Falcon Oil & Gas Ltd.

Form 51-102F1
Management's Discussion & Analysis
For the Year Ended 31 December 2014

(Presented in U.S. Dollars)

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INTRODUCTION

The following management's discussion and analysis (the "**MD&A**") was prepared as at 28 April 2015 and is management's assessment of Falcon Oil & Gas Ltd.'s ("**Falcon**") financial and operating results and provides a summary of the financial information of the Company (as hereinafter defined) for the three months and year ended 31 December 2014. This MD&A should be read in conjunction with the audited consolidated financial statements for the year ended 31 December 2014 and 2013.

The information provided herein in respect of Falcon includes information in respect of its wholly-owned subsidiaries: Mako Energy Corporation, a Delaware company ("**Mako**"); TXM Oil and Gas Exploration Kft., a Hungarian limited liability company ("**TXM**"); TXM Marketing Trading & Service Kft., a Hungarian limited liability company ("**TXM Marketing**"); Falcon Oil & Gas Ireland Ltd., an Irish limited liability company ("**Falcon Ireland**"); Falcon Oil & Gas Holdings Ireland Ltd., an Irish limited liability company ("**Falcon Holdings Ireland**"); Falcon Oil & Gas USA Inc., a Colorado company ("**Falcon USA**"); Falcon Exploration and Production South Africa (Pty) Ltd., a South African limited liability company ("**Falcon South Africa**") and its 98.1% majority owned subsidiary, Falcon Oil & Gas Australia Limited, an Australian limited liability company ("**Falcon Australia**") (collectively, the "**Company**" or the "**Group**").

Additional information related to the Company, including the Company's Annual Information Form ("**AIF**") for the year ended 31 December 2014 dated 28 April 2015 can be found on the System for Electronic Document Analysis and Retrieval ("**SEDAR**") at www.sedar.com and Falcon's website at www.falconoilandgas.com.

Forward-looking statements

Forward-looking statements include, but are not limited to, statements with respect to: the focus of capital expenditures; Falcon's acquisition strategy; the criteria to be considered in connection therewith and the benefits to be derived therefrom; Falcon's goal to sustain or grow production and reserves through prudent management and acquisitions; the emergence of accretive growth opportunities; Falcon's ability to benefit from the combination of growth opportunities and the ability to grow through the capital markets; development costs and the source of funding thereof; the quantity of petroleum and natural gas resources or reserves; treatment under governmental regulatory regimes and tax laws; liquidity and financial capital; the impact of potential acquisitions and the timing for achieving such impact; expectations regarding the ability to raise capital and continually add to reserves through acquisition and development; the performance characteristics of Falcon's petroleum and natural gas properties; realisation of the anticipated benefits of acquisitions and dispositions; Falcon's ability to establish a broad institutional shareholder base in London, Dublin and Toronto and increase the volume of trading in common shares; expectations regarding the ability of Falcon to access additional sources of funding not currently available; and Falcon's ability to leverage its experience in the unconventional oil and gas industry to acquire interests in licenses.

Some of the risks and other factors, which could cause results to differ materially from those expressed in the forward-looking statements include, but are not limited to: general economic conditions in Canada, the Republic of Hungary, the Commonwealth of Australia, the Republic of South Africa and globally; supply and demand for petroleum and natural gas; industry conditions, including fluctuations in the price of petroleum and natural gas; governmental regulation of the petroleum and natural gas industry, including income tax, environmental and regulatory matters; fluctuation in foreign exchange or interest rates; risks and liabilities inherent in petroleum and natural gas operations, including exploration, development, exploitation, marketing and transportation risks; geological, technical, drilling and processing problems; unanticipated operating events which can reduce production or cause production to be shut-in or delayed; the ability of our industry partners to pay their proportionate share of joint interest billings; failure to obtain industry partner and other third party consents and approvals, when required; stock market volatility and market valuations; competition for, among other things, capital, acquisition of reserves, processing and transportation capacity, undeveloped land and skilled personnel; the need to obtain required approvals from regulatory authorities; and the other factors considered under "**Risk Factors**" in Falcon's AIF dated 28 April 2015. The forward-looking statements contained in this document are expressly qualified by this cautionary statement. Falcon disclaims any intention or obligation to update or revise any forward-looking statements whether as a result of new information, future events or otherwise, except as required under applicable securities regulation.

In addition, other factors not currently viewed as material could cause actual results to differ materially from those described in the forward-looking statements.

The following table outlines certain forward looking statements contained in this MD&A and provides material assumptions used to develop such forward looking statements and material risk factors that could cause actual results to differ materially from the forward looking statements.

Page No.	Forward looking statements	Assumptions	Risk factors
7	*Overview of the business and overall performance - About the Group* "Falcon's strategy is to leverage the Group's expertise in the unconventional oil and gas industry to acquire interests in licences covering large acreages of land and to build on its internationally diversified portfolio of unconventional assets and interests, which are located in countries that the Board of Directors of Falcon (the "**Board**") believes support the exploitation of unconventional oil and gas.	The countries in which the Group operates support the exploitation of unconventional oil and gas.	The countries in which the Group operates may change their regulatory environment which might adversely impact the exploitation of unconventional oil and gas resources.
8	*Overview of the business and overall performance – Beetaloo Basin, Northern Territory, Australia* "The area is remote and sparsely populated and the Board believes that it is well suited for oil and gas projects."	The area is well suited for oil and gas projects.	As the Beetaloo Basin is relatively under-explored it may not have shale oil, shale gas and BCGA potential.
9	*Beetaloo basin, Northern Territory, Australia – overview – Discoveries and prospectivity* "The Board believes that the Beetaloo Basin is relatively under-explored and has shale oil, shale gas and basin centered gas accumulations ("**BCGA**") potential."	The Board believes that the Beetaloo Basin is relatively under-explored and has shale oil, shale gas and BCGA potential.	As the Beetaloo Basin is relatively under-explored it may not have shale oil, shale gas and BCGA potential.
9-10	*Beetaloo basin, Northern Territory, Australia – overview – current activity - Transformational Farm out of Beetaloo unconventional acreage* This section in the document from "On 21 August 2014……..dry season ends in 2015." contains forward-looking statements pertaining to the intended work programme, near term expectations and bringing the project toward commerciality.	The work programme will occur as expected and the project will be brought towards commerciality.	The risks are (1) the work programme does not proceed as planned and /or (2) the project is not brought to commerciality.
11	*Karoo basin, South Africa - Overview* "In addition, the South African Department of Mineral Resources ("DMR") informed members of South Africa's parliament in October 2014 that the government was soon expected to issue companies with licences to explore for shale gas."	The awarding of the exploration right over the acreage will occur in 2015.	The finalisation of legislation and regulation in South Africa may be delayed or Falcon may not be awarded the licence.
11	*Karoo basin, South Africa - Overview* "The Board now expects that the exploration right over the acreage will be awarded in 2015."	The awarding of the exploration right over the acreage will occur in 2015.	The finalisation of legislation and regulation in South Africa may be delayed or Falcon may not be awarded the licence.
12	*Makó Trough, Hungary - The Deep Makó Trough* *In the MD&A for the 3 months ended 30 September 2014 the Group had indicated that it intended to re-enter the untested wells and will seek a technically and financially capable partner to test and produce the shale gas and tight gas formations in the Deep Makó Trough. Currently the Group is reviewing its operations and plans in Hungary.*	*This is a factual statement in highlighting a forward looking statement difference between the current MD&A and MD&A of 30 September 2014. No assumptions have been made with regards this statement.*	*This is a factual statement in highlighting a forward looking statement difference between the current MD&A and MD&A of 30 September 2014.*

Page No.	Forward looking statements	Assumptions	Risk factors
13	*Makó Trough, Hungary – Current Activity* "Falcon is currently evaluating, and will pursue, all options available to the Company to derive shareholder value as NIS has not fulfilled its commitments under the Agreement."	The Group assumes it will derive shareholder value.	The Group may not succeed in deriving shareholder value.
14	*Alberta, Canada* "Falcon does not anticipate any further exploration or development of these wells and no further material revenue is expected to be generated or material costs incurred."	The Group does not intend to do any further exploration or development of these wells.	The Group may be called upon to increase its cash commitment to these wells, given its interest.
25	*Liquidity & Capital resources – Going concern* "….has a reasonable expectation that the Group will have adequate resources to continue in operational existence for the foreseeable future."	The Group is a going concern.	Due to unforeseen expenditures, the Group may not have available cash to meet its liabilities as they fall due in the foreseeable future.
25	*Liquidity and capital resources – capital expenditures – Australia – Beetaloo Basin, Northern Territory, Australia* "The Group is planning a 9 well drilling programme with its farm-out partners. ……. to be undertaken in 2018."	The work programme will occur as expected and the project will be brought towards commerciality.	The risks are (1) the work programme does not proceed as planned and /or (2) the project is not brought to commerciality.
26	*Liquidity & Capital resources – capital expenditures - Hungary - Makó Trough, Hungary* "The Group is not planning any independent technical operations in Hungary, and as such no material capital expenditures are expected."	The Group is not planning any independent technical operations in Hungary.	Unforeseen circumstances might require the Group to conduct independent technical operations in Hungary and incur material expense.
26	*Debt and Equity Capital* "The availability of debt and equity capital, and the price at which additional capital could be issued will be dependent upon the success of the Group's exploration activities, and upon the state of the capital markets generally."	The Group will have continued access to raising funds in the capital markets.	The Group will have limited or no access to raising funds in the capital markets.
27	*Legal matters* "The Company may, from time to time, be involved in various claims, lawsuits, disputes with third parties, or breach of contract incidental to the operations of its business. The Company is not currently involved in any claims, disputes, litigation or other actions with third parties which it believes could have a material adverse effect on its financial condition or results of operations."	The Company is not currently involved in any claims, disputes, litigation or other actions with third parties which it believes could have a material adverse effect on its financial condition or results of operations.	The Company becomes involved in claims, disputes, litigation or other actions with third parties which could have a material adverse effect on its financial condition or results of operations.
29-31	*Critical Accounting Estimates – Critical judgements- Exploration and evaluation assets – Australia* "On 21 August 2014, Falcon Australia completed its farm-out agreement and joint operating agreement……….The work programme supports the carry value of the asset and there are no indicators or impairment."	The work programme will occur as expected and the project will be brought towards commerciality.	The risks are (1) the work programme does not proceed as planned and /or (2) the project is not brought to commerciality.

Dollar amounts

All dollar amounts in this document are in United States dollars **"$"**, except as otherwise indicated. "**CDN$**" where referenced represents Canadian Dollars; "**£**" where referenced represents British Pounds Sterling, "**HUF**" where referenced represents Hungarian Forints and "**A$**" where referenced represents Australian Dollars.

The financial information provided herein has been prepared in accordance with International Financial Reporting Standards ("**IFRS**").

