

KAIRIKI ENERGY LIMITED

ABN 34 002 527 906

Half Year Report

31 December 2008

Kairiki Energy Limited

ABN 34 002 527 906

Corporate Directory

Directors

Paul Damien John Fry
Lawrence James Brown
Rae Jefferies
Jyn Sim Baker

Company Secretary

Neville John Bassett

Registered Office

Suite 3, Churchill Court
331-335 Hay Street
Subiaco WA 6005

Tel: (08) 9388 6711
Fax: (08) 9388 6744
Website: www.kairikienergy.com

Share Registry

Computershare Investor Services Pty Ltd
Level 2, Reserve Bank Building
45 St George's Terrace
Perth WA 6000

Investor enquiries:

Tel: 1300 557 010
(08) 9323 2000
Fax: (08) 9323 2033

Auditor

Rothsay
Chartered Accountants
6 O'Connell Street
Sydney NSW 2000

Stock Exchange Listing

ASX Limited
ASX Code: KIK

Kairiki Energy Limited

Directors' Report

The Directors of Kairiki Energy Limited submit herewith the financial report of the consolidated entity for the half-year ended 31 December 2008. In order to comply with the provisions of the Corporations Act 2001, the Directors report as follows:

Directors

The names of Directors who held office during or since the end of the half year and until the date of this report are as below. Directors were in office for this entire period unless otherwise stated.

Current Directors

Paul Damien John Fry	Chairman	
Lawrence James Brown	Managing Director (previously Exploration Director)	
Rae Jefferies	Non-Executive Director	
Jyn Sim Baker	Non-Executive Director	Appointed 10 October 2008

Previous Directors

Craig Moore Gumley	Managing Director	Resigned 18 November 2008
Christopher Francis John Swarbrick	Non-Executive Director	Resigned 13 January 2009

Review and Results of Operations

The principal activities of the company and its subsidiaries during the period were exploration and evaluation of its oil and gas properties. The net loss for the half-year ended 31 December 2008 was \$1,965,000 (31 December 2007 \$2,959,000). The net loss included the following items:

- Interest costs on the Convertible Notes of \$535,000 (non cash expense) (note 6);
- Impairment of the company exploration permits of \$134,000 (non cash expense) (note 5); and
- Exploration costs expensed of \$568,000.

Oil and Gas Interests

Philippines Offshore Oil and Gas Farm-In (SC 54) – 40% Interest

During the half-year, the following progress occurred in respect of the company's Philippine oil and gas operations:

Inboard

In July and August 2008 the Joint Venture completed multiple site surveys, including both analogue and digital grids, covering 17 prospects in both the inboard and outboard to identify any potential hazards and shallow gas at future possible drilling locations. A soil coring program was also completed over key prospects during August.

In September and October 2008, the Joint Venture drilled two wells as part of its SC 54 inboard exploration program - Yakal and Tindalo.

The Yakal-1 well was a discovery, encountering an oil column ranging from 78 metres to a maximum of 93 metres. This column was confirmed with wireline logging, pressure data and samples. The well was cased and suspended and is prepared for future completion and production at a later date.

The Tindalo-1 well was a discovery encountering a minimum oil column of 119 metres, as confirmed by wireline logs, with indications that the column extends a least a further 15 metres (134 metres in total), possibly totalling in excess of 144m. The Tindalo-1 well was cased and suspended and is prepared for future completion and production at a later date.

These discoveries were an important first step in realising the Joint Venture's strategy to rapidly commercialise the SC 54 inboard area. In addition to these two discoveries there are 20+ additional prospects in the SC 54 inboard area covered by 3D seismic data.

Kairiki Energy Limited

Directors' Report

Since drilling these discoveries the Joint Venture has been undertaking significant technical work both internally and through ongoing independent third party studies to better understand the scale of the discovered resource, the impact on the remaining exploration portfolio and the possible options for development including full-field development and early production via a rig-based Extended Well Test.

In March 2009, the Joint Venture commissioned ISIS Petroleum Consultants Pty Ltd. ("ISIS") who have independently estimated the field size, reservoir quality and volumetrics of Yakal and Tindalo. ISIS has confirmed that the in-place probabilistic resource volumes (STOIIP) in the Yakal and Tindalo oil pools are as follows:

	Tindalo				Yakal			
	P90	P50	P10	Mean	P90	P50	P10	Mean
Oil in Place (MMbbls)	5.0	11.0	24.5	13.4	2.4	5.1	10.7	6.0

The resources discovered by the Tindalo-1 and Yakal-1 wells are defined as Contingent Resources in the Development Pending sub-class under the Petroleum Resources Management system approved by the Society of Petroleum Engineers.

Based on production histories of surrounding analogous oil fields (such as Nido and Matinloc), recovery factors for Tindalo and Yakal are expected to be 35% - 45%.

Commercialisation of Resources

The oil volumes identified at Tindalo and Yakal demonstrate favourable economics for commercialisation via either single well production through a jack up drilling rig or a "cluster" development option aggregating several fields.

