

## Eastern Star Gas (ESG.AX / ESG AU)

### UPGRADE RATING

Rating	(from Neutral) <b>OUTPERFORM* [V]</b>
Price (21 Jul 09, A\$)	1.00
Target price (A\$)	(from 0.95) 1.25 <sup>†</sup>
Market cap. (A\$m)	770.78
Yr avg. mthly trading (A\$m)	36
Last month's trading (A\$m)	82
<b>Projected return:</b>	
Capital gain (%)	25.0
Gross yield (%)	—
Total return (%)	25.0
52-week price range (A\$)	1.02 - 0.20

\* Stock ratings are relative to the relevant country benchmark.

<sup>†</sup>Target price is for 12 months.

[V] = Stock considered volatile (see Disclosure Appendix).

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### Upgraded Target Price

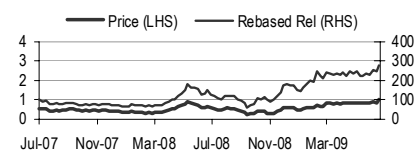
- **Event:** Post the recent Santos acquisition of Gatar's acreage and a 19.9% equity interest in ESG, we have reviewed our valuation and Target Price, upgrading both to \$1.25/share (from 0.95). This calculates to an OUTPERFORM rating (from Neutral).
- **View:** We see the company as a leveraged play on the NSW gas and power markets and although the CSG industry is significantly less developed than in Queensland, ESG, we think, is likely to demonstrate strong reserves and production growth over the next 12–24 months.

The 2009 work programme is designed to continue the exploration and appraisal of PEL 238 and increase the declared 2P reserves. As of the last detailed report on the multi-lateral production pilots (June-18) ESG reported that the Bibblewindi pilots had reached a flow rate of 0.25mmcf/d, with water production steady at approximately 3.5-4kbpd...we see these results as extremely positive but await final sustainable flow rates.

We maintain our view that there are still consolidation opportunities within the CSG space. The interconnectedness of east coast gas markets suggests to us that even NSW gas volumes could have significant attraction as an aggregation play...and STO has demonstrated that case.

- **Risks:** The critical risk to our outlook and forecasts is delivery of commercial outcomes from the Narrabri multi-lateral pilots. Partnering now with Santos, we see as adding significant additional commercial options for ESG accessible within the STO portfolio or leveraging off that company's marketing expertise.
- **Valuation:** Based on a DCF-derived NAV, we value Eastern Star Gas at A\$1.25/share, a 25% premium to the 21 July closing price of A\$1.00/share.

#### Share price performance



The price relative chart measures performance against the Australia S&P/ASX 200 index which closed at 4050.7 on 21/07/09

On 21/07/09 the spot exchange rate was A\$1.24/US\$1

Performance Over	1M	3M	12M
Absolute (%)	18.3	33.3	66.7
Relative (%)	13.9	21.0	106.2

#### Financial and valuation metrics

Year	06/08A	06/09E	06/10E	06/11E
Revenue (A\$m)	0.4	1.0	12.0	26.8
EBITDAX (A\$m)	-5.8	-5.3	2.4	11.7
EBIT (A\$m)	-6.3	-6.4	1.6	10.0
Net income (A\$m)	-4.2	-3.8	2.9	5.1
EPS (CS adj., Ac)	-0.62	-0.49	0.35	0.61
Change from previous EPS (%)	n.a.	—	—	—
Consensus EPS (Ac)	n.a.	-0.30	—	1.10
EPS growth (%)	n.a.	n.a.	n.a.	71.0
P/E (x)	NM	NM	282.0	165.0
Dividend (Ac)	—	—	—	—
Dividend yield (%)	—	—	—	—
EV / EBITDAX (x)	-126.14	-136.25	327.98	70.26
Net debt/equity (%)	net cash	net cash	3.2	33.0

