

18 Jun 2009

Share Price: \$0.78
6mth Price Target: \$1.06

EASTERN STAR GAS LTD

Early Days but Initial Rates Encouraging

Eastern Star Gas Limited ("Eastern Star", "ESG", "Company") has reported an initial flow rate of 250,000 cubic feet of gas per day from its two multi-lateral pilot wells at its Narrabri Coal Seam Gas Project in NSW. The gas flow rate is an aggregate of rates from 6 vertical production wells that are connected to the two multi-lateral wells. ESG has a 65% interest in the project and is the operator, with the remainder held by Gastar Exploration Limited. The wells have only been dewatering for ~6 weeks, with water production continuing at 3,500-4,000 barrels per day.

The water flow rates continue to remain at the high end of expectations, meaning that the dewatering process may take longer than forecast.

On Track for 1,300 PJ by End of Year

Whilst it will take 6-9 months before peak flow rates are achieved from the production pilots, accurate extrapolations of what these peak rates may be and also ultimate gas recovery per well can be made earlier. It is anticipated that an interim reserve upgrade will be announced during Q309 as a result of these calculations. The Company is on track to achieve or exceed its 1,300 petajoules target by the end of the year.

ESG has two MOUs for combined supply of 1,300 petajoules of gas for power generation with Macquarie Generation (up to 500 PJ) and Babcock and Brown (up to 40 PJ/a). Any resource in excess of this would form the basis for a longer term strategy of monetisation via liquefaction to LNG or other liquid fuels.

Potential Development Cost Reduction

The initial results from the pilot wells indicate that pressure communication, as a result of high permeability, is occurring between the wells, which are spaced 400m apart. Conservative development plans by the Company for 400m spacing are likely to be changed to at least twice this distance, meaning that fewer wells will need to be drilled to recover the same amount of gas. This could effectively half the development costs for the project, significantly increasing its economics.

Significant Catalysts Expected for H209

We anticipate sequential re-ratings of the Company as increasing flow rates are reported to the market over the coming months. This should also result in a substantial interim reserve upgrade in Q309, followed by achievement of the 1,300 PJ target by the end of the year. The Company is fully funded for the remainder of the reserve upgrade program and we rate Eastern Star as a **BUY**, with a price target of 106cps.

Brief Business Description:

Coal seam gas developer with assets in New South Wales and South Australia

Hartleys Brief Investment Conclusion

Benefiting from coal seam gas activity in Queensland. Significant production testing in progress.

Chairman & CEO:

John Anderson (Chairman)
David Casey (Managing Director)

Top Shareholders:

Hillgrove Resources Limited (20.1%)
Merrill Lynch Nominees (5.1%)
TRU Energy Investments Pty Ltd (5.1%)

Company Address:

Level 7, 51 Pitt St
Sydney, NSW, 2000

Valuation: \$1.06
Issued Capital: 816.2m
- fully diluted 878.1m
Market Cap: \$636.7m
- fully diluted \$684.9m
Cash (31 Mar '09): \$78.7m
Debt (31 Dec '08): \$0.0m

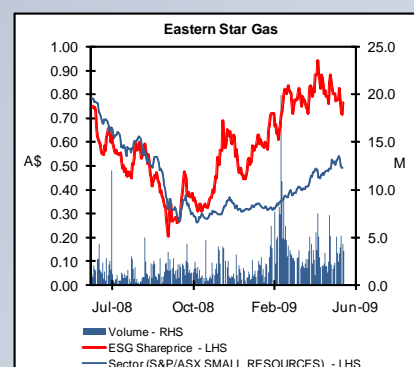
Valuation Summary

Asset	Value \$m	risked cps	unrisked cps
Narrabri	838.9	96	360
Other	27.6	3	3
Cash	78.7	9	9
Debt	-	-	-
O/heads	- 15.0	- 2	- 2
Total	930.2	106	371

FY08a
Chg in Cash \$35.5m
Net Cash End \$37.5m

2P Reserve (PJ gas) 218
EV / 2P Reserve (\$/PJ gas) \$2.56

Source: Hartleys Research



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HARTLEYS RESEARCH COVERAGE LIST