A "cluster" style development option, which could aggregate several fields, including Tindalo and Yakal, into a single production facility for concurrent production would be risk capital intensive and could result in earliest production in 2011. The greatest technical risk associated with such a development is well productivity as neither Tindalo nor Yakal have been production tested.

A simpler, more cost effective solution which also mitigates the productivity risk is to produce the Tindalo-1 well in the first instance through a jack-up drilling rig to appraise the well productivity during an Extended Production Test (EPT) over an initial period of six months. Oil produced during this period would be collected in an offset tanker and sold generating early cash flow from the area. In the event of a successful EPT, Tindalo could either be suspended pending a "cluster" development in the area or continue to produce through the drilling rig until end of field life. Tindalo-1 could be potentially brought to production in this way by early 2010.

The next steps to progress this option (pending the appropriate approvals) are detailed subsurface modelling and reprocessing of the 3D seismic data which will refine volume estimates and allow for reserves certification. This modelling will also more accurately predict the likely production rates. In parallel, engineering design work and contract tendering with a rig, tanker and ancillary service providers would also be completed prior to the Joint Venture making a final investment decision.

Outboard

The Joint Venture completed its preliminary interpretation of the 851 km² Abukay 3D seismic survey data and agreed to undertake pre-stack depth migration processing over the entire 3D volume to help further de-risk the Gindara and Lapu Lapu prospects and improve delineation of the remaining outboard prospectivity. A preliminary version of the pre-stack depth migration data was received in February 2009. Final products are expected to be received in March 2009 and will likely be fully evaluated through April 2009.

Kairiki Energy Limited

Directors' Report

In July and August 2008 the Joint Venture conducted a site survey over the Gindara prospect in preparation for future drilling as part of a larger site survey acquisition program over the inboard shallow water section of the Permit.

Sicily Channel

During the half year, the Group completed the acquisitions of both the Kerkouane and Pantelleria permits in the Sicily channel. Kairiki acquired a 30% interest in each of these Permits from AuDAX Resources Limited (ASX:ADX).

Since acquiring the permits the Joint Venture has been maturing the prospect and leads inventory and undertaking a tendering process for an offshore rig and receiving environmental approvals for offshore drilling in Pantelleria and Kerkouane. Furthermore, the Joint Venture plans to complete 400 km of 2D seismic acquisition in the Kerkouane permit.

In February 2009, AuDAX signed a Memorandum of Understanding ('MoU') on behalf of the joint venture with PGS Overseas AS, Norway ('PGS') for participation in exploration of the offshore permit G.R15.PU (Pantelleria) within Italian waters and the contiguous offshore permit Kerkouane in Tunisian waters.

Under the MOU PGS would earn a 15% interest in the Permits from the joint venture partners on a pro-rata basis by paying 30% of a significant future exploration work program. The MoU is subject to a number of conditions precedent including the signing of a farm in agreement. The execution of the farm in agreement would be subject to PGS satisfactorily concluding due diligence, all necessary government approvals and formal documentation. The parties will use reasonable endeavours to execute the farm in agreement within three months of the date of the MoU.

Romania

The company completed the first year of a study group under an AMI with AuDAX and Nexus Energy Ltd. The company is currently reviewing status of its ongoing involvement under this AMI.

Tunisia

During the half year Kairiki announced that it had elected not to extend the closing date for the acquisition of the Chorbane permit in Tunisia past 31 October 2008 and as a result, it did not complete the proposed acquisition. Kairiki also withdrew from its participation in the Tunisian AMI.

Mineral Interests - Australia

During the half-year, the company's efforts were focussed on the farm-out of its mineral properties.

Corporate

• Issue of Convertible Notes

On 21 October 2008, Kairiki executed an agreement to issue Convertible Notes to raise US\$10,000,000 from the IMC Group ("IMC"). The principle terms and conditions of the Notes are as follows:

- i) Repayment Date: 8 September 2011 (US\$8.5m) 21 October 2011 (US\$1.5m);
- ii) Convertible into ordinary fully paid shares at an issue price determined as the lesser of:
 - a. A\$0.185; and
 - b. the closing price of the ordinary shares on ASX on the conversion date, provided that, if this price is lower than A\$0.16, the conversion price will be A\$0.16;
- iii) Shares issued upon conversion of the Notes, or part thereof, will carry standard rights applicable to quoted ordinary shares in the Company and will, from the date of issue, rank equally with fully paid ordinary shares currently on issue