OVERVIEW OF BUSINESS AND OVERALL PERFORMANCE

About the Group

Falcon is an international oil and gas company engaged in the acquisition, exploration and development of unconventional and conventional oil and gas assets. The Company's interests are located in internationally diversified countries that are characterised by a high regional demand for energy and are close to existing infrastructure allowing for rapid delivery of oil and gas to market.

Falcon's strategy is to leverage the Group's expertise in the unconventional oil and gas industry to acquire interests in licences covering large acreages of land and to build on its internationally diversified portfolio of unconventional assets and interests, which are located in countries that the Board of Directors of Falcon (the "**Board**") believes support the exploitation of unconventional oil and gas. Falcon seeks to add value to its assets by entering into farm-out arrangements with major oil and gas companies that will fully or partially carry Falcon through seismic and drilling work programmes. The Group's principal interests are located in two major underexplored basins in Australia and South Africa; and in Hungary, covering approximately 12.3 million gross acres in total.

Falcon is incorporated in British Columbia, Canada and headquartered in Dublin, Ireland with a technical team based in Budapest, Hungary. Falcon's Common Shares are traded on Toronto's TSX Venture Exchange ("**TSX-V**") (symbol: FO.V); AIM, a market operated by the London Stock Exchange (symbol: FOG) and ESM, a market regulated by the Irish Stock Exchange (symbol: FAC).

Summary of Operations

The following table summarises the principal oil and gas interests of the Company in Australia, South Africa and Hungary:

Assets (Country)	**Interest (%)**	**Operator**	**Status**	**Gross Area (km^2)**
Exploration Permit EP-76 (Beetaloo Basin, Northern Territory, Australia)	30[(i)]	Origin [(iii)]	Exploration	1,891.3
Exploration Permit EP-98 (Beetaloo Basin, Northern Territory, Australia)	30[(i)]	Origin [(iii)]	Exploration	10,316.0
Exploration Permit EP-117 (Beetaloo Basin, Northern Territory, Australia)	30[(i)]	Origin [(iii)]	Exploration	6,412.0
Technical Cooperation Permit, (Karoo Basin, South Africa) [(ii)]	100	Falcon	TCP	30,327.9
Makó Production Licence (Makó Trough, Hungary)	100	TXM	Production	994.6

Notes:
(i) Falcon owns 98.1% of Falcon Australia, which holds a 30% interest in the Beetaloo Exploration Permits. The remaining 1.9% interest of Falcon Australia is held by others.

(ii) In compliance with the terms of the Technical Cooperation Permit ("**TCP**"), the Company submitted its application for an exploration permit in August 2010 prior to the moratorium being introduced in April 2011. Local counsel has confirmed that despite the TCP expiry date of October 2010 having passed, the Company's interests remain valid and enforceable.

(iii) Falcon completed its Farm-out with Origin Energy Resources Limited, a subsidiary of Origin Energy Limited ("**Origin**") and Sasol Petroleum Australia Limited, a subsidiary of Sasol Limited ("**Sasol**"), collectively referred to herein as (the **"Farminees**") on 21 August 2014. On completion, Origin was appointed as operator of the exploration permits.

<u>Beetaloo Basin, Northern Territory, Australia</u>

Overview
Falcon Australia is one of the three registered holders of approximately 4.6 million gross acres (approximately 18,619 km^2), 1.4 million net acres, of three exploration permits in the Beetaloo Basin, Northern Territory, Australia. The Beetaloo Basin is located 600 kilometres south of Darwin close to infrastructure including a highway, two pipelines and a railway, offering transport options to the Australian market and beyond via the existing and proposed liquified natural gas ("**LNG**") capacity in Darwin.

The Beetaloo Basin is a Proterozoic and Cambrian tight oil and gas basin. In its entirety, the Beetaloo Basin covers approximately 8.7 million acres (approximately 35,260 km^2) and is a relatively underexplored onshore exploration basin with, as far as the Company is aware, 11 exploration wells drilled in the Beetaloo Basin to date. The area is remote and sparsely populated and the Board believes that it is well suited for oil and gas projects. Australia has a developed resources industry with a stable political, legal and regulatory system.

Exploration Permits
A summary of Falcon Australia's Beetaloo Exploration Permits is contained in the table on the previous page.

Three of Falcon Australia's then four Beetaloo Permits (EP-76, EP-98 and EP-117) were due for renewal at 31 December 2013. As part of the renewal process, Falcon agreed to relinquish approximately 26% of the three permits which were not considered to be core to the unconventional play in the Beetaloo Basin by Falcon, Origin and Sasol. The renewal of the three Permits was completed on 30 April 2014. Falcon Australia's fourth permit, EP-99, which was due for renewal at 31 December 2014 was surrendered as it too was not considered to be core to the unconventional play**.**

During the first term of the three permits, a significant work program was completed and a major work program is ongoing for the period of the renewal.

In accordance with local law and regulations, all Falcon Australia's acreage interests are subject to combined government royalties on production values of up to approximately 12% and 1% (subject to the exercise of Falcon Australia's call option - see "*Overriding Royalty Beetaloo Basin exploration permits*" for details) to other parties. In addition, Falcon Australia is subject to Commonwealth Government corporation tax of 30%, and to the Commonwealth Government's Petroleum Resource Rent Tax ("**PRRT**") levied at the rate of 40% on the taxable profits derived from the petroleum projects. The PRRT is calculated on the individual projects, and royalties are deductible for PRRT purposes. The PRRT tax system is separate from the company income tax system and is based on cash flow. Both royalties and PRRT are deductible for corporate income tax purposes.

Overriding Royalty Beetaloo Basin exploration permits
On 1 November 2013, Falcon announced that Falcon Australia had entered into an agreement (the **"CRIAG Agreement**") with CR Innovations AG ("**CRIAG**") to acquire its 4% overriding royalty interest ("**ORRI**") relating to its exploration permits in the Beetaloo Basin. The key transaction details were:

- Falcon Australia made an initial payment to CRIAG of $999,000 on signing the CRIAG Agreement;
- Falcon Australia to make a second payment to CRIAG of $999,000 to acquire the first 3% (three fourths) of the ORRI upon completion of a farm-out deal in Australia;
- CRIAG has granted Falcon Australia a five year call option to acquire the remaining 1% (one fourth) for $5 million; and
- All ORRI's acquired under the CRIAG Agreement will be immediately cancelled by Falcon Australia.

On 17 December 2013, Falcon announced that Falcon Australia, had entered into an agreement (the **"TOG Agreement"**) with Malcolm John Gerrard, Territory Oil & Gas LLC and Tom Dugan Family Partnership LLC ("**TOG Group**") to acquire up to 7% (seven eighths) of their 8% private ORRI over Falcon Australia's Exploration Permits in the Beetaloo Basin for the following consideration:

- Falcon Australia will make a payment to TOG Group of $5 million to acquire 5% (five eighths) of their ORRI only on completion of a Beetaloo farm-out transaction;
- TOG Group will grant Falcon Australia a five year call option to acquire a further 2% (two eights) of their ORRI for a payment of $15 million;
- All ORRIs acquired under the Agreement will be immediately cancelled by Falcon Australia; and
- TOG Group will retain a 1% ORRI.

On completion of Falcon's Beetaloo farm-out as announced on 21 August 2014, Falcon Australia made the second payment to CRIAG in the amount of $999,000 and to the TOG Group in the amount of $5 million. The overriding royalty is now at 4%. As detailed in the respective CRIAG agreement and TOG agreement, Falcon Australia and the Farminees have the option to reduce this royalty further to 1% by the exercise of two 5 year call options. The call options will be funded by Falcon Australia and each of the Farminees in proportion to their interest in the permits.

Discoveries and Prospectivity
The Board believes that the Beetaloo Basin is relatively underexplored and has shale oil, shale gas and basin centered gas accumulations ("**BCGA**") potential. As far as the Company is aware, 11 wells have been drilled in the Beetaloo Basin to date. This work was undertaken by a Rio Tinto Group subsidiary company exploring for conventional hydrocarbons and while not leading to a conventional development, the data from the cores demonstrated the presence of tight oil and gas and several horizons were shown to be prospective for unconventional oil and gas.

There are no existing fields but there are numerous mudlog oil and gas shows and oil indications on cores throughout the Beetaloo Basin in prospective formations. The Shenandoah-1 well was a vertical hole well drilled by Sweetpea Petroleum Pty Ltd. ("**Sweetpea**") in 2007. The well was deepened by Falcon Australia in 2009 to finish at 2,714 metres. It was re-entered in Quarter 3 2011 and five short tests were conducted including several fracking operations. Gas was recovered from three zones with some liquids.

During 2011 and 2012 Falcon Australia's previous joint venture partner, Hess Australia (Beetaloo) Pty. Ltd ("**Hess**"), acquired 3,490 kilometres of 2D seismic data investing approximately $80 million at no cost to Falcon. The seismic database, along with existing well data, provided a very solid platform to extrapolate a detailed structural and stratigraphic model for the main parts of the Beetaloo Basin. All the necessary elements of a productive unconventional and conventional petroleum system have been identified in multiple shales and sand reservoirs, and it is now clear that the Beetaloo Basin is an active petroleum system.

Three hydrocarbon plays have been identified:
- the shale gas potential in the basin centre;
- a shale oil play in the northern part of the permits; and
- conventional prospects throughout the acreage.

Interpretation of the seismic database mapped out several conventional drilling targets that are promising areas of hydrocarbons accumulation in the form of structural closures and traps.

Current activity

Transformational Farm out of Beetaloo unconventional acreage

On 21 August 2014, Falcon Australia completed its farm-out agreement and joint operating agreement (collectively the **"Agreements**") with Origin and Sasol, (collectively referred to herein as the **"Farminees**"), each farming into 35% of Falcon Australia's exploration permits in the Beetaloo Basin, Australia (the **"Permits**").

The transaction details were:
- Falcon Australia received A$20 million cash from the farminees.
- Origin was appointed as Operator.
- Farminees to carry Falcon Australia in a nine well exploration and appraisal program over 2014 to 2018 inclusive, detailed as follows:
  - 3 vertical exploration/stratigraphic wells and core studies;
  - 1 hydraulic fracture stimulated vertical exploration well and core study;
  - 1 hydraulic fracture stimulated horizontal exploration well, commercial study and 3C resource assessment; and
  - 4 hydraulic fracture stimulated horizontal exploration/appraisal wells, micro-seismic and 90 day production tests.
- Drilling/testing specifically planned to take the project towards commerciality. Falcon Australia retains a 30% interest in the Permits.
- Farminees will pay for the full cost of completing the first five wells estimated at A$64 million, and will fund any cost overruns. This work is expected to be completed within two years (2015 – 2016).
- Farminees to pay the full cost of the following two horizontally fracture stimulated wells, 90 day production tests and micro seismic data collection with a capped expenditure of A$53 million, any cost overrun funded by each party in proportion to their working interest. This work programme is expected to be undertaken in 2017.
- Farminees to pay the full cost of the final two horizontally fracture stimulated wells and 90 day production tests capped at A$48 million, any cost overrun funded by each party in proportion to their working interest. This work programme is expected to be undertaken in 2018.
- Farminees may reduce or surrender their interests back to Falcon Australia only after:

- The drilling of the first five wells; or
- The drilling and testing of the next two horizontally fracture stimulated wells.

