



26 October 2007

Chief Executive's address to annual meeting of shareholders Intercontinental Hotel, Wellington NZ.

It is a pleasure to be attending my first annual meeting of New Zealand Oil and Gas Limited as Chief Executive. It has certainly been a busy and exciting seven months since I joined the company. A great deal has happened, and for a whole set of reasons New Zealand Oil and Gas is a very different company today. Pike River Coal has been floated; Tui brought into production and Kupe is on track for first production in mid-2009. These three key assets provide a solid and diversified platform for growth. We are committed to enhancing our exploration portfolio and a Board approved growth strategy is in place.

I would like to talk briefly about Tui, Kupe, Pike River Coal and recent exploration, and then discuss our plans for the future.

Tui

The project encompasses the Tui, Amokura and Pateke oil pools discovered by NZOG and its partners in 2003/04. Production is through a Floating Production Storage and Offtake vessel.

On the 30 July oil began flowing from the Tui Area. NZOG's interest in the Tui Area is 12.5%. To date there have been 9 shipments, totalling over 2 and a half million barrels.

NZOG's share to date is approximately 316,000 barrels.

The reservoir is flowing well and the water cut – the amount of water produced along with the oil – is less than anticipated. The FPSO needs some technical modifications to allow the 50,000 barrels a day target to be reached. To date daily production has averaged approximately 40,000 barrels. It is expected that production of around 50,000 barrels a day will be achieved during November.

The oil is being marketed by joint venture partner Mitsui to various refineries, mostly in Australia but also in south-east Asia. It is a high quality sweet, light crude and is being sold against the Tapis benchmark crude oil price, adjusted for quality differences and freight costs.

I know there is quite a bit of interest in the prices being received for Tui oil. However, the revenues accrued to date are commercially sensitive. This is a new crude and the refineries are trying it out.

This is a competitive market and to reveal the revenues at this time would allow each refinery to work out whether their price is high or low relative to the other refineries. That would not be in our commercial interest.

The marketing strategy is to get the refineries comfortable with the crude and then the long term price should move to its inherent value.

The cash received by NZOG in the September quarter was US\$7.5m. This is significantly less than the revenues accrued to date. Payments are typically received up to 30 days after delivery.

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There are a number of variables – including oil price, production rate, and the exchange rate – which make forward revenue predictions difficult. However, a useful rule of thumb is to say that each barrel of oil earns roughly NZ\$100, and we expect NZOG's share of production this financial year to be around 1.2 million barrels. We therefore currently expect NZOG revenue from the Tui Area to comfortably exceed \$100m in 2007/08.

In August, the project operator, AWE, completed a preliminary post-drilling reserves assessment, which indicates that developed proved and probable reserves for the Tui Area – in other words, the volume of oil that is as likely to be produced as not - are 32 million barrels.

This is an increase of approximately 15 % on the pre-drilling reserves assessment. In addition, potential for further undeveloped reserves has been identified.

AWE is undertaking a more comprehensive study which will include evaluation of the economic potential of the undeveloped reserves. Results of this analysis are expected by the end of the year.

Kupe

NZOG has a 15% interest in Kupe.

The Kupe operator, Origin Energy, has completed a comprehensive review of the schedule and costs. Many of the major contracts have been signed and detailed facility design well advanced, and we now have much more certainty around costs and timelines.

The project remains on target for first production in mid-2009 but the project costs have increased by around 10%.

Many of the costs are being incurred in US dollars – and the strong New Zealand dollar has had a significant mitigating effect, helping to keep the lid on cost escalation.

It should be noted that while Kupe is generally regarded as a gas field, around half of the value of this project lies in the liquids, the oil condensate and LPG, even at conservative liquids prices.

In early October the ENSCO 107 drilling rig arrived in New Zealand from Singapore. It will be used to drill the Kupe development wells and install the offshore platform. The platform jacket (essentially the 'legs' of the offshore platform) has also arrived in New Zealand.

Unfortunately the weather has not been co-operating and the rig remains sheltering in Admiralty Bay in the Marlborough Sounds, waiting for calm weather so it can be towed out to the Kupe development site.

The onshore gas plant earth works are largely complete and the civil works are progressing well.

NZOG's share of the Kupe development costs up until the beginning of October of around \$50 million was met from our general sources of funding. The remaining development costs are being funded through a \$125 million debt facility with Westpac Bank.

We have all our funding requirements in place and are not affected by the current uncertainty on the financial markets.

Pike River

The Pike River Coal mine is on the West Coast of the South Island, north of Greymouth. Pike River Coal Ltd is now a separately listed company, in which NZOG holds a stake of 62 million shares (around 31% of ordinary shares), 11 million options and 3.5 million convertible notes.

The successful float of Pike River Coal Ltd was extremely important for NZOG. It has allowed us to return to our core business of exploration and production.