Source: Company data, ASX, Credit Suisse estimates, \* Adj. for goodwill, notional interest and unusual items. Relative P/E against ASX/S&P200 based on pre GW in AUD. Company PE calculation is based on displayed EPS Currency

**DISCLOSURE APPENDIX CONTAINS ANALYST CERTIFICATIONS AND THE STATUS OF NON-US ANALYSTS.** U.S. Disclosure: Credit Suisse does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that the Firm may have a conflict of interest that could affect the objectivity of this report. Investors should consider this report as only a single factor in making their investment decision. Customers of Credit Suisse in the United States can receive independent, third party research on the company or companies covered in this report, at no cost to them, where such research is available. Customers can access this independent research at [www.credit-suisse.com/ir](http://www.credit-suisse.com/ir) or call 1 877 291 2683 or email [equity.research@credit-suisse.com](mailto:equity.research@credit-suisse.com) to request a copy of this research.

Figure 1: Financial summary (year ending 30 June)

**EASTERN STAR GAS LIMITED**

In A\$m, unless otherwise stated

Year ending 30 Jun

Share Price: A\$1.00

Profit & Loss	2007A	2008A	2009F	2010F	2011F
Sales revenue	0.7	0.3	1.0	12.0	26.8
<b>EBITDA</b>	<b>-13.3</b>	<b>-6.0</b>	<b>-6.3</b>	<b>2.4</b>	<b>11.7</b>
Depr. & Amort.	0.5	0.3	0.1	0.8	1.7
Goodwill amort.	0.0	0.0	0.0	0.0	0.0
<b>EBIT</b>	<b>-13.9</b>	<b>-6.3</b>	<b>-6.4</b>	<b>1.6</b>	<b>10.0</b>
Equity adjustment	na	na	na	na	na
Net interest	-0.3	-2.1	-2.6	-2.6	2.7
<b>Profit before tax</b>	<b>-13.5</b>	<b>-4.2</b>	<b>-3.8</b>	<b>4.2</b>	<b>7.3</b>
Income tax	0.0	0.0	0.0	1.3	2.2
<b>Profit after tax</b>	<b>-13.5</b>	<b>-4.2</b>	<b>-3.8</b>	<b>2.9</b>	<b>5.1</b>
Minorities	na	na	na	na	na
<b>Net profit after tax</b>	<b>-13.5</b>	<b>-4.2</b>	<b>-3.8</b>	<b>2.9</b>	<b>5.1</b>
Preferred dividends	na	na	na	na	na
<b>Net profit after tax</b>	<b>-13.5</b>	<b>-4.2</b>	<b>-3.8</b>	<b>2.9</b>	<b>5.1</b>
Unusual item after tax	0.0	0.0	2.4	0.4	0.0
<b>Reported profit after tax</b>	<b>-13.5</b>	<b>-4.2</b>	<b>-1.4</b>	<b>3.3</b>	<b>5.1</b>

Balance Sheet	2007A	2008A	2009F	2010F	2011F
Cash & equivalents	2.1	37.5	46.0	8.6	9.9
Inventories	na	na	na	na	na
Receivables	0.4	2.0	9.0	9.8	19.6
Other current assets	1.6	0.3	0.0	0.0	0.0
<b>Current assets</b>	<b>4.0</b>	<b>39.9</b>	<b>55.1</b>	<b>18.4</b>	<b>29.5</b>
Property, plant & equip.	4.6	8.4	20.8	78.9	132.1
Intangibles	0.0	9.6	9.6	9.6	9.6
Other non-current assets	42.3	50.3	68.2	68.2	68.2
<b>Non-current assets</b>	<b>47.0</b>	<b>68.3</b>	<b>98.5</b>	<b>156.7</b>	<b>209.9</b>
<b>Total assets</b>	<b>51.0</b>	<b>108.1</b>	<b>153.6</b>	<b>175.1</b>	<b>239.4</b>
Payables	na	na	na	na	na
Interest bearing debt	0.1	0.0	0.0	13.5	61.7
Other liabilities	na	na	na	na	na
<b>Total liabilities</b>	<b>2.5</b>	<b>2.6</b>	<b>8.7</b>	<b>23.2</b>	<b>82.5</b>
<b>Net assets</b>	<b>48.5</b>	<b>105.5</b>	<b>144.9</b>	<b>151.8</b>	<b>156.9</b>
Ordinary equity	48.5	105.5	144.9	151.8	156.9
Minority interests	na	na	na	na	na
Preferred capital	na	na	na	na	na
<b>Total shareholder funds</b>	<b>48.5</b>	<b>105.5</b>	<b>144.9</b>	<b>151.8</b>	<b>156.9</b>