Kairiki Energy Limited

Directors' Report

- iv) A Noteholder may convert at any time prior to the Repayment Date, subject to a limit of 3 conversions with each conversion being in respect of a number of Notes which are convertible into at least 10 million shares;
- v) Repayment Rights: The parties will have rights of repayment as follows:
 - a. Kairiki shall have the right up to 31 January 2009 to give notice to repay up to 50% of the outstanding amount in respect of the Notes;
 - b. A relevant Noteholder shall have the right, during the period 1 January to 15 January each year, to require the Company to use all or a specified part of any cash balance held in a special repayment account, established for receipt of future net revenues and option conversion monies, to repay a portion of the outstanding amount in respect of the Notes; and
 - c. A relevant Noteholder has the right to full repayment of the outstanding amount in respect of the Notes on the occurrence or non-fulfillment of specified events or conditions before 31 January 2009. In the event that Kairiki and IMC fail to enter into the KIK/IMC Alliance Agreement by 1 December 2008 or the non-fulfillment of other specified conditions by 31 January 2009 through wilful breach, Kairiki will be liable to pay a break fee of US\$1 million;
- vi) Interest Rate: 12% per annum;
- vii) Security: Fixed and floating charges over all of the assets of the Company and its subsidiary, Yilgarn Petroleum Philippines Pty Ltd, but excluding certain property;
- viii) The Notes shall not provide for any voting rights at shareholder meetings of Kairiki;
- ix) Unless converted or redeemed during the term, the Notes will be redeemed at the Repayment Date at the face value of the Notes;
- x) Drawdown under the Convertible Note Deed will be conditional on, inter alia, IMC having the right to:
 - a. appoint a representative to the Board of the Kairiki;
 - b. an option to participate at up to 20% in the shallow water SC 54 project by reimbursing the Company on a proportionate basis for its past costs at the time the option is exercised. This option must be exercised by 31 March 2009; and
 - c. an option after 1 January 2009 to farm-in at up to 20% to the outboard portion of SC 54 under commercial terms yet to be agreed. This option must be exercised no later than 30 March 2009 or 6 months before spud of an outboard well.

The Notes will be accessed in two tranches by the Company. The first tranche of US\$8.5 million has been placed under the Company's 15% capacity under ASX Listing Rule 7.1. The remaining US\$1.5 million was subject to shareholder approval, which was received on 21 October 2008.

- **Shareholder General Meeting – 21 October 2008**

At a general meeting held the shareholders approved the following resolutions:

- i. The ratification of the issue of a US\$8.5m convertible note to IMC; and
- ii. Approval to issue a US\$1.5m convertible note to IMC.

- **Shareholder General Meeting – 27 November 2008**

At a general meeting held the shareholders approved the following resolutions:

- i. the re-election of directors; and
- ii. adoption of the 2008 remuneration Report.

- **Appointment of New Director**

On 10 October 2008 Ms Jyn Sim Baker of IMC Resources Group ("IMC") was appointed to the Board of Kairiki. Ms Baker brings corporate and commercial skills to the Board having held the role

Kairiki Energy Limited

Directors' Report

of Chief Executive Officer for IMC Resources Group, which spans Australia, China and Indonesia, since June 2006.

- **Appointment of New Managing Director**

In November 2008 the company announced the appointment of Laurie Brown as its new Managing Director. Laurie was previously an executive director of the company and was instrumental in establishing and building Kairiki's oil and gas asset base from 2006 to its current international portfolio.

Equity proceeds

During the half year, the company issued 26,964,401 shares through the conversion of options raising gross proceeds of \$1,435,720.

Going Concern (note 2)

The consolidated entity experienced losses from ordinary activities after income tax for the half year of \$1,965,000. The consolidated entity experienced net cash outflows from operating activities for the half year of \$980,000, and has commitments as detailed in note 11 of the financial report.

The ability of the consolidated entity to continue as a going concern is principally dependent upon the following;

- A successful farm out or sale of some of the Company's oil and gas properties;
- Raising additional capital to fund the Company's ongoing working capital requirements; and
- Renegotiating the terms of its convertible note agreement, including accessing the restricted cash of \$1,015,000 (note 4), if required.

Although the Directors believe that they will be successful in the above measures, if they are not, the Company may be unable to continue as a going concern and therefore may be unable to realise its assets and extinguish its liabilities in the normal course of business and the amount stated in the financial report.

Changes In State Of Affairs

During the half year ended 31 December 2008 there was no significant change in the entity's state of affairs other than that referred to in this Directors' report, the half-year financial statements or notes thereto.

Rounding

The amounts contained in this report and in the financial statements have been rounded to the nearest \$1,000 (where rounding is applicable) under the option available to the Company under ASIC Class Order 98/0100. The Company is an entity to which the Class Order applies.

Auditor's Independence Declaration

The following is a copy of a letter received from the company's auditors:

This report is made in accordance with a resolution of the directors.



Lawrence Brown
Managing Director

PERTH, 16th day of March 2009

Kairiki Energy Limited

Directors' Report



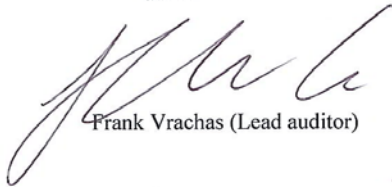
Level 18, 6 O'Connell Street, Sydney NSW 2000 G.P.O. Box 2759, Sydney NSW 2001
Phone 8815 5400 Facsimile 8815 5401 E-mail swan2000@bigpond.com

The Directors
Kairiki Energy Ltd
Suite 3
331 Hay St
Perth WA 6000

Dear Sirs

In accordance with Section 307C of the Corporations Act 2001 (the "Act") I hereby declare that to the best of my knowledge and belief there have been:

- i) no contraventions of the auditor independence requirements of the Act in relation to the audit of the 31 December 2008 financial statements; and
- ii) no contraventions of any applicable code of professional conduct in relation to the audit.



