

Annual Report

CARNARVON PETROLEUM LTD

2004





Carnarvon Petroleum Limited

ABN 60 002 688 851

Directors

- AG Shelton *(Chairman)*
- NC Fearis *(Non-Executive Director)*
- DJ Orth *(Executive Director & COO)*

Company Secretary

- RA Pullia *(Chief Financial Officer)*

Auditors

- Ernst & Young

Solicitors

- Freehills

Bankers

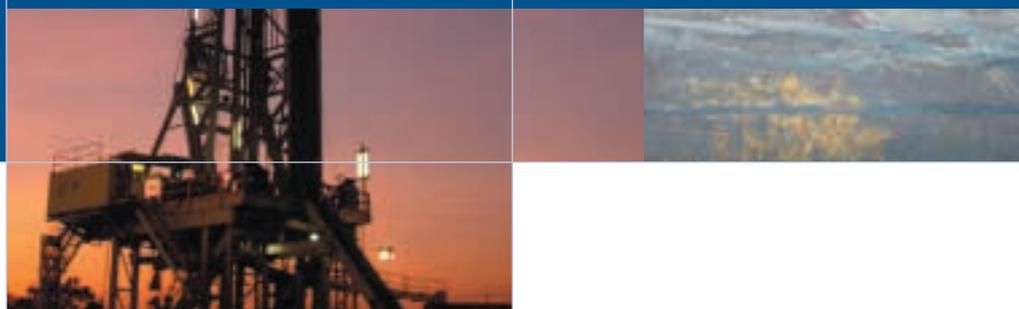
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Chairman's Report	2
Review and Results of Operations	4
Directors' Report	10
Corporate Governance Statement	15
Statement of Financial Performance	20
Statement of Financial Position	21
Statement of Cash Flows	22
Notes to the Financial Statements	23
Directors' Declaration	47
Independent Audit Report	48
Shareholding Information	50
Investor Information	52

The 2004 Annual General Meeting will be held at 10.00am on Tuesday, 30 November 2004 at the Stamford Plaza Melbourne, No. 7 Alfred Place (off Collins Street), Melbourne, Australia.



VISION:
Carnarvon's vision is to be
a successful niche
participant in the oil and
gas exploration and
production industry in
South East Asia and
Australia.

The Company's main focus during 2004 continued to be the further exploration and development of the Wichian Buri Oil Field, in which the Company has a 40% interest through its participation in the SW1A Concession Joint Venture. Pacific Tiger Energy Inc. is the joint venture operator and holder of the remaining 60% interest.

During the year the Company invested \$1.5 million in exploration and development activities. The Joint Venture drilled two field development wells, WB-N7 and WB-N8, as part of the Phase III drilling campaign and one exploration well, Huai Phai-1.

WB-N7 was drilled as a horizontal well into exploration licence L44/43 to establish the extension of the Wichian Buri Oil Field to the north outside the existing production licences, PLs 1 and 2. The well did encounter some 105 meters of net horizontal pay along hole but, due to incorrect completion practices, production was not established. WB-N8 was also drilled as a horizontal well with two multilateral holes coming off the central spine. The spine intersected approximately 164 meters of net horizontal pay but, once again, the well was completed improperly although production was established from a bottom hole location within PL 1.

Although Huai Phai-1 was not commercially successful, it did add to the overall data base and proved the existence of the F Sandstone reservoir to the west of the Wichian Buri Oil Field.

Acquisition of a 3D seismic survey was begun during the year to cover the northern extension of Wichian Buri up to the L44/43 block boundary. The survey was designed to encompass 17 square kilometers making use of the cost efficient mini-Sosie system in an effort to better image the productive F Sandstone and to unravel the structural complexities of the field.

Acquisition was halted when the survey was 40% complete due to the onset of the rainy season. The data acquired to date is far superior to earlier surveys and the cost per square kilometer much lower than traditional acquisition.

In Western Australia the Company added EP424 to its portfolio during the year. The block is contiguous to EP110 and consolidates the Jasper prospect. The blocks lie in a hydrocarbon fairway proximal to both existing oil and gas production. A seismic program is planned to delineate identified leads and prospects.

In Papua New Guinea encouraging engineering studies were conducted over the three gas/condensate discoveries in PRLs 4 and 5. Discussions continue with our partners to determine options to extract value from the blocks.

Mindful of the Company's cash position, corporate overheads are continuously being reviewed and reductions made wherever possible. During the year corporate administration costs were reduced by \$335,000 to \$1.2 million after excluding the remuneration paid



The Company continues to focus on its corporate administration costs and further reductions are anticipated in the current financial year

to the former managing director. The Company continues to focus on its corporate administration costs and further reductions are anticipated in the current financial year.

The group has reported a strong working capital position at 30 June 2004 of approximately \$1 million, including cash reserves of \$528,000, a receivable of \$100,000 from the SW1A joint venture, and a current investment in Ausam Energy Corporation valued at \$460,000, based on recent trades of Ausam shares on the TSX Venture Exchange.

During the year Dr Ken Tregonning retired as a director and on behalf of the Board and shareholders I thank him for his past contribution. Mr Rick Pullia joined the Company as our new Chief Financial Officer and Company Secretary in May. Mr Pullia, a chartered accountant, has over 16 years finance, accounting and secretarial experience with local and overseas companies. He has held senior management, commercial and finance roles with companies in the manufacturing and technology sectors and is a welcome addition to the management team.

The Company recently announced that it had commenced legal proceedings against its joint venture partner, Pacific Tiger Energy, as a result of its concern about the extent of Pacific Tiger Energy's funding of the joint venture. Amongst other financial matters, the Company alleges that Pacific Tiger Energy has not provided recent financial and operational information concerning the joint venture,

including the final report from Navigator Resource Management Inc.

Pacific Tiger Energy commissioned Navigator, on behalf of the joint venture partners, to advise on the status of the Thai operations, options for the remediation of wells WB-N7 and N8 and provision of further information or recommendations on field development. Your Board believes that receipt of this report is essential in order for the Company to be able to review and assess its recommendations, and adequately plan for the next stage of development at Wichian Buri.

Your Board did not take this action lightly, but after exhausting all possible alternatives, it was left with no other option. Your directors are committed to resolving this situation as quickly as possible, whilst safeguarding and protecting the Company's commercial interests.

On behalf of the Board I thank you for your continued support.

Andrew Shelton
Chairman



The operating results
of the consolidated
entity summarised

REVIEW AND RESULTS OF OPERATIONS

The operating results of the consolidated entity is summarised as follows:

	Consolidated 2004 \$	Consolidated 2003 \$
Revenue from oil and gas operations	974,501	1,366,253
Cost of sales	(984,346)	(1,079,902)
Revenue from non-operating activities	17,328	37,937
Corporate administration costs	(1,327,774)	(1,520,739)
Other expenses	(56,817)	(110,198)
Project costs	(6,194)	(62,526)
Other gains/(losses)	83,417	(138,994)
Exploration, evaluation and development expenditure written-off	(117,159)	-
Loss before income tax expense	(1,417,044)	(1,508,169)
Income tax expense	-	-
Loss after income tax	(1,417,044)	(1,508,169)



Carnarvon has a 40% interest in the SW1A Joint Venture. The joint venture produced 76,945 barrels of oil during the year.

Revenue from oil and gas operations for the year ended 30 June 2004 was \$974,501 compared to \$1,366,253 in the previous corresponding period, a reduction of \$391,752.

The consolidated entity's loss, after income tax, for the year ended 30 June 2004 was \$1,417,044, a reduction of \$91,125 on the previous corresponding period's loss of \$1,508,169.

Carnarvon has a 40% interest in the SW1A Joint Venture. The joint venture produced 76,945 barrels of oil during the year. The average price achieved per barrel sold was US\$23.78 and Carnarvon's share of revenue was \$974,501. The decrease in revenue was mainly due to a reduction in the number of barrels sold during the year and the appreciation of the A\$ throughout 2004. In the previous financial year 86,324 barrels of oil were produced by the joint venture. The decline in oil production in 2004 was in line with the normal decline profile of the existing wells. There was limited contribution during the year from the Phase III WB-N7 and N8 wells drilled in February 2004 due to completion problems.

Cost of sales has also decreased but not to the same extent due to the increase in depreciation expense and a higher amortisation charge against production. During the year the directors determined

that estimated ultimate recoverable (EUR) barrels of oil in the fields in which production licences had been granted was a more appropriate basis to amortise carried forward exploration, evaluation and development expenditure, compared to EUR barrels of oil in the joint venture concession area. This resulted in an increase in amortisation charged to cost of sales and a separate charge of \$117,159 relating to prior years.

Corporate administration costs were reduced by \$192,965. After excluding the remuneration paid to the former managing director, corporate administration costs were reduced by \$335,361 to \$1,185,378. Dr KC Tregonning's position has not been replaced. Reduced costs were partially offset by increases in statutory compliance and ancillary share issue costs.

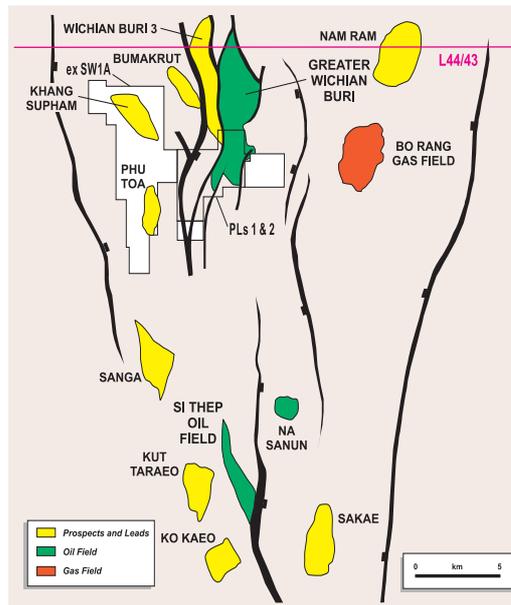
During the year the consolidated entity raised \$3,193,980 through private placements and a 1:5 pro-rata rights issue to shareholders. The proceeds were used to finance further development of the Wichian Buri oilfield, particularly wells N7 and N8.



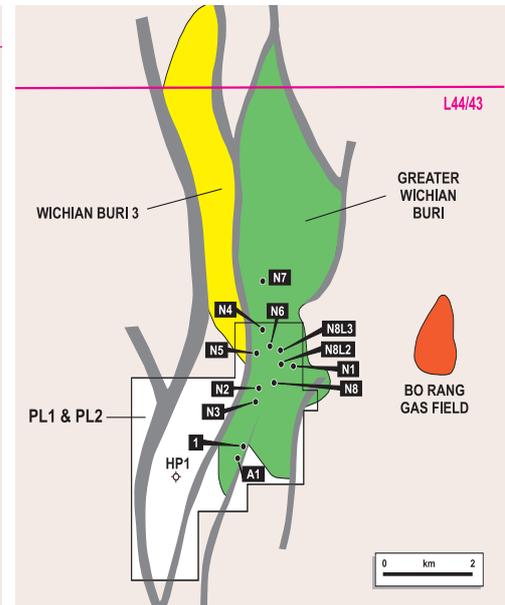
PHASE III DEVELOPMENT OF THE WICHIAN BURI OIL FIELD

(Carnarvon Petroleum 40% / Pacific Tiger Energy 60%)

Completion of the Phase III drilling campaign over the SW-1A area occurred in February. The drilling of wells HP-1 and WB-N7 and N8, which completed the Phase III development, proved up the existence of an extensive accumulation that allowed Carnarvon to confirm earlier reserve estimates provided by Helix RDS.



Northern L44/43 Leads and Prospects



Wichian Buri Oilfield and Huai Phai & WB3 Prospects

	P90 (PROVEN)	P50 (PROVEN + PROBABLE)	P10 (PROVEN + PROBABLE + POSSIBLE)
SW1A Concession area	11 MMBO	23 MMBO	45 MMBO

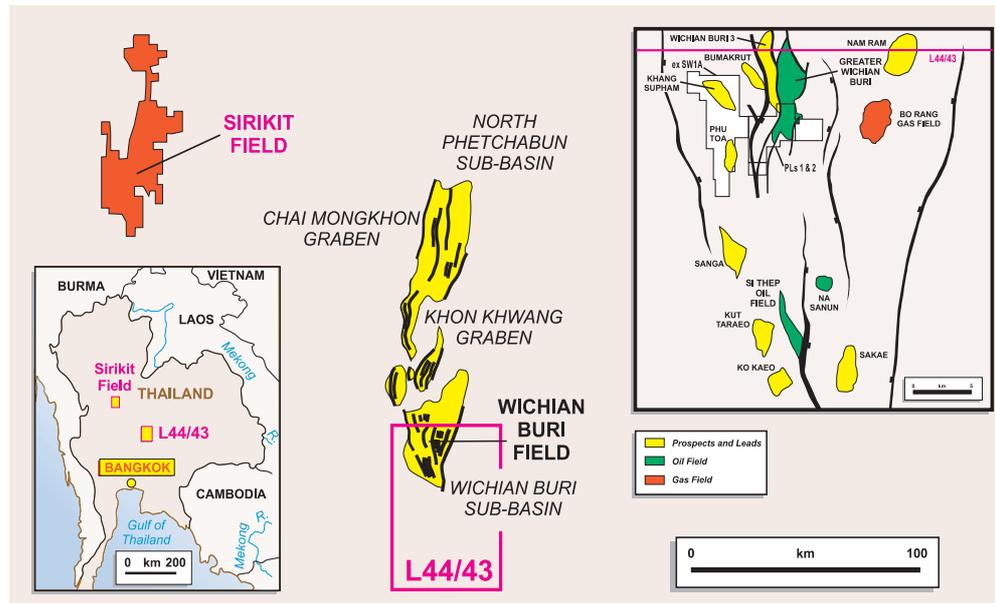
Phase III confirmed the northern extension of the field but also highlighted the variable nature of the reservoir. WB-N7 penetrated 105 meters of net horizontal pay within exploration license L44/43. The well was designed to establish the presence of oil outside PLs 1 and 2 such that application could be made for a new production license. In the event, oil was encountered while drilling and eclectic log interpretations confirmed the presence of hydrocarbons but the methodology used in completing the well did not allow it to be tested properly nor put on stream. Well WB-N8 was drilled as a three legged

multilateral well within the existing PLs as an infill well to extract previously discovered oil. A total of 364 meters of net oil bearing sandstone were penetrated in the three legs. As with WB-N7 the well was not completed properly by the operator and, although it is producing, the production has not been optimized. Engineering studies have been commissioned in an effort to determine how best to remediate the wells to both increase production and to make application for a new production license. At year's end production is at approximately 200 BOPD.

