report, represent the amount that vested in the financial year based on a number of factors including achievement of personal goals, satisfaction of specified performance criteria, retention and motivation of employees.

No amounts vest in future financial years in respect of the short-term incentives and bonus schemes for the 2019 year.

No amounts were forfeited due to the performance or service criteria not being met in relation to the current financial year.

20. Remuneration Report – Audited (continued)

20.7 Equity instruments

Options over equity instruments granted as compensation

All options refer to options over ordinary shares of Petsec Energy Ltd, which are exercisable on a one-for-one basis under the Employee Share Plan and Employee Option Plan.

During 2019, no options were granted to key management personnel under the Employee Option Plan (2018: 10,200,000).

The movement during the reporting period in the number of shares and options under the Employee Share Plan and Employee Option Plan held, directly, indirectly or beneficially, by each key management person, including their related parties, is as follows:

	Held at 1 January 2019	Granted as compensation	Exercised	Other changes [1]	Held at 31 December 2019	Vested during the year	Vested and exercisable at 31 December 2019
Directors							
T Fern	-	-	-	-	-	-	-
S Bokhari	-	-	-	-	-	-	-
D Mortimer	-	-	-	-	-	-	-
A Baden	-	-	-	-	-	-	-
Executives							
R Keogh [2]	2,500,000	-	-	-	2,500,000	-	2,000,000
P Gahdmar [2]	2,700,000	-	-	-	2,700,000	-	1,400,000

[1] *Other changes represent shares and options that expired or were forfeited during the year.*
[2] *Options exercisable at a share price of A$0.20.*

No shares or options under the Employee Share Plan and Employee Option Plan are held by key management personnel related parties.

Exercise of options granted as compensation

No shares were issued on the exercise of options previously granted as compensation to key management personnel during the reporting period (previous corresponding period: Nil).

20. Remuneration Report – Audited (continued)

20.7 Equity instruments (continued)

Movements in shares

The movement during the reporting period in the number of ordinary shares in Petsec Energy Ltd held, directly, indirectly or beneficially, by each key management person, including their related parties, is as follows:

	Held at 1 January 2019	Granted as compensation	Purchases	Received on exercise of options	Sales/ Disposal of relevant interest	Held at 31 December 2019
Directors						
T Fern	37,876,361	-	-	-	-	37,876,361
D Mortimer	12,241,098	-	-	-	-	12,241,098
S Bokhari	-	-	-	-	-	-
A Baden	-	-	-	-	-	-
Executives						
R Keogh	1,612,500	-	-	-	-	1,612,500
P Gahdmar	400,000	-	-	-	-	400,000

Modification of terms of equity-settled share-based payment transactions

No terms of equity-settled share-based payment transactions (including options granted as compensation to key management personnel) have been altered or modified by the issuing entity during the reporting period or the prior period.

Lead Auditor's Independence Declaration under Section 307C of the Corporations Act 2001

To the Directors of Petsec Energy Ltd

I declare that, to the best of my knowledge and belief, in relation to the audit of Petsec Energy Ltd for the financial year ended 31 December 2019 there have been:

i. no contraventions of the auditor independence requirements as set out in the *Corporations Act 2001* in relation to the audit; and

ii. no contraventions of any applicable code of professional conduct in relation to the audit.

KPMG

Daniel Camilleri

Partner

Sydney

28 February 2020

Consolidated statement of profit and loss and other comprehensive income

For the year ended 31 December 2019

	Note	**2019 US$'000**	2018 US$'000 (restated)[1]
Revenues from sale of oil & gas		**1,088**	3,142
Net revenues after royalties		**1,088**	3,142
Other income/(expenses)	5	**(175)**	28
Lease operating expenses		**(1,101)**	(1,691)
Geological, geophysical and administrative expenses		**(3,446)**	(4,395)
Depreciation, depletion, and amortisation and reclamation	12(a)	**(2,593)**	(1,802)
Change in rehabilitation provision		**(505)**	-
Dry hole and impairment expense	12(a)	**(13,831)**	(469)
Financial income	8	**6**	10
Financial expenses	8	**(3,684)**	(4,873)
Profit/(loss) before income tax		**(24,241)**	(10,050)
Income tax benefit/(expense)	9	**-**	-
Profit/(loss) from continuing operations		**(24,241)**	(10,050)
Profit/(loss) for the period		**(24,241)**	(10,050)
Other comprehensive income/(loss)			
Items that may be reclassified subsequently to profit or loss:			
Foreign exchange translation differences		**80**	78
Total comprehensive income/(loss) for the period		**(24,161)**	(9,972)

	Note	**US Cents 2019**	2018
Earnings/(loss) per share			
Basic and diluted earnings/(loss) per share	10	**(6.3)**	(3.1)

1. US$975,000 relating to expenditures incurred in relation to the Group's interests in Block S-1 and Block 7 were reclassified from Geological, geophysical and administrative expenses to Lease operating expenses so as to more accurately reflect the nature of these expenditures.

The statement of profit and loss and other comprehensive income is to be read in conjunction with the notes to the consolidated financial statements set out on pages 38 to 71.

Consolidated statement of changes in equity

For the year ended 31 December 2019

In thousands of USD	Share capital US$'000	Translation Reserve US$'000	Share-based compensation US$'000	Option Reserve US$'000	Accumulated losses US$'000	Total Equity US$'000
Balance at 1 January 2018	193,991	1,656	39	451	(189,152)	6,985
Total comprehensive income for the period						
Profit/(loss) for the period	-	-	-	-	(10,050)	(10,050)
Other comprehensive income						
Foreign exchange translation difference	-	123	-	(45)	-	78
Total other comprehensive income/(loss)	-	123	-	(45)	-	78
Total comprehensive income/(loss) for the period	-	123	-	(45)	(10,050)	(9,972)
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Share issue/(cancelled)	3,806	-	-	-	-	3,806
Vesting of share options	58	-	(58)	-	-	-
Share-based payments expense	-	-	142	-	-	142
Total transactions with owners	3,864	-	84	-	-	3,948
Balance at 31 December 2018	197,855	1,779	123	406	(199,202)	961
Balance at 1 January 2019	**197,855**	**1,779**	**123**	**406**	**(199,202)**	**961**
Total comprehensive income/(loss) for the period						
Profit/(loss) for the period	**-**	**-**	**-**	**-**	**(24,241)**	**(24,241)**
Other comprehensive income/(loss)						
Foreign exchange translation differences	**-**	**80**	**-**	**-**	**-**	**80**
Total other comprehensive income/(loss)	**-**	**80**	**-**	**-**	**-**	**80**
Total comprehensive income/(loss) for the period	**-**	**80**	**-**	**-**	**(24,241)**	**(24,161)**
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Share issue/(cancelled)	**3,109**	**-**	**-**	**-**	**-**	**3,109**
Vesting of share options	**135**	**-**	**(135)**	**-**	**-**	**-**
Share-based payments expense	**-**	**-**	**86**	**-**	**-**	**86**
Total transactions with owners	**3,244**	**-**	**(49)**	**-**	**-**	**3,195**
Balance at 31 December 2019	**201,099**	**1,859**	**74**	**406**	**(223,443)**	**(20,005)**

The statement of changes in equity is to be read in conjunction with the notes to the consolidated financial statements set out on pages 38 to 71.

Consolidated statement of financial position

As at 31 December 2019

	Note	2019 US$'000	2018 US$'000
ASSETS			
Current assets			
Cash and cash equivalents		**645**	2,597
Trade and other receivables	11	**192**	810
Prepayments		**84**	176
Total current assets		**921**	3,583
Non-current assets			
Restricted cash deposits		**46**	1,880
Property, plant and equipment		**22**	117
Right-of-use assets		**134**	-
Oil and gas properties	12	**4,249**	17,952
Total non-current assets		**4,451**	19,949
Total assets		**5,372**	23,532
LIABILITIES			
Current liabilities			
Trade and other payables	14	**1,305**	2,899
Lease liability		**69**	-
Employee benefits provisions		**194**	211
Total current liabilities		**1,568**	3,110
Non-current liabilities			
Secured borrowings	15	**15,772**	9,483
Fair value of derivative instruments	16	**358**	1,977
Provisions	18	**7,428**	7,815
Lease liability		**68**	-
Employee benefits provisions		**183**	186
Total non-current liabilities		**23,809**	19,461
Total liabilities		**25,377**	22,571
Net assets		**(20,005)**	961
EQUITY			
Issued capital	19	**201,099**	197,855
Reserves	19	**2,339**	2,308
Accumulated losses		**(223,443)**	(199,202)
Total equity		**(20,005)**	961

The statement of financial position is to be read in conjunction with the notes to the consolidated financial statements set out on pages 38 to 71.

Petsec Energy

Consolidated statement of cashflows

For the year ended 31 December 2019

	Note	2019 US$'000	2018 US$'000
Cashflows from operating activities			
Cash receipts from customers		**1,620**	2,841
Cash payments to suppliers and employees		**(4,072)**	(4,947)
Interest received		**6**	10
Restricted deposits		**154**	(1,680)
Net cash used in operating activities	28	**(2,292)**	(3,776)
Cashflows from investing activities			
Payments for property, plant and equipment		**(3)**	(3)
Payments for oil and gas, exploration and evaluation properties		**(3,485)**	(2,646)
Aggregate cashflows from acquisitions		**-**	1,327
Net cash used in investing activities		**(3,488)**	(1,322)
Cashflows from financing activities			
Proceeds from drawdown of convertible note facility		**4,000**	4,500
Payments for lease liabilities		**(172)**	-
Net cash from financing activities		**3,828**	4,500
Net (decrease)/increase in cash and cash equivalents		**(1,952)**	(598)
Cash and cash equivalents at 1 January		**2,597**	3,264
Effects of exchange rate changes on cash held		**-**	(69)
Cash and cash equivalents at 31 December		**645**	2,597

The statement of cashflows is to be read in conjunction with the notes to the consolidated financial statements set out on pages 38 to 71.

1. Reporting entity

Petsec Energy Ltd (the "Company") is a company domiciled in Australia. The registered office of the Company is Level 7, BMA House, 135 Macquarie Street, Sydney NSW 2000. The consolidated financial statements of the Company as at and for the year ended 31 December 2019 comprise the Company and its subsidiaries (together referred to as the "Group").

The financial report is presented in United States dollars, which is the Group's choice of presentation currency.

The Group is a for-profit entity and is primarily involved in oil and gas exploration and production with operations in the shallow waters of the Gulf of Mexico and onshore Louisiana, USA, and in the Republic of Yemen.

2. Basis of preparation

(a) Statement of compliance

The financial report is a general purpose financial report which has been prepared in accordance with Australian Accounting Standards ("AASBs") (including Australian Interpretations) adopted by the Australian Accounting Standards Board ("AASB") and the *Corporations Act 2001*. The consolidated financial report of the Group and the financial report of the Company comply with International Financial Reporting Standards ("IFRSs") and interpretations adopted by the International Accounting Standards Board (IASB).

The Board of Directors approved the financial statements on 28 February 2020.

(b) Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis except for the following:

- Derivative financial instruments are measured at fair value;

The methods used to measure fair values are discussed further in note 4.

The Group is of a kind referred to in ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191 and in accordance with that instrument, all financial information presented in US dollars has been rounded to the nearest thousand unless otherwise stated.

(c) Use of estimates and judgements

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

In particular, information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amount recognised in the financial statements are described in note 3 (d) – Exploration, evaluation properties and oil and gas properties, note 3(l) Rehabilitation provision and note 3 (q) – Income tax.

The estimated recoverable amount of oil and gas assets is based on discounted cash flow projections which are based on estimates and assumptions that are subject to change. Key assumptions include the ultimate prices realised on the sale of oil and gas and the reserves ultimately recovered. A sustained deterioration in prices or reduction in reserves may result in future asset impairments.

(d) Going concern basis of preparation

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

As at 31 December 2019, the Group has a cash balance (excluding restricted deposits of US$46,000) of US$645,000 (31 December 2018: US$2.6 million) and current net liabilities of US$647,000 (31 December 2018: current net assets US$0.5 million).

The Group has a Convertible Note Facility of US$15.0 million and an Additional Facility of US$3.0 million excluding interest (refer note 15). As at 31 December 2019, the Group has drawn down US$13.5 million from the Convertible Note Facility. There were no drawdowns from the Additional Facility. Carrying value of the Convertible Note Facility at 31 December 2019 excluding the fair value of the conversion option (refer note 16) and including accrued interest is US$15.8 million (31 December 2018: US$9.5 million) (refer note 15).