Frank Vrachas (Lead auditor)

Rothsay Chartered Accountants

Dated 16th March 2009



Chartered Accountants

Liability limited by the Accountants Scheme, approved
under the Professional Standards Act 1994 (NSW).

Kairiki Energy Limited

Independent Review Report



Level 18, 6 O'Connell Street, Sydney NSW 2000 G.P.O. Box 2759, Sydney NSW 2001
Phone 8815 5400 Facsimile 8815 5401 E-mail swan2000@bigpond.com

Independent Review Report to the Members of Kairiki Energy Ltd

The financial report and directors' responsibility

The interim consolidated financial report comprises the balance sheet, income statement, statement of changes in equity, cashflow statement, accompanying notes to the financial statements, and the directors' declaration for Kairiki Energy Ltd for the half-year ended 31 December 2008.

The Company's directors are responsible for the preparation and fair presentation of the consolidated financial report in accordance with Australian Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Act 2001*. This includes responsibility for the maintenance of adequate accounting records and internal controls that are designed to prevent and detect fraud and error, and for the accounting policies and accounting estimates inherent in the financial report.

Review approach

We conducted our review in accordance with Auditing Standard on Review Engagements ASRE 2410 *Review of an Interim Financial Report Performed by the Independent Auditor of the Entity*, in order to state whether, on the basis of the procedures described, we have become aware of any matter that makes us believe that the interim consolidated financial report is not in accordance with the *Corporations Act 2001* including: giving a true and fair view of the consolidated financial position as at 31 December 2008 and the performance for the half year ended on that date; and complying with Australian Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*. As auditor of Kairiki Energy Ltd, ASRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

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

Independence

In conducting our review we have complied with the independence requirements of the *Corporations Act 2001*.

Conclusion

Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the interim consolidated financial report of Kairiki Energy Ltd is not in accordance with the *Corporations Act 2001*, including:

- giving a true and fair view of the consolidated financial position as at 31 December 2008 and of the performance for the half-year ended on that date; and
- complying with Australian Accounting Standard AASB134 *Interim Financial Reporting* and the *Corporations Regulations 2001*.


Rothsay

Frank Vrachas
Partner

Dated 16th March 2009



Chartered Accountants

Liability limited by the Accountants Scheme, approved
under the Professional Standards Act 1994 (NSW).

Kairiki Energy Limited

Directors' Declaration

In accordance with a resolution of the Directors of Kairiki Energy Limited, I state that:

- 1) the financial statements and notes of the consolidated entity are in accordance with the Corporations Act 2001, including:
 - (a) complying with the Accounting Standard AASB 134: Interim Financial Reporting and the Corporations Regulations 2001;
 - (b) giving a true and fair view of the consolidated entity's financial position as at 31 December 2008 and of its performance for the half-year then ended; and
- 2) there are reasonable grounds to believe that the company will be able to pay its debts when they become due and payable.

On behalf of the Board,



Lawrence Brown
Managing Director

PERTH, 16th day of March 2009

Kairiki Energy Limited

Income Statement

For The Half-Year Ended 31 December 2008

	Consolidated	
	Half-year ended 31 Dec 2008 \$'000	Half-year ended 31 Dec 2007 \$'000
Revenue and Income		
Interest revenue	232	166
Other income – foreign exchange gains	144	14
	<hr/>	<hr/>
	376	180
	<hr/>	<hr/>
Expenses		
Finance costs	603	-
Depreciation expense	8	7
Salaries and employee benefits expense	418	255
Share based payments	221	962
Consultants and directors fees	131	258
Other exploration costs expensed	568	553
Impairment of deferred exploration costs	134	903
Other costs	258	201
	<hr/>	<hr/>
	2,341	3,139
	<hr/>	<hr/>
Loss before income tax expense	(1,965)	(2,959)
Income tax expense	-	-
	<hr/>	<hr/>
Loss for the half-year attributable to members of Kairiki Energy Limited	(1,965)	(2,959)
	<hr/>	<hr/>
	Cents	Cents
Basic loss per share	(0.47)	(0.92)

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Kairiki Energy Limited

Balance Sheet

As at 31 December 2008

	Note	Consolidated	
		As at 31 Dec 2008 \$'000	As at 30 June 2008 \$'000
ASSETS			
Current Assets			
Cash and cash equivalents		2,869	15,171
Restricted cash and cash equivalents	4	1,015	-
Trade and other receivables		346	226
Total Current Assets		4,230	15,397
Non-Current Assets			
Plant and equipment		36	35
Deferred exploration expenditure	5	42,104	8,701
Total Non-Current Assets		42,140	8,736
Total Assets		46,370	24,133
LIABILITIES			
Current Liabilities			
Trade and other payables		1,079	473
Provisions		3	20
Total Current Liabilities		1,082	493
Non-Current Liabilities			
Convertible notes	6	12,602	-
Total Current Liabilities		12,602	-
Total Liabilities		13,684	493
Net Assets		32,686	23,640
Equity			
Issued capital	7	35,218	31,718
Reserves		9,215	1,704
Accumulated losses		(11,747)	(9,782)
Total Equity		32,686	23,640

