

**Activities Report
December 2008 Quarter**

Drillsearch Energy Limited, (ASX:DLS) which listed on the ASX on 2 July 1987, explores and develops conventional oil and gas projects. Drillsearch Energy has recently merged with Great Artesian Oil and Gas (ASX:GOG), by way of Scheme of Arrangement, details of which were announced on 18 April 2008. The merger between the companies has resulted in a strategic spread of petroleum exploration and production acreage in Australia's most prolific onshore oil and gas province, the Cooper and Eromanga Basins in Queensland and South Australia as well as offshore exploration in the Bonaparte, Carnarvon, Otway, and Gippsland Basins. Additionally Drillsearch Energy has interests in PNG and Canada. The company focus is on 'brownfields' exploration where geological risk is reduced and there is access to existing infrastructure, which ensures that any discoveries can be brought into production rapidly.

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Highlights**Financial:**

- Australian production sales revenue for the Quarter of \$3.03M compared with \$2.8M for previous Quarter despite a reduction of 43.5% in average realisable oil price from September to December Quarters
- Cash at 31 December 2008 - \$8.16M – the major cause for the reduction from the previous Quarter is due to payment of exploration, appraisal and development expenditure incurred prior to the Quarter

Production:

- December Quarter Australian production sales volume 92% up on September Quarter
- Australian oil production for the December Quarter of 32,876bbbls and for the half year of 69,736bbbls
- Drillsearch's Canada oil and gas production 16,156boe for Quarter and 32,388boe for the half year.

Development:

- 5 development wells drilled in Quarter in the Naccowlah block (ATP 259P) of which 4 were cased and suspended as future oil producers

Exploration:

- 2 gas discoveries drilled in PEL 106 and cased and suspended as potential future gas producers
- completed 2D seismic in offshore Carnarvon block (WA-352-P) and in onshore ATP 539P in SW Queensland

Corporate:

- Continued rationalisation of permit holdings
- Takeover offer for 3D Oil Limited announced after end of Quarter

Financial

| Oil & Gas Sales Revenue (A\$) | Dec08 Qtr | Sep08 Qtr | Dec08 6 months |
|--|------------------|------------------|-----------------------|
| Australia | 3,029,938 | 2,800,408 | 5,830,346 |
| Canada (A\$) | 1,291,413 | 1,477,212 | 2,768,624 |
| Total | 4,321,351 | 4,277,619 | 8,598,970 |

| Capital Expenditure (A\$) | Dec08 Qtr | Sep08 Qtr | Dec08 6 months |
|--|------------------|------------------|-----------------------|
| DLS Group* | | | |
| Exploration & Appraisal | 862,515 | 735,079 | 1,597,593 |
| Development | 634,102 | 323,428 | 957,530 |
| Total | 1,496,617 | 1,058,506 | 2,555,123 |
| Circumpacific Energy Corporation# | | | |
| Exploration & Appraisal | 132,907 | 0 | 132,907 |
| Development | 229,110 | 107,089 | 336,199 |
| Total | 362,017 | 107,090 | 469,106 |
| Grand Total (A\$) | 1,858,634 | 1,165,596 | 3,024,230 |

* DLS group excluding CER, but including Great Artesian from Sept 08 Quarter

#DLS held 62.63% of Circumpacific until July 08 and 79.5% from July 2008

Cash balance

Drillsearch's cash balance reduced during the Quarter due to timing of various capital payments. These payments largely related to capital expenditure incurred prior to the Quarter, but which were paid during the December Quarter. Actual cash payments for exploration, appraisal and development expenditure for the Quarter was A\$3,195,092 (in contrast to the September Quarter when it was A\$360,321) of which \$1,873,632 related to payment of expenditure incurred prior to the Quarter.

Despite the downturn in oil prices during the Quarter (average realised price for September Quarter was A\$153.10/bbl and for December Quarter was A\$86.52/bbl), Australian production revenue remained strong at A\$3.03 million and at the end of the Quarter the Australian businesses cash balance stood at \$8,160,377. These figures do not include Drillsearch's equity interest in the cash held by Drillsearch's subsidiary, Circumpacific Energy Corporation (TSX.V:CER) being A\$1,364,247¹ nor the revenue from the additional 1% of the Tintaburra block (ATP 299P) being acquired from CPC Energy Pty Ltd.

Oil prices

The December Quarter has been significantly impacted by decreasing oil prices. However, with the falling A\$/US\$ exchange rate Drillsearch has achieved a quarterly average realised oil price of A\$86.52/bbl and for the month of December the average realised oil price was A\$64.57/bbl.