(d) Going concern basis of preparation (continued)

Additional drawdowns of US$1.5 million under the facility are anticipated during FY2020. Consequently, the forecast outstanding payable balance on the maturity date of 23 January 2021, which include the additional drawdown of US$1.5 million and interest accruals for the period from 1 January 2020 to the maturity date, is US$21.6 million.

The directors have approved cash flow projections which support the going concern basis of preparation. The preparation of these projections incorporate a number of significant assumptions including:

- Drawdown of remaining US$1.5 million available under the Convertible Note Facility during 2020;
- Generating net cash inflows from the US assets based on internal estimates of production rates, which are consistent with the current average production rate during the first two months of 2020, and realised commodity prices;
- Further reductions in general and administrative expenditures by closure of offices in Dubai and reduction of head count; and
- Achieving either a deferral of the maturity date or refinancing of the amount due (estimated to be US$21.6m including future drawdowns of US$1.5 million and accrued interest) on 23 January 2021 under the Convertible Note facility, or a combination of these two items.

Due to the significant uncertainties in achieving the following actions, the cash flow projections do not assume:

I. Restart of operations in Yemen to allow for positive cash generation from operations and payment of MENA provisions (refer note 18); or
II. Sale of assets or farm-in by external investors in the group's assets; or
III. Any cash outflow associated with claims made by joint venture partners (refer note 22)

There are material uncertainties in achieving the assumptions noted above. As a result of those material uncertainties, should the Group be unable to continue as a going concern it may be required to realise its assets and discharge its liabilities other than in the normal course of business and at amounts other than those stated in the consolidated financial statements. The consolidated financial statements do not include any adjustments relating to the recoverability and classification of asset carrying amounts or the amount of liabilities that might result should the group be unable to continue as a going concern and meet its debt obligations as and when they fall due.

3. Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, and have been applied consistently by the Company and Group.

(a) Basis of consolidation

(i) Subsidiaries

Subsidiaries are entities controlled by the Company. The Company controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by the Group.

In the Company's financial statements, investments in subsidiaries are carried at cost, less accumulated impairments.

(ii) Joint operating arrangements

Joint operating arrangements are those legal entities over whose activities the Group has joint control, whereby the Company has rights to the assets and obligations for the liabilities relating to the arrangement. The interest of the Group in unincorporated joint operating arrangements and jointly operated assets are brought to account by recognising in its financial statements the Company's share of the arrangements underlying assets and liabilities, and the expenses it incurs and its share of income that it earns from the sale of goods or services by the joint arrangements.

3. Significant accounting policies (continued)

(a) Basis of consolidation (continued)

(iii) Transactions eliminated on consolidation

Intra-group balances and any unrealised gains and losses or income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

(iv) Loss of control

Upon the loss of control, the Group derecognises the assets and liabilities of the subsidiary, any non-controlling interests and the other components of equity related to the subsidiary. Any surplus or deficit arising on the loss of control is recognised in profit or loss. If the Group retains any interest in the previous subsidiary, then such interest is measured at fair value at the date that control is lost. Subsequently it is accounted for as an equity-accounted investee or as an available-for-sale financial asset depending on the level of influence retained.

(b) Foreign currency

(i) Functional and presentation currency

Items included in the financial statements of each of the Group's subsidiaries are measured using the currency of the primary economic environment in which the subsidiary operates ("the functional currency"). The functional currency of the Company and its Australian subsidiaries is Australian dollars (A$) and the functional currency of the Company's overseas subsidiaries is United States dollars (US$).

The financial statements are presented in United States dollars. The Group believes the US dollar is the best measure of performance for Petsec Energy Ltd because oil and gas, the Group's dominant sources of revenue, are priced in US dollars and the Group's main operations are based in jurisdictions where most of the costs incurred are denominated in US dollars.

Prior to consolidation, the results and financial position of each entity within the Group are translated from the functional currency into the Group's presentation currency as follows:

- Assets and liabilities are translated at the closing rate at the date of that balance sheet;
- Income and expenses are translated at average exchange rates (unless this is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions);
- Components of equity are translated at the historical rates; and
- All resulting exchange differences are recognised as a separate component of equity.

ii) Foreign currency transactions and balances

Foreign currency transactions are translated into the functional currency at the exchange rates prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to the respective functional currency at the foreign exchange rate ruling at that date. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the statement of comprehensive income.

Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

Foreign exchange gains and losses arising from a monetary item receivable from or payable to a foreign operation, the settlement of which is neither planned nor likely in the foreseeable future, are considered to form part of a net investment in a foreign operation and are recognised directly in equity in the foreign currency translation reserve (FCTR).

(c) Derivative financial instruments and hedging activities

The Group's revenues are exposed to changes in commodity prices. From time to time, the Group enters into derivative financial instruments to manage a portion of its oil and gas sales price risks.

The Group does not hold derivative financial instruments for speculative purposes.

Derivatives are initially measured at fair value. Subsequent to initial recognition, derivatives are measured at fair value, and changes therein are generally recognised in profit or loss.

3. Significant accounting policies (continued)

(c) Derivative financial instruments and hedging activities (continued)

The Group designates certain derivatives as hedging instruments to hedge the variability in cash flows associated with highly probable forecast transactions arising from changes in foreign exchange rates and interest rates and certain derivatives and non-derivative financial liabilities as hedges of foreign exchange risk on a net investment in a foreign operation.

At inception of designated hedging relationships, the Group documents the risk management objective and strategy for undertaking the hedge. The Group also documents the economic relationship between the hedged item and the hedging instrument, including whether the changes in cash flows of the hedged item and hedging instrument are expected to offset each other.

(i) Cash flow hedge

Changes in the fair value of the derivative-hedging instrument designated as a cash flow hedge are recognised directly in equity to the extent that the hedge is effective. To the extent that the hedge is ineffective, changes in fair value are recognised in the statement of profit or loss.

If the hedging instrument no longer meets the criteria for hedge accounting, expires or is sold, terminated or exercised, then hedge accounting is discontinued prospectively. The cumulative gain or loss previously recognised in equity remains there until the forecast transaction occurs. When the hedged item is a non-financial asset, the amount recognised in equity is transferred to the carrying amount of the asset when it is recognised. In other cases the amount recognised in equity is transferred to the income statement in the same period that the hedged item affects profit or loss.

(ii) Derivative financial instruments that do not qualify for hedge accounting

Certain derivative financial instruments do not qualify for hedge accounting. Changes in the fair value of any derivative financial instrument that does not qualify for hedge accounting are recognised immediately in the statement of profit and loss.

Other derivative financial instruments are recognised initially at fair value; attributable transaction costs are recognised in profit or loss as incurred. Subsequent to initial recognition, derivatives are measured at fair value and changes therein are recognised immediately in profit or loss.

(d) Exploration, evaluation properties and oil and gas properties

Exploration and evaluation expenditure is accumulated in respect of each separate area of interest. The Group's capitalisation policy for its natural gas and crude oil exploration and development activities is to capitalise expenditure of productive exploratory wells, development drilling and productive wells, and expenditure to acquire mineral interests. Exploration expenditure, including personnel costs, certain geological and geophysical expenses including seismic costs where exploration rights have not been obtained for oil and natural gas leases, are charged to expense as incurred. Exploratory drilling expenditures are initially capitalised, but charged to expense if and when the well is determined not to have found reserves in commercial quantities.

Exploration and evaluation expenditures relating to an area of interest are capitalised where exploration rights have been obtained. This expenditure is carried forward only to the extent that they are expected to be recouped through successful development and exploitation, or sale of the area, or where exploration and evaluation activities have not yet reached a stage which permits a reasonable assessment of the existence of economically recoverable reserves, and active and significant exploration operations are continuing. This expenditure is not subject to amortisation. Once management has determined the existence of economically recoverable reserves for an area of interest, expenditure is reclassified from exploration and evaluation to oil and gas properties on the balance sheet. Oil and gas properties are amortised using a units-of-production method, as further discussed in note 3(e).

Exploration and evaluation properties and oil and gas properties are assessed for impairment when facts and circumstances suggest that the carrying amount of the asset may exceed its recoverable amount. In the event that indicators of impairment are present, an impairment loss is recorded based on the higher of an asset's fair value less costs to sell and value in use (see note 3(g)). When an area of interest is abandoned or the directors decide that it is not commercial, any accumulated costs in respect of that area are written off in the financial period the decision is made.

(e) Amortisation of oil and gas properties

Oil and gas properties in the production phase are amortised on a units-of-production method based on the ratio of actual production to remaining proved and probable reserves (2P). Remaining 2P reserves are measured at the lower of 2P reserves estimated by external independent petroleum engineers and internal estimates.

3. Significant accounting policies (continued)

(e) Amortisation of oil and gas properties (continued)

Amortisation is not charged on costs carried forward in respect of areas of interest in the development phase until commercial production commences.

(f) Property, plant and equipment

(i) Recognition and measurement

Items of property, plant and equipment are measured at cost less accumulated depreciation and impairment losses.

Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for its intended use, and the costs of dismantling and removing the items and restoring the site on which they are located. Purchased software that is integral to the functionality of the related equipment is capitalised as part of the equipment.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

Gains and losses on disposal of an item of property, plant and equipment are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment and are recognised net within "other income" in profit and loss.

(ii) Subsequent costs

The cost of replacing part of an item of property, plant and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Group and its costs can be measured reliably. The costs of the day-to-day servicing of property, plant and equipment are recognised in the income statement as incurred.

(iii) Depreciation and amortisation

Depreciation of property, plant and equipment is recognised in the statement of comprehensive income on a straight-line basis over the estimated useful lives of each part of an item. Leased assets are depreciated over the shorter of the lease term and their useful lives. Assets are depreciated or amortised from the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and held ready for use.

Depreciation methods, useful lives and residual values are reassessed at the reporting date. When changes are made, adjustments are reflected prospectively in current and future periods only.

The estimated useful lives or the amortisation method used for each class of asset in the current and comparative periods are as follows:

	2019	2018
Property, plant and equipment		
Furniture and fittings	**5 – 8 years**	5 – 8 years
Office equipment	**3 – 4 years**	3 – 4 years
Leasehold improvements	**5 – 7 years**	5 – 7 years

(g) Impairment - Non-financial assets

The carrying amounts of the Group's and the Company's non-financial assets, other than deferred tax assets (see note 3(q)), are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated. For intangible assets that have indefinite lives or that are not yet available for use, recoverable amount is estimated at each reporting date.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other assets or groups. Impairment losses are recognised in the income statement. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a *pro rata* basis.

3. Significant accounting policies (continued)

(g) Impairment - Non-financial assets (continued)

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessment of the time value of money and the risks specific to the asset.

The measurement of recoverable amount for the Group's exploration, evaluation and oil and gas properties expenditure requires significant estimation and judgement. Note 12 provides further details of the key assumptions adopted by the Group in measuring the recoverable amounts of exploration, evaluation and oil and gas properties expenditure.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(h) Trade and other receivables

Trade receivables, which generally have 30-60 day terms, are recognised and carried at original invoice amount less an allowance for any uncollectible amounts.

An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off when identified.

(i) Cash and cash equivalents

Cash and cash equivalents in the balance sheet comprise cash at bank and on hand and short-term deposits with an original maturity of three months or less.

For the purposes of the Statement of Cash Flows, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

(j) Interest-bearing loans and borrowings

All loans and borrowings are initially recognised at cost, being the fair value of the consideration received net of debt issue costs associated with the borrowing.

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method. Amortised cost is calculated by taking into account any issue costs, and any discount or premium on settlement.

(k) Borrowing costs

Borrowing costs comprise interest payable on borrowings calculated using the effective interest rate method, lease finance charges, amortisation of discounts or premiums relating to borrowings, and the unwinding of discounts on the rehabilitation provisions. Borrowing costs relating to oil and gas properties under development are capitalised as a cost of development up to the date production commences. The actual borrowing costs are capitalised where funds are borrowed specifically for oil and gas properties under development. Borrowing costs on general funding are capitalised based on the weighted average borrowing rate.

(l) Provisions

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability.

Where discounting is used, the increase in the provision due to the passage of time is recognised as a finance cost.

