



26 October 2007

## **Chairman's address to annual meeting of shareholders Intercontinental Hotel, Wellington NZ.**

At last year's annual meeting, I advised that NZOG's three development projects were powering ahead – I am now pleased to report on the very positive outcomes achieved with respect to these projects in the 12 months since then, with the envisaged oil production now taking place from the Tui Area, project financing being in place for and work well advanced in the large Kupe development and the successful sponsorship by NZOG of the public float of Pike River Coal.

### **Tui**

One result of these successes is that NZOG is now generating substantial revenues from its Tui oil production, which started at the end of July this year. A recent interim assessment of Tui reserves indicates that the amount of recoverable oil from the Tui area is 15% greater than the figure on which the original development decision was made.

### **Pike River Coal**

Pike River Coal Ltd was brought to the investment market through a public equity raising of \$85 million. As a result of this float, Pike River became separately listed on the New Zealand and Australian stock exchanges, with its own active board of directors and management and offices, completely separated from those of NZOG. Therefore NZOG's 31% post-float equity shareholding in Pike is now held as an investment.

Pike is an important investment for NZOG and directors consider our key stake in Pike to have significant scope for value accretion in the short-medium term, as the Pike River mine moves closer to production. NZOG has also assumed a financing backstop role to ensure Pike funds its mine through into production, which makes a lot of sense given NZOG's key stakeholding in that company.

That being said, it is a fact that Pike is not an oil and gas activity, such that in due course I expect it will be less relevant to NZOG's future as we expand our mainstream activities.

### **Kupe**

The third project pursued over the past 12 months, Kupe, remains scheduled to deliver first production by mid-2009. Kupe is a big-ticket project and for NZOG to hold a 15% equity in such a development is quite something for a company of our size.

I'm glad to note that bank financing arrangements have been fully bedded down and will fund NZOG's ongoing investment in this development. Once in production, Kupe will provide NZOG with a long-term revenue stream from a product mix of gas, oil condensate and LPG.

### **Exploration**

While these development elements of the company's business (namely Tui, Pike and Kupe) have generally met the expectations outlined to you at last year's annual meeting, our objective of discovering oil by drilling three prospects in the offshore Taranaki Basin failed to deliver, an outcome which reflects the inevitable risk of exploration. However, I believe the potential prizes which may have been won fully supported the expenditures which NZOG made in drilling these prospects.

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Exploration remains a key plank of our ongoing business plan, not only to sustain but to grow the company by increasing both NZOG's petroleum reserves' base and its production profile. In the Board's view, the risks of exploration are more than matched by the rewards, which can and do result from discoveries, as evidenced by the current revenue stream from the Tui Area oilfields.

I should add that the rewards can be far bigger than those of Tui. It's also worth remembering that the Tui and Kupe reserves were only identified by NZOG using the drill bit. So we certainly intend to grow our portfolio of exploration opportunities aggressively in the short to medium term.

### **Financial Results**

As shown in the financial statements contained in the annual report, NZOG recorded a \$6.6 million surplus for the year ended 30th June 2007, which was supported by gains (an accounting adjustment) from the successful IPO of Pike River, and realisation of the company's residual investment in Pan Pacific Petroleum NL.

These essentially one-off transactions in the 2006/07 year do not reflect the outlook for the 2007/08 financial year, in which production from the Tui Area oil fields is forecast to be the key profit generator.

### **Dividend Policy**

In determining its view on dividends for the near-term, the Board has taken account of the expected cash demands on the company.

The cash flow being generated from Tui production during the current financial year is earmarked in part to repay much of the bank loan that NZOG used as the primary source of funding the development; the company also needs to meet its other operational costs and be able to provide financial support to Pike River Coal if needed.

The Board has also examined the tax efficiency for shareholders, of receiving dividends that carry no imputation credits. This is because the company is utilising substantial accumulated tax write-offs that mean the company itself is unlikely to pay income tax for perhaps a few years.

Directors feel that to pay dividends which were fully taxable in the hands of shareholders would be an inefficient way to build value for shareholders of the company.

### **Directors and Management**

Three directors are standing for re-election (including myself). I'd also mention that the Board is actively pursuing the appointment of an additional director.

In today's business concerning directors, you will be asked to vote on an increase in fees for the non-executive members of the Board and also to approve the issue of partly-paid shares to directors (other than myself).

The rationale for an increase in fees has been explained in the notes accompanying the Notice of Meeting, including that the last increase was approved in 2004 and the company is currently in a growth stage. As to the proposed inclusion of non-executive directors in the company's existing share plan for employees, I note that shares issued will be subject to a 20% premium over market at the date of grant, and will be unlisted until fully-paid and held in escrow.

In my view, the inclusion of non-executive directors in the company's share plan recognises the strong inputs which board members are expected to have in the affairs of this company and adds more interest to their roles.

At last year's annual meeting, I noted that NZOG had continued to strengthen its management team. Since then, a very significant event has been the appointment of David Salisbury as CEO.

Coincident with David's appointment, Gordon Ward resigned as NZOG's General Manager and joined Pike River Coal as Managing Director of that company. I would like to recognise the contribution that Gordon made over a long service to NZOG.

Under David's management, further senior positions have been identified and filled. Some shareholders have questioned the cost to NZOG of having this enlarged establishment, a point on which David will re-assure you shortly in his presentation.

There has also been some questioning of the remuneration levels of executive directors in respect of which I refer you to the fact that there is a Board Remuneration Committee (as described in the corporate governance statement on page 43 of the annual report) set up some years ago, which deals with such matters.

### **Share Options**

The listed options in the company have currency until 30th June 2008. These options were issued gratis to all shareholders in late 2005 and have an exercise price of \$1.50.

Some investors have asked whether the term or other conditions of these options may be varied. At this stage, the Board has no such proposal. Having said that, I assure you the directors are cognisant of the fact that the exercise of a prior tranche of options brought a substantial sum of very useful equity capital into the company in June 2005 and that share options can be a valuable trading mechanism for certain investors.

The approximately 140 million options on issue represent a potential source of significant funding for the Company and your directors recognise the substantial opportunity that this can provide for the Company if, as intended, we have the projects in place that justify that level of additional capital raising.

Further, as I stated in my overview in the annual report, your directors firmly intend that the value of NZOG is fully recognised in the marketplace ahead of June 2008.

### **Conclusion**

In summary, I believe NZOG has achieved many good things these past 12 months, but we cannot rest on our laurels. There remains more to be done to grow the company further, in both size and profitability.

I now ask David Salisbury to present you with more detailed information on our past operations and the plan to achieve the objectives set by the Board to substantially increase the company's petroleum reserves' base and production profile.

R A Radford  
On behalf of the Board of Directors

ENDS

**FOR FURTHER INFORMATION PLEASE CONTACT:**

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NZOG stock symbols: NZX shares - NZO      options - NZOOD  
ASX shares - NZO      options - NZOO

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