Cashflow	2007A	2008A	2009F	2010F	2011F
EBIT	-13.9	-6.3	-6.4	1.6	10.0
Net interest	0.3	2.0	2.6	2.6	-2.7
Depr & Amort	0.5	0.3	0.1	0.8	1.7
Tax paid	0.0	0.0	0.0	-0.6	-1.7
Working capital	0.1	-1.6	-7.0	0.0	-8.5
Other	4.0	2.7	7.9	-0.8	7.6
<b>Operating cashflow</b>	<b>-8.9</b>	<b>-2.9</b>	<b>-2.7</b>	<b>3.6</b>	<b>6.4</b>
Capex	0.0	0.0	-12.2	-46.8	-53.2
Acquisitions & Invest	-0.5	-3.1	0.0	0.0	0.0
Asset sale proceeds	1.6	na	na	na	na
Other	-8.2	-9.0	-20.7	-11.4	0.0
<b>Investing cashflow</b>	<b>-7.1</b>	<b>-12.2</b>	<b>-32.8</b>	<b>-58.2</b>	<b>-53.2</b>
Dividends paid	na	na	na	na	na
Equity raised	10.5	48.6	47.6	3.6	0.0
Net borrowings	0.0	0.0	0.0	13.5	48.2
Other	-0.5	1.9	0.0	0.0	0.0
<b>Financing cashflow</b>	<b>10.0</b>	<b>50.5</b>	<b>47.6</b>	<b>17.1</b>	<b>48.2</b>
<b>Net cashflow</b>	<b>-6.0</b>	<b>35.5</b>	<b>12.0</b>	<b>-37.4</b>	<b>1.4</b>

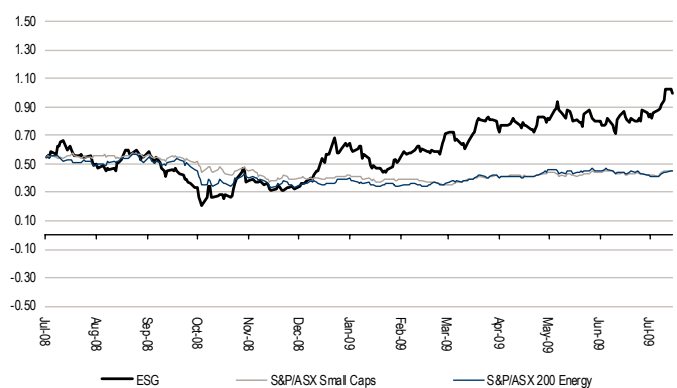
Financial Summary		2007A	2008A	2009F	2010F	2011F
NPAT	\$mn	-13.5	-4.2	-3.8	2.9	5.1
Credit Suisse NPAT	\$mn	-13.5	-4.2	-3.8	2.9	5.1
Credit Suisse EPS	c	-3.0	-0.6	-0.5	0.4	0.6
EPS growth	%	22.5	79.0	20.5	171.6	71.0
P/E	x	-33.7	-160.7	-202.0	282.0	165.0
P/Earnings Growth	x	na	na	na	na	na
Dividend payout ratio	%	0.0	0.0	0.0	0.0	0.0
Dividend	c	0.0	0.0	0.0	0.0	0.0
Yield	%	0.0	0.0	0.0	0.0	0.0
Franking	%	na	na	na	na	na
Operating CFPS	c	-2.0	-0.4	-0.4	0.4	0.8
P/OCF	x	-51.0	-234.9	-281.7	230.8	131.9
EV/EBITDA	x	-60.2	-133.7	-127.5	339.3	68.5
FCF yield	%	-2.0	-0.4	-1.9	-5.2	-5.6