Kairiki Energy Limited

Statement of Changes in Equity

For The Half-Year Ended 31 December 2008

Consolidated	Issued Capital \$'000	Share- based Payments Reserve \$'000	Translation Reserve \$'000	Accumulated Losses \$'000	Total \$'000
Balance at 1 July 2007	18,278	2,139	(95)	(6,033)	14,289
Shares issued	510	-	-	-	510
Transaction costs on share issues	-	-	-	-	-
Share based payments	-	962	-	-	962
Currency translation differences	-	-	(47)	-	(47)
Loss for the six months	-	-	-	(2,960)	(2,960)
Balance at 31 December 2007	18,788	3,101	(142)	(8,993)	12,754
Shares issued	13,542	-	-	-	13,542
Transaction costs on share issues	(612)	-	-	-	(612)
Share based payments	-	(388)	-	-	(388)
Currency translation differences	-	-	(867)	-	(867)
Loss for the six months	-	-	-	(789)	(789)
Balance at 30 June 2008	31,718	2,713	(1,009)	(9,782)	23,640
Shares issued	1,436	-	-	-	1,436
Transaction costs on share issues	-	-	-	-	-
Equity portion of convertible notes	2,064	-	-	-	2,064
Share based payments	-	254	-	-	254
Currency translation differences	-	-	7,257	-	7,257
Loss for the six months	-	-	-	(1,965)	(1,965)
Balance at 31 December 2008	35,218	2,967	6,248	(11,747)	32,686

Kairiki Energy Limited

Cash Flow Statement

For The Half-Year Ended 31 December 2008

	Consolidated	
	Half-year ended 31 Dec 2008 \$'000	Half-year ended 31 Dec 2007 \$'000
Cash Flows from Operating Activities		
Payments to suppliers and employees, including for exploration expenses	(1,282)	(1,015)
Interest received	232	166
Other receipts – net GST refunds	70	-
Net cash flows used in operating activities	<u>(980)</u>	<u>(849)</u>
Cash Flows from Investing Activities		
Purchase of plant and equipment	(3)	(7)
Payments for deferred exploration expenditure	(26,792)	(1,754)
Restricted cash	(1,015)	-
Net cash flows used in investing activities	<u>(27,810)</u>	<u>(1,761)</u>
Cash Flows from Financing Activities		
Proceeds from issue of convertible notes	12,364	-
Proceeds from issue of shares and options	1,436	535
Payment of equity issue costs	(121)	(394)
Net cash flows from financing activities	<u>13,679</u>	<u>141</u>
Net increase in cash and cash equivalents	(15,111)	(2,469)
Cash and cash equivalents at beginning of half year	15,171	8,700
Effect of exchange rate changes	2,809	(14)
Cash and cash equivalents at end of half year	<u><u>2,869</u></u>	<u><u>6,217</u></u>

Kairiki Energy Limited

Notes to the Financial Statements

For The Half-Year Ended 31 December 2008

1. BASIS OF PREPARATION AND ACCOUNTING POLICIES

The half-year financial report is a general purpose financial report prepared in accordance with the Corporations Act 2001 and AASB 134 "Interim Financial Reporting".

The half-year financial report does not include full disclosures of the type normally included in an annual financial report. Therefore, it cannot be expected to provide as full an understanding of the financial performance, financial position and cash flows of the consolidated entity as in the annual financial report.

The half-year financial report should be read in conjunction with the Annual Financial Report of Kairiki Energy Limited as at 30 June 2008. It is also recommended that the half-year financial report be considered together with any public announcements made by Kairiki Energy Limited during the half-year ended 31 December 2008 in accordance with the continuous disclosure obligations arising under the ASX Listing Rules.

The half-year financial report has been prepared in accordance with the historical cost basis. All values are rounded to the nearest thousand dollars (\$'000) unless otherwise stated under the option available to the company under ASIC Class Order 98/100. The Company is an entity to which the class order applies.

The half year consolidated financial statements comprise the financial statements of Kairiki Energy Limited and its subsidiaries ("Group") as at 31 December 2008.

Accounting Policies

The accounting policies and methods of computation adopted in the preparation of the half-year financial report are consistent with those adopted and disclosed in the company's annual financial report for the year ended 30 June 2008, apart from the changes in accounting policy noted below.

Functional Currency

The financial statements are measured using the currency of the primary economic environment in which the entity operates (the 'functional currency'). Changes in the funding structure of the parent, following the issue of the convertible notes in September 2008, together with European exploration commitments based in USD, has given rise to the change in the functional currency of Kairiki Energy Limited from Australian Dollars to US Dollars, effective 1 September 2008. As the company is listed on the Australian Securities Exchange, it has maintained its presentation currency as Australian Dollars.