On 27 November 2014 Falcon announced that preparations for the Group's 2015 Australian drilling programme, comprising the initial three wells in the Beetaloo Basin were at an advanced stage. 2014 saw significant progress of the agreed work programme with the Farminees with the objective of moving the project towards commerciality. A comprehensive technical evaluation undertaken in 2014 has enabled the selection of appropriate well locations to penetrate oil mature through to dry gas mature sections of the Middle Velkerri shale play. The principal objectives of the 2015 drilling programme are to:

- penetrate the Middle Velkerri formation to assess hydrocarbon saturation and reservoir quality;
- evaluate oil versus gas maturity and determine the most prospective areas and depth window;
- provide wide geographical cover of the target Middle Velkerri formation; and
- collect data points for subsequent vertical/horizontal drilling, completion and production testing.

Formation evaluation and reservoir characterisation will be carried out from these initial three wells through petrophysical interpretation, core analysis, geomechanical studies and stimulation design.

Tendering and contracting for the rig and key well services, and recruiting additional project resources are ongoing. Spudding of the first well is expected in mid-2015 subject to weather conditions as the wet season ends. Two further wells will be drilled back-to-back before the dry season ends in 2015.

Karoo Basin, South Africa

Overview

The Company holds a technical co-operation permit ("**TCP**") covering an area of approximately 7.5 million acres (approximately 30,327 km^2), in the southwest Karoo Basin, South Africa, which grants the Company exclusive rights to apply for an exploration right over the underlying acreage. In August 2010, the Company submitted an application to the Petroleum Agency of South Africa (the "**PASA**") for an exploration right over the acreage covered by the TCP and, as part of the application process, the Company submitted an environmental management plan in January 2011.

The Karoo Basin extending to approximately 173 million acres (approximately 700,000 km^2) in size is located in central and southern South Africa. Until recently, the Karoo Basin was not considered prospective for commercial hydrocarbons resulting in very limited modern hydrocarbon exploration onshore in South Africa. In an independent report dated June 2013, the U.S. Energy Information Administration (the "**EIA**") estimated that there are 390 Tcf technically recoverable resources in the Karoo Basin which would rank it fifth in the world after China, USA, Argentina and Mexico for shale gas potential.

On 1 February 2011, the Minister of Mineral Resources (the "**Minister**") published a notice in the Government Gazette declaring a moratorium on the processing of all new applications relating to the exploration and production of shale gas in the Karoo Basin. This moratorium did not extend to existing applications, such as Falcon's, that were submitted prior to 1 February 2011. In April 2011, the Minister announced a further moratorium, which was not officially declared by way of notice in the Government Gazette, prohibiting all new applications and suspending the processing of all pending applications whilst the South African Department of Mineral Resources conducted an environmental feasibility study on the effects of hydraulic stimulation and developed a system to regulate onshore exploration activities (the "**Undeclared Moratorium**"). In September 2012, the South African Government announced a decision to lift the undeclared moratorium on shale gas exploration. The Minister indicated that although the Undeclared Moratorium has been lifted, pending exploration right applications will not be processed and awarded until the regulations regarding unconventional exploration were published. The proposed regulations titled "Proposed technical regulations for petroleum exploration and exploitation" were published in the Republic of South Africa Government Gazette (Notice 1032 of 2013) for comment on 15 October 2013.

In February 2014 the Minister published two new notices which significantly impact the petroleum industry.

The first notice (notice 71 of 2014) provides that the existing moratorium on applications for reconnaissance permits, technical co-operation permits, exploration rights and production rights relating to shale gas in the Karoo region has been extended. However the existing applications, such as Falcon's, received and accepted before 1 February 2011, are excluded from the moratorium. The notice provides that if, in the interim, the existing applications are granted, the applicants will not be entitled to conduct hydraulic fracturing until the technical regulations have been promulgated. This is a reference to the draft regulations published for comment in Notice 1032 of 2013.

The second notice (notice 72 of 2014) states the Minister's intention to declare a moratorium on all new, onshore and offshore, applications for reconnaissance permits, technical co-operation permits, exploration rights and production rights for a period of two years and invited relevant stakeholders to comment on this proposal within 30 days from the date of publication.

The South African Government is entitled to a royalty on the sale of mineral resources of up to 7% of gross sales (in the case of unrefined resources) and 5% of gross sales (in the case of refined resources, such as oil and gas).

The Mineral and Petroleum Resources Development Act, 28 of 2002 empowers the Minister of Mineral Resources, when granting an application for an exploration right, to direct the applicant to sell an interest in the operation to a Historically Disadvantaged South African ("**HDSA**"). The amount of the interest is, in practice, derived from the Liquid Fuels Charter, which is a policy instrument governing participation by HDSAs in the petroleum industry. At production stage of the project, it is a statutory condition for the grant of a production right that an HDSA holds 10% of the interest in the operation. The way in which HDSAs earn or pay for the 10% interest is not legislated, meaning that applicants are free to negotiate suitable terms with prospective HDSAs subject to the "unofficial approval" of the PASA. State participation in exploration and production rights is currently not addressed in legislation. In the past, the practice has been for exploration rights to incorporate a clause giving the State an option to acquire an interest of up to 10% in any production right granted through the national oil company. However, it is not required to pay any consideration for its 10% interest or contribute to past costs, but must contribute pro rata in accordance with its interest towards production costs going forward.

On 12 March 2014, South Africa's parliament approved the Mineral and Petroleum Resources Development Amendment Bill ("**MPRDA Bill**") which amends the Mineral and Petroleum Resources Development Act (28 of 2002), South Africa's main petroleum law. Among the proposed changes, the law provides the state with a free carried interest of 20% in all new gas and oil exploration and production ventures. In addition to this 20% free carried interest, the government introduced a new clause entitling it to further participation in the form of an acquisition at an agreed price or production sharing agreements. No percentage limit on this entitlement has been stated in the amendments. The MPRDA Bill only provides a framework and regulations must be promulgated to give effect to it. In Q2 2014, the new Minister of Mineral Resources requested the President to delay the signature of the MPRDA Bill in order to give him time to investigate the matter. In January 2015, the President has referred the MPRDA Bill back to the National Assembly for reconsideration.

On 3 November 2014 Falcon announced it has been notified by the PASA that a decision has been taken to proceed with processing of the Company's application for a shale gas Exploration Licence in South Africa's Karoo Basin.

In addition, the South African Department of Mineral Resources ("**DMR**") informed members of South Africa's parliament in October 2014 that the government was soon expected to issue companies with licences to explore for shale gas.

The Board now expects that the exploration right over the acreage will be awarded in 2015.

Corporation tax in South Africa is imposed at a rate of 28% of taxable income. Dividends tax is imposed on the shareholder at a rate of 15%, but it may be reduced to 5% in terms of a Double Tax Agreement (if applicable), or to 0% in respect of dividends paid by an oil and gas company out of amounts attributable to its oil and gas income.

Discoveries and Prospectivity

In its entirety, the Karoo Basin is approximately 173 million acres (approximately 700,000 km^2) in size located in central and southern South Africa and contains thick, organic rich shales such as the Permian Whitehill Formation. The Karoo describes a geological period lasting some 120 million years and the rocks laid down during that period of time, covering the late Paleozoic to early Mesozoic interval periods. These rocks were deposited in a large regional basin and resulted in the build-up of extensive deposits. Until recently, the Karoo Basin was not considered prospective for commercial hydrocarbons resulting in very limited modern hydrocarbon exploration onshore in South Africa. In an independent report dated June 2013, the EIA estimated that there are 390 Tcf technically recoverable resources in the Karoo Basin which would rank it fifth in the World after China, USA, Argentina and Mexico for shale gas potential. In particular the Permian Ecca group contains three potential shales identified as having potential for shale gas. The shale in the Whitehall Formation, in particular, is ubiquitous, has a high organic content and is thermally mature for gas.

Current activity

In December 2012, Falcon entered into an exclusive cooperation agreement with Chevron Business Development South Africa Limited ("**Chevron**"**)** to jointly seek unconventional exploration opportunities in the Karoo Basin. The Chevron agreement provides for Falcon to work exclusively with Chevron for a period of five years to jointly seek to obtain exploration rights in the Karoo Basin subject to the parties mutually agreeing participation terms applicable to each right. As part of the Chevron agreement, Chevron made a cash payment to Falcon of $1 million in February 2013 as a contribution to past costs.

As noted above Falcon was notified by the PASA that a decision has been taken to proceed with processing of the Company's application for a shale gas exploration licence in South Africa's Karoo Basin. The PASA had requested Falcon to review and update its already drafted Environmental Management Programme where necessary. This was completed and submitted on the 27 February 2015.

Makó Trough, Hungary

Overview

Falcon has been active in the Makó Trough since 2005 when it acquired two exploration licences, the Makó and the Tisza exploration licences. Between 2005 and 2007, Falcon pursued a work programme consisting of the acquisition of 1,100 km^2 of 3D seismic data and a six-well drilling programme. Each of the six wells encountered thick sequences of hydrocarbon bearing rocks, and tests flowed hydrocarbons from each tested horizon. In 2007, Falcon's subsidiary, TXM, was awarded the 35-year Makó Production Licence which covers some of the acreage originally covered by the Makó and the Tisza exploration licences.

Hungary is an established oil and gas producing country. The Makó Production Licence is in the vicinity of the largest producing field in Hungary, the MOL Group owned and operated Algyő field, which has produced approximately 2.5 Tcf and 220 Mmbo to date. The Makó Production Licence is located approximately ten kilometres to the east of the MOL Group owned and operated Algyő field and is transected by existing gas pipelines and infrastructure, including a 12 kilometre gas pipeline built by Falcon in 2007, together offering transport and potential access to local markets and larger distribution centres for international markets.

Makó Production Licence

The Makó Production Licence was granted by the Hungarian Mining Authority over a gas exploration project in the Makó Trough, located in south-eastern Hungary. The lands within the Makó Production Licence were formerly part of the Group's two hydrocarbon exploration licences – the Tisza exploration licence and the Makó exploration licence.