Our relationship with Pike River Coal Ltd is now as a shareholder. However, NZOG is committed to supporting the development of Pike River Coal. This may require us to provide further financial support on commercial arms-length terms if requested by Pike River Coal Ltd.

I note that the Pike tunnel is now over 70% complete and the share price this week was back up to issue price.

Exploration

It is fair to say that there have been recent disappointments on the exploration front.

The Hector, Taranui and Tieke exploration wells were not successful. We use the best science ahead of drilling to reduce risk and high-grade opportunities. But even with this science, exploration is inherently high risk. However, the rewards of successful exploration justify the risks of exploration and it is through the drill-bit that the industry creates a lot of value for shareholders.

We have elected to relinquish our interest in permit PEP 38729, which contains the Felix prospect. At 75% interest, we do not consider drilling of the Felix prospect to be a good investment for NZOG and we have been unsuccessful in attracting further partners into the permit on sufficiently attractive terms.

We are committed to value-creating expansion – not expansion for the sake of it. We will walk away from unattractive opportunities.

And there are other opportunities. We intend to take part in the upcoming on-shore Taranaki permit allocation round and have been approached by parties interested in joining with us in bids. We are reviewing prospects being sold down by other companies and looking at other opportunities to acquire new exploration acreage.

The Kupe joint venture is planning to drill the Momoho prospect in mid-2008 following completion of drilling the three Kupe development wells. This prospect lies 5 km from the intended location for the Kupe Central Field production platform, which could allow for any production to be routed through these facilities.

Other Kupe features, such as the Denby A, B, C, and D Prospects, need further evaluation.

I would like to make the point that the easiest gains in terms of increasing reserves and bringing on new production can be from existing fields, in our case the Tui Area and Kupe assets. We are looking closely at all the potential near-field prospects and leads, and the opportunity to tie them back into the developments.

Our current exploration portfolio is not as strong as we would like. NZOG remains committed to pursuing attractive exploration opportunities, both within its existing acreage portfolio in the Taranaki region, and elsewhere. Taranaki alone will not provide sufficient opportunities for NZOG going forward. The recent expansion of the geoscience team enables a wider range of opportunities to be aggressively canvassed.

The Future

That brings me onto the company's future plans. We are in a robust financial position, with good cash flows and we can fund a reasonably significant exploration programme – around \$20-25 million in the coming year. With a sound base, the question that needed to be asked was – What next?

The answer is – grow the business.

The Board has approved a growth strategy and set two targets:

- Increase reserves to at least 25 million barrels by 2012
- Increase production output to at least 2 million barrels per year by 2012

These targets are just that – targets. Inevitably, they will prove to be precisely wrong. But what they do is signal an intention and a focus for our actions. And we have put in place the building blocks to try and achieve or exceed these targets.

Having committed to a business development path, you need the right people. We have recruited for growth, bringing in senior technical and corporate employees. We now have the team we need to pursue a growth strategy. That does not mean we have had a huge explosion in staff numbers. We now have 17 staff in total. It is a small, focused and highly skilled team.

I have been asked about the cost of this extra people resource. The cost is about \$1m per annum, excluding savings that will come from a reduced reliance on consultancy services. In a capital intensive business like ours, this is a very worthwhile investment in the right people who can help us grow the business.

We believe that New Zealand has good remaining prospectivity for oil and gas. However, it is unlikely that our growth targets will be met solely through the drill-bit. We are looking at all opportunities: exploration, asset purchase, and corporate acquisition. We do have specific acquisition ideas, but for obvious reasons, we can't talk about those at this point.

We are aiming for a larger portfolio of assets and opportunities. We will cherry-pick the best opportunities and let the less favourable ones go.

Energy Strategy

The Government's recently announced Energy Strategy has been interpreted in some quarters as unquestionably bad news for the exploration sector. NZOG has a more positive view.

In the medium-term, the New Zealand gas market is supply constrained. In other words, we think there will be plenty of demand for new gas and prices are likely to remain strong. And worldwide, demand for oil and oil prices remain very strong.

The economics for NZOG of exploring in New Zealand remain very good.

New Zealand continues to be under-explored. Worldwide the hunt for acreage is on – yet New Zealand is still largely off people's radar screens. But we know that New Zealand has active hydrocarbon systems. There are eight identified basins, but only Taranaki has seen any significant exploration. NZOG is well positioned to capitalise on any attractive opportunities.

There are plenty of reasons to be positive.

Summary

The Tui Area cashflows, the Kupe development and our Pike River Coal investment give NZOG a solid and diversified base.

Growth targets, a business development strategy and a budget have been approved.

We have successfully recruited for growth, we have been actively raising the company's profile – and will continue to do so – and we are looking seriously for new opportunities.

We are focused on growing shareholder value – it's an exciting time and thank you for being part of it.

David Salisbury

ENDS

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

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