Borrowings

Borrowings are initially recognised at fair value, net of transaction costs incurred. Borrowings are subsequently measured at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption amount is recognised in the income statement over the period of the borrowings using the effective interest rate method.

The fair value of the liability portion of convertible notes is determined using a market interest rate for an equivalent non-convertible note. This amount is recorded as a liability on an amortised cost basis until extinguished on conversion or maturity of the note. The remainder of the proceeds is allocated to the conversion option. This is recognised and included in shareholders equity, net of any income tax effects.

Borrowing Costs

Borrowing costs comprise interest and amortisation costs incurred in establishing borrowing facilities. Where borrowings are specifically incurred in relation to qualifying assets, the actual borrowing costs are capitalised into the carrying value of those assets. Where borrowings are not specifically incurred in relation to qualifying assets, the amounts are expensed.

Kairiki Energy Limited

Notes to the Financial Statements

For The Half-Year Ended 31 December 2008

1. BASIS OF PREPARATION AND ACCOUNTING POLICIES - continued

Other Changes in Accounting Policy

Since 1 July 2008 the Group has adopted the following Standards and Interpretations, mandatory for annual periods beginning on or after 1 July 2008. Adoption of these Standards and Interpretations did not have any effect on the financial position or performance of the Group.

- AASB 2007-3 Amendments to Australian Accounting Standards arising from AASB 8.
- AASB 2008-1 Amendment to Australian Accounting Standards Share-based Payments: Vesting Conditions and Cancellations.
- AASB 2008-3. These amendments are consequential amendments to 20 standards and have no significant affect for Integra.
- AASB 2008-5 and 2008-6 Amendments to Australian Accounting Standards arising from the Annual Improvements Projects.

The Group has not elected to early adopted any new standards or amendments.

2. GOING CONCERN

The consolidated entity experienced losses from ordinary activities after income tax for the half year of \$1,965,000. The consolidated entity experienced net cash outflows from operating activities for the half year of \$980,000, and has commitments as detailed in note 11.

The ability of the consolidated entity to continue as a going concern is principally dependent upon the following;

- A successful farm out or sale of some of the Company's oil and gas properties;
- Raising additional capital to fund the Company's ongoing working capital requirements; and
- Renegotiating the terms of its convertible note agreement, including accessing the restricted cash of \$1,015,000 (note 4), if required.

Although the Directors believe that they will be successful in the above measures, if they are not, the Company may be unable to continue as a going concern and therefore may be unable to realise its assets and extinguish its liabilities in the normal course of business and the amount stated in the financial report.

3. EARNINGS PER SHARE

The Company's potential ordinary shares, being its options granted and convertible notes, are not considered dilutive as the conversion of these options and convertible notes would result in a decreased net loss per share.

4. RESTRICTED CASH AND CASH EQUIVALENTS

Included in restricted cash and cash equivalents is cash of \$1,015,000 (June 2008: \$Nil) relating to the conversion of options monies held in a trust account for the benefit of IMC. IMC has until 30 April 2009 to determine whether to use those funds to redeem a portion of its convertible note or to release those funds to the company.

Kairiki Energy Limited

Notes to the Financial Statements

For The Half-Year Ended 31 December 2008

5. DEFERRED EXPLORATION EXPENDITURE

Costs carried forward in respect of areas of interest in the following phases:

	Consolidated	
	31 Dec 2008	30 June 2008
	\$'000	\$'000
Exploration and evaluation phase – at cost		
Balance at beginning of period	8,701	6,038
Expenditure incurred, net of costs recoveries	27,294	3,716
Impairment of deferred exploration	(134)	(1,053)
Foreign currency translation movements	6,243	-
Total deferred exploration expenditure	42,104	8,701
Represented by:		
Deferred oil and gas expenditure	42,104	8,618
Deferred mineral expenditure	-	83
Total deferred exploration expenditure	42,104	8,701
Deferred oil and gas expenditures by country – at cost		
Philippines	41,244	8,421
Tunisia	430	170
Italy	430	27
Total deferred exploration expenditure	42,104	8,618

Ultimate recoupment of exploration and evaluation expenditure carried forward is dependent on successful development and commercial exploitation or, alternatively, sale of the respective areas.

Exploration and evaluation expenditure written off during the period relates to:

- Oil and gas - expensing costs relating to exploration activity that do not meet the criteria for capitalisation under its accounting policies.
- Mineral tenements - low level of current and planned activity to assess the existence of economically recoverable reserves of the tenements.

Kairiki Energy Limited

Notes to the Financial Statements

For The Half-Year Ended 31 December 2008

Consolidated

	31 Dec 2008 \$'000	30 June 2008 \$'000
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6. CONVERTIBLE NOTES

Non-Current

Financial liability measured at amortised cost

12,602

-

On 1 September 2008, Kairiki announced the issue of a Convertible Note ("Note") to IMC for proceeds of US\$10 million. The Note was executed on 8 September 2008 and US\$8.5m was drawn down immediately and a further US\$1.5m was subject to shareholder approval which was subsequently received on 21 October 2008.