3. Significant accounting policies (continued)

(l) Provisions (continued)

Rehabilitation

The Group recognises a provision for the legal obligation associated with the retirement of long-lived assets that results from the acquisition, construction, development, and (or) the normal operation of oil and natural gas properties. The initial recognition of a liability for rehabilitation, which is discounted using a risk-free interest rate, increases the carrying amount of the related long-lived asset by the same amount as the liability. In periods subsequent to initial measurement, period-to-period changes in the liability are recognised for the passage of time (unwinding of discount) as a borrowing cost. Additionally, the capitalised asset retirement cost is subsequently allocated to expense on a units-of-production basis over its estimated useful life.

Changes in the estimate of the liability arising from revised timing or estimated cost-to-complete the rehabilitation are recognised with a corresponding adjustment to the relevant long-lived asset.

The rehabilitation provision requires significant estimation and judgement. These estimates include:

- Expected method of remediation;
- Forecast costs-to-complete the future remediation; and
- Anticipated timing of the remediation work.

The Group monitors the estimates and judgements involved in measuring this provision.

(m) Employee benefits and director benefits

(i) Short-term employee benefits

Liabilities for employee benefits for wages, salaries, annual leave, sick leave and bonuses represent present obligations resulting from employees' services provided to reporting date which are expected to be wholly settled by the Company within the next financial year. Such liabilities are calculated at undiscounted amounts based on remuneration wage and salary rates that the Group expects to pay as at reporting date including related on-costs, such as workers' compensation insurance and payroll tax.

(ii) Long-term employee benefits

The provision for employee benefits for long service leave represents the present value of the estimated future cash outflows to be made resulting from employees' services provided to reporting date.

The provision is calculated using expected future increases in wage and salary rates including related on-costs and expected settlement dates based on turnover history and is discounted using the rates attaching to national government bonds at reporting date which most closely match the terms of maturity of the related liabilities.

(iii) Defined contribution pension plans

The Company and other controlled entities contribute to several defined contribution pension plans. Obligations for contributions to defined contribution pension plans are recognised as an expense in the statement of comprehensive income when they are due.

(iv) Share-based compensation transactions

Share-based compensation benefits are provided to employees of the Group, including directors, via the Company's Employee Option Plan and Employee Share Plan.

The grant date fair value of options granted to employees is recognised as an employee expense, with a corresponding increase in equity, over the period in which the employees become unconditionally entitled to the options.

(n) Leases

The Group has applied AASB 16 using the modified retrospective approach and therefore comparative information has not been restated.

At lease commencement date, the Group recognises a right-of-use asset and a lease liability on the balance sheet. The right-of-use asset is measured at cost, which is made up of the initial measurement of the lease liability, any initial direct costs incurred by the Group, an estimate of any costs to dismantle and remove the asset at the end of the lease, and any lease payments made in advance of the lease commencement date (net of any incentives received).

Notes to the consolidated financial statements

For the year ended 31 December 2019

3. Significant accounting policies (continued)

(n) Leases (continued)

The Group depreciates the right-of-use assets on a straight-line basis from the lease commencement date to the earlier of the end of the useful life of the right-of-use asset or the end of the lease term. The Group also assesses the right-of-use asset for impairment when such indicators exist.

At the commencement date, the Group measures the lease liability at the present value of the lease payments unpaid at that date, discounted using the interest rate implicit in the lease if that rate is readily available or the Group's incremental borrowing rate.

Lease payments included in the measurement of the lease liability are made up of fixed payments (including in substance fixed), variable payments based on an index or rate, amounts expected to be payable under a residual value guarantee and payments arising from options reasonably certain to be exercised.

Subsequent to initial measurement, the liability will be reduced for payments made and increased for interest. It is remeasured to reflect any reassessment or modification, or if there are changes in in-substance fixed payments.

When the lease liability is remeasured, the corresponding adjustment is reflected in the right-of-use asset, or profit and loss if the right-of-use asset is already reduced to zero.

The Group has elected not to recognise right-of-use assets and lease liabilities for short-term leases of 12 months or less and leases of low-value assets, including certain office premises and office equipment. The Group recognises the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

(o) Revenue and other income recognition

Revenue is recognised when (or as) the Group transfers control of goods or services to a customer at a point in time and at the amount to which the entity expects to be entitled. The following specific recognition criteria must also be met before revenue is recognised:

Sale of oil and gas

Revenues from the sale of oil and gas is recognised when the product is in the form in which it is to be delivered and an actual physical quantity has been provided or allocated to a purchaser pursuant to a contract. Revenue from oil and gas sales is measured at the fair value of the consideration receivable.

Revenue from oil and gas royalties is recognised on an accrual basis in accordance with the terms of underlying royalty agreements. Revenue from oil and gas royalties is measured at the fair value of the consideration receivable.

Sale of non-current assets

Gains or losses on sale of non-current assets are recognised as other income at the date control of the asset passes to the buyer, usually when an unconditional contract of sale is signed.

(p) Finance income and finance expense

The Group's finance income and finance expenses include interest income, interest expense, the remeasurement to fair value of financial liabilities, and facility fees in relation to financial liabilities.

Interest income or expense is recognised using the effective interest method, which is the rate that discounts estimated future cash payments or receipts through the expected life of the financial instrument to the amortised cost of the financial liability.

(q) Earnings per share

The Group presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the period. Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares, which comprise share options granted to employees.

(r) Income tax

Income tax expense comprises current and deferred tax. Income tax expense is recognised in the statement of comprehensive income except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

3. Significant accounting policies (continued)

(r) Income tax (continued)

Deferred tax is recognised using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of assets or liabilities that affect neither accounting nor taxable profit nor differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which the temporary difference or tax losses can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(s) Segment reporting

An operating segment is a distinguishable component of the Group whose information is reviewed regularly by the CEO, the Group's chief decision making officer, and that is engaged in providing related products or services which are subject to risk and rewards that are different to other segments.

(t) Changes in accounting policies

Except as described below, the accounting policies applied in these financial statements are the same as those applied in the Group's financial statements as at and for the year ended 31 December 2018.

(i) AASB 16 Leases

AASB 16 introduces a single, on-balance sheet lease accounting model requiring lessees to recognise assets and liabilities of leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee recognises a right-of-use asset representing its right to use the underlying leased asset and a lease liability representing its obligation to make lease payments.

The Group has initially adopted AASB 16 Leases from 1 January 2019 using the modified retrospective approach, as defined in the accounting policy. The Group recognised a right-of-use asset and a lease liability of US$466,000 in respect of certain of its office premises which have a lease term of greater than 12 months. When measuring lease liabilities for leases that were classified as operating leases, the Group discounted lease payments using its incremental borrowing rate at 1 January 2019. The weighted average rate applied is 10%.

Previously, the Group classified its office premises as operating leases under AASB 117. At transition, the right-of-use asset and liability were measured at the present value of future lease payments as at the initial recognition date, by applying the Group's incremental borrowing rate.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term. Subsequent to initial measurement, the Group recognises period-to-period changes in the lease liability for the passage of time (unwinding of discount) as a borrowing cost. Lease payments included in the measurement of the lease liability comprise the base lease rental amount including any annual rent escalations.

The Group has elected not to recognise right-of-use assets and lease liabilities for short-term leases of 12 months or less and leases of low-value assets, including certain office premises and office equipment. The Group recognises the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

	US$000's
Operating lease commitments at 31 December 2018 as disclosed under AASB17 in the Group's consolidated financial statements	754
Discounted using incremental borrowing rate at 1 January 2019	(236)
Recognition exemption for leases with low value items	(52)
Lease liabilities recognised at 1 January 2019	466

During the year ended 31 December 2019, the Group's depreciation expenses included depreciation of right-of-use assets of US$$155,000. Total additions to the right-of-use assets during the year was US$104,000 and the total cash outflow relating to right-of-use assets was US$172,000.

4. Determination of fair values

A number of the Group's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. The Company has applied fair value methodologies that approximate the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Where applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

Derivative Instruments

The fair values of derivative instruments are initially recognised at fair value on the date at which the derivative contracts are entered into and subsequently remeasured to fair value. On subsequent revaluation the derivatives are carried as assets when their fair value is positive and liabilities when their fair value is negative.

When the fair values of financial assets and financial liabilities recorded in the statement of financial position cannot be measured based on quoted prices in active markets, their fair value is measured using valuation techniques including discounted cash flow models. The inputs to these models are taken from observable markets where possible, but where this is not feasible, a degree of judgement is required in establishing fair values. Judgements include considerations of inputs such as liquidity risk, credit risk and volatility. Changes in assumptions relating to these factors could affect the reported fair value of financial instruments.

Equity securities

The fair value of equity securities (level 3 category instruments) is determined using an option pricing model – the Black-Scholes-Merton formula – in arriving at an expected present value for options granted by the Group at period end. Measurement inputs include observable inputs, such as the share price on the measurement date, the exercise price of the instrument, share price target and the risk-free interest rate (based on government bonds), as well as unobservable inputs, such as expected volatility, expected term of the instruments, and expected dividends which represent management's best estimates at period end.

5. Other income and expenses

	2019	2018
	US$'000	US$'000
Other income/(expenses)		
Derecognition of restricted cash [1]	**(1,680)**	-
Reversal of MENA provisions (note 18) [1]	**1,575**	-
Loss on disposal of assets	**(81)**	
Production and project overhead income	**4**	-
Gain on derecognition of operating lease	**14**	-
Net foreign exchange gains/(losses)	**(7)**	28
	(175)	28

[1] *These are non-cash transactions which are not reflected in the cash flow statement.*

6. Employee expenses

	2019	2018
	US$'000	US$'000
Wages and salaries	**1,110**	1,120
Service agreements for executives	**471**	974
Contract labour	**289**	211
Termination payments	**244**	-
Superannuation & 401(k) plans	**50**	62
Share-based payment compensation	**84**	150
Other employee-related expenses	**82**	162
	2,330	2,679

7. Auditor's remuneration

	2019 US$	2018 US$
Audit services:		
Auditors of the Company		
KPMG Australia		
Audit and review of financial reports	**108,000**	97,750
Non-audit services:		
Auditors of the Company		
KPMG Australia		
Agreed upon procedures	**-**	5,977
	108,000	103,727

8. Finance income and expense

	2019 US$'000	2018 US$'000
Interest income – Other parties	**6**	10
Financial income	**6**	10
Interest expense	**(2,542)**	(1,244)
Interest expense on lease liabilities	**(36)**	-
Facility fees	**(3,100)**	(2,991)
Remeasurement to fair value of financial liabilities	**2,013**	(619)
Unwinding of discount	**(19)**	(19)
Financial expense	**(3,684)**	(4,873)
Net financial income/(expense)	**(3,678)**	(4,863)

9. Income tax expense

	2019 US$'000	2018 US$'000
Recognised in the statement of comprehensive income		
Deferred tax expense		
Origination and reversal of temporary differences	**-**	-
Total income tax benefit/(expense) in the statement of comprehensive income	**-**	-

Numerical reconciliation between tax expense and pre-tax net profit/(loss)	2019 US$'000	2018 US$'000
Profit/(loss) before tax	**(24,241)**	(10,050)
Income tax expense/(benefit) using the Australian corporation tax rate of 30% (2018: 30%)	**(7,272)**	(3,015)
Increase/(decrease) in income tax expense due to:		
Non-deductible expenses	**1,069**	1,382
Non-Australian income taxes assessed at different rate	**1,625**	173
Deferred tax movements not brought to account in current year	**4,578**	1,460
Income tax expense/(benefit) on pre-tax net profit/(loss)	**-**	-

10. Earnings per share

The Company has only one type of security, being ordinary shares, included in the basic earnings per share calculation.

As at 31 December 2019, there were 8,200,000 (2018: 12,800,000) options over ordinary shares in Petsec Energy Ltd on issue under the Employee Option Plan ("EOP").

During the year:

1. 1,500,000 options over ordinary shares were granted (2018: 11,800,000) under the EOP;
2. 6,100,000 options over ordinary shares were forfeited (2018: nil); and
3. No options over ordinary shares were exercised.

In addition, 10 million options over ordinary shares are currently on issue to Sing Rim Pte Ltd and are exercisable at 12.5 cents each on or before 23 January 2022.

In determining potential ordinary shares, no share options or options over ordinary shares are dilutive (2018: Nil).