WELL	PERMIT	COUNTRY	INTEREST	METERS	COMMENT
Huai Phai-1	SW1A	Thailand	40%	993 tvd	Wildcat
WB-N7	SW1A	Thailand	40%	959 tvd	Out step
WB-N8	SW1A	Thailand	40%	972 tvd	In fill



The Estimated Ultimate Recovery of oil over the life of the Field is most likely some 23 million barrels



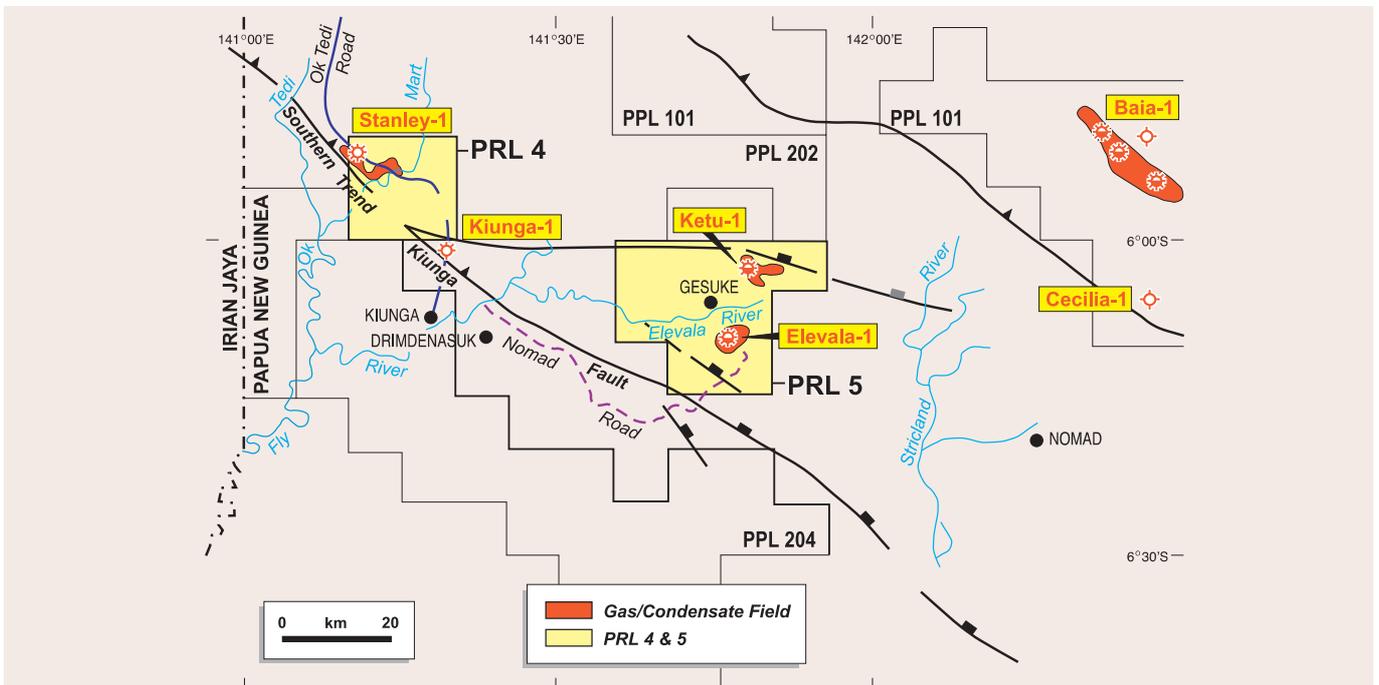
Huai Phai-1 was also drilled as part of the Phase III development. The robust structure was ideally situated to increase the overall reserves of the field and was drilled without incident. Although minor hydrocarbon shows were recorded during drilling operations, no oil was tested. The conclusions drawn from this unsuccessful well were that the F Sandstone reservoir was actually too good in terms of thickness and reservoir properties, and the requisite fault seal to the west was not present to prevent the oil from escaping.

Oil has been found in all valid tests drilled within the confines of L44/43 with the exception of Huai Phai and its presence is extensive throughout the Phetchabun Basin. The Estimated Ultimate Recovery (EUR) of oil over the life of the Field is most likely some 23

million barrels of oil (MMBO) within the confines of PLs 1 and 2 and L44/43. The EUR ranges from a Proved volume of 11 MMBO (P90) to a Proved plus Probable plus Possible of 45 MMBO (P10).

To date approximately 0.7 MMBO has been produced from the Field so that the most likely remaining volume of oil that can be recovered from the Field is approximately 22 MMBO. These estimates compare favorably to those prepared by Gaffney, Cline and Associates on behalf of Pacific Tiger Energy, given the different methodologies and purpose of the studies.

Engineering studies indicate that the key to successful development of Wichian Buri is to drill wells quickly and inexpensively, on a continuous basis,



PRLs 4 & 5, Western Papua New Guinea

so as to reduce unit cost and offset normal production decline. The actual recovery of oil over the life of the Field will depend on a variety of factors including the scale of the development and in particular the number of wells drilled. The volume of recoverable oil can sustain a much higher level of oil production which can only be achieved by drilling many wells to build production.

OTHER EXPLORATION INTERESTS

Carnarvon has been closely monitoring the available opportunities within the region and has compiled a slate of opportunities comprised of open acreage both in Asia and in Australia, fields in decline that no longer meet large company hurdle rates and divestitures resulting from mergers and consolidations. A list of like-minded companies has also been constructed and discussions continue with them in an effort to forge a strong alliance with one or more of them. The corporate objective is for a well balanced spread of assets in terms of the nature of the projects, the number of countries in which they

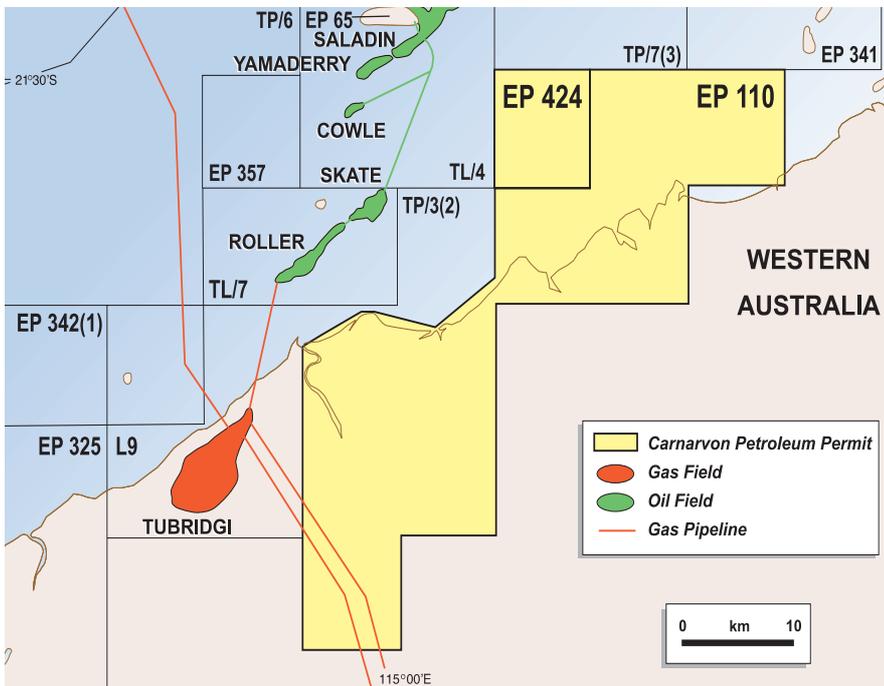
reside, and their upside potential both for the hydrocarbon potential and the access to additional projects.

PAPUA NEW GUINEA

PRL 4 and PRL 5 including the Stanley, Elevala and Ketu discoveries

(Carnarvon Petroleum 15%/Santos 35%/InterOil 20%/AWE 15%/TransOrient 7.5%/Horizon 7.5%)

Petroleum Retention Licenses 4 and 5 were excised from the original PPL 157 which has since been relinquished. The retained licenses are located in the foreland of the Papuan Basin adjacent to the Irian Jayan border in western Papua New Guinea near the town of Kiunga on the Fly River. The permits contain three gas/condensate discoveries. An engineering study was conducted during the year to evaluate various methodologies to commercially produce liquids. The participants have agreed that further studies should be undertaken by the operator, Santos, to determine how best to commercialize the hydrocarbon accumulations.



EP110, Western Australia

CARNARVON BASIN
EP 110/EP 424

(Carnarvon 35%/Strike Oil 40%/Pancontinental 25%)

These permits lie onshore/offshore near to Onslow in Western Australia. During the financial year Carnarvon, Strike Oil and Pancontinental agreed to restructure participation interests and to consolidate the two permits. The consolidation of the permits will give Carnarvon a significant interest in 850 square kilometers of prospective exploration acreage. The onshore portion of the EP110 permit is adjacent to the producing Tubridgi Gas Field while the combined acreage will cover the whole of the Jasper oil prospect near the producing Roller, Skate and Saladina Oil Fields. A number of additional leads have been identified and will be delineated by the upcoming seismic program.

AUSAM ENERGY CORPORATION

Carnarvon owns approximately 2% of Ausam Energy Corporation (formerly AusAm Resources Limited) and retains a royalty of 2.5% by virtue of a sale agreement completed in 2000 over a number of Perth Basin blocks. Ausam Energy Corporation is a public company listed on the TSX Venture Exchange in Canada and has interests in the following permits:

Perth Basin

EP407	92.5%
EP23	100.0%
EP321	92.5%
EP414	51.8%

Surat Basin

ATP 754P	50.00%
ATP 682P	25.00%
ATP 470P	35.55%

Gippsland Basin

PEP 166	50.00%
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Your directors submit
their report for the year
ended 30 June 2004

DIRECTORS

The names and details of the Company's directors in office during the financial year and until the date of this report are shown below. Directors were in office for this entire period unless otherwise stated.

Andrew G Shelton **Chairman**

Bachelor of Arts (Economics and Politics), Master of Arts (Cantab.)

Age 57. Appointed Director and Chairman on 1 April 2002. Chairman of the Audit Committee, Remuneration and Nominations Committee, and Governance Committee. Independent corporate finance adviser specializing in strategic and corporate finance advice, capital raisings, mergers and acquisitions, valuations and financial analysis. Principal and director of Andrew Shelton & Co Pty Limited and a non-executive director of Whise Acoustics Limited. Fellow of the Australian Institute of Company Directors, past President & CEO of JP Morgan Canada.

Neil C Fearis **Non-Executive Director**

Bachelor of Laws (Hons)

Age 53. Appointed Director 30 November 1999. Member of the Audit Committee, Remuneration and Nominations Committee, and Governance Committee. A commercial lawyer with 27 years' experience of legal practice in London, Sydney and Perth. Principal of the Western Australian-based law firm, Fearis Salter Power Shervington. Chairman of Kresta Holdings Limited and a non-executive director of Capital Growth Corp Limited and Perseus Mining Limited. Member of the Australian Institute of Company Directors and Associate of the Securities Institute of Australia.

David J Orth **Executive Director & Chief Operating Officer**

Bachelor of Science, Diploma of GeoSci.

Age 55. Appointed Executive Director 14 December 2000. Appointed Chief Operating Officer July 2003. A geologist with in excess of 25 years' industry experience having worked for Amoco and BHP Petroleum as well as a number of independent oil companies throughout North America, Europe, Africa, the Middle East and Australasia. Member of Petroleum Exploration Society of Australia.

Dr Kenneth C Tregonning

Mr Tregonning retired from the position of Managing Director and Chief Executive Officer on 28 November 2003, and remained a non-executive director until his resignation from the Board on 5 January 2004.