The Makó Production Licence covers approximately 245,775 acres (approximately 1,000 km^2) and is held 100% by TXM, a wholly owned subsidiary of the Group. Under the terms of the Makó Production Licence, the Group is obliged to pay a 12% royalty to the Hungarian Government on any unconventional production and has a further 5% royalty payable under an agreement with Prospect Resources Inc., the previous owners of the acreage covered by the Makó Production Licence. Corporate profits are taxed at 19%. In 2009, an additional profit based energy industry tax, levied on energy supplying companies, was introduced. The rate was originally set at 8% but, as part of Hungary's third package of austerity measures, the rate has increased to 31% from 2013, with deductions allowable for certain capital expenditures. TXM is the operator and there are no outstanding work commitments on the Makó Production Licence.

Discoveries and Prospectivity

The Makó Trough contains two plays:

- a play targeting gas prospects in the shallower Algyő Play at depths between 2,300 metres and 3,500 metres; and
- a deeper unconventional play targeting significant contingent resources in the Deep Makó Trough.

The Algyő Play

The Algyő Play is a relatively shallow play of between 2,300 and 3,500 metres. A number of Falcon wells have been drilled through the Algyő Play in recent years, some of which encountered gas shows, but to date none of these wells tested the shallow play concept at an optimal location, as these wells targeted the Deep Makó Trough, at intervals of up to 6,000 metres. Multiple Algyő prospects have subsequently been identified by the Group through extensive amplitude versus offset analysis, and 3D seismic data has shown the presence of possible gas zones above the Szolnok formation (part of the Deep Makó Trough).

In January 2013, Falcon agreed to a three-well drilling exploration programme with Naftna industrija Srbije jsc ("**NIS**"), 56% owned by Gazprom Group, to target the Algyő Play, whereby NIS made a cash payment of $1.5 million to Falcon in February 2013, and agreed to drill three wells by July 2014. This deadline was extended to 31 December 2014. For additional details refer to section "Current activity" below.

The Deep Makó Trough

This is a deeper unconventional play targeting gas, and to a lesser extent oil, in the low permeability and low porosity rocks in the deeper horizons of the basin.

Between 2005 and 2007, Falcon acquired 1,100 km^2 of 3D seismic data and executed a six-well drilling programme on the Deep Makó Trough. Early exploration efforts focused on proving hydrocarbon potential and delineation of the basin in order to secure the Makó Production Licence. Each of the six wells encountered thick sequences of hydrocarbon bearing rocks, and tests flowed hydrocarbons from each tested horizon. Several wells flowed gas on test and one well, Magyarcsanád-1, tested light oil. The Makó-7 results demonstrated the presence of a very large column of hydrocarbons in the well-bore. In 2007, Falcon constructed a 12 kilometre gas pipeline which connected the Makó-6 and Makó-7 wells with a MOL operated pipeline, offering potential access to local and international markets.

Current activity

In January 2013, the Group and NIS agreed to a three-well drilling programme targeting the relatively shallow Algyő Play by July 2014, whereby NIS made a cash payment of $1.5 million and agreed to carry Falcon 100% over the programme. The July 2014 deadline for completion of drilling and testing of the three well programme was subsequently extended to 31 December 2014.

Drilling operations on Kútvölgy-1, the first joint well between NIS and the Group, were completed in July 2013, the well having reached total depth ("**TD**") of 3,305 metres. As anticipated, the top of the Algyő Formation was encountered at 2,985 metres, the well then penetrating an alternating sequence of sandstones, siltstones and shales over a gross interval of 320 metres to TD, with gas shows throughout. Two conventional cores were taken and extensive wireline logs were run. No operational problems or accidents occurred during drilling.

As announced on 16 May 2014, the testing of the first well, Kútvölgy-1, indicated that the well experienced improved recovery from certain intervals however well production did not meet commercial rates thus was discontinued with the well being plugged and abandoned.

Falcon announced on 27 November 2014 that well testing operations on the second well, Besa-D-1 were completed. The testing of two sand intervals, both part of the tight turbiditic sequence in the lower Algyő Formation, indicated that well production did not meet commercial rates and the well is now being plugged and abandoned.

On 26 January 2015, the Group announced the expiry of the extension granted to NIS, regarding their three-well drilling programme in Falcon's Makó Trough Licence in Hungary. The July 2014 deadline for completion of drilling and testing of the three-well programme was subsequently extended by Falcon to 31 December 2014 to enable NIS to fulfil its three well obligation. As of 31 December 2014, NIS has only drilled and tested two wells. Falcon is currently evaluating, and will pursue, all options available to the Company to derive shareholder value as NIS has not fulfilled its commitments under the Agreement.

At 31 December 2014, an impairment test was completed on the assets in the Hungarian cost pool. The test demonstrated that the estimated recoverable amount of the E&E and PPE in the pool was insufficient to cover the carrying amount of these assets. The principal impairment indicator was the Company's ability to finance future exploration to commercially develop the asset. The capitalised value of the Group's Hungarian assets has been impaired by $26.5 million (which includes $5.1 million which was classified as PPE) at 31 December 2014.

Alberta, Canada

For the year ended 31 December 2014, Falcon had revenue of $26,000 (2013: $17,000) earned from its Alberta, Canada non-operating working interests (the "**Hackett Interest**"). Falcon's Alberta interests are in three producing and one shut-in, natural gas wells. Falcon does not anticipate any further exploration or development of these wells and no further material revenue is expected to be generated or material costs incurred.

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SELECTED ANNUAL INFORMATION

(In thousands of $ unless otherwise indicated)	2014	2013	2012
For the year ended 31 December:			
Revenues	26	17	21
Net loss	(31,768)	(3,570)	(17,715)
Basic & diluted - Loss per share - $	(0.034)	(0.004)	(0.03)
Cash dividend per share	Nil	Nil	Nil
At 31 December:			
Total assets	55,353	89,516	86,013
Non-current liabilities	9,493	11,138	16,247

The Group is an exploration company with limited revenue which is not material. The Group's net loss and net loss per share relate to the Group's operations during a particular period, and are not seasonal in nature.

The net loss had consistently decreased from 2011 to Quarter 3 2014. This was attributed to the focus by the Group's new management (who commenced mid 2012) to reducing costs. In Quarter 4 2014 an impairment charge was recorded against the carrying value of the Group's Hungarian assets in the amount of $26.6 million. This is the primary reason for the increase in the loss from 2013 to 2014.

In Q1, 2013, Falcon announced its application for admission to trading on the AIM market of the London Stock Exchange and the ESM market of the Irish Stock Exchange of the Company's existing share capital and an additional 120,381,973 new common shares in the capital of the Company issued pursuant to the concurrent conditional brokered private placement at a price of £0.14 (CDN$0.215) per share, raising gross proceeds of $25.7 million (£16.9 million). Falcon's liabilities have decreased since 2012 as the Group repaid the full amount outstanding on its convertible loan note of CDN$10.7 million from the proceeds raised in Q1, 2013. This repayment means that the Group is now completely debt free.

The remaining balance of the $25.7 million proceeds raised was used to partially finance the acquisition of certain minority holders' shares in Falcon Australia and fund working capital and exploration costs.

Generally, the Group's total assets, exploration and evaluation costs, working capital and total shareholders' equity fluctuate in proportion to one another until such time as the Group completes additional financing.

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RESULTS OF OPERATIONS

This review of the results of operations should be read in conjunction with the audited consolidated financial statements for the year ended 31 December 2014 and 2013.

Management's Discussion and Analysis of financial condition and results of operations for the three months ended 31 December 2014 as compared to the three months ended 31 December 2013

The Company reported a loss of $27.8 million for the three months ended 31 December 2014 as compared to a net income of $0.2 million for the three months ended 31 December 2013. Changes between 2014 and 2013 were as follows:

	Three months ended 31 December		Changes	
	2014	2013		
	$'000	$'000	$'000	%
Revenue				
Oil and natural gas revenue	**4**	6	(2)	(33)
	4	6	(2)	(33)
Expenses				
Exploration and evaluation expenses	**(256)**	(285)	29	(10)
Production and operating expenses	**(5)**	(10)	5	(50)
Depreciation	**(26)**	(46)	20	(43)
General and administrative expenses	**(929)**	(912)	(17)	2
Share based compensation	**75**	(206)	281	(136)
Foreign exchange (loss) / gain	**(7)**	129	(136)	(105)
Other income	**110**	192	(82)	(43)
Impairment	**(26,526)**	-	(26,526)	-
Restructuring expenses	**(444)**	-	(444)	-
	(28,008)	(1,138)	(26,870)	2,361
Results from operating activities	**(28,004)**	(1,132)	(26,872)	2,374
Fair value gain – outstanding warrants	**377**	1,375	(998)	(73)
Finance (expense) / income				
Interest income on bank deposits	**13**	15	(2)	(13)
Accretion of decommission provisions	**(68)**	(47)	(21)	45
Net foreign exchange (loss) / gain	**(112)**	(51)	(61)	119
	(167)	(83)	(84)	101
(Loss) / income and comprehensive (loss) / income	**(27,794)**	160	(27,954)	(17,471)
(Loss) / income and comprehensive (loss) / income attributable to:				
Equity holders of the company	**(27,790)**	166	(27,956)	(16,841)
Non-controlling interest	**(4)**	(6)	2	(33)
(Loss) / income and comprehensive (loss) / income	**(27,794)**	160	(27,954)	(17,471)

Oil and natural gas revenue
Oil and natural gas revenue of $4,000 (2013: $6,000) consists of the sale of natural gas from the Hackett Interest in Alberta, Canada. The Company has not yet realised significant revenue from its planned operations elsewhere.

Exploration and evaluation expenses
Exploration and evaluation expenses are consistent year on year. 2014 and 2013 expenses represent recurring maintenance and landowners costs in maintaining and safeguarding the Company's existing Hungarian wells.

Depreciation
2014 and 2013 depreciation expense consists of depreciating assets and equipment at the Group's Budapest and Dublin offices. Depreciation reduced period on period due to the expiration of certain assets' useful economic lives.

General and administrative expenses

	Three months ended 31 December		Change	
	2014	2013		
	$'000	$'000	$'000	%
Accounting and audit fees	**(84)**	(83)	(1)	1
Consulting fees	**(108)**	(162)	54	(33)
Legal fees	**(35)**	(13)	(22)	169
Investor relations	**(96)**	(80)	(16)	20
Office and administrative costs	**(163)**	(206)	43	(21)
Payroll and related costs	**(298)**	(278)	(20)	7
Directors' fees	**(67)**	(67)	-	-
Travel and promotion	**(78)**	(23)	(55)	239
	(929)	(912)	(17)	2

General and administrative expenses increased by $0.0 million to $0.9 million in 2014 from $0.9 million in 2013. The main changes were as follows:

- Accounting and audit fees: The increase is minimal and is due to focus on managing the costs of accounting and audit fees incurred by the Group.
- Consulting and Legal fees: The decrease in consulting fees is attributable to a continued decrease in the use of outside consultants and increased focus on cost containment by management during the period. Legal fees have increased in the quarter due to increased activity in South Africa.
- Investor relations: One of the main focuses of the Group's management is to actively engage with its shareholders and investors. For the six months ended 31 December 2014 expenditure was $0.2 million, which is comparable to the six months ended 31 December 2013. In the three months ended 31 December 2014 in comparison with the three months ended 31 December 2013, the movement is a result of the timing of investor events in the second half of the respective years.
- Office and Administrative expenses have decreased on the prior year 3 month comparative in 2013 due to the on-going focus on managing the costs incurred by the Group.
- Travel and promotion increased in the current 3 month period over the comparative three months to December 2013. The quarterly costs up to December 2014 included significant costs for travel relating to management's active engagement in South Africa and the Group's management of its farm-out project in Australia. There was no similar travel in the same three months period in 2013. Certain levels of travel and promotion costs are due to the international geography of the Group's assets and investor base.