Basic earnings/ (loss) per share

The calculation of basic earnings/ (loss) per share at 31 December 2019 was based on the loss attributable to ordinary shareholders of US$24,241,000 (2018: Loss of US$10,050,000) and a weighted average number of ordinary shares outstanding during the year ended 31 December 2019 of 385,263,026 (2018: 326,523,300), calculated as follows:

Profit/ (loss) attributable to ordinary shareholders

	2019 US$'000	2018 US$'000
Profit/(loss) for the period	**(24,241)**	(10,050)

Weighted average number of shares (basic)

In thousands of shares	**2019**	2018
Issued ordinary shares at 1 January	**333,588**	322,288
Effect of shares issued in 2019 and 2018, respectively	**51,675**	4,235
Weighted average number of ordinary shares at 31 December	**385,263**	326,523

Earnings/(loss) per share

In USD cents	**2019**	2018
Basic and diluted earnings/(loss) per share	**(6.3)**	(3.1)

11. Trade and other receivables

	2019 US$'000	2018 US$'000
Current		
Trade receivables	**160**	717
Other receivables	**32**	93
	192	810

12. Oil and gas properties

	2019 US$'000	2018 US$'000
Balance at 1 January	**17,952**	15,679
Additions	**2,320**	3,771
Capitalised interest [1]	**288**	234
Dry hole and impairment expense [2]	**(13,964)**	-
Current year amortisation expense	**(2,347)**	(1,732)
Balance at 31 December	**4,249**	17,952

1. *Interest has been capitalised on specific borrowings in respect of oil and gas properties under development.*
2. *Dry hole and impairment expense mainly comprised the dry hole cost of the Main Pass Block 273 B-2 well of US$6.4 million and the recognition of an impairment expense of US$7.4 million against the Hummer Gas/Oil Field due to a reduction of reserves, based on the results of the B-2 well.*

Recoverable amount

The ultimate recoupment of costs carried forward for exploration and evaluation phases is dependent on the successful development and commercial exploitation or sale of the respective areas.

The estimated recoverable amount of all cash generating units in the development and production phases is determined by discounting the estimated future cash flows to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the assets. The Group utilises discounted future cash flows as estimated by independent petroleum engineers for this assessment. The key assumptions used include:

- Estimated proved and probable reserves (2P reserves);
- Hydrocarbon prices that the Group estimates to be reasonable taking into account historical prices, current prices, and prices used in making its exploration and development decisions;
- Operating costs directly applicable to the leases or wells and allocation of corporate overheads;
- Development costs based on authorisations for expenditure for the proposed work or actual costs for similar projects;
- Pre-tax discount rate of 10%.

Risk of future impairments

- The determination of the estimated recoverable amount of Petsec's producing oil and gas properties is highly sensitive to a change in estimated recoverable reserves, oil and gas prices, discount rates and cost allocations.
- As a result of historical impairments, certain properties are carried at recoverable amounts. Consequently any reduction in recoverable reserves or a reduction in the oil or gas price may trigger the need for further impairment on these specific properties.

A 2% increase in the discount rate could cause the carrying amount to exceed its recoverable amount by approximately US$406,000.

A 10% decrease in hydrocarbon prices or reserves could cause the carrying amount to exceed its recoverable amount by approximately US$609,000.

12. Oil and gas, and exploration and evaluation properties (continued)

(a) Dry hole and impairment expense

The estimated recoverable amount of all oil and gas assets is based on value in use discounted cash flow projections that are based on a range of estimates and assumptions that are subject to change. Key assumptions include the ultimate prices realised on the sale of oil and gas and the reserves ultimately recovered. A sustained deterioration in prices or reduction in reserves may result in further future asset impairments.

During the current period, the Group recognised total dry hole and impairment expense of US$13,714,000. This comprised the dry hole cost of the Main Pass Block 273 B-2 well of US$6,366,000 and the recognition of an impairment expense of US$7,348,000 against the Hummer Gas/Oil Field due to a reduction of reserves, based on the results of the B-2 well.

In the previous corresponding period, the Group recognised an impairment provision of US$469,000 against its Block 7, Yemen assets due to the inability to recommence activities in Yemen as a result of the ongoing conflict. This impairment provision may be reversed in the future once a successful resolution to the conflict is achieved and production at the An Nagyah Oilfield has been restarted.

13. Deferred tax assets

Deferred tax assets and liabilities

	Assets		Liabilities		Net	
	2019 US$'000	2018 US$'000	**2019 US$'000**	2018 US$'000	**2019 US$'000**	2018 US$'000
Oil and gas, and exploration and evaluation properties	**3,229**	1,824	**-**	-	**3,229**	1,824
Other items	**140**	35	**-**	-	**140**	35
Deferred tax balances not brought to account	**(3,369)**	(1,859)	**-**	-	**(3,369)**	(1,859)
Deferred tax assets/(liabilities)	**-**	-	**-**	-	**-**	-

Unrecognised deferred tax assets

Deferred tax assets have not been recognised in respect of the following items:

	2019 US$'000	2018 US$'000
Deductible temporary differences in USA	**3,369**	1,859
Tax operating loss carry-forwards in USA	**27,673**	24,367
Deductible temporary differences in Canada	**1,717**	1,717
Tax operating loss carry-forwards in Canada	**246**	246
Tax operating loss carry-forwards in Australia	**3,843**	3,491
	36,848	31,680

13. Deferred tax assets (continued)

Under Australian Accounting Standards, the Group is required to assess at each reporting period, the extent to which deferred tax assets in respect of the carry-forward of unused tax losses and temporary differences qualify for recognition on the balance sheet based on current facts and circumstances, including projected future taxable profits.

Historically, no deferred tax assets have been recognised in relation to the Australian operations as they do not qualify for recognition of deferred tax assets until such time that it is probable that future taxable profits will be available against which unused tax losses and temporary differences in the relevant tax jurisdictions can be utilised.

The deductible temporary differences and tax losses in Australia do not expire under current tax legislation though these losses are subject to testing under loss recoupment rules, in order for them to be utilised. USA and Canada loss carry forwards begin to expire in 2021 and later.

Movement in temporary differences during the year

	Balance 1 Jan 18 US$'000	Recognised in income US$'000	Recognised in equity US$000	Balance 31 Dec 18 US$'000
Oil and gas, and exploration and evaluation properties	3,232	(1,408)	-	1,824
Other items	60	(25)	-	35
Deferred tax balances not brought to account	(3,292)	1,433	-	(1,859)
	-	-	-	-

	Balance 1 Jan 19 US$'000	**Recognised in income US$'000**	**Recognised in equity US$000**	**Balance 31 Dec 19 US$'000**
Oil and gas, and exploration and evaluation properties	**1,824**	**1,405**	**-**	**3,229**
Other items	**35**	**105**	**-**	**140**
Deferred tax balances not brought to account	**(1,859)**	**(1,510)**	**-**	**(3,369)**
	-	**-**	**-**	**-**

14. Trade and other payables

	2019 US$'000	2018 US$'000
Current		
Trade and other payables, stated at cost		
Trade payables	**157**	180
Oil and gas, and exploration and evaluation accruals	**619**	1,853
Operational and administration accruals	**407**	428
Related party payables	**122**	438
	1,305	2,899

15. Interest bearing loans and borrowings

	2019 US$'000	2018 US$'000
Non-current		
Secured borrowings – convertible notes	**15,772**	9,483
	15,772	9,483

15. Interest bearing loans and borrowings (continued)

Secured borrowings – convertible notes

Secured borrowings represent the outstanding balance at 31 December 2019 under a convertible note facility with Republic Investment Management and associates in Singapore, managed through the registrar Sing Rim Pte Ltd of Singapore. The Group entered into a US$15 million facility in August 2016.

The key terms and conditions of the convertible note facility have been varied subsequent to the initial terms agreed in the secured convertible notes Deed Poll dated 23 August 2016. The terms have been amended by a Deed of Variation dated 14 September 2016, Letter of Variation dated 28 December 2016, Letter of Variation dated 30 March 2017, Letter of Variation dated 17 August 2017, Letter of Variation dated 18 February 2018, Letter of Variation dated 26 March 2018, Letter of Variation dated 9 May 2018, Letter of Variation dated 20 August 2018, Letter of Variation dated 6 September 2018, Letter of Variation dated 19 December 2018, the Amended and Restated Secured Convertible Note Deed Poll dated 5 March 2019, Letter of Variation dated 8 April 2019, and Letter of Variation dated 28 June 2019. The specific details of each of these variations are outlined within the announcements lodged with the ASX.

The key terms and conditions of the convertible note facility (Tranches 1, 2 & 3) as varied on 28 June 2019 are as follows:

(a) Facility amount – US$15 million.

(b) Facility drawdown – available in three tranches of US$5 million each.

- Tranche 1 fully drawn as at 31 December 2018 (US$5 million);
- Tranche 2 drawn down to US$3.5 million as at 31 December 2019 (US$5 million).
- Tranche 3 fully drawn as at 31 December 2019 (US$5 million).

(c) Facility term – redemption date of 23 January 2021.

(d) Interest – interest accrues daily at 12.5% per annum for the period of 1 January 2018 through to the 23 January 2019, and thereafter increasing to 15% compounding monthly.

(e) Security – the convertible notes constitute unsubordinated and secured obligations of the Company. The Company and the registrar entered into a general security deed on 23 August 2016 under which the Company granted the registrar a general security interest over all of the Company's assets as security for the Company's obligations under the convertible notes. In addition, the Company granted the registrar mortgages over certain assets of its U.S. subsidiaries.

The Noteholders have agreed to a forbearance till 23 January 2021 in the exercise of their rights under the Secured Convertible Note Deed Poll and associated Collateral, such that they will either exercise their rights of conversion or limit any claim they may have to the Secured Collateral only.

(f) Conversion to Petsec Energy Ltd shares – the noteholder will be entitled to convert up to 50% of the outstanding amount of the convertible notes into shares, by delivering a conversion notice at any time prior to the maturity date. The maximum number of shares issued on conversion is restricted to 170 million shares.

(g) Conversion price – 12.5 cents per share or reducing to the net issue price of stock in the period to redemption should that price be less than 12.5 cents per share.

(h) Provision of an additional facility of US$3 million that can be drawn upon up until the Redemption Date of 23 January 2021 to apply to the restart operations of the An Nagyah Oilfield.

In consideration of its continued and extended support, on 28 June 2019, the Company agreed to issue 40 million shares to Sing Rim subject to shareholder approval, if necessary. At the date of this report, these shares had not been issued. The Company will seek shareholder approval for the issue of these shares at its next General Meeting, currently scheduled for May 2020.

As at 31 December 2019, US$13.5 million has been drawn down under the US$15 million facility and nil has been drawn down under the US$3 million additional facility.

Petsec Energy

Notes to the consolidated financial statements

For the year ended 31 December 2019

16. Fair value of financial derivative instruments

	2019	2018
Non-current	**US$'000**	US$'000
Fair value of financial derivatives	**358**	1,977
	358	1,977

The fair value of the financial derivative instrument of US$358,000 represents the embedded derivative component within the secured convertible note (refer note 15).

Embedded derivatives are separated from the host contract and accounted for separately if certain criteria are met.

Derivatives are initially valued at fair value; subsequent to initial recognition, derivatives are measured at fair value, and changes therein are recognised in profit and loss.

The fair value of the financial derivative was determined at initial recognition and subsequent reporting dates using a Monte Carlo model.

17. Employee benefits

(a) Superannuation/pension plans

The Group contributes to several defined contribution employee superannuation plans in Australia. Employer contributions are based on various percentages of their gross salaries. The Group is under no legal obligation to make contributions in excess of those specified in Superannuation Industry (Supervision) legislation. The amount recognised as expense was US$30,000 for the year ended 31 December 2019 (2018: US$42,000).

U.S. based employees are eligible to participate in a voluntary retirement savings plan under Section 401(k) of the US tax code ("401(k) plan"). Employer matching contributions under the 401(k) plan recognised as an expense was US$20,000 for the year ended 31 December 2019 (2018: US$20,000).

(b) Share-based payments

The Employee Share and Employee Option Plans, established by shareholder resolutions on 29 November 1994, provide for employees, executives and directors to be granted ordinary shares or options over ordinary shares at the discretion of the Nomination and Remuneration Committee.

Employee Share Plan

The following sets forth the share-based compensation transactions under the Company's Employee Share Plan ("ESP").

