

Swift Energy Company 2012 Annual Report

Letter to Stockholders

The future of Swift Energy Company has never been more promising. Our past success in our South Texas operations will enable us to maintain a strong drilling program in that core area during 2013 and beyond, with a continued emphasis on liquids-rich production. And as part of our on-going planning for the future, we have developed three strategic opportunities that we expect to advance significantly this year. Two are in our other core areas of operation, Southeast Louisiana and Central Louisiana/East Texas. The third is in southwestern Colorado, where we expect to spud our first well in the Niobrara shale during the second half of this year. These initiatives hold the promise of adding gamechanging growth to our company in the years ahead. With the resources we now have at our disposal—our properties, financial flexibility, technical expertise, and management experience—we are confident we are in an excellent position to carry out these projects as we continue achieving our mission of balanced, sustainable growth in production and proved reserves.



Crude oil and other liquids represented 53% of Swift's production in the fourth quarter of 2012 and 48% of its year-end proved reserves.

In 2012, we laid the foundation for our future success. In particular, our emphasis on liquids-rich projects in the Eagle Ford shale and Olmos sand in South Texas has yielded higher-margin production and increased liquids reserves from that area. Company-wide, crude oil and other liquids comprised 53% of our total production in the fourth quarter of 2012, and by year-end we had increased our crude oil reserves by 40% and our natural gas liquids reserves by 90% over 2011 levels. We also secured by production the majority of the leases associated with these higher-margin projects.

In addition, we took steps during the year to improve our financial liquidity in order to weather the ups and downs inherent in our industry. Along the way, we improved efficiencies, found ways to cut costs, and honed our technological expertise. Because of these achievements, each of our core areas still has considerable potential to grow.

We are now ready to apply our knowledge and experience to the three strategic growth initiatives we are pursuing in 2013, each of which is prospective for crude oil development. We have

committed 5% to 10% of this year's capital budget to these three initiatives. None of them will immediately impact our production volumes significantly, but any one of them, if successful, will open a new period of growth for our company in 2014 and beyond.

The first initiative is already under way. It consists of applying the horizontal drilling technology we have used in South Texas to the Wilcox formation in our South Bearhead Creek field in Beauregard Parish, Louisiana. We spudded our first horizontal well in the Wilcox earlier this year. The second initiative is our expansion to southwestern Colorado, where we anticipate spudding a horizontal test well in the Niobrara by year-end. The third is drilling an exploratory well to a sub-salt formation lying beneath our Lake Washington field in Plaquemines Parish, Louisiana. We expect to see the results of the Lake Washington project within 24 months.

2012 Achievements



In 2012, Swift Energy began using walking rig technology that enables rigs to be moved from one drilling location to another without having to be dismantled. This reduces rig down time and lowers costs.

As we were laying the groundwork for future growth, we set all-time record highs in 2012 for both annual U.S. production volumes and year-end reserves. Our oil and gas production climbed to 11.7 million barrels of oil equivalent (Boe), up 11% from the previous year, and our year-end reserves rose to 192 million Boe, an increase of 20%. Notably, this was the second year in a row in which we increased reserves by 20%, and in the process our year-end 2012 crude oil and natural gas liquids reserves rose to approximately 48% of our total reserves, up significantly from 36% at year-end 2011.

We did not accomplish these milestones without challenges. We were confronted with price declines of 35% for dry natural gas and 33% for natural gas liquids that caused our total revenues to fall 7% to \$557 million in 2012. Nationwide, natural gas prices collapsed in the spring of 2012 following the warmest winter heating season on record, and prices for natural gas liquids plunged as demand growth failed to keep up with rapidly expanding supplies. Oil prices remained relatively flat, with Swift Energy continuing to receive premium average prices of \$106 per barrel, compared to average spot prices for West Texas Intermediate crude oil of \$94 per barrel over the same time frame.