Share based compensation
Share based compensation decreased in the three months ended 31 December 2014 in comparison to the three months ended 31 December 2013. The 3 months to 31 December 2013, contains primarily the apportioned cost of the 6 million options granted in May 2012 and 9.9 million share options issued in April 2013. The 3 months ended 31 December 2014 contains a reduced charge for the 6 million options of May 2013 and a reduced charge for the 9.9 million options of April 2013. 4.9 million options granted in April 2013 were forfeited in 2014 with 1.9 million specifically in quarter 4 2014, which resulted in the credit during the period.

Foreign exchange loss
Previously the Group attributed the majority of its foreign exchange gains and losses to the 11% debentures. Thus, exchange gains / (losses) were recorded in finance income / (expense). The Group repaid the debenture on 30 June 2013. All exchange gains and losses not related to financing are recorded in operating expenses.

Other Income
Other income has decreased in the current period primarily due to decreased work being carried out by TXM in providing geological and geophysical services to NIS as part of NIS's drilling programme.

Impairment
In January 2013, the Group and NIS agreed to a three-well drilling programme targeting the relatively shallow Algyő Play with a deadline for completion of work extended to the 31 December 2014 from the originally agreed date of July 2014.

Drilling operations on Kútvölgy-1, the first joint well between NIS and the Group, were completed in July 2013, the well having reached total depth ("TD") of 3,305 metres. Testing indicated that the well experienced improved recovery from certain intervals however well production did not meet commercial rates thus was discontinued with the well being plugged and abandoned.

The well testing operations on the second well, Besa-D-1 were also completed. The testing of two sand intervals, both part of the tight turbiditic sequence in the lower Algyő Formation, indicated that well production did not meet commercial rates and the well is also being plugged and abandoned.

As of 31 December 2014, NIS has only drilled and tested two wells.

Based on the above, management concluded that indicators of impairment were present at 31 December 2014. An impairment test was completed. The principal impairment indicator was the Company's ability to finance future exploration to commercially develop the asset. The capitalised value of the Group's Hungarian assets has been impaired by $26.5 million (which includes $5.1 million which was classified as PPE) at 31 December 2014.

Restructuring expenses
The Group restructured its technical function in Budapest during Quarter 4, 2014 to meet the changing needs to the Group. This has resulted in provision of $0.5 million. These provisions will be utilised in 2015.

Fair value gain – outstanding warrants
Fair value gain – outstanding warrants decreased from a gain of $1.4 million in 2013 to a gain of $0.4 million in 2014. The movement occurred due to the volatility changes in the fair value of the instruments. The 3 months to December 2014 consists of fair value movement of the hess warrant. The primary factor associated with this valuation was Falcon's share price (as quoted on the TSX-V) which moved from CDN15 cents at 30 September 2014 to CDN11.5 cents at 31 December 2014. Quarter 4 2013 included movement on the hess warrant and the private placement warrants which expired H1 2014 and therefore had no similar movement in the 3 month period to December 2014. The hess warrant and private placement warrants outstanding in Q3 2013 were also affected by share price movement, with a drop from CDN18.5 cents at 30 September 2013 to CDN18 cents at 31 December 2013. Movements in exchange in the CDN$ and US$ also contributed to the variability in both 2014 and 2013 respectively.

Finance (expense) / income
Net Finance (expense) / income decreased from an expense of $0.1 million in 2013 to an expense of $0.2 million in 2014, a movement of approximately $0.1 million. The increase occurred primarily due to unfavourable foreign exchange rates on Australian Dollar and Euro relative the strong performance of the US Dollar.

Loss attributable to non-controlling interest
The amounts reflected in 2014 and 2013 represent Falcon Australia's losses attributable to shareholders other than Falcon.

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RESULTS OF OPERATIONS

Management's Discussion and Analysis of financial condition and results of operations for the year ended 31 December 2014 as compared to year ended 31 December 2013

The Company reported a loss of $31.8 million for the year ended 31 December 2014 as compared to a loss of $3.6 million for the year ended 31 December 2013. Changes between 2014 and 2013 were as follows:

	Year ended 31 December		Changes	
	2014	**2013**		
	$'000	**$'000**	**$'000**	**%**
Revenue				
Oil and natural gas revenue	**26**	17	9	53
	26	17	9	53
Expenses				
Exploration and evaluation expenses	**(852)**	(899)	47	(5)
Production and operating expenses	**(27)**	(27)	-	-
Depreciation	**(128)**	(307)	179	(58)
General and administrative expenses	**(4,046)**	(4,656)	610	(13)
Share based compensation	**(197)**	(693)	496	(72)
Foreign exchange (loss) / gain	**(189)**	326	(515)	(158)
Other income	**482**	683	(201)	(29)
Impairment	**(26,526)**	-	(26,526)	-
Restructuring expenses	**(444)**	-	(444)	-
	(31,927)	(5,573)	(26,354)	473
Results from operating activities	**(31,901)**	(5,556)	(26,345)	474
Fair value gain – outstanding warrants	**883**	3,895	(3,012)	(77)
Finance (expense) / income				
Interest income on bank deposits	**49**	102	(53)	(52)
Derivative gain	**-**	26	(26)	(100)
Effective interest on loans and borrowings	**-**	(2,352)	2,352	(100)
Accretion of decommission provisions	**(173)**	(158)	(15)	9
Net foreign exchange (loss) / gain	**(626)**	473	(1,099)	(232)
	(750)	(1,909)	1,159	(61)
Loss and comprehensive loss	**(31,768)**	(3,570)	(28,198)	790
Loss and comprehensive loss attributable to:				
Equity holders of the company	**(31,744)**	(3,411)	(28,333)	831
Non-controlling interest	**(24)**	(159)	135	(85)
Loss and comprehensive loss	**(31,768)**	(3,570)	(28,198)	790

Oil and natural gas revenue
Oil and natural gas revenue of $26,000 (2013: $17,000) consists of the sale of natural gas from the Hackett Interest in Alberta, Canada. The Group has not yet realised significant revenue from its planned operations elsewhere.

Exploration and evaluation expenses
Exploration and evaluation expenses are consistent year on year. 2014 and 2013 expenses represent recurring maintenance and landowners costs in maintaining and safeguarding the Group's existing Hungarian wells.

Depreciation
2014 and 2013 depreciation expense consists of depreciating assets and equipment at the Group's Budapest and Dublin offices. The decrease in depreciation is partially attributable to the expiration of certain assets' useful economic lives.

General and administrative expenses

	Year ended 31 December		**Change**	
	2014	**2013**		
	$'000	**$'000**	**$'000**	**%**
Accounting and audit fees	(384)	(534)	150	(28)
Consulting fees	(484)	(617)	133	(22)
Legal fees	(91)	(250)	159	(64)
Investor relations	(457)	(349)	(108)	31
Office and administrative costs	(722)	(870)	148	(17)
Payroll and related costs	(1,326)	(1,450)	124	(9)
Directors' fees	(279)	(281)	2	(1)
Travel and promotion	(303)	(305)	2	(1)
	(4,046)	(4,656)	610	(13)

General and administrative expenses decreased by $0.6 million to $4.1 million in 2014 from $4.7 million in 2013. The main changes were as follows:

- Accounting and audit fees: The decrease occurred due to focus on managing the costs of accounting and audit fees incurred by the Group.
- Consulting and Legal fees: The decrease is attributable to a continued reduction in the use of outside consultants and counsel and increased focus on cost containment by management during the period.
- Investor relations: One of the main focuses of the Group's management is to actively engage with its shareholders and investors. This has resulted in increased expense in this area in 2014.
- Office and Administrative expenses have decreased due to focus on managing the costs of office and administrative expenses incurred by the Group.
- Travel and promotion remained relatively constant year on year. Certain levels of travel and promotion costs are due to the international geography of the Group's assets and investor base.

Share based compensation
Share based compensation decreased in the year ended 31 December 2014 in comparison to the year ended 31 December 2013. The twelve months to 31 December 2013, contains primarily the apportioned cost of the 6 million options granted in May 2012 and the 9.9 million share options issued in April 2013; the twelve months ended 31 December 2014 contains the apportioned cost of the options granted in May 2012, the 9.9 million share options issued in April 2013 and the reversing cost of 4.9 million options granted in April 2013 which were forfeited in 2014.

Foreign exchange loss
Previously the Group attributed the majority of its foreign exchange gains and losses to the 11% debentures. Thus, exchange gains / (losses) were recorded in finance income / (expense). The Group repaid the debenture on 30 September 2013. All exchange gains and losses not related to financing are recorded in operating expenses.

Other Income
Other income has decreased in the current period primarily due to reduced work being carried out by TXM in providing geological and geophysical services to NIS as part of NIS's drilling programme.

Impairment
In January 2013, the Group and NIS agreed to a three-well drilling programme targeting the relatively shallow Algyő Play with a deadline for completion of work extended to the 31 December 2014 from the originally agreed date of July 2014.

Drilling operations on Kútvölgy-1, the first joint well between NIS and the Group, were completed in July 2013, the well having reached total depth ("**TD**") of 3,305 metres. Testing indicated that the well experienced improved recovery from certain intervals however well production did not meet commercial rates thus was discontinued with the well being plugged and abandoned.

The well testing operations on the second well, Besa-D-1 were also completed. The testing of two sand intervals, both part of the tight turbiditic sequence in the lower Algyő Formation, indicated that well production did not meet commercial rates and the well is also being plugged and abandoned.

As of 31 December 2014, NIS has only drilled and tested two wells.

Based on the above, management concluded that indicators of impairment were present at 31 December 2014. An impairment test was completed. The principal impairment indicator was the Company's ability to finance future exploration to commercially develop the asset. The capitalised value of the Group's Hungarian assets has been impaired by $26.5 million (which includes $5.1 million which was classified as PPE) at 31 December 2014.

Restructuring expenses
The Group restructured its technical function in Budapest during Quarter 4, 2014 to meet the changing needs to the Group. This has resulted in provision of $0.5 million. These provisions will be utilised in 2015.