The number and weighted average share price, is as follows:

	Weighted average exercise price 2019	**Number of shares 2019**	**Weighted average exercise price** 2018	**Number of shares** 2018
Outstanding at the beginning of the period	-	-	A$0.20	3,700,000
Granted during the period	-	-	-	-
Forfeited during the period	-	-	A$0.20	(3,700,000)
Outstanding at the end of the period	-	-	A$0.20	-

During the current year, no shares were granted under the Company ESP to employees as long term incentive compensation (2018: nil).

17. Employee benefits (continued)

(b) Share-based payments (continued)

Employee Option Plan

The following sets forth the share-based compensation transactions under the Company's Employee Option Plan ("EOP"). The number and weighted average exercise prices of options over ordinary shares, is as follows:

	Weighted average exercise price 2019	**Number of options 2019**	**Weighted average exercise price** 2018	**Number of options** 2018
Outstanding at the beginning of the period	**A$0.20**	**12,800,000**	A$0.20	1,000,000
Granted during the period	**A$0.20**	**1,500,000**	A$0.20	11,800,000
Exercised during the period	**-**	**-**	-	-
Forfeited during the period	**A$0.20**	**(6,100,000)**	-	-
Outstanding at the end of the period	**A$0.20**	**8,200,000**	A$0.20	12,800,000
Exercisable at the end of the period	**A$0.20**	**3,900,000**	A$0.20	2,500,000

At 31 December 2019, there were 8,200,000 options over ordinary shares outstanding (2018: 12,800,000). During the year, 1,500,000 options were granted (2018: 11,800,000), 6,100,000 options were forfeited (2018: nil), and no options were exercised.

Share and option grants to key management personnel

No options over ordinary shares were granted to key management personnel during the year ended 31 December 2019 (2018: 10,200,000).

The following table summarises the fair value assumptions of options and shares granted to key management personnel during the years ended 31 December 2019 and 2018, respectively.

	Key management personnel 2019	Key management personnel 2018
Weighted average fair value at measurement date	**-**	A$0.014
Weighted average share price	**-**	A$0.106
Weighted average exercise price	**-**	A$0.20
Expected volatility (expressed as weighted average used in the modelling under Black-Scholes model)	**-**	82.82%
Expected option life (expressed as weighted average used in the modelling under Black-Scholes model)	**-**	2.9 years
Expected dividends	**-**	-
Risk-free interest rate (based on national government bonds)	**-**	2.165%

The expected volatility is based on historic volatility (calculated based on the weighted average remaining life of the shares and options), adjusted for any expected changes to future volatility due to publicly available information.

18. Provisions

	MENA [1]		Rehabilitation [2]		Total	
	2019 US$'000	2018 US$'000	**2019 US$'000**	2018 US$'000	**2019 US$'000**	2018 US$'000
Non-current						
Balance at 1 January	**7,617**	-	**198**	179	**-**	179
Amounts transferred from trade and other payables	**-**	7,617	**-**	-	**-**	7,617
Changes in provision estimate	**(2,100)**	-	**505**	-	**-**	-
Provisions made during the year	**1,195**	-	**-**	-	**-**	-
Unwind of discount	**-**	-	**13**	19	**13**	19
Balance at 31 December	**6,712**	7,617	**716**	198	**7,428**	7,815

1. In the previous year, trade and other payables of US$7,617,000 associated with the Group's interests in Block S-1 and Block 7 were reclassified to provisions due to these cash outflows being subject to the receipt of Yemen government approvals to restart operations. There is uncertainty associated with the expected timing of this approval and judgement applied in estimating the related cash outflows.

   The MENA change in provision estimate includes US$1,575,000 which has been recorded in other income/(expenses) during the year in relation to Block 7.

2. Refer to note 3 (l) for details of the Group's accounting policy on rehabilitation.

19. Capital and reserves

Share capital

	Ordinary Shares	
In thousands of shares	**2019**	2018
On issue at 1 January	**333,588**	322,288
Shares issued	**65,000**	15,000
Shares cancelled [1]	**-**	(3,700)
On issue at 31 December – fully paid	**398,588**	333,588

[1] *Buyback and cancellation of share options previously held by the trustee under the Employee Share Plan.*

The Company does not have authorised capital or par value in respect of its issued shares.

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company.

Translation reserve

The translation reserve comprises all foreign currency differences arising from the translation of the financial statements of operations where their functional currency is different to the presentation currency of the reporting entity.

Option reserve

The option reserve comprises the fair value of options to be issued as an underwriting fee in relation to the fully underwritten rights issue.

Share-based compensation

The share-based compensation represents the value of unvested options issued under the Company's Employee Option Plan. The value of vested options are transferred to share capital on vesting.

20. Risk management framework and additional financial instruments disclosures

Capital management

The Board's policy is to maintain an appropriate capital base to sustain future development of the Group. This capital base may comprise equity and borrowings.

Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

Risk Management Framework

The Board of Directors has overall responsibility for the establishment and oversight of the risk management framework. There is no separate risk management committee.

Risk management policies are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities. The Group, through their training and management standards and procedures, aim to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

The forecast financial position of the Group is continually monitored and derivative financial instruments can be used to hedge exposure to fluctuations in commodity prices (refer to *Commodity Price Risk* below for further details).

The Board oversees how management monitors compliance with the Group's risk management policies and procedures and reviews the adequacy of the risk management framework in relation to the risks faced by the Group.

Additional financial instruments disclosures

Overview

The Group has exposure to the following risks from its use of financial instruments:

- Credit risk
- Liquidity risk
- Market risk

This note presents information about the Group's exposure to each of the above risks, their objectives, policies and processes for measuring and managing risk, and the management of capital. Further quantitative disclosures are included throughout this financial report.

Credit risk

Credit risk represents the loss that would be recognised if counterparties failed to perform as contracted. The credit risk on financial assets of the Group that have been recognised is the carrying amount, net of any provision for doubtful debts. The Group has assessed that the counterparty's credit ratings determined by a recognised ratings agency remains acceptable.

Exposure to credit risk

The carrying amount of the Group's financial assets represents the maximum credit exposure. The Group's maximum exposure to credit risk at the reporting date was:

	Consolidated	
	2019	2018
	US$'000	US$'000
Cash and restricted cash deposits	**691**	4,477
Trade and other receivables	**192**	810
	883	5,287

As at 31 December 2019, exposure to credit risk in relation to cash held by banks was managed with the equivalent of US$0.5 million being held with Australian financial institutions rated AA and the remaining balances are held with other international financial institutions rated A or higher.

20. Risk management framework and additional financial instruments disclosures (continued)

Where possible, the Group manages its credit risk on trade receivables by dealing with only large reputable customers for its oil and gas sales. At balance date, 100% of trade receivable were due from three such customers. The Group does not consider there to be any impairment indicators associated with these debtors. The Group's credit risk is limited to the carrying value of its financial assets. None of the Group's receivables are materially past due (2018: is consistent with 2019).

Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

Ultimate responsibility for liquidity risk management rests with the Board of Directors. The Group manages liquidity risk by monitoring of future rolling cash flow forecasts. These reflect management's expectations of the settlement of financial assets and liabilities.

The following are the contractual maturities of financial liabilities, including estimated interest payments.

31 December 2019

		Contractual cashflows				
	Carrying amount US$000	**6 mths or less US$000**	**6 – 12 mths US$000**	**1 – 2 years US$000**	**2 – 5 years US$000**	**5 years or more US$000**
Trade and other payables	**1,305**	**1,305**	**-**	**-**	**-**	**-**
Secured borrowings	**15,772**	**-**	**-**	**19,952**	**-**	**-**
Total	**17,077**	**1,305**	**-**	**19,952**	**-**	**-**

31 December 2018

		Contractual cashflows				
	Carrying amount US$000	**6 mths or less US$000**	**6 – 12 mths US$000**	**1 – 2 years US$000**	**2 – 5 years US$000**	**5 years or more US$000**
Trade and other payables	2,899	2,899	-	-	-	-
Secured borrowings	9,483	-	-	-	14,786	-
Total	12,382	2,899	-	-	14,786	-

20. Risk management framework and additional financial instruments disclosures (continued)

Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, commodity prices, interest rates will affect the Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return.

Foreign exchange risk

During 2018 and 2019, operating costs were incurred in US, Australian and Canadian dollars, Arab Emirates Dirham and Yemeni Rials.

Throughout 2018 and 2019, the Group held the majority of its liquid funds in US dollars.

Fluctuations in the Australian dollar/US dollar exchange rate have impacted the underlying performance of the Group. The Group's policy is not to hedge the Australian dollar/US dollar exchange rate risk as income (cash inflows) and expenses (cash outflows), are predominantly denominated in US dollars, with the exception of Australian dollar denominated equity funding, consequently surplus funds are primarily held in US dollars. The impact of Arab Emirates Dirham, Canadian dollars and Yemeni Rials was not material.

Commodity price risk

The revenue and income of the Group are affected by changes in natural gas and crude oil prices, and from time to time various financial transactions (swap contracts and collar contracts involving NYMEX commodity prices for natural gas and crude oil) may be undertaken to reduce the effect of these changes. The Group ensures that it has sufficient proved reserves of these commodities to cover all these transactions and it only enters into such derivatives to match its anticipated underlying physical production and reserves. The Group also limits the term of the transactions and the percentage of the Company's expected aggregate oil and natural gas production that may be hedged at any time.

Swaps

In a natural gas swap agreement the Group receives from the counterparty the difference between the agreed contracted fixed price and the quoted or published reference settlement price if the latter is lower than the fixed price. If the reference settlement price is higher than the agreed fixed price, the Group will pay the difference to the counterparty.

Collars

In a collar agreement, a floor price and a ceiling price are established. If there is no cash outlay upon entering a collar arrangement, it is called a "costless" or "cashless" collar. If quoted reference prices at the specified date (expiration date) are lower than the floor price, then the counterparty pays the price difference multiplied by the notional quantity to the Group. If the quoted reference prices at the specified date are higher than the ceiling price, then the Group pays the price difference multiplied by the notional quantity to the counterparty.

At 31 December 2019, the Group had no outstanding oil or natural gas hedges in place (previous corresponding period: Nil).

Interest rate risk

The Group's exposure to market interest rates primarily relates to the Group's cash holdings (2018: cash holdings).

The financial instruments exposed to interest rate risk are as follows:

	2019 **US$'000**	2018 US$'000
Financial assets		
Cash and restricted cash deposits	**691**	4,477
	691	4,477

20. Risk management framework and additional financial instruments disclosures (continued)

Sensitivity analysis

In managing commodity price and interest rate risks the Group aims to reduce the impact of short-term fluctuations on the Group's earnings. However, credit considerations limit the amount of hedging with derivative instruments that the Group can enter into. The Group and the Company do not use derivative instruments to manage foreign exchange rate risk. Over the longer-term, permanent changes in commodity prices, interest rates and exchange rates will have an impact on profit.

The estimated impact of a 10 per cent change in the average commodity price for the year ended 31 December 2018 would have increased or decreased the Group's profit or loss by US$109,000 (2018: US$313,000) excluding potential impact of impairments. The estimated impact of a change of 100 basis points in interest rates would have increased or decreased the Group's profit or loss by US$1,000 (2018: US$1,000). The estimated impact of a 10 per cent change in the USD/AUD and USD/CAD exchange rates would have increased or decreased the Group's profit or loss by a total of US$74,000 (2018: US$126,000).

Fair values of financial assets and liabilities

The carrying values of financial assets and liabilities of the Group approximate their fair values.

The Group measures and recognises in the statement of financial position on a recurring basis certain assets and liabilities at fair value in accordance with AASB13 Fair value measurement. The fair value must be estimated for recognition and measurement or for disclosure purposes in accordance with the following hierarchy:

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2: Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (as priced) or indirectly (derived from prices); and

Level 3: Inputs for the asset or liability which are not based on observable market data (unobservable inputs).

The fair values of financial assets and liabilities, together with the carrying amounts shown in the balance sheet, are as follows:

	2019		2018	
	Carrying amount US$'000	**Fair value US$'000**	Carrying amount US$'000	Fair value US$'000
Trade and other receivables	**192**	**192**	810	810
Cash and restricted cash deposits	**691**	**691**	4,477	4,477
Trade and other payables	**(1,305)**	**(1,305)**	(2,899)	(2,899)
Secured borrowings	**(15,772)**	**(15,772)**	(9,483)	(9,483)
Financial derivative instruments	**(358)**	**(358)**	(1,977)	(1,977)
	(16,552)	**(16,552)**	(9,072)	(9,072)

The financial derivative instrument of US$358,000 (2018: US$1,977,000) is a level 2 instrument.