¹ This represents 79.5% of CAD 1,448,505 held by Circumpacific Energy Corporation converted to Australian Dollars using an exchange rate of .8441 which gives an amount of AUD 1,716,034.

The net operating cash flow² remained stronger for the calendar year than the previous year even with the impact of delayed sales in December 2008.

DLS Group*
Net Operating Cash Flow (Gross Margins)

| Quarter | Net Operating Cash Flow (Gross Margins) | |
|---------|---|--------------|
| | Cumulative AU\$ | Quarter AU\$ |
| Mar-07 | 2,599,140 | 2,599,140 |
| Jun-07 | 3,235,190 | 636,049 |
| Sep-07 | 3,575,610 | 340,420 |
| Dec-07 | 7,486,483 | 3,910,873 |
| Mar-08 | 11,184,600 | 3,698,116 |
| Jun-08 | 15,055,149 | 3,870,549 |
| Sep-08 | 18,732,672 | 3,677,523 |
| Dec-08 | 19,607,151 | 874,479 |

**DLS held 62.63% of Circumpacific until July 08 and 79.5% from July 2008. These figures also include the Great Artesian business in the Sept 2008 and Dec 2008 Quarters*

Exploration Expenditure

There have been significant outlays in this Quarter on Australian exploration and appraisal of \$862,514 and development of \$634,102. Actual cash payments on these items during the Quarter were much greater, as noted above, but they largely related to prior Quarters' activities. Activity during the December Quarter was largely funded by other parties.

Operations
Production

Despite recent drilling and production optimisation, production in Tintaburra and Naccowlah continues to decline. The programme for the 2009 calendar year is aimed at improving production as new wells are brought on.

² Net operating cash flow is total revenue less cost of sales less total site restoration expenses less depreciation plus any inventory movement.

Production DLS Group (BOE's)

| | 2006-07 | | | | 2007-08 | | | | 2008-09 | |
|----------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|
| | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 |
| Tintaburra | 24,686 | 27,201 | 24,454 | 26,342 | 24,972 | 38,378 | 34,216 | 27,477 | 31,328 | 28,101 |
| Naccowlah | 3,154 | 2,935 | 2,814 | 3,221 | 2,237 | 2,752 | 4,759 | 5,603 | 4,701 | 4,239 |
| Pickanjinie | 1311 | 791 | 1291 | 1118 | 927 | 936 | 914 | 801 | 271 | 800 |
| Kiana | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 831 | 536 |
| Circumpacific* | 12,959 | 13,272 | 14,176 | 10,991 | 13,075 | 14,613 | 12,706 | 12,379 | 16,232 | 16,156 |
| Total | 42,110 | 44,199 | 42,735 | 41,673 | 41,210 | 56,679 | 52,595 | 46,259 | 53,363 | 49,832 |

*DLS held 62.63% of Circumpacific until July 08 and 79.5% from July 2008. Great Artesian production included in Sept 2008 and Dec 2008 Quarters.

Development

Naccowlah Block (ATP 259P) – Cooper Basin QLD (Drillsearch 2%)

Drilling continued during the Quarter resulting in a further 4 of 5 development wells cased and suspended (C&S) as future oil producers, bringing the total for the year to 8 of 10 wells cased and suspended. Results of drilling are tabulated below:

| Well Name | Type | Spud | Rig Release | TD (m) | Result | Comment |
|------------------|------|-----------|-------------|--------|--------|---|
| Jackson South 14 | Dev | 11-Oct-08 | 22-Oct-08 | 1591 | P&A | Reservoir section interpreted as swept |
| Jackson South 16 | Dev | 24-Oct-08 | 02-Nov-08 | 1592 | C&S | Westbourne and Birkhead oil producer |
| Watson 3 | Dev | 06-Nov-08 | 14-Nov-08 | 1674 | C&S | Hutton oil producer |
| Watson 4 | App | 15-Nov-08 | 23-Nov-08 | 1691 | C&S | Hutton oil producer |
| Watkins 1 | NFE | 25-Nov-08 | 08-Dec-08 | 1722 | C&S | Hutton/ Westbourne/ basal Jurassic Producer |

Tintaburra Block (ATP 299P) – Cooper Basin, QLD (Drillsearch 11%)

The current permit term of ATP299P expired on 31 December 2008. The joint venture has lodged an application to renew the permit over a reduced area for a further 4 year term. As part of the renewal process, 138 of the current 417 sub-blocks must be relinquished.

Commercialisation of gas discoveries in PELs 91 & 106

Progress continued during the Quarter on the gas processing facility project. This Quarter continued to be focused the economic modelling and business case analysis. Discussions with potential business partners and governments were also progressed.