Principal activities continued to be directed towards oil and gas exploration

Interests in the shares and options of the Company and related bodies corporate

Relevant interest in the shares and options of the Company as at the date of this report:

Directors	Ordinary Shares	Options over Ordinary Shares
AG Shelton	9,208,906	1,600,743
NC Fearis	3,871,400	300,000
DJ Orth	1,569,127	47,428

CORPORATE INFORMATION

Corporate structure

Carnarvon Petroleum Ltd is a limited liability company incorporated and domiciled in Australia. Carnarvon Petroleum Ltd has prepared a consolidated financial report incorporating the following entities:

Entity Name	% Ownership
Carnarvon Petroleum Ltd	100
Lassoc Pty Ltd	100
S.R.L. Exploration Pty Ltd	100
Strategic Exploration (Asia) Limited	100

Principal activities

During the course of the 2004 financial year the consolidated entity's principal activities continued to be directed towards oil and gas exploration, development and production.



Employees

The consolidated entity employed 2 employees as at 30 June 2004 (2003: 2 employees).

EARNINGS PER SHARE	Cents
Basic earnings per share	(0.6)
Diluted earnings per share	(0.6)

DIVIDENDS

The directors have not recommended the payment of any dividend in respect of the financial year ending 30 June 2004. No dividends were declared or paid during the financial year.

REVIEW AND RESULTS OF OPERATIONS

A review of the operations during the financial year of the consolidated entity and the results of those operations is contained in the previous section and the directors adopt and endorse that review which is to be regarded as incorporated herein.

SIGNIFICANT CHANGES IN THE STATE OF AFFAIRS

There were no significant changes in the state of affairs of the consolidated entity during the financial year.

SIGNIFICANT EVENTS AFTER BALANCE DATE

There were no significant events that occurred subsequent to year end other than as disclosed in note 26 to the financial statements.

LIKELY DEVELOPMENTS

The review of operations outlines likely developments in the operations of the consolidated entity. The directors are not presently in a position to predict the results of those developments.

The directors are of the opinion that further information as to the likely developments in the operations of the consolidated entity would prejudice the interests of the Company and the consolidated entity and it has accordingly not been included.

ENVIRONMENTAL REGULATION AND PERFORMANCE

The consolidated entity's oil and gas exploration and development activities are concentrated in Western Australia, Thailand and Papua New Guinea. Environmental obligations are regulated under both State and Federal Law in Western Australia, under the Department of Mineral Fuels regulations in Thailand, and under the Oil and Gas Act in Papua New Guinea. No significant environmental breaches have been notified by any government agency during the year ended 30 June 2004.

SHARE OPTIONS

Unissued shares

As at the date of this report, there were 37,492,101 options to subscribe for shares in the Company exercisable at 6 cents and expiring on 31 December 2005.

Option holders are entitled to participate in any new pro-rata issue of securities of the Company only on the prior exercise of the options.

Shares issued as a result of exercise of options

There have been no options exercised during or since the end of the financial year.

Expiry of options

On 31 December 2003, 10,000,000 options exercisable at 20 cents each expired.

INDEMNIFICATION AND INSURANCE OF DIRECTORS AND OFFICERS

The Company has arranged Directors and Officers insurance to cover losses or liabilities incurred by a person as an officer of the Company or of a related body corporate as permitted by law. Full details of the cover and premium are not disclosed as the insurance policy prohibits the disclosure.



DIRECTORS' AND OTHER OFFICERS' EMOLUMENTS

The Remuneration and Nominations Committee, established in August 2003, advises the Board on remuneration policies and practices, evaluates the performance of senior management against pre-agreed goals, and makes recommendations to the Board on remuneration for senior management and executive directors.

Total non-executive directors' fees are approved by shareholders and the Board is responsible for the allocation of those fees amongst the individual members of the Board. All directors are eligible to participate in the company's Employee Share Plan, details of which are disclosed in note (17) to the financial statements.

Details of the nature and amount of each element of the emolument of each director and each of the executive officers of the Company are as follows:

Emoluments of directors of Carnarvon Petroleum Ltd

	Annual Emoluments Base Fee \$	Termination & Similar Payments \$	Long Term Emoluments Superannuation \$	Total \$
<u>Non-Executive Directors</u>				
AG Shelton	45,200	-	4,800	50,000
NC Fearis	27,000	-	3,000	30,000
<u>Executive Directors</u>				
Dr KC Tregonning	50,000	80,839	11,557	142,396
DJ Orth	160,750	-	25,000	185,750

There are no performance bonus plans offered to directors of the Company.

Emoluments of executive officers of Carnarvon Petroleum Ltd

	Annual Emoluments Base Fee \$	Long Term Emoluments Superannuation \$	Total \$
RA Pullia	16,450	1,481	17,931
TS Irwin	178,959	9,645	188,604



The terms 'director' and 'officer' have been treated as mutually exclusive for the purposes of this disclosure.

The value of emoluments have been determined on the basis of cost to the Company and consolidated entity. Executive officers are those directly accountable and responsible for the operational management and strategic direction of the Company and the consolidated entity.

DIRECTORS' MEETINGS

During the year, 12 directors' meetings were held. The number of meetings attended by each director is as follows:

Director	Number of Directors' Meetings Held while in Office	Number of Directors' Meetings Attended
AG Shelton	12	11
NC Fearis	12	12
Dr KC Tregonning	8	8
DJ Orth	12	12

The Audit Committee met twice during the year with all members present. The Remuneration and Nomination Committee met twice with all members present. The Governance Committee met once with all members present.



CORPORATE GOVERNANCE

In recognising the need for the highest standards of corporate behaviour and accountability, the directors of Carnarvon Petroleum Ltd support and have adhered to the principles of good corporate governance. The Company's corporate governance statement is contained in the next section of the Annual Report.

Signed in accordance with a resolution of the directors.

AG Shelton
Director

Melbourne
29 September 2004



Practices were in place throughout the year and have followed the guidelines within the Council's Recommendation

The Board of Directors of Carnarvon Petroleum Limited ("the Company") is responsible for the corporate governance of the consolidated entity. The Board guides and monitors the business and affairs of Carnarvon on behalf of the shareholders by whom they are elected and to whom they are accountable.

The format of the Corporate Governance Statement has changed in comparison to the previous year due to the introduction of the Australian Stock Exchange Corporate Governance Council's ("the Council") 'Principles of Good Corporate Governance and Best Practice Recommendations' ("the Recommendations"). In accordance with the Council's recommendations, the Corporate Governance Statement must now contain certain specific information and must disclose the extent to which the Company has followed the guidelines during the period. Where a recommendation has not been followed, that fact must be disclosed, together with reasons for the departure. The Company's Corporate Governance Statement is now structured with reference to the Council's principles and recommendations, which are as follows:

- Principle 1. Lay solid foundations for management and oversight**
- Principle 2. Structure the board to add value**
- Principle 3. Promote ethical and responsible decision making**
- Principle 4. Safeguard integrity in financial reporting**
- Principle 5. Make timely and balanced disclosure**
- Principle 6. Respect the rights of shareholders**
- Principle 7. Recognise and manage risk**
- Principle 8. Encourage enhanced performance**
- Principle 9. Remunerate fairly and responsibly**
- Principle 10. Recognise the legitimate interests of stakeholders**

A description of the Company's main corporate governance practices is set out below. These practices were in place throughout the year and have followed the guidelines within the Council's Recommendations, unless otherwise stated.



Principle 1:
Lay solid foundations for management and oversight

The Board’s primary responsibility is to oversee the Company’s business activities and management for the benefit of shareholders.

The key responsibilities of the Board include:

- Developing long-term corporate objectives and strategy with management and approving plans, new investments, major capital and operating expenditures and major funding activities proposed by management
- Defining and setting performance expectations for the Company and monitoring actual performance
- Appointing and reviewing the performance of senior management
- Assuring itself that there are effective health, safety, environmental and operational procedures in place.
- Satisfying itself that there are effecting reporting systems that will assure the Board that proper financial, operational, compliance, risk management and internal control processes are in place and function appropriately
- Satisfying itself that the annual financial statements of the Company fairly and accurately set out the financial position at year end, and the financial performance for the year; and
- Reporting to and advising shareholders.

Principle 2:
Structure the board to add value

Board Composition

The skills, experience and expertise relevant to the position of Director held by each Director in office at the date of this report is disclosed in the Directors’ Report. The composition of the Board, and the term in office held by each Director at the date of this report, is as follows:

AG Shelton	Chairman, non-executive director	2 years
NC Fearis	Non-executive director	5 years
DJ Orth	Executive director	4 years

Directors of the Company are considered to be independent when they are independent of management and free from any business or other relationship that could materially interfere with – or could reasonably be perceived to materially interfere with – the exercise of their unfettered and independent judgement. The Chairman, AG Shelton, is not considered independent as he is a principal and director of a company that provided financial consulting services to Carnarvon during the year. This has resulted in the Company not following Recommendations 2.1 and 2.2, which suggest that a majority of the board be independent directors and the Chairman be an independent director.

The Board believes that while the Chairman is not independent and a majority of directors are not independent, the current composition of the Board, given its combined skills and capability, the size of Carnarvon and the scale of its activities, best serve the interests of shareholders.

Independent Professional Advice

The Directors may, in carrying out their duties to the Company, seek external professional advice. They are entitled to reimbursement of all reasonable costs where such requests for advice is approved by the Chairman.

Remuneration and Nominations Committee

The Remuneration and Nominations Committee advises the Board on remuneration policies and practices, evaluates the performance of senior management against pre-agreed goals, and makes recommendations to the Board on remuneration for senior managers. The Committee considers independent advice on policies and practices to attract, motivate, reward and retain strong performers. It is also the Committee’s role to consider the appropriate size and composition of the Board, criteria for Board membership, candidates for Board membership, and the terms and conditions of appointment to the Board.



Directors and employees observe the highest standards of behaviour and business ethics when engaging in corporate activity.

The composition of the Board is determined in accordance with the following principles and guidelines:

- the Board should comprise a majority of non-executive directors;
- the chairman should be a non-executive director;
- the Board should comprise directors with an appropriate range of qualifications and expertise; and
- the Board should meet at least bi-monthly and follow meeting guidelines set down to ensure all directors are made aware of, and have available all necessary information, to participate in an informed discussion of all agenda items.

Members of the Remuneration and Nominations Committee are Mr AG Shelton (Chairman) and Mr NC Fearis. The Chief Operating Officer and Company Secretary attend Committee meetings by invitation. The Remuneration Committee was established in December 2002 and its brief was expanded in August 2003 to include Board nominations. Details of these Directors' qualifications and attendance at Committee meetings are set out in the Directors' Report.

**Principle 3:
Promote ethical and responsible decision-making**

The Company recognizes the need for Directors and employees to observe the highest standards of behaviour and business ethics when engaging in corporate activity.

Conflict of Interest

The Board has approved 'Conflict-of-Interest Guidelines' which apply if there is, or may be, a conflict between the personal or other interests of a Director and the business of the Company. In that event, when the matter comes before the Board for discussion, the Director withdraws from the meeting for the period the matter is considered and takes no part in the discussions or decision-making process.

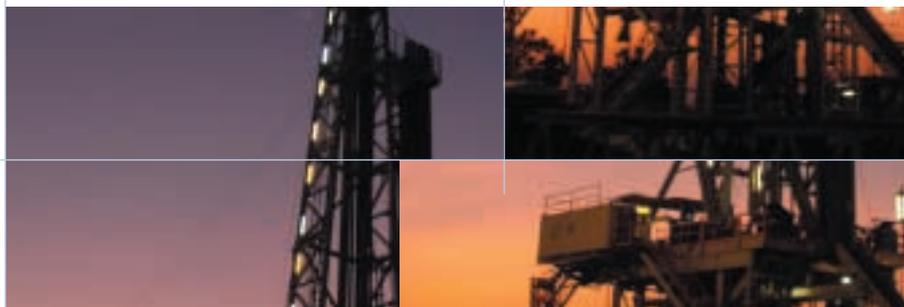
Dealing in Company Securities

The Company has a share trading policy, binding on Directors and employees, designed to assist Directors and employees to avoid insider trading, and provide guidelines for trading in the Company's securities. The policy stipulates that the only appropriate time for a Director or employee to acquire or sell Carnarvon securities is when he or she is not in possession of price-sensitive information that is not generally available to the market. Directors wishing to buy or sell the Company's securities in accordance with the policy may only do so after first having advised the Chairman of his or her intention. In the case of employees, there is a correspondence notification requirement.

**Principle 4:
Safeguard integrity in financial reporting**

Audit Committee

The Audit Committee was established in September 2002 and is the custodian of the external audit relationship and assists



the Board to assure itself that there are effective accounting, auditing, internal control, business risk management, compliance and reporting systems, processes and practices in place.

The Audit Committee consists of Mr AG Shelton (Chairman) and Mr NC Fearis. The external auditors, the Chief Operating Officer and the Chief Financial Officer attend Committee meetings by invitation. Details of these Directors' qualifications and attendance at audit committee meetings are set out in the Directors' Report.

The Audit Committee further requires that the Company's Chief Executive Officer (or equivalent) and Chief Financial Officer annually certify that the Company's financial statements present a true and fair view, in all material respects, of the Company's financial condition and operating results and are in accordance with relevant accounting standards, and that the integrity of the financial statements are founded on a sound system of risk management and internal compliance and control which, in all material respects, implements the policies adopted by the Board.