Refer to note 4 for the determination of fair values.

21. Capital and other commitments

	2019 US$'000	2018 US$'000
Capital expenditure commitments		
Exploration, evaluation and development expenditure		
Contracted but not provided for and payable:		
Within one year	**-**	1,776
One year or later and no later than five years	**-**	-
	-	1,776

22. Contingencies and legal matters

The Group is a defendant from time to time in legal proceedings. Where appropriate the Group takes legal advice. The Group does not consider that the outcome of any current proceedings is likely to have a material effect on its operations or financial position.

The production, handling, storage, transportation and disposal of oil and natural gas, by-products thereof and other substances and materials produced or used in connection with oil and natural gas operations were subject to regulation under U.S. federal, state and local laws and regulations primarily relating to protection of human health and environment. To date, expenditure related to complying with these laws and for remediation of existing environmental contamination has not been significant in relation to the results of operations of the Company.

From time to time, the Group is required to provide bonding or security for the benefit of U.S. and Yemen regulatory authorities in relation to its obligations to pay lease rentals and royalties, the plugging and abandonment of oil and natural gas wells, the removal of related facilities, and to meet minimum exploration expenditure commitments. As at 31 December 2019, the Group had US$1.7 million in secured guarantees in place to meet minimum exploration expenditure commitments (December 2018: US$1.7 million).

Subsequent to balance date, a claim was made against the US$4.2 million Letter of Credit supporting the exploration obligations in Block 7 in Yemen, of which the Group's share is US$1.7 million. Refer to note 31 Subsequent Events for further details.

23. Deed of cross guarantee

Pursuant to ASIC Corporations Instrument 2016/785, relief is granted to certain wholly owned Australian subsidiaries of the Company from the Corporations Act requirements for preparation, audit, and publication of Financial Reports and Directors' Reports.

It is a condition of the Class Order that the Company and each of its subsidiaries enter into a Deed of Cross Guarantee Indemnity. The effect of the deed is that the Company guarantees to each creditor payment in full of any debt in the event of winding up of any of the subsidiaries under certain provisions of the Corporations Act. If a winding-up occurs under other provisions of the Act, the Company will only be liable in the event that after six months any creditor has not been paid in full. The subsidiaries have also given similar guarantees in the event that the Company is wound up.

The subsidiaries subject to the Deed are:

- Petsec Investments Pty. Limited
- Petroleum Securities Pty. Limited
- Najedo Pty. Ltd
- Petroleum Securities Share Plan Pty Limited
- Laurel Bay Petroleum Limited
- Ginida Pty. Limited
- Western Medical Products Pty. Limited

A consolidated statement of comprehensive income and consolidated balance sheet, comprising the Company and subsidiaries which are a party to the Deed, after eliminating all transactions between parties to the Deed of Cross Guarantee, as at 31 December 2019 and 2018, is set out as follows:

Summarised consolidated statement of profit or loss and other comprehensive income and retained earnings/(accumulated losses)

	2019 US$000	2018 US$000
Other income and expenses	**5,276**	11,304
Operating expenses	**(1,193)**	(1,653)
Finance income/(expense)	**(2,686)**	(3,600)
Net movement in provisions against loans and investments in controlled entities	**(51,584)**	(30,009)
Profit/(loss) before tax	**(50,187)**	(23,958)
Income tax benefit/(expense)	**-**	-
Profit/(loss) after tax	**(50,187)**	(23,958)
Other comprehensive income	**-**	-
Total comprehensive income for the period	**(50,187)**	(23,958)
Retained earnings/(accumulated losses) at beginning of year	**(188,625)**	(164,667)
Retained earnings/(accumulated losses) at end of year	**(238,812)**	(188,625)

Notes to the consolidated financial statements

For the year ended 31 December 2019

23. Deed of cross guarantee (continued)

Balance sheet

	2019 US$000	2018 US$000
Assets		
Cash and cash equivalents	**420**	2,215
Other receivables	**21**	8
Prepayments	**25**	92
Total current assets	**466**	2,315
Restricted deposits	**46**	200
Other financial assets	**-**	40,992
Right-of-use assets	**98**	
Property, plant and equipment	**7**	95
Total non-current assets	**151**	41,287
Total assets	**617**	43,602
Liabilities		
Trade and other payables	**230**	453
Lease liability	**30**	-
Employee benefits provision	**22**	38
Total current liabilities	**282**	491
Secured borrowings	**15,772**	9,483
Fair value of derivative instruments	**358**	1,977
Employee benefits provision	**183**	186
Lease liability	**69**	-
Total non-current liabilities	**16,382**	11,646
Total liabilities	**16,664**	12,137
Net assets	**(16,047)**	31,465
Equity		
Issued capital	**201,099**	197,855
Reserves	**21,666**	22,235
Retained earnings/(accumulated losses)	**(238,812)**	(188,625)
Total equity	**(16,047)**	31,465

24. Consolidated entities

	Country of Incorporation	Ownership interest 2019 %	Ownership interest 2018 %
Parent entity			
Petsec Energy Ltd			
Significant subsidiaries			
Petsec Investments Pty. Limited	Australia	**100**	100
Petroleum Securities Pty. Limited	Australia	**100**	100
Najedo Pty. Limited	Australia	**100**	100
Petroleum Securities Share Plan Pty. Limited	Australia	**100**	100
Petsec America Pty. Limited	Australia	**100**	100
Petsec (U.S.A.) Inc.	USA	**100**	100
Petsec Energy Inc.	USA	**100**	100
Petsec Exploration and Production LLC	USA	**100**	100
Petsec Energy Resources Inc.	USA	**100**	100
Petsec Energy Canada Ltd	Canada	**100**	100
Laurel Bay Petroleum Limited	Australia	**100**	100
Ginida Pty. Limited	Australia	**100**	100
Western Medical Products Pty. Limited	Australia	**100**	100
Petsec Energy Yemen Ltd	British Virgin Islands	**100**	100
Petsec Energy (Middle Eastern) Limited	British Virgin Islands	**100**	100
West Yemen Oil (Block S-1), Inc.	Turks and Caicos Islands	**100**	100
Yemen (Block S-1), Inc.	Cayman Islands	**100**	100
Oil Search (ROY) Limited	British Virgin Islands	**100**	100

With the exception of Petsec Energy (Middle Eastern) Limited, Petsec Energy Yemen Ltd, West Yemen Oil (Block S-1), Inc., Yemen (Block S-1), Inc., and Oil Search (ROY) Limited, all entities carry on business in the country where they were incorporated.

25. Segment reporting

The Group operates in the oil and gas industry.

Segment information is presented in the consolidated financial statements in respect of the Group's geographic segments, which reflects the presentation of information to the chief operating decision maker.

Segment results include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Segment acquisition of property, plant and equipment, intangibles and exploration, evaluation and development assets is the total cost incurred during the period to acquire segment assets that are expected to be utilised for more than one period.

In presenting information on the basis of geographical segments, segment assets and liabilities, segment revenue and net profit/(loss) after tax are based on the geographical location of operations.

	Australia		USA		MENA		Canada		Consolidated	
	2019 US$'000	2018 US$'000	**2019 US$'000**	2018 US$'000	**2019 US$'000**	2018 US$'000	**2019 US$'000**	2018 US$'000	**2019 US$'000**	2018 US$'000
Oil and gas sales	**-**	-	**1,088**	3,142	**-**	-	**-**	-	**1,088**	3,142
Net revenues after royalties *	**-**	-	**1,088**	3,142	**-**	-	**-**	-	**1,088**	3,142
Segment net profit/(loss) before tax	**(3,952)**	(5,226)	**(17,962)**	(1,865)	**(2,327)**	(2,917)	**-**	(42)	**(24,241)**	(10,050)
Income tax expense	**-**	-	**-**	-	**-**	-	**-**	-	**-**	-
Profit/(loss) after tax	**(3,952)**	(5,226)	**(17,962)**	(1,865)	**(2,327)**	(2,917)	**-**	(42)	**(24,241)**	(10,050)
Depreciation, depletion, amortisation & reclamation	**126**	12	**2,461**	1,742	**6**	7	**-**	41	**2,593**	1,802
Change in rehabilitation provision	**-**	-	**505**	-	**-**	-	**-**	-	**505**	-
Dry hole, impairment and abandonment expense	**-**	-	**13,714**	-	**117**	469	**-**	-	**13,831**	469
Segment assets	**616**	2,611	**4,640**	18,935	**116**	1,986	**-**	-	**5,372**	23,532
Acquisition of property, plant and equipment and exploration, evaluation and development assets	**3**	-	**3,485**	2,647	**-**	2	**-**	-	**3,488**	2,649

** There are no inter-segment sales*

*** 100% of the Group's oil and gas sales and royalties are derived from three customers.*

25. Segment reporting (continued)

	Australia		USA		MENA		Canada		Consolidated	
	2019 US$'000	2018 US$'000	**2019 US$'000**	2018 US$'000	**2019 US$'000**	2018 US$'000	**2019 US$'000**	2018 US$'000	**2019 US$'000**	2018 US$'000
Segment liabilities	**16,663**	12,138	**1,095**	1,972	**7,608**	8,451	**11**	10	**25,377**	22,571
Cash flows used in operating activities	**(1,079)**	(1,422)	**(180)**	668	**(1,033)**	(2,991)	**-**	(31)	**(2,292)**	(3,776)
Cash flows used in investing activities	**(3)**	-	**(3,485)**	(2,647)	**-**	1,325	**-**	-	**(3,488)**	(1,322)
Cash flows from financing activities	**3,869**	4,500	**(41)**	-		-		-	**3,828**	4,500

26. Interests in unincorporated joint operating arrangements

Included in the assets of the Group are the following items which represent the Group's interest in the assets and liabilities in joint operating arrangements:

Assets	**2019 US$'000**	2018 US$'000
Oil and gas properties:		
Producing leases – at cost	**19,468**	23,366
Less: accumulated amortisation and impairment	**(15,219)**	(5,531)
	4,249	17,835
Represented by the following lease carrying values:		
- Offshore Gulf of Mexico	**4,233**	16,576
- Onshore Louisiana	**16**	1,259
- MENA	**-**	-
Total oil and gas properties	**4,249**	17,835

Liabilities	**2019 US$'000**	2018 US$'000
Rehabilitation provision:		
- Offshore Gulf of Mexico	**501**	99
- Onshore Louisiana	**215**	99
	716	198

The contribution of the Group's joint operating arrangements to EBIT (including exploration write-offs and impairments; and excluding the effects of hedging and any gain on sale of interests):	**2019 US$'000**	2018 US$'000
- Offshore Gulf of Mexico	**(14,672)**	1,459
- Onshore Louisiana	**(1,355)**	(617)
- Onshore Canada	**-**	(42)
- MENA	**(455)**	(1,296)
	(16,482)	(496)

The principal activity of all the joint operating arrangements is oil & gas exploration. Listed below is the geographic location of each of the joint operating arrangements and the percentage working interest held in the joint operating arrangement by the Group as at and during the year ended 31 December:

	Interest held 2019	Interest held 2018
- Offshore Gulf of Mexico	**12.50%**	12.50%
- Onshore Louisiana	**12.50% to 25.00%**	12.50% to 25.00%
- MENA	**75.00% to 100.00%**	75.00% to 100.00%

In respect of the joint operating arrangements listed above, the voting powers of the Group align with its ownership percentages listed in all cases. Management has determined that the Group has joint control of these arrangements by virtue of the agreements it has with its other partners. The Group accounts for its share of the individual assets and liabilities of the joint operating arrangements in light of the fact that all of these arrangements lack legal form as separate vehicles.