Fair value gain / (loss) – outstanding warrants
Fair value gain / (loss) – outstanding warrants decreased from a gain of $3.9 million in 2013 to a gain of $0.9 million in 2014. The movement occurred due to the volatility changes in the fair value of the instruments. The primary variables are the movement in Falcon's share price over the period and the time elapsed to maturity. In addition the 65.3 million private placement warrants outstanding at 31 December 2013 which expired in February 2014 and April 2014 were not exercised. In addition in Q2 2014, the hess warrant was extended from 13 January 2015 to 13 January 2020. The expiration of the private placement warrants resulted in a $1 million gain for the 12 month period to December 2014 which was offset by a $0.2 million valuation loss directly attributable to the hess warrant in the same 12 month period.

Finance income / (expense)
Net Finance income / (expense) decreased from an expense of $1.9 million in 2013 to an expense of $0.8 million in 2014, a movement of $1.1 million. The decrease occurred primarily due to the repayment of the Group's debentures on 30 June 2013, which was partially offset in the current 12 month period to December 2014 by unfavourable foreign exchange rates on Australian Dollar and Euro relative the strong performance of the US Dollar. The Group has no outstanding debt.

Loss attributable to non-controlling interest
The amounts reflected in 2014 and 2013 represent Falcon Australia's losses attributable to shareholders other than Falcon.

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SUMMARY OF QUARTERLY RESULTS

The following is a summary of the eight most recently completed quarters:

(In thousands of $ unless otherwise stated)

As of:	31 March 2014	30 June 2014	30 September 2014	31 December 2014
Total assets	88,389	87,172	86,007	55,353
Exploration and evaluation assets	74,720	74,869	61,431	39,619
Working capital	5,916	3,752	14,930	13,213
Total shareholders' equity	74,577	72,520	71,029	43,164

For the three months ended:	31 March 2014	30 June 2014	30 September 2014	31 December 2014
Revenue	10	7	5	4
(Loss)	(333)	(2,074)	(1,567)	(27,794)
(Loss) attributable to common shareholders	(329)	(2,069)	(1,556)	(27,790)
(Loss) per share-basic and diluted (cent)	0.000	(0.002)	(0.002)	(0.030)

As of:	31 March 2013	30 June 2013	30 September 2013	31 December 2013
Total assets	107,448	94,475	90,288	89,516
Exploration and evaluation assets	72,643	72,777	72,456	74,517
Working capital	12,342	7,662	7,314	6,193
Total shareholders' equity	65,851	64,186	74,330	74,711

For the three months ended:	31 March 2013	30 June 2013	30 September 2013	31 December 2013
Revenue	3	4	4	6
(Loss) / income	(4,746)	(1,896)	2,912	160
(Loss) / income attributable to common shareholders	(4,701)	(1,805)	2,929	166
(Loss) / income per share-basic and diluted (cent)	(0.007)	(0.002)	0.003	0.000

The Group is an exploration company with limited revenue which is not material. The Group's (loss) / income and (loss) / income per share relate to the Group's operations during a particular period, and are not seasonal in nature.

Quarter 1 2013: In January 2013, the Group agreed to a three-well drilling programme with NIS, 56% owned by Gazprom Group, to target the Algyő Play, whereby NIS made a cash payment of $1.5 million to the Group in February 2013, and agreed to drill three wells by July 2014. This deadline was extended to 31 December 2014.

Quarter 1 2013: On 14 March 2013 the Group announced its application for admission to trading on the AIM market of the London Stock Exchange and the ESM market of the Irish Stock Exchange of the Company's existing share capital and an additional 120,381,973 new common shares in the capital of the Company issued pursuant to the concurrent conditional brokered private placement at a price of £0.14 (CDN$0.215) per share, raising gross proceeds of $25.7 million (£16.9 million). Trading in these shares commenced on AIM and ESM on 28 March 2013.

Quarter 2 2013: On 30 April 2013, the Group announced that under the stock option plan approved at Falcon's annual shareholders meeting held on 25 September 2012, it had granted incentive stock options ("**options**") to purchase an aggregate of 9.9 million common shares of Falcon. A total of 3 million options were granted at an exercise price of CDN$0.215 to Falcon's then Chief Financial Officer pursuant to the terms of his employment contract. A further 5.5 million options were granted at an exercise price of CDN$0.24 to Falcon directors and 1.4 million options were granted to Falcon employees also at CDN$0.24. The options all have a vesting schedule allowing for 1/3 of the options to vest on the first anniversary of the grant with an additional 1/3 vesting each subsequent year until the options are fully vested on 30 April 2016, and an expiry date of the options of 29 April 2018. Immediately after this award, there were 42,737,000 options outstanding, representing 5.2% of the issued share capital of the company.

Quarter 2 2013: Falcon repaid the full amount outstanding on its convertible loan note of CDN$10.7 million. This repayment means that the Company is now completely debt free.

Quarter 3 2013: In order to consolidate its interest in Falcon Australia, Falcon acquired Sweetpea's 50 million shares or 24.2% interest in Falcon Australia in July 2013. Following the completion of the share purchase, Falcon owned 96.9% of the issued share capital of Falcon Australia. The total value of the consideration was CDN$22.6 million consisting of $3 million in cash and the balance in Falcon common shares. Sweetpea, a wholly owned subsidiary of PetroHunter Energy Corporation, then held 10.7% of the issued share capital of Falcon. Falcon further consolidated its position in September 2013 when it has completed the purchase of 2,462,686 shares from certain of the remaining shareholders in Falcon Australia. The consideration was 2.25 common shares in Falcon for every one Falcon Australia ordinary share held. The valuation used in this offer was the same used in the acquisition of the Sweetpea 24.2% holding. As a result of this transaction, 5,541,044 new Falcon common shares were issued. Following the completion of the above transactions, Falcon holds 202,462,686 shares in Falcon Australia, representing 98.1% of its issued share capital.

Quarter 4 2013: On 1 November 2013, Falcon announced that Falcon Australia, had entered into an agreement with CR Innovations AG ("**CRIAG**") to acquire its 4% Overriding Royalty Interest ("**ORRI**") relating to its exploration permits in the Beetaloo Basin. On 17 December 2013, Falcon announced that Falcon Australia, had entered into an agreement with Malcolm John Gerrard, Territory Oil & Gas LLC and Tom Dugan Family Partnership LLC ("**TOG Group**") to acquire up to 7% (seven eighths) of their 8% private ORRI over Falcon Australia's Exploration Permits in the Beetaloo Basin. The Group completed the two agreements to acquire 8% of the privately held ORRI at a total cost of just $7 million, of which $1 million was paid in November 2013 and the further $6 million was paid on completion of the 2014 Beetaloo farm–out with Origin and Sasol. In addition, the Group has secured agreement to acquire a further 3% based on two five year call options granted to Falcon Australia at a future combined cost to Falcon Australia and its farminee partners, in their proportionate share of $20 million leaving only a 1% royalty in private hands.

Quarter 2 2014: On 2 May 2014, the Group announced that Falcon Australia, had executed definitive agreements including a Farm-Out Agreement and Joint Operating Agreements (collectively the **"Agreements**") with Origin Energy Resources Limited, a subsidiary of Origin Energy Limited ("**Origin**") and Sasol Petroleum Australia Limited, a subsidiary of Sasol Limited ("**Saso**l"), to each farm into 35% of Falcon's Exploration Permits in the Beetaloo Basin, Australia (the **"Permits**"). The Agreements completed on 21 August 2014. Falcon Australia received A$20 million cash on completion.

Quarter 2 2014: Three (EP-76, EP-98 and EP-117) of Falcon Australia's then four Beetaloo Permits were due for renewal at 31 December 2013. As part of the renewal process, Falcon agreed to relinquish approximately 26% of the three Permits which was not considered to be core to the unconventional play in the Beetaloo Basin by Falcon, Origin and Sasol. The renewal of the three Permits was completed on 30 April 2014. Falcon Australia's fourth permit, EP-99, which was due for renewal at 31 December 2014 was surrendered as it too was not considered to be core to the unconventional play**.**

Quarter 3 2014: On 21 August 2014, the Group completed its Farm-Out Agreement and Joint Operating Agreement with Origin (appointed Operator) and Sasol (collectively the "**farminees**"), each farming into 35% of Falcon's exploration permits in the Beetaloo Basin, Australia. Falcon received A$20 million cash from the farminee, with the Farminees to carry Falcon in a nine well exploration and appraisal program over the next four years.

Quarter 4 2014: In January 2013, the Group and Naftna industrija Srbije jsc ("**NIS**") agreed to a three-well drilling programme targeting the relatively shallow Algyő Play with a deadline for completion of work extended to the 31 December 2014 from the originally agreed date of July 2014.

Drilling operations on Kútvölgy-1, the first joint well between NIS and the Group, were completed in July 2013, the well having reached total depth ("TD") of 3,305 metres. Testing indicated that the well experienced improved recovery from certain intervals however well production did not meet commercial rates thus was discontinued with the well being plugged and abandoned.

The well testing operations on the second well, Besa-D-1 were also completed. The testing of two sand intervals, both part of the tight turbiditic sequence in the lower Algyő Formation, indicated that well production did not meet commercial rates and the well is also being plugged and abandoned.

As of 31 December 2014, NIS has only drilled and tested two wells.

Based on the above, management concluded that indicators of impairment were present at 31 December 2014. An impairment test was completed. The principal impairment indicator was the Company's ability to finance future exploration to commercially develop the asset. The capitalised value of the Group's Hungarian assets has been impaired by $26.5 million (which includes $5.1 million which was classified as PPE) at 31 December 2014.

Quarter 1 2015: On 27 January 2015 Falcon granted incentive stock options ("**Options**") to purchase an aggregate of 6 million common shares of Falcon to a number of recipients, including directors and officers under the stock option plan approved at Falcon's annual shareholders meeting held on 10 December 2014. A maximum of 10% of the issued and outstanding shares of Falcon are reserved for issuance pursuant to Falcon's stock option plan. The Options were granted at an exercise price of CDN$0.15 (a 26% premium to the closing share price on 23 January 2015) to the following:

	Number of Options granted	**Total number of Options held after grant**
John Craven - Non-Executive Chairman	1,000,000	4,100,000
Philip O'Quigley - CEO	2,000,000	8,000,000
Michael Gallagher - CFO	3,000,000	3,300,000
Total	**6,000,000**	**15,400,000**

The Options granted to Mr. Craven and Mr. O'Quigley vest immediately. The Options have an expiry date of 25 January 2020. The Options granted to Mr. Gallagher have a vesting schedule allowing for 1/3 of the Options to vest on the first anniversary of the grant with an additional 1/3 vesting on each subsequent anniversary until the Options are fully vested on 25 January 2018. The Options have an expiry date of 25 January 2020. After this grant, there were 34,752,000 Options outstanding, representing 3.77% of the issued and outstanding common shares of Falcon.