The principal terms and conditions of the Note are as follows:

- i) Note Holder – IMC
- ii) Maturity date – September 2008 and October 2011 (3 years from issue).
- iii) Interest payable at 12% per annum with interest accruing but unpaid through to 31 December 2008 and thereafter payable monthly.
- iv) Conversion price is as the lesser of:
 - (a) A\$0.185; and
 - (b) the closing price of the ordinary shares on ASX on the conversion date, provided that, if this price is lower than A\$0.16, the conversion price will be A\$0.16;
- v) IMC may convert at any time prior to the Repayment Date, subject to a limit of 3 conversions with each conversion being in respect of a number of Notes which are convertible into at least 10 million shares;
- vi) Repayment Rights: The parties will have rights of repayment as follows:
 - (a) Kairiki shall have the right up to 31 January 2009 to give notice to repay up to 50% of the outstanding amount in respect of the Notes;
 - (b) IMC shall have the right, during the period 1 January to 15 January each year, to require the Company to use all or a specified part of any cash balance held in a special repayment account, established for receipt of future net revenues and option conversion monies, to repay a portion of the outstanding amount in respect of the Notes; and
- vii) Interest rate – 12% per annum
- viii) Other redemption provisions for such things as failure to participate in a commercial SC 54 shallow water development, change of control, event of default, delisting from stock exchange, etc.
- ix) Security – fixed and floating charge over all the assets of Kairiki Energy Limited and its subsidiary Yilgarn Petroleum Philippines Pty Ltd, but excluding certain property.

The Note has been classified into two components: a debt component (a contractual arrangement to deliver cash) and an embedded derivative call option component (a call option granting the holder the right, for a specified period of time, to convert it into a number of ordinary shares of Kairiki, based on the outstanding balance at date of conversion).

	31 Dec 2008 \$'000	30 June 2008 \$'000
Face Value of Notes (US\$10,000,000)		
- Debt portion (US\$8,328,576)	10,300	-
- Equity portion (US\$1,671,424) – refer note 7	2,064	-
	12,364	-

Kairiki Energy Limited

Notes to the Financial Statements

For The Half-Year Ended 31 December 2008

Consolidated

31 Dec 2008
\$'000

30 June 2008
\$'000

6. CONVERTIBLE NOTES – continued

Movement in Debt

- Debt portion (US\$8,328,576)	10,300	-
- Issuance costs	(121)	-
- Amortisation of issuance costs	7	-
- Accrued interest to 31 December 2008 (US\$369,833)	535	-
- Accretion of debt to 31 December	134	-
- Foreign currency translation movements	1,746	-
	<u>12,602</u>	<u>-</u>

7. ISSUED CAPITAL

(a) Issued and paid up capital

Number of Shares	Summary of Movements:	Issue Price	\$'000
313,970,368	Opening balance 1 July 2007		18,278
9,445,276	Issued on exercise of options	5c	472
2,500,000	Issued on exercise of options	15c	37
325,915,644	Closing Balance at 31 December 2007		18,788
25,580,223	Issued on exercise of options	5c	1,279
10,000,000	Issued on exercise of options	7c	700
750,000	Issued on exercise of options	10c	75
49,949,730	Share placement	23c	11,488
	Costs of share placement		(612)
412,195,597	Closing Balance at 30 June 2008		31,718
1,250,000	Issued on exercise of options	12c	150
25,714,401	Issued on exercise of options	5c	1,286
	Equity portion of convertible notes – refer note 6		2,064
439,159,998	Closing Balance at 31 December 2008		35,218

(b) Options

	Number	Exercise Price	Expiry Date
Unlisted Options	4,250,000	10 cents	On or before 30/06/2009
Unlisted Options	3,750,000	12 cents	On or before 30/06/2009
Unlisted Options	2,500,000	10.5 cents	On or before 3/10/2009
Unlisted Options	2,750,000	13.5 cents	On or before 3/10/2010
Unlisted Options	500,000	30 cents	On or before 31/05/2011
Unlisted Options	3,300,000	30 cents	On or before 30/11/2009
Unlisted Options	2,200,000	35 cents	On or before 30/11/2009
Closing Balance at 31 December 2008	<u>19,250,000</u>		

Kairiki Energy Limited

Notes to the Financial Statements

For The Half-Year Ended 31 December 2008

7. ISSUED CAPITAL - continued

During the half-year:

- (i) 25,714,401 listed options were exercised at 5 cents;
- (ii) 116,610,100 listed options expired;
- (iii) 1,250,000 unlisted options were exercised at 12 cents;
- (iv) 7,500,000 options were granted to director, Craig Gumley, but these were subsequently forfeited upon resignation;
- (v) 2,500,000 employee options were forfeited upon resignation of other key management personnel; and
- (vi) 500,000 employee options were granted with an exercise price of 30 cents.

Refer to note 8 for share based payment details.