Financial Ratios		2007A	2008A	2009F	2010F	2011F
<b>Profitability Ratios</b>						
EBITDA margin	%	-1808.8	-2256.4	-653.1	19.6	43.6
EBIT margin	%	-1881.0	-2373.3	-668.6	13.1	37.1
Return on equity	%	-27.9	-4.0	-2.6	1.9	3.2
Return on assets	%	-28.3	-8.9	-6.0	0.9	4.3
ROCE	%	-46.2	-11.0	-7.7	1.2	5.5
Effective tax rate	%	0.0	0.0	0.0	30.0	30.0

Balance Sheet Ratios		2007A	2008A	2009F	2010F	2011F
Net debt	\$mn	-2.0	-37.5	-46.0	4.9	51.7
Net debt/Equity	%	-4.1	-35.6	-31.8	3.2	33.0
Net debt/Capital	%	-4.2	-55.2	-46.6	3.1	24.8
Interest cover	x	40.0	3.0	2.5	-0.6	3.7
Capex/Sales	%	0.0	0.0	-1261.6	-388.5	-198.2
Capex/Deprn	%	0.0	0.0	-81.6	-59.1	-30.4
Working capital/Sales	%	9.9	-610.2	-727.8	0.2	-31.8

Share Items		2007A	2008A	2009F	2010F	2011F
Equiv. FPO (period avg.)	mn	456	672	771	828	840

Share Price Performance 52 week range: \$0.21 - \$1.03



Source: ASX Share price as of 21 Jul 09, 18:41 AET

Source: Company data, Credit Suisse estimates

## Eastern Star Gas – upgraded Target Price

As a result of the recent Santos corporate transaction in both Eastern Star's assets and share register; and ongoing field results we have upgraded our valuation of the company and consequently our Target Price, which is now estimated at \$1.25/share.

We have upgraded our Target Price to \$1.25/share

We note that as with all companies leveraged to CSG, there could be significant upside to our valuation based on continuing (we think) corporate activity, stronger unit reserves volumes and values; and commercial opportunities.

## The Santos deal – implications

On 2 July, Santos announced the acquisition of Gastar Exploration's 35% interest in a range of permits joint ventured with ESG and a 19.99% equity interest in the ESG from Hillgrove Resources Limited for a total cost of \$476mn.

Based on the cost split, the deal implied transaction multiples per 3P reserves of \$0.66-74/GJ and a look through valuation into ESG of around \$1.00/share (compared with our previous TP of (\$0.95/share).

The STO transaction underpins the stock at \$1.00/share we think

We saw the deal as being positive for ESG on balance:

- Reducing the commercialisation risk.
- Allowing ESG to link into the Santos east coast gas development plans, which may involve LNG outcomes at some stage in the future.

This deal continues our sector thematic of consolidation based on the requirement to control gas resources, especially heading into the expected CSG-LNG FID points over the next 12 months or so.

## The drilling results to date

As of the last detailed report on the multi-lateral production pilots (June-18) ESG reported that the Bibblewindi pilots had reached a flow rate of 0.25mmcf/d with water production steady at approximately 3.5-4kbp/d.

It was noted that gas flow rates were increasing...we add though that ultimately we expect to see gas flow rates at well in excess of 1mmcf/d (perhaps nearer 2mmcf/d) to ultimately define the success of the programme and justify the cost.