Exploration

PEL 106 – Cooper Basin, SA (Drillsearch 100%)

The Brownlow-1 and Canunda-1 wells were successfully drilled during the quarter resulting in further gas discoveries in the Patchawarra Formation. These wells were the first drilled on the back of the Spinel 3D seismic acquisition interpretation. Both wells were cased and suspended (C&S) as potential future gas producers. In the case of Brownlow-1, Mudlog shows while drilling and wireline logs confirmed gas pay in a 7 metre sand at 2583 to 2590 metres within the Patchawarra Formation. The sand is analogous to

sands that have produced prolifically in the nearby Middleton and Raven gasfields. In the case of Canunda-1 the drilling encountered hydrocarbon shows in sands throughout the Patchawarra section. Wireline logging confirmed probable gas pay in three zones - a 16 metre package of sands from 2560 to 2576 metres, a 4 metre sand from 2517.5 to 2522 metres and a 12 metre sand at 2639 to 2651 metres. Up to 100% fluorescence was seen in the upper two sands.

Beach Petroleum operated and funded the two wells pursuant to a farmin agreement. After the wells have been completed and tested later in the year, Beach will earn a 50% participating interest in the Beach Farmin Block, which is in the south western part of PEL 106. Results of drilling are tabulated below:

| Well Name | Type | Spud | Rig Release | TD (m) | Result | Comment |
|------------|------|-----------|-------------|--------|--------|---------------------------------|
| Brownlow 1 | WC | 19-Oct-08 | 07-Nov-08 | 2784 | C&S | Future Patchawarra gas producer |
| Canunda1 | WC | 14-Nov-08 | 03-Dec-08 | 2799 | C&S | Future Patchawarra gas producer |

PEL 106 was renewed effective 9 October 2008 for a final five year term expiring 8 October 2013. The renewed area has been reduced to 504sqkm following a 50% relinquishment.

PEL 107 – Cooper Basin, SA (Drillsearch 40%)

PEL 107 was renewed effective 2 December 2008 for a final five year term expiring 1 December 2013. The renewed area has been reduced to 406 sqkm following a 50% relinquishment.

WA-318-P – Bonaparte Basin, Offshore WA (Drillsearch 25%)

A three month suspension and extension of the permit term was granted extending the current Permit Year 5 to 12 March 2009 allowing the joint venture time to interpret data from the 1,000km Bernier 2D Seismic Survey acquired in May 2008 and to decide whether or not to enter Permit Year 6 and drill another well as part of the permit work commitment. The new seismic acquisition and the 2,600km of seismic reprocessing were designed to follow-up the Marina-1 gas-condensate discovery drilled in 2007. The joint venture will meet in February to review the results and decide on a forward plan.

WA-352-P – Carnarvon Basin, Offshore WA (Drillsearch 100%)

A suspension and extension of the licence term was granted to allow completion of the work commitments for the primary term. As a result, Permit Year 3 ended on 8 January 2009 and the permit now expires on 8 January 2012. In satisfaction of the permit work obligations 300km of 2D seismic data were acquired during the period 8-10 January 2009, using the CGGVeritas seismic vessel the 'Pacific Sword'. The seismic program is designed to delineate a number of structural leads targeting potential oil reserves in the range of 50-300 mmbbls updip to the Amulet-1 oil discovery. This seismic survey satisfies the Year 3 work commitment.

Turtle-Barnett Retentions Leases – WA-13-R and NT/RL3, Offshore WA & NT (Drillsearch 100%)

The Joint Authorities responsible for administering the Retention Leases for the Turtle field (WA-13-R) and the Barnett field (NT/RL 3) determined not to renew the two Retention Leases and as a result they returned to vacant acreage. Drillsearch no longer has any interest in either of the Leases. The sale agreement with DVM International that was announced on 5 August 2008, as a result, now has no effect.

EPP27 – Otway Basin, Offshore SA (Drillsearch 40%)

Permit EPP27 in the offshore Otway Basin of South Australia was due to expire on 24 August 2008. Until this time the joint venture had enjoyed the benefit of several suspensions and extension to the permit term to enable it to drill the commitment well, which was to be fully funded by farminees. Having failed to drill the well, the joint venture is currently negotiating a Good Standing Agreement with the Designated

Authorities that will allow the permit to be surrendered without the well being drilled and with Drillsearch being free of any further obligations.

ATP 539P – Cooper Basin, QLD (Drillsearch 100%)

Under terms of a revised farmin agreement with Bandanna Energy (formerly Enterprise Energy), Bandanna will earn a 50% interest in the block by fully funding a minimum 50km 2D seismic survey and funding 50% of two wells to be drilled during the current permit term by 31 January 2009. Acquisition of the 50km 'Sungai' 2D Seismic Survey was carried out during 23-28 October 2008.