**Principle 5:
Make timely and balanced disclosure**

The Company follows the disclosure requirements of the Corporations Act 2001 and the ASX Listing Rules, in particular:

- Continuous disclosure – which is its core disclosure obligation and primary

method of informing the market and shareholders

- Periodic disclosure – in the form of full-year, half-year reporting and quarterly reporting
- Specific information disclosure – as and when required, of administrative and corporate details, usually in the form of ASX releases.

Directors are committed to the promotion of investor confidence by ensuring that trade in the Company's securities takes place in an efficient, competitive and informed market. In compliance with ASX continuous disclosure requirements, the Company has procedures in place to ensure that all price sensitive information is identified, reviewed by senior management and disclosed to the ASX in a timely manner and that all information provided to the ASX is immediately available to shareholders and the market on the Company's website.

The Company is in the process of preparing written policies and procedures on information disclosure that will be available in a separate Corporate Governance section of the Company's website.

**Principle 6:
Respect the rights of shareholders**

The Board aims to ensure that shareholders are kept informed of all major developments affecting the Company. Information is communicated to shareholders through:

- Annual and Half Yearly Reports;
- The Chairman's Address delivered at the Annual General Meeting;
- Notice of all meetings of shareholders and explanatory notes of proposed resolutions;
- Shareholder mailing list allowing each ASX release to be forwarded by email directly to every shareholder on the list; and
- Company website www.carnarvonpetroleum.com offering shareholders access to ASX releases, company media releases and other company data.

Shareholders are encouraged at Annual General Meetings to ask questions of Directors and senior management and also the Company's external auditors, who are required to be in attendance.

**Principle 7:
Recognise and manage risk**

The Board has as one of its main objectives the oversight of the management of areas where risk to the Company is perceived to be significant. Board papers and management presentations routinely address the risks associated with proposals submitted to the Board for approval.

The Company formed a Governance Committee in August 2003 which has two roles. It advises on and monitors the Company's governance practices and assists the Board to assure itself that there is an appropriate and effective process for the direction and control of the Company.



Governance practices assist the Board to assure itself that there is an appropriate and effective process for the direction and control of the Company

In particular it:

- monitors the management systems and processes in place for compliance with laws and regulatory requirements, and
- monitors the management systems in place for addressing significant business risks and the framework of internal management controls.

Members of the Governance Committee are Mr AG Shelton (Chairman) and Mr NC Fearis. The Chief Operating Officer and Chief Financial Officer attend Committee meetings by invitation.

The Committee will prepare a written risk management strategy that will be posted on the Company's website when it is approved by the Board. This will be completed during the next reporting period.

**Principle 8:
Encourage enhanced performance**

The performance of the Board, its committees and each individual director, is to be evaluated by the Remuneration and Nominations Committee. A formal review procedure will be prepared and a performance evaluation conducted during the next reporting period.

**Principle 9:
Remunerate fairly and responsibly**

Non-executive directors are paid directors' fees out of the maximum aggregate amount approved by shareholders for the remuneration of non-executive directors.

A discussion of the Remuneration Committee and its role is disclosed in Principle 2. Remuneration of directors and executives is disclosed in the Directors' Report.

**Principle 10:
Recognise the legitimate interests of stakeholders**

The Company is developing a Code of Conduct and Business Ethics that will formally document the Company's approach to all stakeholders. A copy of this Code will be available in a separate Corporate Governance section of the Company's website.

Disclosure on the Company's website

Some of the Council's Recommendations suggest that several policies and procedures dealt with by Recommendations should be available on the Company's website in a section clearly marked for corporate governance. The Company currently does not have a separate corporate governance section on its website but will introduce one in the current reporting period and will include those matters recommended for inclusion by the Council.



STATEMENT OF FINANCIAL PERFORMANCE

FOR THE YEAR ENDED 30 JUNE 2004

	Notes	Consolidated		Carnarvon Petroleum Ltd	
		2004 \$	2003 \$	2004 \$	2003 \$
REVENUE FROM ORDINARY ACTIVITIES	2(a)	991,829	1,404,190	17,328	37,937
Cost of sales	2(b)	(984,346)	(1,079,902)	–	–
General administration		(554,865)	(434,230)	(554,865)	(434,230)
Directors' emoluments		(408,146)	(442,160)	(408,146)	(442,160)
Salaries and employee benefits		(183,934)	(281,851)	(183,934)	(281,851)
Legal and consulting fees		(144,736)	(228,954)	(144,736)	(228,954)
Other expenses from ordinary activities	2(c)	(92,910)	(243,742)	(92,910)	(243,742)
Other gains/(losses)	2(d)	83,417	(138,994)	85,159	(709,430)
Project costs		(6,194)	(62,526)	(6,194)	(62,526)
Exploration, evaluation and development expenditure written-off	2(e)	(117,159)	–	–	–
LOSS FROM ORDINARY ACTIVITIES BEFORE INCOME TAX EXPENSE		(1,417,044)	(1,508,169)	(1,288,298)	(2,364,956)
INCOME TAX EXPENSE RELATING TO ORDINARY ACTIVITIES	3	–	–	–	–
LOSS FROM ORDINARY ACTIVITIES AFTER INCOME TAX EXPENSE		(1,417,044)	(1,508,169)	(1,288,298)	(2,364,956)
NET LOSS ATTRIBUTABLE TO MEMBERS OF CARNARVON PETROLEUM LTD		(1,417,044)	(1,508,169)	(1,288,298)	(2,364,956)
Capital raising costs		(232,756)	(146,574)	(232,756)	(146,574)
TOTAL REVENUES, EXPENSES AND VALUATION ADJUSTMENTS ATTRIBUTABLE TO MEMBERS OF CARNARVON PETROLEUM LTD AND RECOGNISED DIRECTLY IN EQUITY		(232,756)	(146,574)	(232,756)	(146,574)
TOTAL CHANGES IN EQUITY OTHER THAN THOSE RESULTING FROM TRANSACTIONS WITH OWNERS AS OWNERS ATTRIBUTABLE TO MEMBERS OF CARNARVON PETROLEUM LTD		(1,649,800)	(1,654,743)	(1,521,054)	(2,511,530)
Basic earnings per share (cents per share)	25	(0.6)	(0.9)		
Diluted earnings per share (cents per share)	25	(0.6)	(0.9)		

STATEMENT OF FINANCIAL POSITION

AS AT 30 JUNE 2004

	Notes	Consolidated		Carnarvon Petroleum Ltd	
		2004 \$	2003 \$	2004 \$	2003 \$
CURRENT ASSETS					
Cash assets		527,882	357,112	504,556	321,383
Receivables	4	246,191	140,603	44,771	16,164
Inventories	5	104,841	73,359	-	-
Other financial assets	7	282,876	-	282,876	-
Other	6	76,225	68,806	6,200	7,000
TOTAL CURRENT ASSETS		1,238,015	639,880	838,403	344,547
NON-CURRENT ASSETS					
Receivables	4	61,265	158,160	3,593,282	2,029,285
Other financial assets	7	-	212,697	1,482,962	1,695,659
Plant and equipment	9	190,188	171,950	6,089	19,399
Deferred exploration, evaluation and development costs	10	5,722,278	4,387,531	-	-
TOTAL NON-CURRENT ASSETS		5,973,731	4,930,338	5,082,333	3,744,343
TOTAL ASSETS		7,211,746	5,570,218	5,920,736	4,088,890
CURRENT LIABILITIES					
Payables	11	259,322	369,798	156,880	205,784
Provisions	12	880	25,812	880	25,812
TOTAL CURRENT LIABILITIES		260,202	395,610	157,760	231,596
TOTAL LIABILITIES		260,202	395,610	157,760	231,596
NET ASSETS		6,951,544	5,174,608	5,762,976	3,857,294
EQUITY					
Contributed equity	13	45,318,074	42,124,094	45,318,074	42,124,094
Accumulated losses	14	(38,366,530)	(36,949,486)	(39,555,098)	(38,266,800)
TOTAL EQUITY		6,951,544	5,174,608	5,762,976	3,857,294

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED 30 JUNE 2004

	Notes	Consolidated		Carnarvon Petroleum Ltd	
		2004 \$	2003 \$	2004 \$	2003 \$
CASH FLOWS FROM OPERATING ACTIVITIES					
Receipts from customers		994,871	1,318,422	–	–
Payments to suppliers and employees		(2,421,370)	(2,641,243)	(1,381,490)	(1,506,000)
Interest received		17,328	10,740	17,328	10,740
Exploration costs		(6,194)	(62,526)	(6,194)	(62,526)
NET CASH FLOWS FROM/(USED IN) OPERATING ACTIVITIES	15(a)	(1,415,365)	(1,374,607)	(1,370,356)	(1,557,786)
CASH FLOWS FROM INVESTING ACTIVITIES					
Purchase of interests in permits		–	(19,075)	–	(19,075)
Exploration and development expenditure		(1,515,074)	(1,920,397)	–	–
Contributions for development expenditure		–	1,473,704	–	1,473,704
Purchase of plant & equipment		(86,205)	(126,804)	(4,713)	(17,831)
Advances to controlled entities		–	–	(1,635,738)	(1,913,920)
NET CASH FLOWS FROM/(USED IN) INVESTING ACTIVITIES		(1,601,279)	(592,572)	(1,640,451)	(477,122)
CASH FLOWS FROM FINANCING ACTIVITIES					
Proceeds from issue of shares & options		3,426,736	1,977,075	3,426,736	1,977,075
Capital raising costs		(232,756)	(146,574)	(232,756)	(146,574)
Proceeds from sale of employee shares disposed of by the Company as agent		–	27,197	–	27,197
NET CASH FLOWS FROM/(USED IN) FINANCING ACTIVITIES		3,193,980	1,857,698	3,193,980	1,857,698
NET INCREASE/(DECREASE) IN CASH HELD					
Cash at beginning of period		357,112	466,928	321,383	498,593
Effects of foreign exchange rate changes on cash		(6,566)	(335)	–	–
CASH AT END OF PERIOD	15(b)	527,882	357,112	504,556	321,383

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of accounting

The financial report is a general-purpose financial report, which has been prepared in accordance with the requirements of the Corporations Act 2001 including applicable Accounting Standards. Other mandatory professional reporting requirements (Urgent Issues Group Consensus Views) have also been complied with.

The financial report has been prepared in accordance with the historical cost convention.

Going concern

The consolidated financial report has been prepared on a going concern basis, which contemplates continuity of normal business activities and realisation of assets and discharge of liabilities in the ordinary course of business.

The consolidated entity has incurred an operating loss of \$1,417,044 for the financial period ended 30 June 2004. The ability of the consolidated entity to continue as a going concern, including the ability of the consolidated entity to pay its debts as and when they fall due, is dependent upon:

- oil sales revenue derived from the SW1A Joint Venture;
- generation of future profits from the SW1A Joint Venture; and
- injection of capital

Without the generation of future profits and the injection of capital, there is significant uncertainty as to whether the consolidated entity will be able to continue as a going concern and therefore whether it will be able to realise its assets and extinguish its liabilities in the normal course of business and at the amounts stated in the financial report.

It is on the basis that the consolidated entity will generate profits in the future from oil sales derived from the SW1A Joint Venture and an injection of capital will occur to cover future exploration and development expenditure, that the directors have prepared the financial report on a going concern basis. Consequently, no adjustments have been made relating to the recoverability and classification of recorded asset amounts or to the amounts and classification of liabilities that might be necessary should the consolidated entity not continue as a going concern.

(b) Changes in accounting policies

The accounting policies adopted are consistent with those of the previous year.

(c) Cash and cash equivalents

Cash on hand and in banks and short-term deposits are stated at nominal value.

For the purposes of the Statement of Cash Flows, cash includes cash on hand and in banks, and money market investments at call readily convertible to cash.

(d) Recoverable amount

Non-current assets measured using the cost basis are not carried at an amount above their recoverable amount, and where carrying values exceed this recoverable amount, the asset is written down. In determining recoverable amount, the expected net cash flows have been discounted to their present value.

(e) Investments

Listed shares are classified as current investments and valued at the lower of cost and recoverable amount. Other non-current investments are carried at the lower of cost and recoverable amount.

(f) Plant and equipment

Cost and valuation

All classes of plant and equipment are measured at cost.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Depreciation

Depreciation is provided on a straight-line basis on all plant and equipment. Major depreciation periods for plant and equipment are between 2 and 5 years (2003: 2 and 5 years).

(g) Joint ventures

Interest in the joint venture operation is recognised by including in the respective classifications, the share of individual assets employed and share of liabilities and expenses incurred.

(h) Exploration, evaluation and development costs

Costs carried forward

Costs arising from exploration and evaluation activities are carried forward provided such costs are expected to be recouped through successful development, or by sale, or where exploration and evaluation activities have not, at reporting date, reached a stage to allow a reasonable assessment regarding the existence of economically recoverable reserves.

Amortisation

Costs on productive areas are amortised over the life of the area of interest to which such costs relate on the production output basis.

(i) Employee benefits

Provision is made for employee benefits accumulated as a result of employees rendering services up to the reporting date. These benefits include wages and salaries and annual leave. Sick leave is not accrued as it is not of a material nature and any entitlement is not vested on termination of employment.