At this stage we have no reason to suggest these targets will not be met and remain confident, as does ESG of the company achieving its reserves upgrades by early in 2010.

## Valuation

We have upgraded our valuation (to \$1.25/share) through the adjusting of risk weightings as a result of the positive gas flow indications and the Santos transaction.

We have upgraded our valuation to \$1.25/share

We have significantly upgraded our value for exploration based on the company's estimated GIIP potential but underpinned by the positive results (to date) of the pilot drilling programme, which lifts our confidence in delivery and the commercial potential.

We add though that the resource and valuation estimates remain highly conjectural in volume and commercial opportunity terms; and is subject to sufficient capital investment to realise the upside.

Eastern Star has indicated a GIIP resource potential from PEL 238 of 17000PJ (100% basis) – assuming a 65% working interest and 60% conversion to 3P, that would be a net equivalent to ESG of 6630PJ, or some 4630PJ above the volumes valued and committed to various development options.

We are taking a very conservative view to GIIP and conversion rates

We note that the current GIIP estimate is probably well under-stated given it was calculated prior to the new development techniques being applied, but acknowledge that any GIIP estimate is extremely subjective and feel the current volume represents an adequate (but conservative) representation of the exploration potential remaining within the acreage at this stage.

**Figure 2: NAV valuation**

Project	ESG share	A\$m	\$ps	Pr	Comments
Wilga Park	65%	22	\$0.03	100%	
Narrabri	65%	178	\$0.21	75%	Or B&B equivalent
Mac Gen MoU	65%	130	\$0.15	50%	Or Mac Gen equivalent
Uncommitted target Narrabri gas volumes		159	\$0.19	70%	The Narrabri JV is working to secure additional MoUs which could bring 2P reserves from its current target of 1300PJ to 2000PJ...we see the addition of STO gas marketing expertise to lift the probability of success here
PEL 434 and 433		10	\$0.01		Notional value only
Orion Petroleum		10	\$0.01		Notional value only
<b>Underlying NPV</b>		<b>508</b>	<b>\$0.60</b>		
Exploration upside		564	\$0.66	20%	We base our exploration assumption on the company's notional GIIP estimate
<b>Total</b>		<b>1073</b>	<b>\$1.26</b>		
Net cash		(7)	(\$0.01)		We forecast 12-month forward net debt after including the capex planned over the next 12 months
<b>Total</b>		<b>1066</b>	<b>\$1.25</b>		

Source: Company data, Credit Suisse estimates

Ultimately this methodology demonstrates that the capital gains for ESG from the current share price lies within the company's capacity to convert its 'exploration upside' (GIIP) into commercially defined reserves.

The upside value to the stock lies in its GIIP ('exploration') potential

### Comparative reserves multiples

Using a like-for-like reserves comparison indicates that at the moment ESG represents a more expensive option within the sub-sector on a relative valuation basis.

**Figure 3: CSG compco**

	Share price	EV	2P (PJ)	3P (PJ)	Target 2P Reserves	EV/2P Reserves	EV/3P Reserves	EV/Target Reserves	
Arrow Energy	AOE	\$3.62	2,274	1,521	4,501	2,007	\$1.49	\$0.51	\$1.13
Eastern Star Gas	ESG	\$1.00	813	218	845	845	\$3.72	\$0.96	\$0.96
Molopo	MPO	\$1.06	73	88	367	650	\$0.83	\$0.20	\$0.11
Metgasco	MEL	\$0.52	95	264	1,419	660	\$0.36	\$0.07	\$0.14
Bow Energy	BOW	\$1.07	218	19	279	100	\$11.45	\$0.78	\$2.18
Icon Energy	ICN	\$0.30	126	-	-	170	n/a	n/a	\$0.74
Queensland Gas	QGC	\$5.75	4,841	2,163	5,683	7,000	\$2.24	\$0.85	\$0.69
Sunshine Gas	SHG	\$3.49	1,001	469	1,097	1,500	\$2.13	\$0.91	\$0.67
Pure Energy	PES	\$8.25	1,011	522	2,510	1,750	\$1.94	\$0.40	\$0.58

Source: Company data, Credit Suisse estimates

We note that ESG is cum a significant reserves upgrade once it is able to establish sustainable flow-rates on the Narrabri pilot programme. The JV is currently aiming to declare 1300PJ of 2P reserves and 2000PJ of 3P reserves in the Narrabri field (gross) by the end of the year (early 2011).