Generally, the Group's total assets, exploration and evaluation costs, working capital and total shareholders' equity fluctuate in proportion to one another until such time as the Group completes additional financing.

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LIQUIDITY AND CAPITAL RESOURCES

Going Concern

For the year ended 31 December 2014, the Group incurred a loss of $31.8 million and had operating cash outflows of $5.3 million had a retained deficit of $382.3 million. For the year ended 31 December 2013, the Group incurred additional losses of $3.6 million, had operating cash outflows of $5.3 million and a retained deficit of $350.6 million.

As at 31 December 2014 the Group had a cash balance including cash and cash on deposit of $14.8 million.

Having given due consideration to the cash requirements of the Group and having received the A$20 million for the Australian farm-out, the Board has a reasonable expectation that the Group will have adequate resources to continue in operational existence for the foreseeable future. For this reason, the Board continues to adopt the going concern basis in preparing this financial information which assumes the Group will be able to meet its liabilities as they fall due for the foreseeable future.

Working Capital

Cash and cash on deposit as at 31 December 2014 was $14.8 million, an increase of $6.4 million from $8.4 million as at 31 December 2013. Working capital as at 31 December 2014 increased to $13.2 million from working capital of $6.2 million as at 31 December 2013.

The increase to cash and cash equivalents was the result of net cash generated from investing activities of $5.7 million and net cash used in operating activities of $5.3 million.

Accounts Receivable

Current accounts receivable as at 31 December 2014 were $0.5 million, which includes $0.2 million receivable and prepayments of $0.3 million.

Accounts Payables and Accrued Expenses

Accounts payable and accrued expenses as at 31 December 2014 were $1.5 million which includes $0.3 million for accounts payable and $1.2 million accrued expenditure.

Capital Expenditures

For the period ended 31 December 2014 the following expenditure commitments were incurred.

Australia - Beetaloo Basin, Northern Territory, Australia

Expenditures were incurred in negotiating the Beetaloo Basin farm-out agreement, as completed on 21 August 2014. The Group is planning a 9 well drilling programme with its farm-out partners. The details are as follows:

- Farminees will pay for the full cost of completing the first five wells estimated at A$64 million, and will fund any cost overruns. This work is expected to be completed within two years (2015 – 2016).
- Farminees to pay the full cost of the following two horizontally fracture stimulated wells, 90 day production tests and micro seismic with a capped expenditure of A$53 million, any cost overrun funded by each party in proportion to their working interest. This work programme is expected to be undertaken in 2017.
- Farminees to pay the full cost of the final two horizontally fracture stimulated wells and 90 day production tests capped at A$48 million, any cost overrun funded by each party in proportion to their working interest. This work programme is expected to be undertaken in 2018.

South Africa - Karoo Basin, South Africa

On granting of an approved exploration right in South Africa, the Group will be required to make a payment to the South African government of approximately $0.7 million.

Hungary - Makó Trough, Hungary
As at 31 December 2014, the Group's cumulative expenditures for the Production License and Exploration Licenses, including the acquisition, seismic testing, drilling of exploratory wells, and initial testing and completion of wells, was approximately $245 million.

At 31 December 2014, the Group had forward looking deposit commitments regarding its Hungarian exploration licences for approximately $2.4 million.

The Group is not planning any independent technical operations in Hungary, and as such no material capital expenditures are expected.

Lease commitments

The Group has entered into lease agreements for office space in:

- Denver, Colorado, expiring April 2015;
- Budapest, Hungary expiring October 2015;
- Dublin, Ireland, with a break clause exercisable in October 2017; and

The Group is obligated to pay the following minimum future rental commitments under non-cancelable operating leases at 31 December 2014 and 31 December 2013 during the following periods:

	As at 31 December 2014 $'000	As at 31 December 2013 $'000
2014	**-**	533
2015	**298**	284
2016	**118**	120
2017	**98**	100
Thereafter	**-**	-
Total	**514**	1,037

Debt and Equity Capital

The availability of debt and equity capital, and the price at which additional capital could be issued will be dependent upon the success of the Group's exploration activities, and upon the state of the capital markets generally.

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DISCLOSURE OF OUTSTANDING SHARE DATA

The following is a summary of the Company's outstanding share data as at 31 December 2014 and 28 April 2015:

Class of securities	31 December 2014	28 April 2015
Common shares	921,537,517	921,537,517
Stock options	30,085,333	34,752,000
Hess warrant(i)	10,000,000	10,000,000

Note:
(i) In April 2011, Falcon Australia entered into a joint venture with Hess Australia (Beetaloo) Pty. Ltd ("**Hess**"). Under the terms of the agreement, Hess was granted a warrant to acquire 10,000,000 common shares in the capital of Falcon exercisable from 14 November 2011 through 13 January 2015 at an exercise price of CDN$0.19 per share (the "**Hess Warrant**"). In June 2014, the term of the Hess warrant was extended to 13 January 2020 to facilitate the termination of the Participation Agreement and Joint Operating Agreements with Hess. All other terms remained unchanged.

LEGAL MATTERS

The Company may, from time to time, be involved in various claims, lawsuits, disputes with third parties, or breach of contract incidental to the operations of its business. The Company is not currently involved in any claims, disputes, litigation or other actions with third parties which it believes could have a material adverse effect on its financial condition or results of operations.

TRANSACTION WITH NON - ARMS LENGTH PARTIES AND RELATED PARTY TRANSACTIONS

The following are the related party transactions which occurred during the period:

Dr. György Szabó Consulting Agreement
On 27 February 2009, Dr. György Szabó (former Executive Director and Co-Managing Director of Falcon –TXM) entered into a consulting agreement (the "**GS Consulting Agreement**") with Falcon TXM ("**TXM**"), pursuant to which Dr. Szabó agreed to act as Managing Director of TXM, to perform certain oil and gas services for TXM and to not compete directly or indirectly with TXM during his employment with TXM. Dr. Szabó was paid a monthly fee of $5,000. The GS Consulting Agreement contained standard confidentiality provisions. TXM could terminate the GS Consulting Agreement at any time, with or without cause, for any lawful reason whatsoever, upon TXM providing Dr. Szabó with sixty days' prior written notice. The GS Consulting Agreement expired on 31 December 2009, however Dr. Szabó continued to provide general managerial services to TXM and to receive the same monthly fee. Dr. Szabó was paid $59,000 pursuant to the GS Consulting Agreement in the year ending 31 December 2014. The GS Consulting Agreement is now terminated with an effective date of 31 December 2014.

P&S Consulting Agreement
On 4 May 2005, P&S Mérnöki Kereskedelmi-Tanácsadó Bt. ("**P&S**") entered into a consulting agreement (the "**P&S Agreement**") with TXM, pursuant to which P&S agreed to provide certain consulting services to TXM in connection with TXM's objectives of drilling wells on the Makó and Tisza licences. The P&S Agreement was amended on 28 November 2005 and further amended on 1 June 2006, 1 January 2008, 1 January 2009 and 1 April 2010. P&S is wholly-owned by a family member of Dr. György Szabó, a current Director of the Company. Under the terms of the P&S Agreement, TXM was obligated to pay P&S a monthly services fee of HUF 750,000. The P&S Agreement contained standard confidentiality provisions and provides that P&S shall not compete with TXM during the term of the P&S Agreement.

TXM could have terminated the P&S Agreement at any time, with or without cause, for any lawful reason whatsoever, upon TXM providing P&S with 30 days, prior written notice. TXM and P&S further amended the terms of the P&S Agreement by oral agreement. Pursuant to the amended P&S Agreement, P&S was paid a monthly fee of $6,057 (effective 1 February 2014) plus reasonable expenses incurred by Dr. Szabó as an employee of P&S, such amounts thereafter paid to Dr. Szabó from P&S. P&S was paid $75,000 pursuant to the agreement in the year ending 31 December 2014. The P&S Agreement is now terminated with an effective date of 31 December 2014.

Senzus Kft
On 1 January 2013, Dr. Gábor Bada verbally agreed the terms on which he was to provide geological services to TXM as a consultant. Dr. Gábor Bada (Head of Technical) will be paid a yearly consultancy fee of $20,000 in relation to this work. Dr. Bada invoices TXM through his company Senzus Kft. Dr. Gábor Bada received a consultancy fee of $20,000 through his company in the year ended 31 December 2014.

Oakridge Financial Management Inc.
The Group has engaged Oakridge Financial Management Inc. to assist in submitting returns to the Canadian Revenue Agency. Mr. Greg Smith, a current director of Falcon, is the sole shareholder in Oakridge Financial Management Inc.. The Group has incurred costs of approximately CDN$1,060 to Oakridge Financial Management Inc. during the year ended 31 December 2014.

OFF-BALANCE SHEET ARRANGEMENTS AND PROPOSED TRANSACTIONS

The Company does not have any off-balance sheet arrangements, other than operating leases (as disclosed on page 26 in this document), payments with regards overriding royalties as disclosed within section "Overriding Royalty Beetaloo Basin exploration permits" on page 8, and forward looking deposit commitments regarding its Hungarian exploration license as disclosed on page 26 of this document. The Company has no proposed transactions.

FINANCIAL INSTRUMENTS AND OTHER INSTRUMENTS

Derivative financial instruments

Derivatives (including embedded derivatives) are initially recognised at fair value of the date a derivative contract is entered into and subsequently re-measured at their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Group has not designated any derivatives as hedges as at 31 December 2014 or 31 December 2013.

Embedded derivatives are separated from the host contract and accounted for separately if the economic characteristics and risks of the host contract and the embedded derivative are not closely related. Changes in the fair value of separable embedded derivatives are recognised immediately in the statement of operations and comprehensive loss.

The Group has / had the following financial instruments – warrants and the conversion feature of the Group's debentures. The Group has not entered into contract for "other instruments" during 2014. The Group has no "Other Instruments" as at 31 December 2014 or 31 December 2013.

Warrants

Warrants which do not meet the criteria to be classified as an equity instrument are classified at fair value through the statement of operations and comprehensive loss and are recorded on the statement of financial position at fair value. Transaction costs are recognised in the statement of operations and comprehensive loss as incurred.

The fair value of the warrant and the incentive stock options granted to employees is calculated using a Black Scholes option pricing model. Measurement inputs include share price on measurement date, exercise price of the instrument, expected volatility (based on weighted average historic volatility adjusted for changes expected due to publicly available information), weighted average expected life of the instruments (based on historical experience and general option holder behavior), expected dividends, and the risk-free interest rate (based on government bonds). A forfeiture rate is estimated on the grant date and is adjusted to reflect the actual number of incentive stock options that vest.