Liabilities arising in respect of wages and salaries, annual leave and any other employee entitlements expected to be settled within twelve months of the reporting date are measured at their nominal amount based on remuneration rates which are expected to be paid when the liability is settled. All other employee benefit liabilities are measured at the present value of the estimated future cash outflow to be made in respect of services provided by employees up to the reporting date. In determining the present value of future cash outflows, the market yield as at reporting date on national government bonds, which have terms to maturity approximating the terms of the related liability, are used.

Employee benefit expenses and revenues arising in respect of the following categories:

- wages and salaries, non-monetary benefits, annual leave and other leave entitlements; and
- other types of employee benefits

are recognised against profits on a net basis in their respective categories.

The value of the employee share scheme described in note 17 is not being charged as an employee benefits expense. Any contributions made to superannuation plans are recognized against profits when due.

(j) Revenue recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the entity and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Sale of goods

Control of the goods has passed to the buyer.

Interest

Control of the right to receive the interest payment.

(k) Comparatives

Where necessary, comparatives have been reclassified and repositioned for consistency with current year disclosures.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(l) Leases

Leases are classified at their inception as either operating or finance leases based on the economic substance of the agreement so as to reflect the risks and benefits incidental to ownership.

Operating leases

The minimum lease payments of operating leases, where the lessor effectively retains substantially all of the risks and benefits of ownership of the leased item, are recognised as an expense on a straight-line basis.

(m) Principles of consolidation

The consolidated financial statements are those of the consolidated entity, comprising Carnarvon Petroleum Ltd (the parent company) and all entities that Carnarvon Petroleum Ltd controlled from time to time during the year and at reporting date.

The financial statements of subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies. Adjustments are made to bring into line any dissimilar accounting policies that may exist.

All intercompany balances and transactions, including unrealised profits arising from intra-group transactions, have been eliminated in full. Unrealised losses are eliminated unless costs cannot be recovered.

(n) Foreign currencies

Translation of foreign currency transactions

Transactions in foreign currencies of entities within the consolidated entity are converted to local currency at the rate of exchange ruling at the date of the transaction. Foreign currency monetary items that are outstanding at reporting date are translated using the spot rate at the end of the financial year.

All exchange differences arising from the translation of assets and liabilities are recognised as revenues and expenses for the financial year.

Translation of financial reports of overseas operations

Strategic Exploration (Asia) Limited ("SEAL"), a wholly owned subsidiary, is accounted for in its functional currency, being the US dollar. SEAL is an integrated operation with its financial report being translated using the temporal rate method and any exchange differences are taken directly to the Statement of Financial Performance.

(o) Taxes

Income taxes

Tax effect accounting is applied using the liability method whereby income tax is regarded as an expense and is calculated on the accounting profit after allowing for permanent differences. To the extent timing differences occur between the time items are recognised in the financial statements and when items are taken into account in determining taxable income, the net related taxation benefit or liability, calculated at current rates, is disclosed as a future income tax benefit or a provision for deferred income tax. The net future income tax benefit relating to tax losses and timing differences is not carried forward as an asset unless the benefit is virtually certain of being recognised.

Goods and Services Tax (GST)

Revenues, expenses and assets are recognised net of the amount of GST except:

- where the GST incurred on a purchase of goods and services is not recoverable from the taxation authority, in which case the GST is recognised as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- receivables and payables are stated with the amount of GST included.

The net amount of GST recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the Statement of Financial Position.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Cash flows are included in the Statement of Cash Flows on a gross basis and the GST component of cash flows arising from investing and financing activities, which is recoverable from, or payable to, the taxation authority are classified as operating cash flows.

Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the taxation authority.

(p) Earnings per share

Basic EPS is calculated as net profit or loss attributable to members, adjusted to exclude costs of servicing equity (other than dividends), divided by the weighted average number of ordinary shares, adjusted for any bonus element.

Diluted EPS is calculated as net profit or loss attributable to members, adjusted for:

- costs of servicing equity (other than dividends);
- the after tax effect of dividends and interest associated with dilutive potential ordinary shares that have been recognised as expenses; and
- other non-discretionary changes in revenue or expenses during the period that would result from the dilution of potential ordinary shares divided by the weighted average number of ordinary shares and dilutive potential ordinary shares, adjusted for any bonus element.

(q) Contributed equity

Issued and paid up capital is recognised at the fair value of the consideration received by the Company.

Any transaction costs arising on the issue of ordinary shares are recognised directly in equity as a reduction of the share proceeds received.

(r) Payables

Liabilities for trade creditors and other amounts are carried at cost which is the fair value of the consideration to be paid in the future for goods and services received, whether or not billed to the consolidated entity.

Payables to related parties are carried at the principal amount. Interest, when charged by the lender, is recognised as an expense on an accrual basis.

(s) Receivables

Trade receivables are recognised and carried at original invoice amount less a provision for any uncollectible debts. An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off as incurred.

Receivables from related parties are recognised and carried at the nominal amount due. Interest is taken up as income on an accrual basis.

(t) Provision for rehabilitation

The provision for rehabilitation is recognised when the liability arises from production. The directors believe that the rehabilitation provision is not material at this stage of production and therefore a provision for restoration has not been recorded in the financial statements.

(u) Employee share loans

The carrying value of advances made to eligible employees is the lower of the equivalent market value of the shares from time to time or the price of the shares at the time the shares were issued to eligible employees.

(v) Inventories

Inventories relate to warehouse stores and materials. These represent consumable supplies and maintenance spares expected to be used in production and are valued at the lower of cost and net realisable value. Cost comprises purchase, inspection and transportation costs.

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

	Notes	Consolidated		Carnarvon Petroleum Ltd	
		2004 \$	2003 \$	2004 \$	2003 \$
2. PROFIT/(LOSS) FROM ORDINARY ACTIVITIES					
Loss from ordinary activities before income tax is arrived at after taking into account:					
(a) Revenue from ordinary activities					
<i>Revenue from operating activities:</i>					
Oil and Gas operations					
Oil Revenue – SW1A joint venture		974,501	1,366,253	–	–
Total revenue from operating activities		974,501	1,366,253	–	–
<i>Revenue from non-operating activities</i>					
Interest – other persons/corporations		17,328	10,740	17,328	10,740
Proceeds from the sale of employee shares disposed of by the Company as agent		–	27,197	–	27,197
Total revenue from non-operating activities		17,328	37,937	17,328	37,937
Total revenue from ordinary activities		991,829	1,404,190	17,328	37,937
(b) Cost of sales					
Production		(301,907)	(354,225)	–	–
Royalty and excise		(162,406)	(224,538)	–	–
Transportation		(69,429)	(95,204)	–	–
Depreciation of production assets		(49,944)	(33,333)	–	–
Amortisation		(93,146)	(15,342)	–	–
Selling, general and administration		(307,514)	(357,260)	–	–
Total cost of sales		(984,346)	(1,079,902)	–	–

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

	Notes	Consolidated		Carnarvon Petroleum Ltd	
		2004 \$	2003 \$	2004 \$	2003 \$
2. PROFIT/(LOSS) FROM ORDINARY ACTIVITIES (continued)					
(c) Other expenses from ordinary activities					
Depreciation – plant & equipment		(7,849)	(11,528)	(7,849)	(11,528)
Rental premises – operating lease		(36,093)	(133,544)	(36,093)	(133,544)
Carrying value of employee loans for shares sold		–	(42,500)	–	(42,500)
Provision for non-recovery of employee share loans		(47,820)	(56,170)	(47,820)	(56,170)
Interest expense		(1,148)	–	(1,148)	–
Total other expenses from ordinary activities		(92,910)	(243,742)	(92,910)	(243,742)
(d) Other gains/(losses)					
Net loss on disposal of plant & equipment		(10,174)	–	(10,174)	–
Increment/(decrement) in value of investment		70,179	(70,179)	70,179	(70,179)
Unrealised foreign exchange gain/(loss) on:					
Translation of integrated subsidiary		23,412	(68,815)	–	–
Loan to subsidiary		–	–	25,154	(639,251)
Total other gain/(losses)		83,417	(138,994)	85,159	(709,430)
(e) Specific item					
Exploration, evaluation and development expenditure written-off		(117,159)	–	–	–

During the year the directors determined that estimated ultimate recoverable (EUR) barrels of oil in the fields in which production licences had been granted was a more appropriate basis to amortise carried forward exploration, evaluation and development expenditure, compared to EUR barrels of oil in the joint venture concession area. This resulted in a write-off of \$117,159 to reflect the adjustment to the carried forward expenditure balance as if this basis had been adopted in the prior year.

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

	Notes	Consolidated		Carnarvon Petroleum Ltd	
		2004 \$	2003 \$	2004 \$	2003 \$
3. INCOME TAX					
The prima facie income tax on operating loss differs from the income tax provided in the financial statements as follows:					
Prima facie income tax benefit on operating loss		425,113	452,451	386,489	709,487
Tax effect of permanent differences:					
Foreign sourced income/(loss)		(2,954)	85,905	–	–
Foreign sourced project costs		(1,550)	(5,603)	(1,550)	(5,603)
Exploration, evaluation & development expenditure written-off		(35,148)	–	–	–
Receipt from Gemini		–	(409,347)	–	(409,347)
Increment/(decrement) in value of investment		21,054	(21,054)	21,054	(21,054)
Non-deductible expenditure		(17,993)	(40,468)	(22,294)	(40,468)
Current year tax benefit not brought to account		(388,522)	(61,884)	(383,699)	(233,015)
Income tax benefit attributable to operating loss		–	–	–	–
Income tax losses					
Future income tax benefit arising from tax losses of a controlled entity not brought to account at balance date as realisation of the benefit is not regarded as virtually certain		1,795,424	1,406,902	1,961,327	1,577,628

This future income tax benefit will only be obtained if:

- future assessable income is derived of a nature and an amount sufficient to enable the benefit to be realised;
- the conditions for deductibility imposed by tax legislation continue to be complied with; and
- no changes in tax legislation adversely affect the consolidated entity in realising the benefit.

Tax Consolidation

As at the date of this report, the Carnarvon Petroleum Ltd Group has not yet decided whether and when it will be consolidating for tax purposes. However, as there are no provisions for deferred tax liabilities or future income tax benefits brought to account in this financial report, the decision about Tax Consolidation is not expected to have a material effect.

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

	Notes	Consolidated		Carnarvon Petroleum Ltd	
		2004 \$	2003 \$	2004 \$	2003 \$
4. RECEIVABLES					
CURRENT					
Trade debtors	4(a)	96,097	116,466	–	–
Other debtors		50,316	24,137	44,771	16,164
Receivable from SW1A joint venture		99,778	–	–	–
		246,191	140,603	44,771	16,164
NON-CURRENT					
Permit security deposits		1,490	50,565	1,490	50,565
Amounts receivable from controlled entities	4(a)	–	–	4,225,366	2,564,474
Provision for non-recovery	4(a)	–	–	(693,349)	(693,349)
		–	–	3,532,017	1,871,125
Employee share loans	17(a)	478,900	478,900	478,900	478,900
Provision for non-recovery	17(a)	(419,125)	(371,305)	(419,125)	(371,305)
		59,775	107,595	59,775	107,595
		61,265	158,160	3,593,282	2,029,285
(a) Terms and Conditions					
Terms and conditions relating to the above financial assets:					
(i) Trade debtors are generally settled in the month after invoicing.					
(ii) Details of the terms and conditions of related party receivables are set out in note 22.					
5. INVENTORIES					
CURRENT					
Production materials – at lower of cost and net realisable value		104,841	73,359	–	–
6. OTHER CURRENT ASSETS					
Prepayments and other current assets		76,225	68,806	6,200	7,000

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

	Notes	Consolidated		Carnarvon Petroleum Ltd	
		2004 \$	2003 \$	2004 \$	2003 \$
7. OTHER FINANCIAL ASSETS					
CURRENT					
Shares in AusAm Resources Limited – at cost	(i)	282,876	–	282,876	–
NON-CURRENT					
Shares in controlled entities – at cost	24	–	–	1,482,962	1,482,962
Shares in AusAm Resources Limited – at cost	(i)	–	282,876	–	282,876
Provision for diminution of investment		–	(70,179)	–	(70,179)
		–	212,697	1,482,962	1,695,659

(i) At 30 June 2004 AusAm Resources Limited was an unlisted public company in which Carnarvon Petroleum Limited held a 3.0% (2003: 6.7%) ownership interest. Its main activity is the exploration and development of oil and gas. Refer to note 26 – Subsequent Events and note 1(e) Accounting Policies.