ESG looks expensive against recent sector transactions – but this does not reflect the reserves upside

We add though that there should be some pricing discount reflected in the reserves multiples against Queensland CSG equivalents based on the commercial end use of the gas – contract limited domestic volumes versus oil priced benchmarked export volumes.

If we compare ESG's current value to the recent CSG transactions in the market, the stock looks expensive but highlight that the underlying reserves position is considerably higher than its current booked volumes with reserves certification being market constrained.

**Figure 4: CSG transaction summary**

	CSG takeover bids	\$/GJ 2P	\$/GJ 3P	\$/GJ 4P (contingent+res)
Jul-09	STO- Gastar	\$2.56	\$0.66	
Apr-09	AOE-BPT (tot payment)	\$0.86	\$0.36	
Apr-09	AOE-BPT (upfront payment)	\$0.71	\$0.30	
Feb-09	BG-PES	\$1.97	\$0.41	\$0.13
Dec-08	AGL-SGL	\$4.55	\$3.46	
Dec-08	MPO-AJL-AGK	\$2.07	\$0.98	\$0.53
Oct-08	BG-QGC	\$1.98	\$0.75	\$0.61
Sep-08	ORG-COP (tot payment)	\$4.44	\$2.07	\$0.81
Sep-08	ORG-COP (upfront pymt)	\$3.28	\$1.52	\$0.59
Sep-08	QGC-SHG	\$1.68	\$0.72	\$0.52
Jun-06	AOE-Shell (total pymt)	\$2.72	\$0.77	
Jun-06	AOE-Shell (upfront pymt)	\$1.83	\$0.52	
May-08	STO-Petronas	\$3.96	\$1.33	\$0.72
Feb-08	QGC-BG	\$1.58	\$0.67	\$0.29

Source: Company data, Credit Suisse estimates

In comparison, we think a number of CSG companies book reserves despite the absence of announced options for commercialising gas, particularly when under a takeover scenario, thus lowering the apparent \$/GJ of reserves value.

## Target price

Our 12-month forward target price is A\$1.25/share based on our current valuation and success in the proposed work programme to deliver the nominated reserves target (at 2P and 3P).

We note our valuation assumptions are subjective, but we feel we have covered the risk sufficiently within our probability weightings and the long-dated nature of our forecasts.

The CSG market dynamic continues to change rapidly as the current reserves delineation phase progresses and corporate consolidation remains a focus of the (potential) LNG project participants.

## Gas reserves

Eastern Star Gas released its resource estimate for the Narrabri CSG project (based on the PEL 238 area) in mid-February 2009. We note that the Contingent Resource estimate is in addition to the 1300PJ (100% basis) of independently certified 3P gas reserves and the company has indicated that 85% of the estimated resource lies within the Bohena Seam, which the company is currently developing.

The PEL 238 acreage is independently estimated to contain up to 17Tcf of CSG (GIIP) within the two thickest coal seams (Bohena and Hoskissons). Although a significant recovery discount would need to be applied to this estimate, it is indicative of the strong upside potential located within this area.

We note that the GIIP estimate is based on data recovered prior to the drilling of the multi-lateral wells and we believe could be significantly upgraded once definite results are to hand at the completion of the pilot scheme.