The current term for ATP539P expires on 31 January 2009. An application for renewal over a reduced area was lodged on 24 December 2008. 16 of the current 48 graticular blocks must be relinquished as part of the renewal.

March Quarter Planned Activities**Naccowlah Block (ATP 259P) – Cooper Basin, QLD (Drillsearch 2%)**

Drilling continues with plans for 3 more wells this quarter, including further development/appraisal wells at Jackson, Jackson East, and Chilla. Drilling results since 31 December 2008 are shown below:

| Well Name | Type | Spud | Rig Release | TD (m) | Result | Comment |
|----------------|------|-----------|-------------|--------|---------|---|
| Jackson 58 | Dev | 16-Jan-09 | 24-Jan-09 | 1518 | C&S | Westbourne and Birkhead-Hutton producer |
| Jackson East 2 | App | 30-Jan-09 | | | spudded | |

Tintaburra Block (ATP 299P) – Cooper Basin, QLD (Drillsearch 11%)

Drilling is expected to resume at Tintaburra following the Naccowlah campaign in February. The operator has proposed four wells of which Drillsearch has elected to only participate in one, a development well in the Mulberry oilfield.

ATP 539P – Cooper Basin, QLD (Drillsearch 100%)

The Planet Downs-1 location was chosen as the site for the first Bandanna Energy farmin well and was planned to spud in late January. Rain in the area has caused road closures that have delayed mobilisation of the rig. Planet Downs-1 is targeting possible reserves in the order of 1mmbbl on a four-way closure located approximately 60 km southwest of the Inland Oilfield on the western margin of the Cooper-Eromanga Basin. The well is planned to take 12-16 days and will reach a total depth of 1880m.

CorporateRestructured Board

As advised on 21 October 2008, the Board has completed its review and restructure and the Board is now of a size and structure more appropriate to the Company.

Peter Simpson remains as Chairman, the Non Executive Directors are Russell Langusch, Jim McKerlie and Peter Wicks and David Williams is the Managing Director.

On 19 December 2008, the Company advised that Mr Williams had tendered his resignation as Managing Director, which resignation will take effect on 18 June 2009. The Company has commenced a search for a replacement.

Rationalisation of portfolio

Despite the sale agreement with DVM International Limited (ASX:DVM) the relevant regulators determined to not renew the Retention Leases for the Turtle/Barnett blocks (WA-13-R & NT/RL3). As a result those leases ended during the quarter and the sale agreement to DVM came to an end. The Company no longer has an interest in those blocks, nor does it have any ongoing liabilities or obligations.

Discussions with the joint venture partners in EPP 27 continued during the quarter and the parties are now close to resolving the situation. It is expected that that will mean there will be no drilling activity in the Permit.

During the Quarter the review of the Company's portfolio of permits continued. It was determined that the 2 Surat Basin blocks (ATP 552P and ATP 823P) did not meet the Company's continuing investment criteria and as a result it was determined to exit these blocks.

Since then Drillsearch has entered into an agreement with Primary Petroleum Pty Ltd to transfer Drillsearch's interests in its 2 permits in the Surat Basin, Queensland (ATP 552P and ATP 823P) to Primary. The sale is subject to a number of conditions precedents, including due diligence and approval of the Regulator, with completion of the transaction anticipated for the end of February. On completion of the sale, Drillsearch will have no further interest in, nor obligations in relation to, these Permits.

3D Oil Limited

On Monday 12 January 2009 Drillsearch announced that it had a 19.90% relevant interest (41,105,450 shares) in 3D Oil Limited (ASX:TDO) and was seeking to have discussions with the Board of 3D Oil to explore the possibility of combining the companies.

Drillsearch was unsuccessful in opening a dialogue with 3D Oil and on 16 January 2009 announced its intention to proceed with an off market takeover bid for 3D Oil on the basis of four (4) Drillsearch shares for each one (1) 3D Oil share. The Offer is subject to certain conditions including a 50.1% minimum acceptance condition.

On 9 January 2009, the trading day immediately prior to the announcement of 12 January 2009, Drillsearch's share price closed at 2.9 cents and the 3D Oil share price closed at 7.9 cents. The Drillsearch offer of four (4) Drillsearch shares for each one (1) 3D Oil share implies a premium of 47% to 3D Oil's closing price on 9 January 2009.

Drillsearch expects to lodge its Bidders Statement with ASIC and 3D Oil within the time frame required by the Corporations Act.