8. JOINT VENTURES

The economic entity has the following interests in joint venture operations:

Joint Venture	Principal Activities	Ownership Interest %	Related Party %
Thailand			
SW1A Concession, Exploration Block L44/43	Exploration, development, production and marketing of crude oil	40%	–
Western Australia (Carnarvon Basin)			
EPs110 & 424	Exploration for hydrocarbons	35%	–
Papua New Guinea (Papuan Basin)			
PRLs 4 & 5 including the Stanley, Elevala and Ketu discoveries	Exploration for hydrocarbons	15%	–

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

	Notes	Consolidated		Carnarvon Petroleum Ltd	
		2004 \$	2003 \$	2004 \$	2003 \$
8. JOINT VENTURES (continued)					
Assets and liabilities relating to the joint ventures are included in the financial statements as follows:					
CURRENT ASSETS					
Cash assets		23,305	35,729	–	–
Receivables		101,642	124,440	–	–
Inventories		104,841	73,359	–	–
Prepayments and other		70,025	61,806	–	–
TOTAL CURRENT ASSETS		299,813	295,334	–	–
NON-CURRENT ASSETS					
Plant and equipment		184,099	150,556	–	–
Exploration, evaluation and development costs		5,722,278	4,387,531	–	–
TOTAL NON-CURRENT ASSETS		5,906,377	4,538,087	–	–
TOTAL ASSETS		6,206,190	3,833,421	–	–
CURRENT LIABILITIES					
Payables		79,952	92,635	–	–
TOTAL LIABILITIES		79,952	92,635	–	–
NET ASSETS		6,126,238	4,740,786	–	–
Capital expenditure commitments and contingent liabilities in respect of the joint venture are disclosed in Notes 16 and 18 respectively.					

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

9. PLANT AND EQUIPMENT

Plant and equipment at cost

Accumulated depreciation

Notes	Consolidated		Carnarvon Petroleum Ltd	
	2004 \$	2003 \$	2004 \$	2003 \$
	298,692	257,483	11,316	51,599
	(108,504)	(85,533)	(5,227)	(32,200)
9(a)	190,188	171,950	6,089	19,399

(a) Reconciliation

Reconciliation of the carrying amount of plant and equipment at the beginning and end of the current financial year

Plant and equipment

Carrying amount at beginning

Additions

Disposals

Depreciation expense

Carrying amount at end of financial year

Consolidated
2004

Consolidated
2003

171,950

86,206

(10,175)

(57,793)

190,188

90,007

126,804

–

(44,861)

171,950

10. DEFERRED EXPLORATION, EVALUATION AND DEVELOPMENT EXPENDITURE

Exploration, evaluation and development costs carried forward in respect of the SW1A Concession:

Production

Exploration & development phases

Less: accumulated amortisation

Consolidated

Carnarvon Petroleum Ltd

2004
\$

2003
\$

2004
\$

2003
\$

5,972,454

4,427,402

(250,176)

(39,871)

5,722,278

4,387,531

–

–

–

–

The ultimate recoupment of costs carried forward is dependent on the successful development and commercial exploitation or sale of the SW1A Concession.

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

	Notes	Consolidated		Carnarvon Petroleum Ltd	
		2004 \$	2003 \$	2004 \$	2003 \$
11. PAYABLES					
CURRENT					
Trade creditors	11(a)	59,642	25,865	–	–
Other creditors	11(a)	199,680	283,933	156,880	145,784
Payables to controlled entities		–	–	–	60,000
Cash calls payable to SW1A JV		–	60,000	–	–
		259,322	369,798	156,880	205,784
(a) Terms and Conditions					
Terms and conditions relating to the above financial liabilities:					
(i) Trade and other creditors are non-interest bearing and are normally settled on 30 day terms.					
12. PROVISIONS					
CURRENT					
Employee leave entitlements	17	880	25,812	880	25,812
13. CONTRIBUTED EQUITY					
(a) Issued and paid up capital					
Ordinary shares fully paid		45,318,074	42,124,094	45,318,074	42,124,094
(b) Movements in shares on issue					
		2004		2003	
		Number of Shares	\$	Number of Shares	\$
Beginning of the financial year		171,591,623	42,124,094	124,518,423	40,293,593
Issued during the year					
– public equity raising		100,720,890	3,426,736	47,073,200	1,977,075
less transaction costs		–	(232,756)	–	(146,574)
End of the financial year		272,312,513	45,318,074	171,591,623	42,124,094

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

13. CONTRIBUTED EQUITY (continued)

(c) Share options

During the financial year 37,492,101 options over ordinary shares were issued.

Unissued ordinary shares of the Company under option:

Expiry Date	Grant Date	Exercise Price	Number of Options \$	2004	2003
31 December 2005		22/03/2004	0.06	37,492,101	–
31 December 2003 (since expired)		07/12/2000	0.20	–	10,000,000

(d) Terms and conditions of contributed equity

Ordinary Shares

Ordinary shares have the right to receive dividends as declared and, in the event of a winding-up of the Company, to participate in the proceeds from the sale of all surplus assets in proportion to the number of, and amounts paid up on, shares held.

14. ACCUMULATED LOSSES

	Notes		Consolidated		Carnarvon Petroleum Ltd	
	2004 \$	2003 \$	2004 \$	2003 \$	2004 \$	2003 \$
Balance at the beginning of the year	(36,949,486)	(35,441,317)	(38,266,800)	(35,901,844)	(38,266,800)	(35,901,844)
Operating loss attributable to members of Carnarvon Petroleum Ltd	(1,417,044)	(1,508,169)	(1,288,298)	(2,364,956)	(1,288,298)	(2,364,956)
Balance at the end of the year	(38,366,530)	(36,949,486)	(39,555,098)	(38,266,800)	(39,555,098)	(38,266,800)

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

	Notes	Consolidated		Carnarvon Petroleum Ltd	
		2004 \$	2003 \$	2004 \$	2003 \$
15. STATEMENT OF CASH FLOWS					
(a) Reconciliation of the operating loss after tax to the net cash flows used in operations					
Loss from ordinary activities after tax		(1,417,044)	(1,508,169)	(1,288,298)	(2,364,956)
Provision for diminution – employee share loans		47,820	56,170	47,820	56,170
Write down of employee loans		–	15,303	–	15,303
Amortisation and write-off of deferred exploration, evaluation and development costs		210,305	15,342	–	–
Depreciation – plant & equipment		57,793	44,861	7,849	11,528
Net loss on disposal of plant & equipment		10,174	–	10,174	–
Unrealised foreign exchange (gain)/loss		(23,412)	68,815	(25,154)	639,251
(Increment)/decrement in value of investment		(70,179)	70,179	(70,179)	70,179
<i>Changes in assets and liabilities:</i>					
(Increase)/decrease in receivables		(56,513)	(47,831)	20,468	872
(Increase)/decrease in inventories		(31,482)	(7,801)	–	–
(Increase)/decrease in other current assets		(7,419)	(13,311)	800	7,931
Increase/(decrease) in payables		(110,476)	(88,963)	(48,904)	(14,862)
Increase/(decrease) in employee entitlements		(24,932)	20,798	(24,932)	20,798
Net cash flows used in operating activities		(1,415,365)	(1,374,607)	(1,370,356)	(1,557,786)
(b) Reconciliation of cash					
Cash balance comprises:					
Cash at bank and at call		527,882	357,112	504,556	321,383
Closing cash balance		527,882	357,112	504,556	321,383
(c) Financing facilities available					
At balance date the following financing facilities were available:					
Bank overdraft		30,000	30,000	30,000	30,000
Letter of credit		–	60,000	–	60,000
The bank overdraft facility is unused at balance date.					

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

	Notes	Consolidated		Carnarvon Petroleum Ltd	
		2004 \$	2003 \$	2004 \$	2003 \$
16. EXPENDITURE COMMITMENTS					
(a) Capital expenditure commitments					
Estimated capital expenditure contracted for at balance date, but not provided for, payable:					
Not later than one year					
Joint venture		-	-	-	-
(b) Lease expenditure commitments					
Operating lease (non cancellable)					
Not later than one year		9,450	33,600	9,450	33,600
Aggregate lease expenditure contracted for at balance date		9,450	33,600	9,450	33,600
Aggregate expenditure commitments comprise:					
Amounts not provided for at balance date					
Rental commitments		9,450	33,600	9,450	33,600

Operating lease refers to rental of office space which has a term of less than one year.

Due to the nature of the consolidated entity's operations in exploring and evaluating areas of interest, it is difficult to accurately forecast the nature or amount of future expenditure, although it will be necessary to incur expenditure in order to retain the entity's present permit interests. Expenditure commitments on exploration permits can be reduced by selective relinquishment of exploration tenure, by the renegotiation of expenditure commitments, or by farming out portions of the entity's equity. The Company forecasts its expenditure for exploration commitments for the year ending 30 June 2005 to be approximately \$100,000 (actual 2004: \$18,384).

17. EMPLOYEE ENTITLEMENTS

Aggregate employee entitlements, including on-costs

The aggregate employee entitlement liability comprises:

	Notes	2004 \$	2003 \$	2004 \$	2003 \$
Provisions (Current)	12	880	25,812	880	25,812

17. EMPLOYEE ENTITLEMENTS (continued)

(a) Employee share plan

At the Annual General Meeting held on 16 October 1997 the shareholders approved the Carnarvon Employee Share Plan and a loan arrangement scheme to assist in funding the acquisition of Plan Shares.

Under the terms of the Plan:

- (i) the Company may, in its absolute discretion, make an offer of ordinary fully paid shares in Carnarvon Petroleum Ltd to any eligible employee;
- (ii) an eligible employee is any person who is a director or employee of Carnarvon Petroleum Ltd or any of its subsidiaries;
- (iii) the issue price is determined by the directors and is not to be less than the weighted average market price of the Company's shares on the five trading days prior to the proposed date of offer;
- (iv) transfer of shares is limited within the first two years;
- (v) eligible employees receive an interest free advance to acquire the shares;
- (vi) the maximum liability of the advance is the market value of the shares from time to time;
- (vii) the carrying value of advances made to eligible employees is the lower of the equivalent market value of the shares from time to time or the price of the shares at the time the shares were issued to eligible employees;
- (viii) the eligible employee is the legal owner of the shares subject to the provisions of the loan agreement between the Company and the eligible employee;
- (ix) Australian Stock Exchange Listing Rules require the Company to obtain shareholder approval for the issue of shares to directors; and
- (x) the Company is empowered to sell, as agent, any shares held under the Plan by an eligible employee upon the cessation of his employment, and to apply the net sale proceeds in discharging the employee's loan from the Company.

At balance date there were 10 (2003: 10) eligible participant employees.

During the financial year, no (2003: nil) shares were issued under the Plan.

In respect to the eligible employee who ceased employment during the year, no (2003: Nil) shares were disposed of by the Company as agent. During the year, no amounts (2003: \$nil) were repaid under the loan arrangement scheme.

During the year the Company as agent did not sell any shares (2003: 500,000) on market for employees who ceased employment in previous years. In 2003 shares were disposed of on market for a consideration of \$27,197.

At balance date, there were 3,985,000 (2003: 3,985,000) shares on issue under the Plan, with a market value of \$59,775 (2003: \$107,595).

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

17. EMPLOYEE ENTITLEMENTS (continued)

(b) Superannuation Commitments

Employees make contributions to individual superannuation plans based on various percentages of their salary and wage. The consolidated entity has a legal obligation to contribute to the plans to the extent of the superannuation guarantee legislation and the specific terms of individual employment contracts.

	Notes	Consolidated	Carnarvon Petroleum Ltd		
		2004 \$	2003 \$	2004 \$	2003 \$
Employer contributions to the plans		46,127	55,917	46,127	55,917

18. CONTINGENT ASSETS AND CONTINGENT LIABILITIES

Controlled Entities

- (a) Carnarvon Petroleum Ltd has agreed not to recall the loans owing by its controlled entities where it would result in the controlled entity not being able to meet its debts and commitments as they fall due.
- (b) In accordance with normal petroleum industry practice, the consolidated entity has entered into joint ventures and farmin agreements with other parties for the purpose of exploring and developing its petroleum permit interests. If a party to a joint venture defaults and does not contribute its share of joint venture obligations, then the other joint venturers are liable to meet those obligations. In this event, the interest in the permit held by the defaulting party may be redistributed to the remaining joint venturers.
- (c) Securities have been placed in favour of the Independent State of Papua New Guinea in respect of the compliance with the conditions of Petroleum Prospecting Licences (PPL's) granted to the Company and its joint venturers, totalling \$1,490 (2003: \$31,490).
- (d) If a discovery is made within an Australian exploration permit in which a Native Title claim has been made and a production licence is sought in respect of that exploration permit, the issue of the production licence may be subject to the right to negotiate procedures set out in the Native Title Act. If no agreement is reached with the claimants, the National Native Title Tribunal will conduct a hearing to determine whether the licence can be granted, and if so on what conditions. A condition of the grant may be the payment of compensation.

19. SEGMENT INFORMATION

The consolidated entity operated predominantly in oil and gas exploration and development in Australia, Thailand and Papua New Guinea.

Segment accounting policies

Segment accounting policies are the same as the consolidated entity's policies as described in note 1. During the financial year, there were no changes in segment accounting policies that had a material effect on the segment information.