**Figure 5: ESG reserves and resources**

	Net Reserves (PJ)		Net Resources (PJ)
1P	14	1C	777
2P	218	2C	1,984
3P	845	3C	3,983

Source: Company data

We set our target price at \$1.25/share based on a roll-forward valuation

Initial 3P volumes of 1300PJ (100%) already declared...

...with an estimated GIIP potential of 17Tcf

We believe that the company will deliver further 2P and 3P reserves upgrades after the four multi-lateral production pilot wells (Bibblewindi and Dewhurst) are completed.

In the medium term, reserves certification for ESG is likely to be market constrained. The company's initial aim for 1300PJ of 2P reserves (100% basis) in 2009 is based on the company's two existing MoUs. We add the note that these MoUs still need to be converted to binding gas sales agreements.

Partnering now with Santos, we see as adding significant additional commercial options for ESG accessible within the STO portfolio or leveraging off that company's marketing expertise.

The company is confident it can technically exceed this gross target of 1300PJ, with a potential upside case of 2000PJ at 2P reserves in 2009.

As we have maintained for some time, CSG is about reserves definition and growth and that is no different for ESG although the end game may not ultimately be about reserves aggregation for any LNG project.

Note that in comparison to the majority of its industry peers, ESG has a low level of current reserves, which is not a reflection of the potential of its acreage but rather the market constraint under which the company is developing its resources. The large indicated volumes attributable to other companies are dominantly leveraged into LNG projects, all of which remain somewhat conjectural at this stage, but the volume of gas effectively being quarantined for export highlights the strong domestic position as a gas provider available to ESG.

Reserves declarations will be market constrained although the technical potential is likely to be much higher

**Figure 6: CSG reserves comparison (PJ) – last releases**

		2P	3P	Comments
ORG-COP		5482	11110	On a 100% basis with Conoco
BG		3694	10710	Includes the SHG, QGC and PES acquisitions
Santos	STO	2350	3599	Needs to aggregate reserves to support its LNG project
Petronas		1298	2400	
Arrow Energy	AOE	1644	4791	Inc Tipton West, but Shell has a pre-emptive right over 12% of reserves from the acquisition. Pending a reserve upgrade.
Shell		504	1575	
AGL Energy	AGL	731	1716	
Metgasco	MEL	247	1389	Still in a 'R&D' phase
<b>Eastern Star Gas</b>	<b>ESG</b>	<b>218</b>	<b>845</b>	<b>Pending a reserves upgrade</b>
CS Energy		120	709	
Anglo Coal		386	529	To be a seller?
Molopo	MPO	178	526	Recent multi-lateral flow results are impressive but permeabilities are very low
Gastar Exploration		118	455	
Bow Energy	BOW		279	Still to commence its drilling programme
AJ Lucas	AJL	41	126	To be a seller?

Source: Company data, Credit Suisse estimates; RLMS data

#### Companies Mentioned (Price as of 21 Jul 09)

AGL Energy (AGK.AX, A\$13.96, OUTPERFORM, TP A\$16.55)  
 AJ Lucas Group Ltd (AJL.AX, A\$3.55)  
 Arrow Energy (AOE.AX, A\$3.62, OUTPERFORM [V], TP A\$4.00)  
 Beach Petroleum Ltd (BPT.AX, A\$.84)  
 BG Group plc (BG.L, p1055.00, OUTPERFORM [V], TP p1075.00, MARKET WEIGHT)  
 Bow Energy Ltd (BOW.AX, A\$1.07)  
 ConocoPhillips (COP, \$43.19, NEUTRAL, TP \$43.00)  
 Eastern Star Gas (ESG.AX, A\$1.00, OUTPERFORM [V], TP A\$1.25)  
 Gastar Exploration Ltd. (GST, \$0.65)  
 Hillgrove Resources Ltd. (HGO.AX, A\$0.235)  
 Icon Energy Limited (ICN.AX, A\$0.30)  
 Metgasco Limited (MEL.AX, A\$.51)  
 Molopo Australia (MPO.AX, A\$1.06, OUTPERFORM [V], TP A\$1.30)