Our cash flows from operations also declined in 2012, falling 16% to \$315 million, and our net income from continuing operations decreased 75% to \$21 million. Both measures were impacted by the fall in product prices as well as by a rise in our costs and expenses, which totaled \$521 million in 2012, up 12% from 2011. This increase in our costs and expenses was driven primarily by increasing production in the highly competitive South Texas area, as well as by greater workover costs in Southeast Louisiana. Our costs and expenses per unit of production, however, were about the same as in the previous year.

To help finance the cash flow needed to execute our plans, we accessed the debt market in October 2012. We issued \$150 million of notes with a yield of less than 7%. We used the proceeds to pay down the balance on our credit facilities and to fund current activity. In addition to this debt offering, we extended our credit facility through November 2017, enhanced the tiered interest-rate terms of the agreement, and increased our borrowing base and commitment amount to \$450 million. The combination of these activities ensures that we are maintaining the liquidity necessary to continue to execute our strategic plans.

Out in the field, we achieved a 100% drilling success rate for the 71 wells we drilled in our three core areas in 2012, all of which were development wells. The majority of these wells (55 of 71) were in our South Texas core area, which holds 82% of our proved reserves and accounted for 73% of our 2012 production. Of these, 22 wells were in the Eagle Ford shale formation in our Artesia Wells field in La Salle County, and another 22 were in the Eagle Ford shale in our AWP field in McMullen County, three as joint venture wells. Nine wells were in the tight Olmos sand in our AWP field, and two were in the Eagle Ford shale in our Fasken field in Webb County. As we conducted this South Texas drilling program, we increasingly focused on liquids, at the same time securing leaseholds for the majority of our liquids-rich acreage.



Among Swift's strategic growth initiatives, the company is pursuing a deep sub-salt prospect beneath its Lake Washington field, where operations take place in shallow inland waters.

All 55 of the South Texas wells were drilled horizontally and completed with multi-stage fracturing, and as the drilling program proceeded we introduced several advanced technologies to improve efficiencies. We initiated the use of a walking rig that is more easily moved from one drilling location to another. We conducted our first multi-well pad drilling project, in which four wells in close proximity were drilled in succession on a common pad. We also introduced zipper fracturing, in which adjacent wells are hydraulically fractured simultaneously or in sequence.

The precise locations for almost all of the South Texas wells were determined using three-dimensional datasets that we have collected, merged, and processed for that area. During 2012, we further refined our three-dimensional seismic analysis capability to better locate the most productive pay zone for each well, targeting the most brittle section of the formation for optimum fracturing. We also enhanced our well designs and applied lessons learned that were often unique within each area. In addition, we successfully negotiated less constrictive, shorter-term contracts for drilling and completion services and equipment. We reduced the number of days needed to drill a well, increased the number of hydraulic fracture stages we can complete per month, and lowered the overall cost per stage for hydraulic fracturing.

Another important endeavor in South Texas during 2012 was the further delineation of our high-value Eagle Ford acreage with respect to well spacing. We conducted down-spacing tests in the Artesia Wells and AWP fields that affirmed the potential for increased amounts of drilling locations in these liquids-rich areas. Altogether, our efforts to improve our drilling and completion methods in South Texas in 2012 allowed us to improve efficiencies, keep per-unit costs down, and substantially increase our reserves. By year-end, we had increased our South Texas liquids reserves by 122%.

In the Lake Washington field in our Southeast Louisiana core area, we drilled 10 development wells and performed 20 recompletions in 2012, along with numerous production enhancement operations such as sliding sleeve changes. We also drilled one well in our Bay de Chene field. In our Central Louisiana/East Texas core area, we drilled four non-operated wells and one operated well as part of our joint venture in the Burr Ferry field with a large independent oil and gas producer.

2013 Initiatives



By utilizing zipper fracking, Swift Energy can hydraulically fracture multiple wells in less time, increasing the number of fracking stages completed per month.

In 2013, we plan to scale back our drilling activity in order to balance capital expenditures with expected cash flows given the current low pricing environment for natural gas and natural gas liquids. Our 2013 capital budget is \$440 to \$480 million, a reduction of 30% to 40% from 2012 levels. As a result, we anticipate that our year-end 2013 reserves will increase by 7% to 12% and

that our 2013 production will rise by up to 3%, with crude oil and other liquids comprising about half of our year-end reserves and 50% to 55% of our production.