27. Wholly owned areas of interest

Included in the assets and liabilities of the Group are the following items which represent the Group's wholly owned areas of interest:

Assets	2019 US$'000	2018 US$'000
Oil and gas properties:		
Producing leases – at cost	**3,556**	3,556
Less: accumulated amortisation and impairments	**(3,556)**	(3,439)
	-	117
Represented by the following lease carrying values:		
- MENA	**-**	117
	-	117

Liabilities	2019 US$'000	2018 US$'000
Rehabilitation provision:		
- MENA	**-**	-
	-	-

	2019 US$'000	2018 US$'000
The contribution of the Group's areas of interest to EBIT (including exploration write-offs and impairments; and excluding the effects of hedging):		
- MENA	**(872)**	(742)
	(872)	(742)

28. Reconciliation of cash flows from operating activities

	2019 US$'000	2018 US$'000
Cash flows from operating activities		
Loss for the period	**(24,241)**	(10,050)
Adjustments for:		
Depreciation, depletion and amortisation	**2,593**	1,802
Dry-hole and impairment expense	**13,831**	469
Change in rehabilitation provision	**505**	-
Derecognition of restricted cash	**1,680**	-
Reversal of MENA provisions	**(1,575)**	-
Loss on disposal of assets	**81**	-
Net foreign exchange gains	**7**	(28)
Share-based payment expenses	**86**	142
Operating loss before changes in working capital and provisions	**(7,033)**	(7,665)
Decrease/(increase) in restricted cash deposits	**154**	(1,680)
Decrease/(increase) in receivables and prepayments	**710**	(83)
Increase/(decrease) in payables and provisions	**3,877**	5,652
Net cash used in operating activities	**(2,292)**	(3,776)

29. Related parties

The following were key management personnel of the Group at any time during the reporting period and unless otherwise indicated were key management personnel for the entire period:

Non-executive director	*Executive director*
D A Mortimer	T N Fern (Executive Chairman)
A P Baden	S W Bokhari (Managing Director) [1]

1 *Mr Bokhari was appointed Managing Director of Petsec Energy Ltd effective from 1 May 2019.*

Executives
M Petkovski (Chief Executive Officer, Petsec Energy (Middle Eastern) Limited) [2]
R A Keogh (Group Chief Financial Officer and President, Petsec Energy Inc.)
P Gahdmar (Company Secretary and Group Financial Controller, Petsec Energy Ltd)

1 *Mr Petkovski resigned on 30 April 2019.*

Key management personnel compensation

The key management personnel compensation included in personnel expenses (see note 6) is as follows:

	2019 US$	2018 US$
Wages and salaries	**693,464**	537,338
Service agreements	**433,307**	717,696
Termination benefits	**243,845**	-
Post-employment benefits	**36,358**	32,597
Share-based payment compensation	**71,681**	124,726
Other benefits [1]	**88,239**	115,162
	1,566,894	1,527,519

1. *Other benefits represent amounts paid on behalf of the Managing Director and Executive Officers in respect of insurance, car parking, fringe benefits and sign-on bonuses.*

Individual directors and executive compensation disclosures

Information regarding individual directors' and executives' compensation and some equity instruments disclosures as required by Corporations Act s300A and Corporations Regulations 2M.3.03 are provided in the Remuneration Report section of the Directors' Report on pages 24 to 32.

Apart from the details disclosed in this note, no director has entered into a material contract with the Company or Group since the end of the previous financial year and there were no material contracts involving directors' interests existing at year-end.

Non-executive directors appointed prior to 2003 are entitled to receive a retirement benefit that is equivalent to the remuneration received in the three years prior to retirement. Incoming non-executive directors appointed thereafter are not entitled to receive retirement benefits in accordance with the recommendations made by the ASX Corporate Governance Council. Directors' retirement obligations are presently US$137,000 in total (2018: US$137,000).

Transactions with key management personnel

Key management personnel of the Company and their immediate relatives control approximately 13.1 percent of the voting shares of the Company.

During the year, no options were issued by the Company under its shareholder approved Employee Option Plan ("EOP") to key management personnel as long term incentive compensation (2018: 10,200,000).

The aggregate amounts recognised in service agreements during the year relating to key management personnel and their personally related entities, were a total expense of US$433,000 (2018: US$718,000). Refer to Remuneration Report for further details.

29. Related parties (continued)

Assets and liabilities arising from the above related party transactions

	2019 US$'000	2018 US$'000
Current assets		
Related party receivables	**-**	-
Current liabilities		
Related party payables	**122**	438

Other related party disclosures

Information relating to subsidiaries is set out in note 24.

30. Parent entity disclosures

As at, and throughout, the financial year ending 31 December 2019 the parent entity of the consolidated group was Petsec Energy Ltd.

	2019 US$'000	2018 US$'000
Result of parent entity		
Profit/(loss) for the period	**(50,186)**	(12,593)
Other comprehensive income	**(506)**	(3,667)
Total comprehensive income/(loss) for the period	**(50,692)**	(16,260)
Financial position of parent entity at year end		
Current assets	**465**	2,315
Total assets	**616**	47,565
Current liabilities	**252**	491
Total liabilities	**16,663**	16,100
Total equity of the parent entity comprising of:		
Share capital	**201,099**	197,855
Share-based payment compensation reserve	**74**	126
Foreign currency translation reserve	**21,534**	22,040
Option reserve	**405**	417
Accumulated losses	**(239,159)**	(188,973)
Total equity	**(16,047)**	31,465

Parent entity guarantees in respect of the debts of its subsidiaries

The parent entity has entered into a Deed of Cross Guarantee with the effect that the Company guarantees debts in respect of its subsidiaries. Further details of the Deed of Cross Guarantee and the subsidiaries subject to the deed are disclosed in note 23.

Parent entity contingencies and capital commitments

The parent entity had no contingent liabilities and capital commitments outstanding at 31 December 2019.

31. Subsequent events disclosure

As announced to the ASX on 19 February 2020, a claim was made on the Letter of Credit issued under the Production Sharing Agreement on Block 7. In Petsec's opinion, the claim is fraudulent and was made by the illegitimate rebel Houthi Minister for Oil and Minerals. Despite concerted efforts by Petsec to prevent any action on the claim, the Qatar National Bank released the US$1.68 million of restricted cash that was on deposit as collateral to support the Group's Letter of Credit. Other banks also responded to the fraudulent claim and the Company is working with its legal advisors to pursue all options it has to recover the funds.

The Company was also advised by Mitsui that the Commonwealth Bank Australia had also released US$1.05 million of AWE/Mitsui's funds in response to a similar claim. Mitsui is seeking to recover these funds from Petsec and the Company is seeking further information from AWE/Mitsui and will defend any action to recover the funds.

Other than the matter disclosed above, there has not arisen in the interval between the end of the financial year and the date of this report any item, transaction or event of a material and unusual nature likely, in the opinion of the directors of the Company, to affect significantly the operations of the Group, the results of those operations, or the state of affairs of the Group, in future years.

Directors' Declaration

1 In the opinion of the directors of Petsec Energy Ltd (“the Company”):

(a) the financial statements and notes and the Remuneration report in the Directors’ Report, set out on pages 24 to 71, are in accordance with the Corporations Act 2001 including:

(i) giving a true and fair view of the financial position of the Company and the Group as at 31 December 2019 and of their performance, as represented by the results of their operations and their cash flows, for the year ended on that date; and

(ii) complying with Australian Accounting Standards and the Corporations Regulation 2001; and

(b) the financial report also complies with International Financial Reporting Standards as disclosed in note 2; and

(c) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

2 There are reasonable grounds to believe that the Company and the controlled entities identified in note 25 will be able to meet any obligations or liabilities to which they are or may become subject to by virtue of the Deed of Cross Guarantee between the Company and those controlled entities pursuant to ASIC Corporations Instrument 2016/785.

3 The directors have been given the declarations required by Section 295A of the Corporations Act 2001 from the Chief Executive Officer and Chief Financial Officer for the financial year ended 31 December 2019.

Signed in accordance with a resolution of the directors:

Terrence N. Fern
Director

Sydney, 28 February 2020

Independent Auditor's Report

To the shareholders of Petsec Energy Ltd

Report on the audit of the Financial Report

Opinion

We have audited the ***Financial Report*** of Petsec Energy Ltd (the Company).

In our opinion, the accompanying Financial Report of the Company is in accordance with the *Corporations Act 2001*, including:

- giving a true and fair view of the ***Group's*** financial position as at 31 December 2019 and of its financial performance for the year ended on that date; and
- complying with *Australian Accounting Standards* and the *Corporations Regulations 2001*.

The ***Financial Report*** comprises:

- Consolidated statement of financial position as at 31 December 2019;
- Consolidated statement of profit or loss and other comprehensive income, Consolidated statement of changes in equity, and Consolidated statement of cash flows for the year then ended;
- Notes including a summary of significant accounting policies; and
- Directors' Declaration.

The ***Group*** consists of the Company and the entities it controlled at the year end or from time to time during the financial year.

Basis for opinion

We conducted our audit in accordance with *Australian Auditing Standards*. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the Financial Report* section of our report.

We are independent of the Company and Group in accordance with the *Corporations Act 2001* and the ethical requirements of the *Accounting Professional and Ethical Standards Board's APES 110 Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the Financial Report in Australia. We have fulfilled our other ethical responsibilities in accordance with the Code.

Material uncertainty related to going concern

We draw attention to Note 2(d), "Going concern basis of preparation" in the financial report. The conditions disclosed in Note 2(d), indicate a material uncertainty exists that may cast significant doubt on the Group's ability to continue as a going concern and, therefore, whether it will realise its assets and discharge its liabilities in the normal course of business, and at the amounts stated in the financial report. Our opinion is not modified in respect of this matter.

In concluding there is a material uncertainty related to going concern we evaluated the extent of uncertainty regarding events or conditions casting significant doubt in the Group's assessment of going concern. Our approach to this involved:

- evaluating the feasibility, quantum and timing of the Group's plans to renegotiate the maturity of existing convertible note facility and the additional facility, and reduce general and administrative expenditures to address going concern;
- assessing the Group's cash flow forecasts for incorporation of the Group's operations and plans to address going concern, in particular in light of the history of loss making operations and repayment schedule for the Convertible Note; and
- determining the completeness of the Group's going concern disclosures for the principle matters casting significant doubt on the Group's ability to continue as a going concern, the Group's plans to address these matters, and the material uncertainty.

Key Audit Matters

The ***Key Audit Matters*** we identified are:

- Oil and Gas Properties.

Key Audit Matters are those matters that, in our professional judgment, were of most significance in our audit of the Financial Report of the current period.

These matters were addressed in the context of our audit of the Financial Report as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

KPMG

Oil and Gas properties $4.3m	
Refer to Note 12(a) to the financial report.	
The key audit matter	**How the matter was addressed in our audit**
The Group's Oil and Gas properties were a significant portion (80%) of the Group's total assets, and their carrying value was a key audit matter due to the high level of judgement required by us to assess the carrying value. The key judgements involved in the carrying value assessment are forward looking assumptions, as used in the Group's value in use models. The key assumptions are forecast production, oil and gas prices, discount rates and reserve estimates. Management obtain a reserve report from a third party expert to assist in their carrying value assessment. Our assessment is made more challenging given certain recent operating conditions, intermittent production issues, political instability in Middle Eastern located wells and the oil and gas price volatility, each of which are uncertain as to their future improvement.	Our audit procedures included, amongst others: • We held discussions with management and read the minutes of directors meetings and ASX announcements to understand if the Group had decided to discontinue production at any well. We used this knowledge when assessing forecast production assumptions and the recoverability of the oil and gas properties. • We compared historical production profiles for consistency with forecast production trends. We analysed the impact of the political instability in the Middle East to forecast production. We compare forecast production to third party expert reserve reports and investigated inconsistencies. • For all oil and gas properties we performed sensitivity analysis on key assumptions in the value in use models such as production forecasts, discount rates and oil and gas prices to identify areas of increased audit focus. • We compared management's oil and gas price assumptions against published forecasts such as the (WTI oil price) and investigated inconsistencies. • We obtained the Group's value in use models and agreed amounts to Board approved production plans, budgets and the third party reserve report. • We assessed the competence and the independence of the third party experts who prepare the third party reserve report used by management to assist in their carrying value assessment of oil and gas properties.

Other Information

Other Information is financial and non-financial information in Petsec's annual reporting which is provided in addition to the Financial Report and the Auditor's Report. The Directors are responsible for the Other Information.

Our opinion on the Financial Report does not cover the Other Information and, accordingly, we do not express any form of assurance conclusion thereon.

In connection with our audit of the Financial Report, our responsibility is to read the Other Information. In doing so, we consider whether the Other Information is materially inconsistent with the Financial Report or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

We are required to report if we conclude that there is a material misstatement of this Other Information, and based on the work we have performed on the Other Information that we obtained prior to the date of this Auditor's Report we have nothing to report.