Hartleys Research Coverage					Hartleys Research	
Name	Ticker	Last Price*	M. CAP (A\$m)	EV (A\$m)	Recommendation	Industry
Oil & Gas						
1.	Woodside Petroleum Ltd	WPL	40.85	28,536	31,433	Buy Major
2.	Eastern Star Gas Ltd	ESG	0.730	596	517	Buy Producer / Explorer
3.	Carnarvon Petroleum Ltd	CVN	0.830	567	500	Buy Producer / Explorer
4.	Nexus Energy Ltd	NXS	0.395	255	412	Speculative Buy Developer / Explorer
5.	Tap Oil Ltd	TAP	1.17	183	129	Speculative Buy Producer / Explorer
6.	Cooper Energy Ltd	COE	0.480	140	46	Speculative Buy Producer / Explorer
7.	Red Fork Energy Ltd	RFE	0.925	84	76	Buy Explorer / Producer
8.	Amadeus Energy Ltd	AMU	0.390	77	143	Buy Producer / Explorer
9.	Strike Oil Ltd	STX	0.200	66	59	Speculative Buy Explorer / Producer
10.	First Australian Resources Ltd	FAR	0.070	40	27	Speculative Buy Explorer / Producer
11.	Oilex Ltd	OEX	0.170	30	15	Speculative Buy Explorer / Producer
12.	Sun Resources NL	SUR	0.080	28	18	Speculative Buy Explorer / Producer
13.	European Gas Ltd	EPG	0.130	26	90	Speculative Buy Producer / Explorer
14.	Adelphi Energy Ltd	ADI	0.070	10	3	Speculative Buy Junior
			Sub-Total	30,637	33,469	
Resources						
1.	Riversdale Mining Limited	RIV	6.25	1,178	852	Speculative Buy Coal
2.	Western Areas NL	WSA	5.48	922	1,056	Buy Nickel
3.	Andean Resource Ltd	AND	1.98	802	773	Speculative Buy Gold Developer
4.	Atlas Iron Limited	AGO	1.82	551	501	Buy Iron Ore
5.	Dominion Mining Limited	DOM	4.79	493	541	Speculative Buy Gold
6.	Medusa Mining Limited	MML	2.01	335	307	Buy Gold
7.	Gold One International Limited	GDO	0.290	199	120	Buy Gold
8.	Intrepid Mines Limited	IAU	0.370	158	136	Speculative Buy Gold
9.	Jabiru Metals Limited	JML	0.315	157	150	Buy Zinc-Copper
10.	Magma Metals Limited	MMB	0.455	74	54	Speculative Buy PGM-Cu-Ni
11.	Peninsula Minerals Ltd	PEN	0.034	37	23	Speculative Buy Uranium Developer / Explorer
12.	Ausquest Limited	AQD	0.155	35	5	Speculative Buy Junior Explorer
13.	Emmerson Resources Limited	ERM	0.165	34	22	Speculative Buy Junior Explorer
14.	Shaw River Resources Limited	SRR	0.250	33	30	Speculative Buy Junior Explorer
15.	Southern Gold Limited	SAU	0.145	18	16	Speculative Buy Junior Explorer
16.	Hazelwood Resources Ltd	HAZ	0.115	12	11	Speculative Buy Junior Explorer
			Sub-Total	5,038	4,599	
Industrials						
1.	Monadelphous Group Limited	MND	11.79	987	857	Neutral Mining Services
2.	West Australia News Hdgs Ltd	WAN	4.62	951	1,268	Buy Media
3.	Clough Limited	CLO	0.715	478	523	No Rating Oil & Gas Services
4.	Austral Limited	ASB	2.39	449	355	Speculative Buy Capital Goods
5.	Mermaid Marine Australia Ltd	MRM	1.75	318	370	Buy Oil & Gas Services
6.	Fleetwood Corporation	FWD	6.25	315	326	Buy Consumer & Mining Services
7.	Macmahon Holdings Limited	MAH	0.360	257	289	Speculative Buy Mining & Civil Construction
8.	NRW Holdings Ltd	NWH	0.890	215	268	Buy Mining & Civil Construction
9.	Ausdrill Limited	ASL	1.02	177	345	Buy Mining Services
10.	Neptune Marine Ltd	NMS	0.585	171	201	Speculative Buy Marine Services
11.	Index Ltd	IMD	0.680	128	156	Buy Oil & Gas / Mining Services
12.	Cash Converters Ltd	CCV	0.475	114	117	Buy Retail & Consumer Finance
13.	Southern Cross Electrical	SXE	0.920	110	87	Buy Mining & Civil Construction
14.	GRD Limited	GRD	0.510	98	133	Buy Mining & Civil Services
15.	Nomad Building Solutions Ltd	NOD	0.600	81	107	Speculative Buy Residential & Mining Services
16.	Decmil Group Limited	DCG	0.570	66	62	Buy Mining & Civil Construction
17.	RCR Tomlinson Ltd	RCR	0.530	65	117	Speculative Buy Mining & Industrial Services
18.	Swick Mining Services Ltd	SWK	0.420	64	118	Speculative Buy Mining Services
19.	Lycopodium Limited	LYL	1.48	56	53	Neutral Mining & Industrial Services
20.	VDM Group Limited	VMG	0.205	23	107	Speculative Buy Mining & Civil Construction
			Sub-Total	5,124	5,860	
50.	GRAND TOTAL			40,798	43,927	

Source: IRESS, Hartleys Research. * 18 Jun 2009

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Hartleys Recommendation Categories

No Rating	No recommendation.
Buy	Share price appreciation anticipated
Speculative Buy	Share price appreciation anticipated but it is higher risk than a "Buy". For the share price to rise it may be contingent on the outcome of an uncertain or distant event.
Neutral	Take no action. Stock is already trading near the share price target and there are no foreseeable near term catalysts.
Reduce / Take profits	Stock is trading above the share price target and there is a near term negative catalyst that could cause temporary weakness.
Sell	Significant price depreciation anticipated

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