During 2013, four types of activities will likely have the most immediate impact on growth. One is our continued focus on drilling liquids-rich wells in identified brittle areas of the Eagle Ford formation in South Texas. The second is our Eagle Ford down-spacing tests. A third is potential initiatives for accelerating our South Texas drilling program. The fourth is our horizontal drilling in the Wilcox formation. Meanwhile, we will also move forward in 2013 with our two longer-term strategic growth initiatives: our Niobrara shale acreage in southwestern Colorado and our sub-salt prospect beneath the Lake Washington field in Southeast Louisiana.

As part of our emphasis on liquids-rich projects, we are concentrating the majority of our 2013 drilling activity in our Eagle Ford acreage in our South Texas core area. Specifically, we are pursuing higher value, but lower volume, development wells that are prospective for crude oil, condensate, and natural gas liquids. This core area is also where we are closely monitoring the results of our two down-spacing tests undertaken last year. Initial results for Artesia Wells, which was a 60-acre down-spacing test, and AWP, which was a 50-acre down-spacing test, appear to confirm the concept of well spacing that is tighter than our previous assumption of 80 acres per well. We are currently projecting that we could potentially increase our Eagle Ford drilling locations by 30% or more as a result of these tests. Additional tests may be conducted later this year mainly targeting liquids-rich areas, though we also plan a two-well downspacing test in our Fasken field, which is prospective for natural gas.

As a result of the tighter spacing of Eagle Ford wells indicated by these preliminary results, we have created a portfolio of crude oil and other liquids-rich opportunities that would have an enhanced value if developed at a faster pace than our internally generated cash flows will allow. This has led us to consider options for accelerating production from our highest-value Eagle Ford acreage in order to bring forward meaningful net present value for our reserves.



Swift has three core areas of operation: South Texas, Southeast Louisiana, and Central Louisiana/East Texas. One of Swift's three strategic growth initiatives for 2013 is located outside its core areas in the Niobrara shale in southwestern Colorado. [Note: [Click here to see a larger version of the above map.](#)]

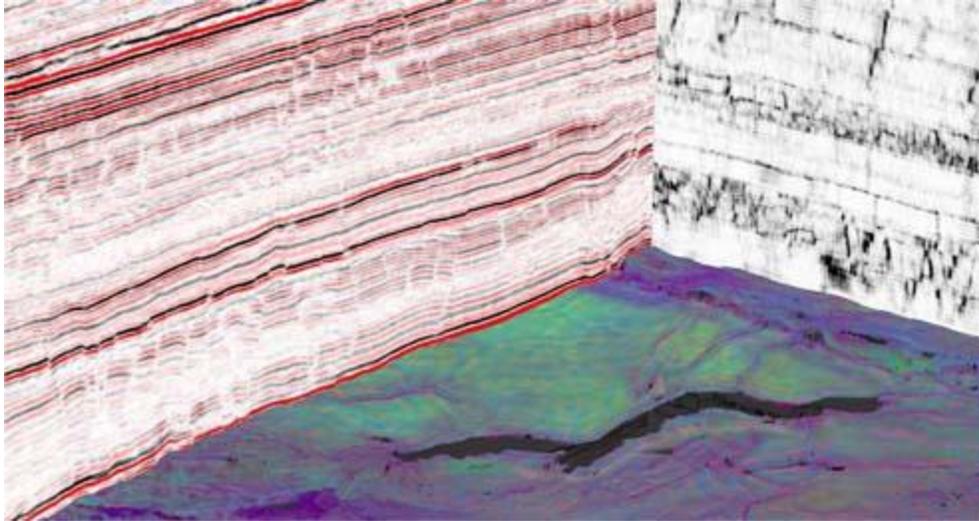
We also believe we can add value through improved performance of our existing wells. Now that we have delineated much of our highest-value acreage in the Eagle Ford, we can make efficiency gains in our production, maintenance, and optimization operations that will rival the efficiency gains we have achieved in our drilling and completion methods over the past several years.

