

**Eastern Star Gas (ESG) \$0.61**

**Recommendation: BUY**

**Analyst: Scott Simpson**

## Event

- ESG together with its JV Partner, Gastar Exploration, has entered into a Heads of Agreement (HOA) with the APA Group to investigate options for delivery of gas from its Narrabri CSG project into the NSW market. APA owns and operates six major pipelines across Australia including the Moomba to Sydney Pipeline (MSP) and a number of lateral pipelines that intersect the MSP, including the Central West Pipeline (CWP).
- Under the HOA, ESG and APA will investigate construction of a lateral pipeline to connect the Narrabri CSG Project to the existing APA pipeline network. The lateral will connect into the CWP, providing ESG early access to the NSW gas market. While the CWP is a smaller capacity pipeline, APA will likely expand its NSW pipeline infrastructure as the local gas industry grows, providing access for larger production volumes. As the announcement suggests, by matching production and capacity in this manner it ensures that capital efficiency is maintained and provides a lower tariff environment for ESG.

## Impact

- The final piece in ESG's development plan has fallen into place with access to a local markets to facilitate long term growth.
- **This announcement is a significant milestone for ESG.** It provides a means to monetise early production gas prior to possible delivery into its MOU's with Macquarie Generation and Babcock & Brown. In order to deliver into these MOU's a substantial number of wells will be drilled and brought into production. This ramp up production gas will be well in excess of the requirements of the JV's upgraded Wilga Park Power Station. Hence by providing a link into the NSW markets this early gas will be monetised, providing a steady cash flow to fund further development.
- The agreement provides a means to maximise utilisation of development expenditure.
- It provides a flexible marketing arrangement by allowing for sale of fixed quantities of gas under Gas Sales Agreements and/or access to the spot market for sale of variable production volumes.
- ESG remains a strong BUY and provides great exposure to the emerging CSG market. We anticipate the share price to increase significantly over the short term with 2P reserves forecast to grow from 185PJ (130PJ net) at PEL-238 to 1300PJ (910PJ net) within 18-months.
- **We maintain a BUY recommendation and a 12-month price target of \$0.96/sh based on an evaluation of their current 2P reserves, projected 12-month 2P reserves target, risked 3P reserves plus a DCF based valuation of the Wilga Park Power Station.**

**Disclosure: Patersons Securities was the Lead Manager to the rights issue in 2005, Lead Manager for a \$10M Share Placement in Feb 2007 and Lead Manager for a \$28.85M Share Placement in Sept 2007. It was paid a fee for these services.**

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