8. SHARE BASED PAYMENTS

The following share-based payments were made during the half-year:

Granted to Director, Craig Gumley and approved by shareholders on 14 August 2008:

- 2,500,000 options expiring 31 May 2011, exercisable at 20 cents each, vesting 31 May 2009;
- 2,500,000 options expiring 31 May 2011, exercisable at 25 cents each, vesting 31 May 2010; and
- 2,500,000 options expiring 31 May 2011, exercisable at 30 cents each, vesting 31 May 2010.

These options were forfeited on 18 November 2008, consequently the net effect of share based payments for these options is nil.

Granted an employee on 10 November 2008 and approved by shareholders on 14 August 2008:

- 500,000 options expiring 31 May 2001, exercisable at 30 cents each, vesting 31 May 2010.

The assessed fair values of the options were determined using a binomial option pricing model, taking into account the exercise price, term of option, the share price at grant date and expected price volatility of the underlying share, expected dividend yield and the risk-free interest rate for the term of the option. The inputs to the model used were:

Grant date	10/11/08
Dividend yield (%)	-
Expected volatility (%)	77.79
Risk-free interest rate (%)	6.75%
Expected life of options (years)	2.553
Option exercise price (\$)	0.30
Share price at grant date (\$)	0.071

The expected life of the options is based on historical data and is not necessarily indicative of exercise patterns that may occur. The expected volatility reflects the assumption that the historical volatility is indicative of future trends, which may also not necessarily be the actual outcome.

Kairiki Energy Limited

Notes to the Financial Statements

For The Half-Year Ended 31 December 2008

9. SEGMENT REPORTING

The consolidated entity operated in two industry segments, being petroleum exploration and mineral exploration. Geographically, the consolidated entity operates in the Philippines, Africa/Europe (Romania, Italy and Tunisia, considered as one area due to their relative close proximity) and Australia.

The following table presents the revenue and earnings information regarding geographical segments for the half-year periods ended 31 December 2008 and 31 December 2007.

Consolidated	Australia \$'000	Philippines \$'000	Africa/Europe \$'000	Total \$'000
31 December 2008				
Segment revenue	374	2	-	376
Segment results	(1,471)	(33)	(461)	(1,965)
Assets and liabilities				
Segment assets	4,002	41,508	860	46,370
Segment liabilities	12,665	768	251	13,684
31 December 2007				
Segment revenue	161	19	-	180
Segment results	(2,608)	21	(372)	(2,959)
Assets and liabilities				
Segment assets	5,903	7,049	-	12,952
Segment liabilities	198	-	-	198

10. CONTINGENT LIABILITIES

There has been no change in contingent liabilities since the last annual reporting date.

11.COMMITMENTS

	Consolidated	
	31 Dec 2008 \$'000	30 June 2008 \$'000
Operating leases (non-cancellable)		
Within one year	78	106
More than one year but not later than five years	6	35
	84	141

Exploration commitments

In order to maintain current rights of tenure to exploration permits, the consolidated entity has certain obligations to perform minimum exploration work and expend minimum amounts of money. These commitments may be varied as a result of renegotiations, relinquishments, farm-outs, sales or carrying out work in excess of the permit obligations. The following exploration expenditure requirements have not been provided for in the financial report and are payable:

Within one year	171	5,469
More than one year but not later than five years	-	-
	171	5,469

Kairiki Energy Limited

Notes to the Financial Statements

For The Half-Year Ended 31 December 2008

	Consolidated	
	31 Dec 2008	30 June 2008
	\$'000	\$'000
11.COMMITMENTS - continued		
Joint venture capital commitments		
The consolidated entity's share of capital expenditures contracted for at the balance date for which no amounts have been provided for in the financial statements are payable:		
Within one year	-	8,158

Mineral Tenement Commitments:

The Company and the Group are required to maintain current rights of tenure to tenements which requires outlays of expenditure in 2008/2009. Estimated expenditure commitments and rents on mining, exploration and prospecting leases for 2008/2009 by the Group is \$400,000. Other commitments relating to tenement lease rentals and the minimum expenditure requirements of the Western Australian Department of Industry and Resources attaching to tenements have been undertaken by non related Joint Venture participants. Due to the nature of the Group's operations in exploring and evaluating areas of interest, it is difficult to accurately forecast the nature and amount of future expenditure beyond the next year. Expenditure may be reduced by seeking exemption from individual commitments, by relinquishment of tenure or by new Joint Venture arrangements. Expenditure may be increased when new tenements are granted or Joint Venture agreements amended.

Tunisia and Italian exploration permits

The Kerkouane Permit has a two year exploration period from 22 February 2008. Acquisition of 400km 2D seismic and the drilling of one well is required in the two year period. A letter of credit is required by the Tunisian Ministry in the amount of US\$450,000, net to Kairiki, until commencement of drilling. The letter of credit has not yet been issued.

12. EVENTS SUBSEQUENT TO REPORTING DATE

There are no matters or circumstances which have arisen since the end of the half-year which significantly affected or may significantly affect the operations of the consolidated entity, the results of those operations, or the state of affairs of the consolidated entity in subsequent financial periods.