Among our strategic opportunities in 2013, our prospect in the Wilcox formation in the South Bearhead Creek field has the most immediate potential for growth. We have previously had success drilling vertical oil wells in this field, and we believe that this oil-rich formation is a natural fit for the horizontal drilling and multistage fracturing techniques we have successfully honed in South Texas. We anticipate favorable results with the first horizontal well we spudded in this formation earlier this year, and should that occur, we plan to move forward with additional activity before year-end. We believe we can develop our inventory in this field in a fairly self-funding manner because of the higher margin nature of the expected production. Our Wilcox prospects could potentially hold up to 20 to 28 million gross Boe of unbooked resources.

In southwestern Colorado, where we plan to spud our first horizontal well in the Niobrara shale formation in the second half of the year, we hold leaseholds covering over 50,000 net acres. While projects in this part of the country require longer lead times, successful testing would potentially expose our company to 125 to 200 million gross Boe of unbooked resources. As we prepare to drill this first well, we have already conducted detailed analysis of the basin, its production history, and the current activity by other operators in the area. This groundwork will enable us to move forward more quickly if we achieve successful results.

The project before us that perhaps has the greatest rewards, and the greatest risks, is our sub-salt prospect in our Lake Washington field in Louisiana, where we plan to drill a deep exploratory well within 24 months. Based on our initial analysis, it is our belief that a successful exploratory test in this crude oil prospect could very likely discover a "new Lake Washington" beneath our existing assets. We are currently considering conducting this deep sub-salt test with a highly recognized, experienced industry partner. The time line of this initial exploratory well will depend on whether we decide, in consultation with any future partner, to conduct further seismic evaluation and on the final determination of how deep we plan to drill the test well. This prospect could potentially hold 200 to 350 million gross Boe of unbooked resources.

Building on Past Success



Using merged three-dimensional seismic and geologic databases, Swift Energy can target the most brittle zones in shale formations, optimizing fracking effectiveness and well performance.

Here at Swift Energy, we find ourselves in the enviable position of having more projects in our portfolio than we can pursue in a timely fashion. The prospects for our company—and for the U.S. oil and gas industry as a whole—are today the most promising that they have been in decades as advanced technologies unlock unconventional resources once thought uneconomical.

We are confident in our ability to tackle the opportunities before us because of our long track record in applying the two primary technologies that have merged to bring about the current revolution in our industry. From our founding in 1979, we have used hydraulic fracturing technology, applying it to our first wells in the West Virginia mountains. In 1989 we began applying and perfecting our "fracking" expertise on hundreds of vertical wells in the tight Olmos sand in our AWP field in South Texas. A few years later, we initiated horizontal drilling in a decade-long program in the Austin Chalk trend in and around Fayette County, Texas. By 1998, we were applying the knowledge gained from that program to the Austin Chalk trend in our Central Louisiana/East Texas area. In 2008, we combined these two technologies to drill our first-ever hydraulically fractured horizontal well in the AWP field's Olmos sand. A year later, we initiated a highly successful and still on-going horizontal drilling program in the Eagle Ford shale that lies below the Olmos. To date, we have drilled more than 100 successful hydraulically fractured horizontal wells in South Texas.

Now in 2013, after having fine-tuned these technologies in several existing fields, we are introducing them to our acreage in the Wilcox formation and the Niobrara shale. Meanwhile, our exploratory prospect in the Lake Washington field lies in a property where we have used three-dimensional seismic technology to achieve tremendous results since taking over operation of the property in 2001. We believe that the combination of our technological expertise, built over decades, and our ample portfolio of exciting opportunities creates a promising environment for fulfilling our mission of growth in production and reserves over the long term. In 2013 and beyond, we intend to take all of these advantages and turn them into value for our shareholders.

Terry E. Swift
Chairman and Chief Executive Officer,
Swift Energy Company