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Arrow Energy (ASX code: AOE) has previously articulated some aggressive growth ambitions for Arrow International. How is the business build progressing? Which recent deals do you consider as pivotal in the development of Arrow International?

MD Nick Davies

Just over two years ago, following the merger between Arrow and CH4, Arrow decided it was time to apply some of our lessons from the Australian CBM sector to pursuit of high margin CBM opportunities in the coal rich, high-growth economies of Asia. Our strategy defined a plan to build businesses in each of China, India and Indonesia that would match our current Australian businesses by 2015. I am happy to report that two years later that strategy has been followed closely and that we are well on track for those ambitious goals.

Specifically, our current plan now shows our International business producing 50 PJ p.a. net to arrow by 2015 – assuming that Shell backs into all projects for 50%. That is about three times our current production in Australia. We are also projecting net cash flow to Arrow of about A\$150 million a year by the same time.

Importantly, this plan is now made up of well defined projects – for which we either already have title or for which title is imminent. The International business now has tremendous momentum and there is a wealth of opportunities from large, grass roots CBM Production Sharing Contracts (PSCs) to farm-ins to coal mine de-gassing projects.

In particular, we believe the recently announced farm-in and corporate equity position with Far East Energy is a pivotal move in our expansion in China. The Qinnan block, to which we have farmed in, is a highly prospective block in one of the most attractive CBM localities in China. The block has over 12 TCF of resource within it – supported by a great deal of available data due to extensive coal mining in the area. We are looking forward to starting an extensive drilling program here in the near future.

Secondly, our relationship with PT Ephindo and Pertamina in Indonesia and our consequent farm-in to the prospective Sangatta West block, which is near to the Bontang LNG plant in East Kalimantan, represents our first firm title to a PSC in Indonesia and is a major step forward for us in a country with CBM resources estimated at over 400 TCF.

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Can you provide an update on your current asset portfolio and how you see it developing over the next 12 months?

MD Nick Davies

We currently have 6 International projects under firm title – three in India and 1 each in China, Vietnam and Indonesia and have commenced drilling in the first three countries. We also have a significant number of projects under negotiation or business development and we are projecting a doubling of blocks under firm title to twelve by the end of this calendar year. Those twelve blocks have an estimated gross resource on them of over 80 TCF and our partners on these blocks are some of the leading companies in Asia; including Tata Power, GAIL (India) Limited, ONGC, PetroChina, PetroVietnam, Pertamina and PT Medco. We believe these blocks represent a balanced and diversified approach to the coal rich high demand, high gas price economies of Asia. Whilst we have many ideas to pursue to continue to broaden and deepen this portfolio, our focus will shift gradually over the next 12 months to a higher emphasis on execution and operations to ensure we rapidly deliver exploration success and reserve certification on those blocks.

In many ways our position in the International business now is similar to our position in Queensland some 5 years ago, where we had acquired an excellent spread of exploration acreage and had begun drilling to convert that acreage into certified reserves. We are already seeing signs of the growing interest by companies in the CBM sector internationally and, we believe, we are now well positioned (as we were in Queensland) with assets before the rush begins.

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What has been the effect of the global financial crisis on the Asian CBM sector? Has it changed your qualitative parameters in assessing suitable growth opportunities for the Group? How is Arrow mitigating any risk to its international business during this crisis?

MD Nick Davies

Clearly the financial crisis has had an effect on the Asian CBM sector – in particular on the smaller, niche companies who have been finding it difficult to obtain financing and funds over the last nine months. But for us this means a time of tremendous opportunity.

We were fortunate enough to complete our deal with Shell for International (and domestic) funding prior to the financial crisis and has meant that we have had an additional competitive advantage, on top of our previous advantage of substantial experience in actual CBM field development, which we can use to obtain access to high quality, select assets throughout the region.

As you suggest, it has also led us to tighten our evaluation criteria and allowed us to be more selective so that we are dealing only with top tier opportunities. Because of the breadth of opportunities and our cash and technology position we are spending even more time on in-depth technical analysis before we make a decision.

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What is the outlook for gas market fundamentals in your target countries? Does Arrow International have expansion intentions beyond these countries?

MD Nick Davies

Long term gas market fundamentals remain extremely strong in all of the countries in which we are doing business, despite any short term impact of the financial crisis.

Gas demand projections in China remain particularly strong with demand expected to increase from around 3000 BCF per annum today (Queensland is 140 BCF p.a.!) to around 7500 BCF p.a. by 2020. These are enormous numbers, but even these only have gas contributing around 6% of their total energy supply versus around 15% in Korea and Japan. And the Chinese Government's priority will always be to supply this gas from domestic sources wherever possible.

In China, potential well-head price netbacks are projected to be anything from US\$5-\$10 per mcf depending on the ultimate end user of the gas.

Similarly in Indonesia we expect demand to grow from around 900 BCF per annum today to around 1600 BCF p.a. by 2020. While in India we expect growth from around 1900 BCF p.a. to 3800 BCF p.a. by 2020 – and all of this with prices in roughly the same range as China's.

Finally, in Vietnam, we believe the local industrial market demand and prices remain strong in and around Hanoi in various market sectors all within 100 kilometres of our block.

Outside of our current areas of interest, Arrow continues to do scoping studies in various areas of strong market fundamentals and strong resource base. Included in these studies are South Africa and Europe.

The latter is of particular interest because of all of the current security of supply issues for Western European countries and the strong CBM resource potential in some coal rich European countries. However, we have been keen to secure our path forward in our existing countries before we venture further afield – but the recent successes and momentum in International has brought this closer.

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You have outlined a reasonably aggressive growth strategy for Arrow International. Are you confident you can achieve all your objectives? How will you fund all of these ambitions?

MD Nick Davies

Yes, we are confident. We now have a staff of 50+ and offices in five countries and we continue to hire quality local staff as and when needed. We have some very strong and highly experienced technical experts in our International business and that has enabled to perform rapid initial screening and then undertake follow-up in-depth technical analysis only when needed. It also helps attract expertise and engage governments so that we can build our extended staff network rapidly.

On the funding front, we have received an initial US\$50 million from Shell and there are additional potential bonuses of another US\$75 million from that transaction. Whilst this goes a long way towards financing our plan, we would not discount additional strategic investors into Arrow International provided it brought some additional competitive advantage to our business.

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Thank you Nick.

For further information on Arrow Energy Limited please visit www.arrowenergy.com.au or call Nick Davies on +61 7 3105 3400.

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