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

19. SEGMENT INFORMATION (continued)

Geographical Segments

	Australia		Thailand		Papua New Guinea		Consolidated	
	2004	2003	2004	2003	2004	2003	2004	2003
	\$	\$	\$	\$	\$	\$	\$	\$
Revenue								
Sales to customers outside the consolidated entity	–	–	974,501	1,366,253	–	–	974,501	1,366,253
Other revenue from outside the consolidated entity	17,328	37,937	–	–	–	–	17,328	37,937
Total segment revenue	17,328	37,937	974,501	1,366,253	–	–	991,829	1,404,190
Results								
Operating result	(1,290,040)	(1,692,372)	(9,845)	184,203	–	–	(1,299,885)	(1,508,169)
Specific item	–	–	(117,159)	–	–	–	(117,159)	–
Total segment result	(1,290,040)	(1,692,372)	(127,004)	184,203	–	–	(1,417,044)	(1,508,169)
Assets								
Exploration and development costs	–	–	5,722,278	4,327,531	–	–	5,722,278	4,327,531
Other	904,267	630,905	583,711	501,217	1,490	50,565	1,489,468	1,182,687
Total segment assets	904,267	630,905	6,305,989	4,828,748	1,490	50,565	7,211,746	5,510,218
Liabilities								
Total segment liabilities	157,760	171,596	102,442	164,014	–	–	260,202	335,610
Other segment information:								
Acquisition of property, plant and equipment and other non-current assets	4,713	17,831	81,493	108,973	–	–	86,206	126,804
Depreciation	7,849	11,528	49,944	33,333	–	–	57,793	44,861
Amortisation	–	–	210,305	15,342	–	–	210,305	15,342
Other non-cash expenses	47,820	126,349	–	–	–	–	47,820	126,349

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

20. DIRECTOR AND EXECUTIVE DISCLOSURES

Specified Directors

The following persons were directors of Carnarvon Petroleum Limited during the financial year:

A G Shelton – Chairman
 N C Fearis – Non-executive director
 D J Orth – Executive director and Chief Operating Officer
 K C Tregonning – Non-executive director

K C Tregonning retired from the position of Managing Director and Chief Executive Officer on 28 November 2003, and remained a non-executive director until his resignation from the Board on 5 January 2004.

Specified Executives

T S Irwin – Chief Financial Officer and Company Secretary (resigned 17 May 2004)
 R A Pullia – Chief Financial Officer and Company Secretary (appointed 17 May 2004)

Remuneration of Specified Directors and Specified Executives

The Remuneration and Nominations Committee advises the Board on remuneration policies and practices, evaluates the performance of senior management and makes recommendations to the Board on remuneration for senior managers. Remuneration is in the form of cash remuneration and superannuation contributions. The Board assesses the appropriateness of the nature and amount of remuneration on an annual basis by reference to industry and market conditions, and with regard to the Company's financial and operational performance. The Company paid no bonuses during the financial year ended 30 June 2004.

All specified directors and specified executives have the opportunity to qualify for participation in the Carnarvon Employee Share Plan. The issue of shares under this Plan is at the discretion of the Board. No equity-based remuneration was paid to specified directors or specified executives during the year.

The Company has an agreement with a controlled entity of DJ Orth for a term expiring on 31 March 2005, with a three month notice period. The Company has an employment agreement with RA Pullia for an unspecified term with a one month notice period. There are no formal retainer agreements with non-executive directors.

		Primary Salary & Fees	Post Employment Superannuation	Termination Benefits	Total
Specified Directors					
A G Shelton	2004	45,200	4,800	–	50,000
	2003	34,002	3,498	–	37,500
N C Fearis	2004	27,000	3,000	–	30,000
	2003	24,900	2,415	–	27,315
D J Orth	2004	160,750	25,000	–	185,750
	2003	117,096	24,997	–	142,093
Dr K C Tregonning	2004	50,000	11,557	80,839	142,396
	2003	200,004	25,007	–	225,011
Total remuneration	2004	282,950	44,357	80,839	408,146
	2003	376,002	55,917	–	431,919

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

20. DIRECTOR AND EXECUTIVE DISCLOSURES (continued)

		Primary Salary & Fees	Post Employment Superannuation	Total
Specified Executives				
R A Pullia	2004	16,450	1,481	17,931
	2003	–	–	–
T S Irwin	2004	178,959	9,645	188,604
	2003	–	–	–
Total remuneration	2004	195,409	11,126	206,535
	2003	206,000	19,263	225,263

*Total in respect of the financial year ended 2003 does not equal the sum of amounts disclosed for 2003 for individuals specified in 2004, as different individuals were specified in 2003.

Equity instrument disclosures relating to directors and executives

Shareholdings

	Balance at 1 July 2003	Granted as Remuneration	On exercise Of options	Net Change Other	Balance at 30 June 2004 (or when resigned)
Specified Directors					
A G Shelton	4,567,421	–	–	4,641,485	9,208,906
N C Fearis	1,771,400	–	–	2,100,000	3,871,400
D J Orth	2,858,067	–	–	(1,288,940)	1,569,127
Dr K C Tregonning	6,588,067	–	–	(200,000)	6,388,067
Total	15,784,955	–	–	5,252,545	21,037,500

Specified Executives

Nil

Option holdings

	Balance at 1 July 2003	Granted as Remuneration	Options Exercised	Net Change Other	Balance at 30 June 2004 (or when resigned)
Specified Directors					
A G Shelton	–	–	–	1,600,743	1,600,743
N C Fearis	–	–	–	300,000	300,000
D J Orth	5,000,000	–	–	(4,952,572)	47,428
Dr K C Tregonning	5,000,000	–	–	(5,000,000)	–
Total	10,000,000	–	–	(8,051,829)	1,948,171

Option holdings of specified directors at 30 June 2004 are not related to remuneration and have vested. The options are exercisable and were acquired pursuant to the February 2004 rights issue of ordinary shares. The options are listed on the ASX.

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

20. DIRECTOR AND EXECUTIVE DISCLOSURES (continued)

Specified Executives

Nil

All equity transactions with specified directors have been entered into under terms and conditions no more favourable than those the entity would have adopted if dealing at arm's length.

Other transactions with specified directors

Mr AG Shelton is a director of Andrew Shelton & Co Pty Ltd. That company provided financial consulting services to the consolidated entity in relation to various strategic and corporate finance matters concerning the Company and the SW1A Concession in Thailand. The total value of consulting fees paid during the year was \$117,000 (2003: \$42,000). Of this amount, \$42,000 related to services provided in the prior financial year for which invoices were not rendered until after completion of the Company's capital raisings in November 2003. Furthermore, \$66,000 of fees was satisfied by the issue of shares pursuant to the February 2004 rights issue.

Mr NC Fearis is a director of Pendomer Investments Pty Ltd. In previous years that company provided services to the consolidated entity in relation to general corporate matters. The total value of fees paid during the year ended 30 June 2004 was nil (2003: \$1,200).

Dr KC Tregonning is a director of Winlen Pty Ltd. That company provided a Melbourne based fully serviced office to the consolidated entity. The total value of licence fees paid was \$nil in 2004 (2003: \$79,700).

The terms and conditions of the above transactions were no more favourable to the counterparties than those available, or which might reasonably be expected to be available, in respect of similar transactions entered into with non-director related entities on an arm's length basis.

21. REMUNERATION OF AUDITORS

Amounts received or due and receivable by the auditors of Carnarvon Petroleum Ltd and the consolidated entity for an audit and review of the financial report of the Company and any other entity in the consolidated entity.

Other services in relation to the entity and any other entity in the consolidated entity.

Audit of overseas operations by an overseas office of the auditors of Carnarvon Petroleum Ltd.

Other services relate to taxation and other accounting assistance.

	Consolidated		Carnarvon Petroleum Ltd	
	2004 \$	2003 \$	2004 \$	2003 \$
Amounts received or due and receivable by the auditors of Carnarvon Petroleum Ltd and the consolidated entity for an audit and review of the financial report of the Company and any other entity in the consolidated entity.	66,120	41,500	66,120	41,500
Other services in relation to the entity and any other entity in the consolidated entity.	39,964	59,150	39,964	59,150
Audit of overseas operations by an overseas office of the auditors of Carnarvon Petroleum Ltd.	19,694	9,000	–	–
	125,778	109,650	106,084	100,650

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

22. RELATED PARTY DISCLOSURES

Ultimate parent

Carnarvon Petroleum Limited is the ultimate parent company.

Wholly owned group transactions

During the reporting period there have been transactions between the Company and its controlled entities. The Company provided accounting and administrative services to its controlled entities for which it did not charge a management fee.

The Company also provided interest-free funding for exploration and development expenditure to its controlled entities during the year amounting to \$1,635,738 (2003: \$1,913,920). The outstanding balance of loans made by Carnarvon Petroleum Ltd to its controlled entities at 30 June 2004 was \$4,225,366 (2003: \$2,564,474), of which \$693,349 (2003: \$693,349) has been provided for. These loans are unsecured and have no fixed terms of repayment.

23. FINANCIAL INSTRUMENTS

(a) Interest rate risk

The consolidated entity's exposure to interest rate risk is considered minimal and the effective interest rates of financial assets and liabilities at the reporting date are as follows:

	Floating interest rate \$	Non-interest bearing \$	Total carrying amount as per the statement of financial position \$	Weighted average effective interest rate \$
2004				
Financial assets				
Cash	527,822	–	527,822	4.8%
Receivables	–	307,456	307,456	
Investments – shares	–	282,876	282,876	
Total financial assets	527,822	590,332	1,118,154	
Financial Liabilities				
Trade and other creditors	–	259,322	259,322	
Total financial liabilities	–	259,322	259,322	
2003				
Financial assets				
Cash	357,112	–	357,112	4.5%
Receivables	–	298,763	298,763	
Investments – shares	–	212,697	212,697	
Total financial assets	357,112	511,460	868,572	
Financial Liabilities				
Trade and other creditors	–	309,798	309,798	
Cash calls payable	–	60,000	60,000	
Total financial liabilities	–	369,798	369,798	

NOTES TO THE FINANCIAL STATEMENTS

AS AT 30 JUNE 2004

23. FINANCIAL INSTRUMENTS (continued)

(b) Net fair values

All financial assets and financial liabilities have been recognised in the statement of financial position at balance date at their net fair values. The following methods and assumptions are used to determine the net fair values of financial assets and liabilities.

Cash and investments: The carrying amount approximates fair value because of their short term to maturity.

Receivables and trade and other creditors: The carrying amount approximates fair value.

(c) Credit risk exposures

The consolidated entity's maximum exposures to credit risk at reporting date in relation to each class of recognised financial assets, is the carrying amount of those assets as indicated in the statement of financial position.

Concentrations of credit risk

The consolidated entity considers its exposure to credit risk as minimal. Amounts receivable by the Company relate to either:

- (i) costs charged to related entities for which the Company awaits reimbursement; or
- (ii) amounts advanced to employees, which are repayable under the terms of the Carnarvon Employee Share Plan, which requires repayment on sale of the shares.

24. CONTROLLED ENTITIES AND CONTRIBUTION TO CONSOLIDATED ENTITY PROFIT/(LOSS)

Name	Country of Incorporation	% held by parent entity		Book value of shares held		Contribution to consolidated entity profit/(loss)	
		2004	2003	2004	2003	2004	2003
				\$	\$	\$	\$
Carnarvon Petroleum Ltd						(1,290,040)	(1,692,372)
Controlled entities of Carnarvon Petroleum:							
Lassoc Pty Ltd	Australia	100	100	20	20	–	–
SLR Exploration Pty Ltd	Australia	100	100	10	10	–	–
Strategic Exploration (Asia) Limited	British Virgin Islands	100	100	1,482,932	1,482,932	(127,004)	184,204
				<u>1,482,962</u>	<u>1,482,962</u>	<u>(1,417,044)</u>	<u>(1,508,168)</u>

25. EARNINGS PER SHARE

	2004	2003
(a) Basic earnings per share (cents per share)	(0.6)	(0.9)
(b) Diluted earnings per share (cents per share)	(0.6)	(0.9)
(c) Weighted average number of ordinary shares on issue used in the calculation of earnings per share	215,422,141	162,305,169
(d) Earnings used in calculating basic and diluted earnings per share	\$(1,417,044)	\$(1,508,169)

All potential ordinary shares, being options to acquire ordinary shares are not considered dilutive as the exercise of the options would not decrease the basic loss per share.

26. SUBSEQUENT EVENTS

During the June 2004 quarter, shareholders of AusAm Resources Limited voted to approve a Scheme of Arrangement whereby shareholders of that company would exchange every five shares held for one share in Northlinks Ltd, a Canadian company listed on the TSX Venture Exchange and subsequently renamed Ausam Energy Corporation ("Ausam Energy"). The issue price of each Ausam Energy share is C\$0.75. Existing shareholders of Ausam Energy also approved the Scheme. In August 2004, Ausam Energy announced that it had completed the acquisition of AusAm Resources Limited. Ausam Energy raised C\$5.2 million in new capital at a price of C\$0.75 and recommenced trading on the TSX Venture Exchange on 15 September 2004. The investment in AusAm Resources Limited is disclosed in Note 7.

On 29 September 2004 the consolidated entity announced that it had issued proceedings in Alberta, Canada seeking orders directing Pacific Tiger (Energy) Thailand Limited and Pacific Tiger Energy Inc. to comply with provisions of the Farmin Agreement and Joint Operating Agreement. These two agreements govern relations between the partners in the Wichian Buri SW1A joint venture in Thailand. The Company has taken this action because of its concerns relating to the extent of funding of the joint venture by Pacific Tiger, the failure of Pacific Tiger to remit to Carnarvon its share of joint venture revenue for June and July, and failure to provide financial and operational information. The court has set a date of 24 November 2004 for a hearing of Carnarvon's claims in relation to the Joint Operating Agreement.