Origin Energy (ORG.AX, A\$14.76, OUTPERFORM, TP A\$16.70)  
 Royal Dutch Shell plc (RDSa.L, p1551.00, UNDERPERFORM, TP p1420.00, MARKET WEIGHT)  
 Santos (STO.AX, A\$14.61, OUTPERFORM [V], TP A\$16.50)

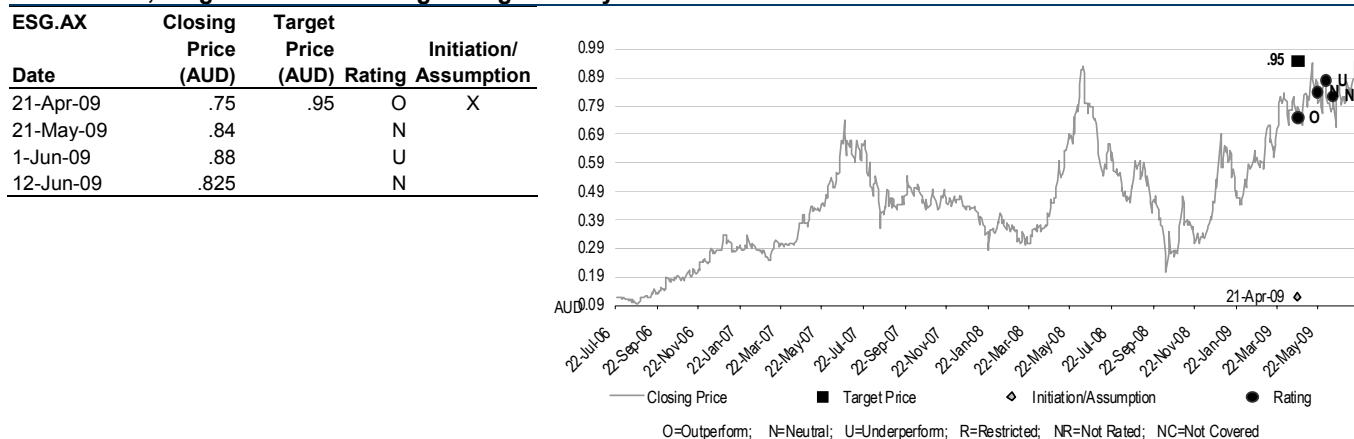
## Disclosure Appendix

### Important Global Disclosures

I, Andrew Williams, certify that (1) the views expressed in this report accurately reflect my personal views about all of the subject companies and securities and (2) no part of my compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this report.

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### 3-Year Price, Target Price and Rating Change History Chart for ESG.AX



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<b>Restricted</b>	2%	

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**Price Target:** (12 months) for (ESG.AX)

**Method:** We set our \$1.25 Target Price for ESG based on our valuation. We value ESG today at \$1.25/share using a discounted cashflow valuation derived valuation, the components of which lead to a discount rate of 11%. We model (where possible) domestic gas production and electricity generation; and applying risk weightings for the contracts where the MoUs are yet to be converted to Gas Sales Agreements

**Risks:** The critical risk associated with our \$1.25 ESG target is the assumption that ESG will be able to deliver commercial flow rates from its Narrabri field. The recently completed dual-lateral is currently de-watering and the company has yet to announce flow-rates. ESG's reserves goals will also depend on the success of its multi-lateral wells programme at Narrabri and will also require ESG to outline and complete commercial outcomes for its gas. The earnings are sensitive to changes in gas price assumptions, and the key risk (to either the upside or downside) to longer-term gas prices, in our view, will be the outcome of the CSG to LNG developments currently in planning. Although these projects are all based in Queensland, failure of these projects would release potentially over 2000PJ of gas into the east coast market. Under this scenario we'd expect that gas price along East-Coast Australia will face downward pressure or at the very least remain static for a significant period

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