The composition of the derivative liabilities as at 31 December 2014 and 31 December 2013, and the changes therein for the periods then ended, are as follows:

	Convertible Debt Conversion Feature $'000	Private Placement Warrants $'000	Hess Warrant $'000	Total $'000
At 1 January 2013	26	4,505	787	5,318
Derivative gains - debt conversion feature	(26)	-	-	(26)
Derivative gains - outstanding warrants	-	(3,556)	(339)	(3,895)
At 31 December 2013	-	949	448	1,397
Derivative (gains) / loss – outstanding warrants	**-**	**(949)**	**66**	**(883)**
At 31 December 2014	**-**	**-**	**514**	**514**

The terms of the warrant are as follows:

Warrant issue	Date of issue	Number of common shares issuable under warrant	Exercise Price CDN$	Proceeds from warrant* CDN$'000	Expiry date
Hess Warrant	13 July 2011	10,000,000	0.19	1,900	13 January 2020
Total		**10,000,000**		**1,900**	

*Proceeds from warrant are subject to the warrant holders exercising their warrants.

NEW ACCOUNTING PRONOUNCEMENTS

Several new standards and amendments to existing standards and interpretations, which have been issued by the IASB, and which are expected to apply to the Group are not yet effective and have not been applied in preparing these financial statements. The Group does not expect adoption of these new standards and interpretations, to have a material impact on the financial statements.

Pronouncement	Nature of change
Amendments to IFRS 10 'Consolidated Financial Statements' and IAS 28 'Investments in Associates and Joint Ventures' (i) (ii)	The amendments address an inconsistency between the requirements in IFRS 10 and those in IAS 28 (2011), in dealing with the sale or contribution of assets between an investor and its associate or joint venture. The main consequence of the amendments is that a full gain or loss is recognised when a transaction involves a business (whether it is housed in a subsidiary or not). A partial gain or loss is recognised when a transaction involves assets that do not constitute a business, even if these assets are housed in a subsidiary.
Amendment to IFRS 11 'Accounting for Acquisitions of Interests in Joint Operations' (i) (ii)	IFRS 11 addresses the accounting for interests in joint ventures and joint operations. The amendments add new guidance on how to account for the acquisition of an interest in a joint operation that constitutes a business. The amendments specify the appropriate accounting treatment for such acquisitions

Pronouncement	Nature of change
Amendments to IAS 16 'Property, Plant and Equipment' and IAS 38 'Intangible Assets' (i) (ii)	IAS 16 and IAS 38 both establish the principle for the basis of depreciation and amortisation as being the expected pattern of consumption of the future economic benefits of an asset. The IASB has clarified that the use of revenue-based methods to calculate the depreciation of an asset is not appropriate because revenue generated by an activity that includes the use of an asset generally reflects factors other than the consumption of the economic benefits embodied in the asset. The IASB also clarified that revenue is generally presumed to be an inappropriate basis for measuring the consumption of the economic benefits embodied in an intangible asset. This presumption, however, can be rebutted in certain limited circumstances.
Amendments to IAS 27 'Separate financial statements' (i) (ii)	These amendments will allow entities to use the equity method to account for investments in subsidiaries, joint ventures and associates in their separate financial statements. The amendments will help some jurisdictions move to IFRS for separate financial statements, reducing compliance costs without reducing the information available to investors.
IFRS 15 'Revenue from Contracts with Customers' (ii) (iii)	IFRS 15 specifies how and when an IFRS reporter will recognise revenue as well as requiring such entities to provide users of financial statements with more informative, relevant disclosures. The standard provides a single, principles based five-step model to be applied to all contracts with customers.
IFRS 9 'Financial instruments' (ii) (iv)	IFRS 9 'Financial instruments', addresses the classification, measurement and recognition of financial assets and financial liabilities. The complete version of IFRS 9 was issued in July 2014. It replaces the guidance in IAS 39 that relates to the classification and measurement of financial instruments. IFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortised cost, fair value through OCI and fair value through P&L. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. Investments in equity instruments are required to be measured at fair value through profit or loss with the irrevocable option at inception to present changes in fair value in OCI without recycling to the income statement. IFRS 9 contains a new expected credit losses model that replaces the incurred loss impairment model used in IAS 39. For financial liabilities there are no changes to classification and measurement except for the recognition of changes in own credit risk in other comprehensive income, for liabilities designated at fair value through profit or loss. IFRS 9 relaxes the requirements for hedge effectiveness by replacing the bright line hedge effectiveness tests. It requires an economic relationship between the hedged item and hedging instrument and for the 'hedged ratio' to be the same as the one management actually uses for risk management purposes.

(i) Effective Date: Financial periods beginning on or after 1 January 2016.

(ii) Impact: These amendments are not expected to have a significant impact on the financial position of the Group.

(iii) Effective Date: Financial periods beginning on or after 1 January 2017.

(iv) Effective Date: Financial periods beginning on or after 1 January 2018.

CRITICAL ACCOUNTING ESTIMATES

Preparation of financial statements pursuant to IFRS requires a significant number of judgemental assumptions and estimates to be made. This impacts the income and expenses recognised in the statement of operations and comprehensive loss together with the valuation of the assets and liabilities in the statement of financial position. Such estimates and judgements are based on historical experience and other factors, including expectation of future events that are believed to be reasonable under the circumstances and are subject to continual re-evaluation. It should be noted that the impact of valuation in some assumptions and estimates can have a material impact on the reported results.

The following are key sources of estimation uncertainty and critical accounting judgements in applying the Group's accounting policies:

Critical judgments
(i) Exploration and evaluation assets
The carrying value of exploration and evaluation assets was $39.6 million at 31 December 2014 (2013: $74.5 million). The Group has determined that there are no indicators of impairment present in accordance with IFRS 6 "Exploration for and evaluation of mineral interests" regarding its Australian exploration and evaluation assets. It was concluded indicators of impairment existed relating to its exploration and evaluation assets in Hungary and thus impairment evaluations were performed on these assets.

Management's conclusion on the facts and circumstances regarding its Australian and Hungarian assets required judgment based on experience and the expected progress of current exploration and evaluation activities and the successful completion of farm-out projects.

The critical judgments were as follows:

Australia
On 21 August 2014, Falcon Australia completed its farm-out agreement and joint operating agreement with Origin and Sasol, (collectively the **"Farminees**") each farming into 35% of Falcon Australia's exploration permits in the Beetaloo Basin, Australia.

The transaction details were:
- Falcon Australia received A$20 million cash from the farminees.
- Farminees to carry Falcon Australia in a nine well exploration and appraisal program over 2014 to 2018 inclusive.
- Drilling/testing specifically planned to take the project towards commerciality. Falcon Australia retains a 30% interest in the Permits.
- Farminees will pay for the full cost of completing the first five wells estimated at A$64 million, and will fund any cost overruns. This work is expected to be completed within two years (2015 – 2016).
- Farminees to pay the full cost of the following two horizontally fracture stimulated wells, 90 day production tests and micro seismic data collection with a capped expenditure of A$53 million, any cost overrun funded by each party in proportion to their working interest. This work programme is expected to be undertaken in 2017.
- Farminees to pay the full cost of the final two horizontally fracture stimulated wells and 90 day production tests capped at A$48 million, any cost overrun funded by each party in proportion to their working interest. This work programme is expected to be undertaken in 2018.
- Farminees may reduce or surrender their interests back to Falcon Australia only after:
  - The drilling of the first five wells or
  - The drilling and testing of the next two horizontally fracture stimulated wells.

Preparations for the Group's 2015 Australian drilling programme, comprising the initial three wells in the Beetaloo Basin are at an advanced stage. 2014 saw significant progress of the agreed work programme with the Farminees with the objective of moving the project towards commerciality. A comprehensive technical evaluation undertaken in 2014 has enabled the selection of appropriate well locations to penetrate oil mature through to dry gas mature sections of the Middle Velkerri shale play. The principal objectives of the 2015 drilling programme are to:

- penetrate the Middle Velkerri formation to assess hydrocarbon saturation and reservoir quality;
- evaluate oil versus gas maturity and determine the most prospective areas and depth window;
- provide wide geographical cover of the target Middle Velkerri formation; and
- collect data points for subsequent vertical/horizontal drilling, completion and production testing.

Formation evaluation and reservoir characterisation will be carried out from these initial three wells through petrophysical interpretation, core analysis, geomechanical studies and stimulation design.

Tendering and contracting for the rig and key well services, and recruiting additional project resources are ongoing. Spudding of the first well is expected in mid-2015 subject to weather conditions as the wet season ends. Two further wells will be drilled back-to-back before the dry season ends in 2015.

The work programme supports the carrying value of the asset and there are no indicators of impairment present.

Hungary

In January 2013, the Group and Naftna industrija Srbije jsc ("**NIS**") agreed to a three-well drilling programme targeting the relatively shallow Algyő Play with a deadline for completion of work extended to the 31 December 2014 from the originally agreed date of July 2014.

Drilling operations on Kútvölgy-1, the first joint well between NIS and the Group, were completed in July 2013, the well having reached total depth ("TD") of 3,305 metres. Testing indicated that the well experienced improved recovery from certain intervals however well production did not meet commercial rates thus was discontinued with the well being plugged and abandoned.

The well testing operations on the second well, Besa-D-1 were also completed. The testing of two sand intervals, both part of the tight turbiditic sequence in the lower Algyő Formation, indicated that well production did not meet commercial rates and the well is also being plugged and abandoned.

As of 31 December 2014, NIS has only drilled and tested two wells.

Based on the above indicators, an impairment test was completed on the assets in the Hungarian cost pool. The test demonstrated that the estimated recoverable amount of the E&E and PPE in the pool was insufficient to cover the carrying amount of these assets. The principal impairment indicator was the Company's ability to finance future exploration to commercially develop the asset. The capitalised value of the Group's Hungarian assets has been impaired by $26.5 million (which includes $5.1 million which was classified as PPE) at 31 December 2014.

Critical estimates

(ii) Going concern
The consolidated financial statements have been prepared on the going concern basis. In considering the financial position of the Group, the Group has considered the forecasted operating and capital expenditures for the foreseeable future and cash flows relating to its financing. Forecasting those cash flows requires significant judgment when estimating expected operating expenditure, capital expenditure, decommissioning of suspended wells, expected monies to be received from potential farm-in partners and proceeds from share issuances.

(iii) Decommissioning Provision
The decommissioning provision represents the Group's best estimate of the costs involved in the various exploration and production licence areas to return them to their original condition in accordance with the licence terms. These estimates include certain management assumptions with regard to future costs, inflation rates and discount rates.

MANAGEMENT'S RESPONSIBILITY FOR MD&A

The information provided in this MD&A is the responsibility of management. In the preparation of this MD&A, estimates are sometimes necessary to make a determination of future values for certain assets or liabilities. Management believes such estimates have been based on careful judgments and have been properly reflected in this MD&A.

The audit committee has reviewed the MD&A with management, and has reported to the Board. The Board has approved the MD&A as presented.

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