27. IMPACT OF ADOPTING AASB EQUIVALENTS TO IASB STANDARDS

Carnarvon Petroleum has commenced transitioning its accounting policies and financial reporting from current Australian Standards to Australian equivalents of International Financial Reporting Standards (IFRS). The company has allocated internal resources to perform diagnostic and conduct impact assessments to isolate key areas that will be impacted by the transition to IFRS. As the company has a 30 June year end, priority has been given to considering the preparation of an opening balance sheet as at 1 July 2004 in accordance with AASB equivalents to IFRS. This will form the basis of accounting for Australian equivalents of IFRS in the future, and is required when the company prepares its first fully IFRS compliant financial report for the year ended 30 June 2006. Set out below are the key areas where accounting policies will change and may have an impact on the financial report of the company. At this stage the company has not been able to reliably quantify the impacts on the financial report as a result of the adoption of IFRS.

Impairment of Assets

Under AASB 136 Impairment of Assets, the recoverable amount of an asset is determined as the higher of fair value less costs to sell and value in use which is required to be determined using a pre-tax discount rate which is assets specific. Additionally, AASB 136 requires entities to look at impairment indicators to determine if assets are required to be impairment tested. This will result in a change in the group's current accounting policy. Under the new policy it is likely that impairment of assets will be recognised sooner and that the amount of write-downs will be greater.

Extractive Industries Standard – Exploration and Development Costs

Australian Generally Accepted Accounting Principles ("AGAAP") currently has a specific accounting standard on extractive industries, which includes the appropriate accounting treatment for exploration and development expenditure. At this stage an equivalent Australian IFRS standard is not expected until late in 2004. Accordingly, it is too early to comment on the differences, if any, between this standard and existing AGAAP. The International Accounting Standards Board ("IASB") has announced its intention to grandfather national GAAP, such as Australia's existing area of interest method of accounting for exploration costs, for both producers and explorers, until such time as the IASB produces a comprehensive extractive industry IFRS. However, final detail of the IASB's proposed grandfathering has not yet been released. As soon as the IASB has incorporated this decision into its Standards the AASB will produce an Australian equivalent so as to allow extractive industry companies to take advantage of the grandfathering in their 2005 transition to IFRS.

Income Taxes

Under AASB 112 Income Taxes, the company will be required to use a balance sheet liability method which focuses on the tax effects of transactions and other events that affect amounts recognised in either the Statement of Financial Position or a tax-based balance sheet. It is not expected that there will be a material impact as a result of adoption of this standard.

Functional Currency

Under AASB 121 The Effects of Changes in Foreign Exchange Rates, each entity in the reporting entity is required to determine its functional currency and measure its results and financial position in that currency. Furthermore, the results and financial position of each individual entity included in the reporting entity are to be translated into the currency in which the reporting entity presents its financial statements. This may result in a change in the group's current accounting policy where a controlled entity currently measures its results and financial position in US\$. At this point, the directors have not assessed and determined the functional currencies of each entity in the reporting entity, however, it is not expected that there will be a material impact as a result of adoption of this standard.

DIRECTORS' DECLARATION

AS AT 30 JUNE 2004

DIRECTORS' DECLARATION

In accordance with a resolution of the directors of Carnarvon Petroleum Ltd, we state that:

In the opinion of the directors:

- (a) the financial statements and notes of the company and of the consolidated entity are in accordance with the Corporations Act 2001, including:
 - (i) giving a true and fair view of the company's and consolidated entity's financial position as at 30 June 2004 and of their performance for the year ended on that date; and
 - (ii) complying with Accounting Standards and Corporations Regulations 2001; and
- (b) there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.

On behalf of the Board



AG Shelton
Director

Melbourne, 29 September 2004

INDEPENDENT AUDIT REPORT

TO THE MEMBERS OF CARNARVON PETROLEUM LIMITED

INDEPENDENT AUDIT REPORT

SCOPE

The financial report and directors' responsibility

The financial report comprises the statement of financial position, statement of financial performance, statement of cash flows, accompanying notes to the financial statements, and the directors' declaration for Carnarvon Petroleum Limited (the company) and the consolidated entity, for the year ended 30 June 2004. The consolidated entity comprises both the company and the entities it controlled during that year.

The directors of the company are responsible for preparing a financial report that gives a true and fair view of the financial position and performance of the company and the consolidated entity, and that complies with Accounting Standards in Australia, in accordance with 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.

Audit approach

We conducted an independent audit of the financial report in order to express an opinion on it to the members of the company. Our audit was conducted in accordance with Australian Auditing Standards, in order to provide reasonable assurance as to whether the financial report is free of material misstatement. The nature of an audit is influenced by factors such as the use of professional judgement, selective testing, the inherent limitations of internal control, and the availability of persuasive rather than conclusive evidence. Therefore, an audit cannot guarantee that all material misstatements have been detected.

We performed procedures to assess whether in all material respects the financial report presents fairly, in accordance with the Corporations Act 2001, including compliance with Accounting Standards in Australia, and other mandatory financial reporting requirements in Australia, a view which is consistent with our understanding of the company's and the consolidated entity's financial position, and of their performance as represented by the results of their operations and cash flows.

We formed our audit opinion on the basis of these procedures, which included:

- examining, on a test basis, information to provide evidence supporting the amounts and disclosures in the financial report, and
- assessing the appropriateness of the accounting policies and disclosures used and the reasonableness of significant accounting estimates made by the directors.

While we considered the effectiveness of management's internal controls over financial reporting when determining the nature and extent of our procedures, our audit was not designed to provide assurance on internal controls.

We performed procedures to assess whether the substance of business transactions was accurately reflected in the financial report. These and our other procedures did not include consideration or judgement of the appropriateness or reasonableness of the business plans or strategies adopted by the directors and management of the company.

Independence

We are independent of the company, and have met the independence requirements of Australian professional ethical pronouncements and the *Corporations Act 2001*. In addition to our audit of the financial report, we were engaged to undertake the services disclosed in the notes to the financial statements. The provision of these services has not impaired our independence.

INDEPENDENT AUDIT REPORT

TO THE MEMBERS OF CARNARVON PETROLEUM LIMITED

INDEPENDENT AUDIT REPORT

Audit opinion

In our opinion, the financial report of Carnarvon Petroleum Limited is in accordance with:

- (a) the *Corporations Act 2001*, including:
 - (i) giving a true and fair view of the financial position of Carnarvon Petroleum Limited and the consolidated entity at 30 June 2004 and of their performance for the year ended on that date; and
 - (ii) complying with Accounting Standards in Australia and the *Corporations Regulations 2001*; and
- (b) other mandatory financial reporting requirements in Australia.

Inherent uncertainty regarding going concern

Without qualification to the opinion expressed above, attention is drawn to the following matter. As a result of the matters described in Note 1 of the financial report relating to going concern, there is significant uncertainty whether Carnarvon Petroleum Limited and the consolidated entity will be able to continue as a going concern without obtaining further funds to continue its exploration and development activities and therefore whether it will be able to pay its debts as and when they fall due and realise its assets and extinguish its liabilities in the normal course of business at the amounts stated in the financial report. The financial report does not include any adjustments relating to the recoverability and classification of recorded asset amounts or to the amounts and classification of liabilities that might be necessary should the entity not continue as a going concern.



Ernst & Young



R C Piltz

Partner

Melbourne

29 September 2004

SHAREHOLDING INFORMATION

Additional information required by the Australian Stock Exchange Limited and not shown elsewhere in this report is as follows. The information is current as at 27th September 2004.

Distribution of equity securities

Size of Holdings	Number of Shareholders	Number of Option Holders
1 – 1,000	1,834	331
1001 – 5,000	1,307	140
5,001 – 10,000	414	71
10,001 – 100,000	987	102
100,000 – and over	456	68
Total Number of Holders	4,998	712

The number of shareholders holding less than a marketable parcel was 3,886.

Voting rights

Votes of shareholders are governed by Rules 32 and 33 of the Company's Constitution. In broad summary, but without prejudice to the provision of these rules, on a show of hands every shareholder present in person shall have one vote and upon a poll every shareholder present in person or by proxy or attorney shall have one vote for every share held.

Twenty largest holders of securities

Carnarvon Petroleum's Top Twenty Shareholders

Listed ordinary shares

	No. of Shares	% of Shares
Hamilton Capital Partners Limited	11,168,596	4.10
Arne Investments Pty Ltd	9,208,906	3.38
Merrill Lynch (Australia) Nominees Pty Ltd	6,289,905	2.31
ANZ Nominees Limited	5,967,217	2.19
Oasis International Trading LLC	5,333,205	1.96
National Nominees Limited	5,095,585	1.87
Citicorp Nominees Pty Limited	4,203,500	1.54
Westpac Custodian Nominees Pty Ltd	3,977,220	1.46
Pendomer Investments Pty Ltd	3,600,000	1.32
Jeffrey Frank Fradd	3,190,000	1.17
Dalkeith Resources Pty Ltd	2,741,633	1.01
Tregoning Trailers Distributors Pty Ltd	2,700,000	0.99
Alakor Corporation Inc	2,487,703	0.91
James Daniel Cooper Blore & Marie Jean Blore	2,440,000	0.90
John Bernard Porteous	2,233,800	0.82
William Douglas Goodfellow	2,171,680	0.80
Doral Mineral Industries Ltd	2,049,282	0.75
Malcolm Thom	2,000,000	0.73
Commodity Traders (NZ) Limited	1,954,500	0.72
John Meek Pty Ltd	1,850,000	0.68
Total	80,662,732	29.61

SHAREHOLDING INFORMATION

Twenty largest holders of securities (continued)

Carnarvon Petroleum's Top Twenty Option Holders

Listed options expiring 31/12/05
exercisable at 6 cents

	No. of options	% of options
Wilabenson Pty Ltd	2,711,876	7.23
De Min Zhang	2,000,000	5.33
Gregory Michael Josephson & Mary Margaret Josephson	1,842,879	4.92
Yue Li	1,661,161	4.43
Arne Investments Pty Ltd	1,600,743	4.27
Dalkeith Resources Pty Ltd	1,515,152	4.04
Julal Pty Limited	1,253,000	3.34
Goffacan Pty Ltd	1,200,000	3.20
Catherine Baker	1,150,000	3.07
Thorpe Road Nominees Pty Ltd	1,000,000	2.67
Paxevanos Investments Pty Ltd	750,000	2.00
Portfolio Investments International Pty Ltd	750,000	2.00
Jin Xiang Hanpo	660,000	1.76
Bellset Nominees Pty Ltd	600,000	1.60
John Arharidispo	531,543	1.42
Naomi Barbaro	500,000	1.33
Martin Brennan	500,000	1.33
Darlo Pty Ltd	500,000	1.33
Melissa Ann Josephson	500,000	1.33
Lawrence Crowe Consulting Pty Ltd	500,000	1.33
Total	21,726,354	57.93

Share Registry

Shareholders and option holders with queries relating to their security holdings should contact the Company's Share Registry in Melbourne:

by telephone **1300 850 505** or **+61 3 9415 5000**

by facsimile **+61 3 9473 2500**.

Alternatively, security holders may prefer to write to:

Carnarvon Petroleum Share Registry
C/- Computershare Investor Services Pty Limited
Yarra Falls
452 Johnston Street
Abbotsford Victoria 3067
Australia

Details of individual security holdings can be checked conveniently and simply by visiting our Registrar's website at www.computershare.com/au/investors and clicking on the Investor Centre button. For security reasons, you will need to key in your Security Reference Number (SRN) or Holder Identification Number (HIN), your family name and postcode to enable access to personal information.

Change of Address

Issuer sponsored shareholders should notify the Share Registry immediately, in writing, signed by the shareholder/s, of any change to their registered address. For added security, shareholders should quote their previous address and HIN or SRN. CHESS uncertificated shareholders should advise their sponsoring broker or non-broker participant.

Change of Name

Shareholders who change their name should notify the Share Registry, in writing, and attach a certified copy of relevant marriage certificate or deed poll, and include their HIN or SRN.

Lost Holding Statements

Shareholders should inform the Share Registry immediately, in writing, so that a replacement statement can be arranged.

Annual General Meeting

The 2004 Annual General Meeting will be held at 10.00am on Tuesday, 30 November 2004 at the Stamford Plaza Melbourne, No. 7 Alfred Place (off Collins Street), Melbourne, Australia.

Stock Exchange Listing

Securities of Carnarvon Petroleum Limited are listed on the Australian Stock Exchange (ASX).

ASX Codes: CVN - ordinary shares
CVNO - options expiring 31/12/05
exercisable at 6 cents

Publications

The Company's full year annual report is the main source of information for investors and is mailed to shareholders in October. Other sources of information are:

1. The Chairman's address to the Annual General Meeting, which will be available on the Company's website.
2. The half year financial report reviewing the July to December half year, which will be available on the Company's website in March.

Website

Our internet website www.carnarvonpetroleum.com is an important means of keeping investors continuously informed about the Company, including announcements to the ASX. The site also offers investors copies of news releases, financial presentations, half yearly and annual reports to shareholders.

Removal from Mailing List

Shareholders who do not wish to receive the full year annual report should advise the Share Registry, in writing, and include their HIN or SRN.