Responsibilities of the Directors for the Financial Report

The Directors are responsible for:

- preparing the Financial Report that gives a true and fair view in accordance with *Australian Accounting Standards* and the *Corporations Act 2001;*
- implementing necessary internal control to enable the preparation of a Financial Report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.
- assessing the Company and Group's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate. This includes disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to liquidate the Company and Group or to cease operations, or have no realistic alternative but to do so.

Auditor’s responsibilities for the audit of the Financial Report

Our objective is:

- to obtain reasonable assurance about whether the Financial Report as a whole is free from material misstatement, whether due to fraud or error; and
- to issue an Auditor’s Report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Australian Auditing Standards will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error. They are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this Financial Report.

A further description of our responsibilities for the Audit of the Financial Report is located at the Auditing and Assurance Standards Board website at: http://www.auasb.gov.au/auditors_responsibilities/ar1.pdf This description forms part of our Auditor’s Report.

KPMG

Report on the Remuneration Report

Opinion

In our opinion, the Remuneration Report of Petsec Energy Ltd for the year ended 31 December 2019, complies with *Section 300A* of the *Corporations Act 2001*.

Director's responsibilities

The Directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with *Section 300A* of the *Corporations Act 2001*.

Our responsibilities

We have audited the Remuneration Report included in pages 24 to 32 of the Director's report for the year ended 31 December 2019.

Our responsibility is to express an opinion on the Remuneration Report, based on our Audit conducted in accordance with *Australian Auditing Standards*.

KPMG

KPMG

Daniel Camilleri

Partner

Sydney

28 February 2020

Exploration and Production Interests

USA				
Geographical Location	**Field/Prospect**	**Status**	**Working Interest**	**Revenue Interest**
USA				
Onshore Louisiana	Jeanerette	Shut-in	12.5%	9.22%
	Mystic Bayou	Producing	25.0%	18.50%
	Ouiski Bayou	Evaluation	12.5%	9.22%
Gulf of Mexico	Hummer Gas/Oil Field (Main Pass Blocks 270/273/274)	Producing/Evaluation	12.5%	10.70454% [1]

MENA Region				
Geographical Location	**Licence**	**Status**	**Working Interest**	**Participating Interest**
Yemen				
Shabwah Basin	Block 7, Al Barqa Permit	Evaluation	35.0%	29.75%
	Block 7, Al Barqa Permit	Evaluation	40.0%	34.00%
	Block 7, Al Barqa Permit [1]	Evaluation	25.0%	21.25%
	Block S-1, Damis Production Licence	Shut-in	100.0%	82.50%

1. *Comprises N.R.I. 10.26354% and ORRI: 0.441%.*
2. *The Company has an agreement with KUFPEC (25% W.I.) to acquire its interests in the Block 7, Al Barqa Permit, in the Republic of Yemen. The agreement was not completed as of 31 December 2019 and is subject to customary approvals from the Government of Yemen and the Ministry of Oil and Minerals. The agreement has expired.*

Shareholder Information

Number of Shareholders

Issued capital was 398,587,924 ordinary shares held by 1,744 shareholders.

All issued shares carry equal voting rights on a one for one basis.

Size of Holding	No. of Holders
1 – 1,000	171
1,001 – 5,000	256
5,001 – 10,000	385
10,001 – 100,000	688
100,001 and over	244
Total number of shareholders	**1,744**
Number holding less than a marketable parcel	653

Largest Twenty Shareholders

The largest twenty shareholders held 278,242,330 ordinary shares being 69.807% of the issued ordinary capital.

Name of Shareholder	Number of Shares Held	% of Issued Capital
Martin Place Securities Nominees Pty Ltd	143,648,336	36.039
Canning Oil Pty Ltd	25,709,116	6.450
Citicorp Nominees Pty Limited	15,242,711	3.824
Arc Investments Inc.	11,602,679	2.911
Mr David A Mortimer & Mrs Barbara L Mortimer	11,335,339	2.844
HSBC Custody Nominees (Australia) Limited	10,551,356	2.647
Geofin Consulting Services Pty Limited	8,989,610	2.255
Alcardo Investments Limited	6,933,095	1.739
Mr Edward Gacka & Mrs Beryl Gacka	6,905,925	1.733
BNP Paribas Nominees Pty Ltd	6,130,062	1.538
Martin Place Securities Nominees Pty Ltd <Gulf Stream A/c>	5,300,549	1.330
Mangaroo Pty Ltd	3,840,000	0.963
Mr Peter Gacka & Mrs Jenny Gacka	3,800,000	0.953
Hestian Pty Ltd	3,127,843	0.785
Den Duyts Corporation Pty Ltd	3,057,635	0.767
Ms Dan Luo	2,649,943	0.665
Calveston Worldwide Ltd	2,460,000	0.617
Sino Champion Development Limited	2,459,579	0.617
Asian Corporate Advisers (BVI) Limited	2,250,000	0.564
Solus Consultants Pty Ltd	2,248,552	0.564
Substantial shareholders disclosed in substantial shareholder notices given to the Company are as follows:		
Canning Oil Pty Ltd including its associates	37,876,361	9.503

Petsec Energy

5 Year Comparative Data Summary

		2015	2016	2017	2018	2019	% change
Financial Performance							
Net Production (MMcfe) [1]		511	313	347	796	368	(54%)
Average Gas Equiv. Price Received	(US$/Mcfe)	$3.07	$3.48	$3.79	$3.93	$2.96	(25%)
US$ million							
Net Revenue	(US$m)	$1.6	$1.1	$1.3	$3.1	$1.1	(65%)
Net Profit/(Loss) after Tax	(US$m)	($10.6)	($13.0)	($12.0)	($10.1)	($24.2)	n/a
Depreciation, depletion & amortisation	(US$m)	$0.5	$0.8	$1.4	$1.8	$2.6	44%
Exploration write-offs, impairments, abandonment and work-over expenses	(US$m)	$6.4	$2.1	$4.0	$0.5	$13.8	2,660%
Net financial expense	(US$m)	$0.2	$0.8	$0.3	$4.9	$3.7	(24%)
Change in rehabilitation provision	(US$m)	-	-	($0.5)	-	$0.5	n/a
Income tax (benefit)/expense	(US$m)	-	-	-	-	-	-
EBITDAX [2]	(US$m)	($3.5)	($9.3)	($6.8)	($2.9)	($3.6)	n/a
EBITDAX Margin/Mcfe	(US$/Mcfe)	($6.81)	($29.84)	($19.53)	($3.69)	($9.85)	n/a
Balance Sheet							
Total Assets	(US$m)	$32.5	$35.4	$20.2	$23.5	$5.4	(77%)
Cash [3]	(US$m)	$12.8	$13.1	$3.5	$4.5	$0.7	(84%)
Debt	(US$m)	-	$3.3	$5.6	$9.5	$15.8	66%
Shareholders' Equity	(US$m)	$23.8	$18.1	$7.0	$1.0	($20.0)	n/a
Cashflow and Capital Expenditures							
Net cashflow from:							
Operations	(US$m)	($5.8)	($6.8)	($4.9)	($3.8)	($2.3)	n/a
Investing	(US$m)	($12.3)	($2.8)	($4.3)	($1.3)	($3.5)	n/a
Financing	(US$m)	-	$10.0	$2.5	$4.5	$3.8	(11%)
		($18.1)	$0.4	($6.7)	($0.6)	($2.0)	n/a
Capital Expenditures [4]							
Exploration	(US$m)	$12.2	$1.3	-	-	-	n/a
Development	(US$m)	$0.5	$1.2	$5.0	$4.0	$2.6	(35%)
Acquisition	(US$m)	$3.4	$3.0	$0.1	$0.2	-	(100%)
		$16.1	$5.5	$5.1	$4.2	$2.6	
A$ million							
EBITDAX [2]	(A$m)	($4.7)	($12.5)	($8.9)	($3.9)	($5.2)	n/a
Net Profit/(Loss) after Tax	(A$m)	($14.1)	($17.5)	($15.7)	($13.5)	($34.7)	n/a
USD/AUD exchange rate		0.7517	0.7420	0.7655	0.7476	0.6967	(7%)
Operating Margins & Costs							
Average Gas Price Received	(US$/Mcfe)	$3.07	$3.48	$3.79	$3.93	$2.96	(25%)
+ Other Income	(US$/Mcfe)	$1.50	$0.63	$0.07	$0.04	($0.48)	n/a
- Operating Costs (GG&A + LOE)	(US$/Mcfe)	$11.38	$33.95	$23.39	$7.66	$12.36	61%
= EBITDAX [2] Margin	(US$/Mcfe)	($6.81)	($29.84)	($19.53)	($3.69)	($9.88)	n/a
Depreciation, Depletion & Amortisation	(US$/Mcfe)	$1.05	$2.53	$4.08	$2.27	$7.05	211%
Proved and Probable Reserves (2P) [5]							
USA	(MMboe)	3.7	3.9	3.8	3.5	2.8	(20%)
Yemen [6]	(MMboe)	5.6	5.6	5.6	5.6	5.6	-
		9.3	9.5	9.4	9.1	8.4	(8%)

1 *MMcfe = million cubic feet of gas equivalent. Mcfe = thousand cubic feet of gas equivalent. Conversion ratio: 1 barrel of oil = 6 Mcf of gas.*

2 *EBITDAX = earnings before interest (financial income and expense), income tax, depreciation, depletion and amortisation, and exploration (including dry hole and impairment expense, exploration and work-over expense). EBITDAX is a non-IFRS number and is unaudited.*

3 *FY2019 includes US$0.1 million of restricted cash deposits.*

4 *Excludes minor (non-oil & gas) property, plant & equipment expenditure and investments.*

5 *2P reserve estimates are based on independent reserve assessments.*

6 *An Nagyah Oilfield reserves as attributed by DeGolyer and McNaughton Canada Limited as of 1 January 2016. This is unchanged from the initial reserves assessment prepared by DeGolyer and McNaughton Canada, and announced to the ASX on 15 March 2016.*

Glossary

1P	Proved reserves
2P	Proved and probable reserves
AMI	Area of mutual interest
Bcf	Billion cubic feet of gas
Bcfe	Billion cubic feet of gas equivalent
Bopd	Barrels of oil per day
Capex	Capital expenditure
cps	Cents per share
DD&A	Depreciation, depletion and amortisation
EBITDAX	Earnings before Interest, taxation, depreciation, amortisation and exploration expense. EBITDAX is a non-IFRS number
Field	An area consisting of a single reservoir or multiple reservoirs all grouped on or related to the same individual geological structural feature and/or stratigraphic condition
JV	Joint venture
Mbbls	Thousand barrels of crude oil or other liquid hydrocarbons
Mbo	Thousand barrels of oil
Mboe	Thousand barrels of oil equivalent
MMbbls	Million barrels of crude oil or other liquid hydrocarbons
MMbo	Million barrels of oil
MMboe	Million barrels of oil equivalent
Mcfe	Thousand cubic feet of gas equivalent
MMcf	Million cubic feet of gas
MMcfe	Million cubic feet of gas equivalent
MMcfpd	Million cubic feet of gas per day
NRI	Net revenue interest
Oil	Crude oil and condensate
Proved reserves	The estimated quantities of crude oil, natural gas and natural gas liquids that geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions
Proved undeveloped reserves	Proved reserves that are expected to be recovered from new wells on undrilled acreage or from existing wells where a relatively major expenditure is required for recompletion
Working Interest or W.I.	The operating interest which gives the owner the right to drill, produce and conduct operating activities on the property and a share of production

Corporate Directory

Board of Directors
Terrence N Fern – Executive Chairman
Syed W Bokhari – Managing Director
David A Mortimer – Non-executive Director
Alan P Baden – Non-executive Director

Company Secretary
Paul Gahdmar

Corporate Management
Terrence N Fern – Executive Chairman
Syed W Bokhari – Managing Director
Ross A Keogh – Group Chief Financial Officer
Paul Gahdmar – Company Secretary and Group Financial Controller

MENA Management
John L Rees – Vice President Technical of PEMEL
Ajay Goyal – General Manager Finance of PEMEL

USA Management
Ross A Keogh – President of PEI

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International Towers Sydney
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Sydney NSW 2000 Australia

Stock Exchange
Listed on the Australian Stock Exchange, Symbol: PSA
Traded in USA on ADRs, Symbol: PSJEY

Corporate Governance Statement
http://www.petsec.com.au/about-us/corporate-governance/

For further information
Web: www.petsec.com.au