

Date of issue

05.10.09

Company Update

INVESTMENT DATA

Share price	\$0.31
Issued capital	
Ordinary shares	1,125.6m
Options + other	31.3m
Fully diluted	1,156.9m
Market capitalisation	\$315.7m
52 week low/high	\$0.105 / \$0.35
Valuation	\$0.41
Price target (12 months)	\$0.41

Horizon Oil (HZN)

Buy

Good Kiwi oil flows, PNG gas shaping up

We maintain a Buy recommendation on HZN, despite the recent rally. Last month's asset transaction in PNG was great as it put a higher value on the Stanley gas/liquids project and it could lead to a longer term gas development with Talisman Energy. Our upgraded valuation of \$0.41 still leaves 32% upside from the current price, and short term news from two New Zealand oil wells could be good.

PNG asset transaction enhances value

The recent sale of 50% in HZN's wholly owned Stanley gas discovery in Western PNG for US\$60m to Talisman Energy of Canada was an excellent transaction. Not only did it put a US\$5m higher value on the asset than the prior offer from P3 Global Energy of Thailand, but it allowed HZN to retain a 50% ownership in the Ketu and Eivala gas discoveries and Talisman appears highly motivated to commercialise the gas discoveries made in the region.

New Zealand oil field performing well, more to come?

The Maari oil field offshore New Zealand is producing above the design capacity of 35,000bopd, as the gas-oil ratio is lower than anticipated. A production test of the Manaia oil prospect to the SW of Maari will be conducted in the coming week, to be followed by a test of the M2A sandstone reservoir which is situated above the producing Moki oil reservoir. Both of these tests could flow thousands of barrels/day and add up to 30m barrels of reserves. HZN's 10% interest could be worth about \$0.05/share. We maintain a Buy recommendation on HZN with our valuation increasing from \$0.36 to \$0.41, mainly due to lower net debt on the balance sheet.

Year end Jun	09a	10f	11f	12f	
Revenue	\$USm	8.7	71.8	102.1	164.2
EBITDA	\$USm	3.5	44.2	66.8	110.7
NPAT (adj)	\$Am	-2.7	18.9	40.5	79.3
EPS (adj)	A¢	-0.3	1.6	3.5	6.9
EPS growth	%	n/a	n/a	119	97
PER	x	n/a	19.4	8.9	4.5
EV/EBITDA	x	83.4	6.1	4.2	1.7
DPS	¢	0.0	0.0	0.0	0.0
Yield	%	0.0	0.0	0.0	0.0



Johan Hedstrom

■ jhedstrom@bellpotter.com.au

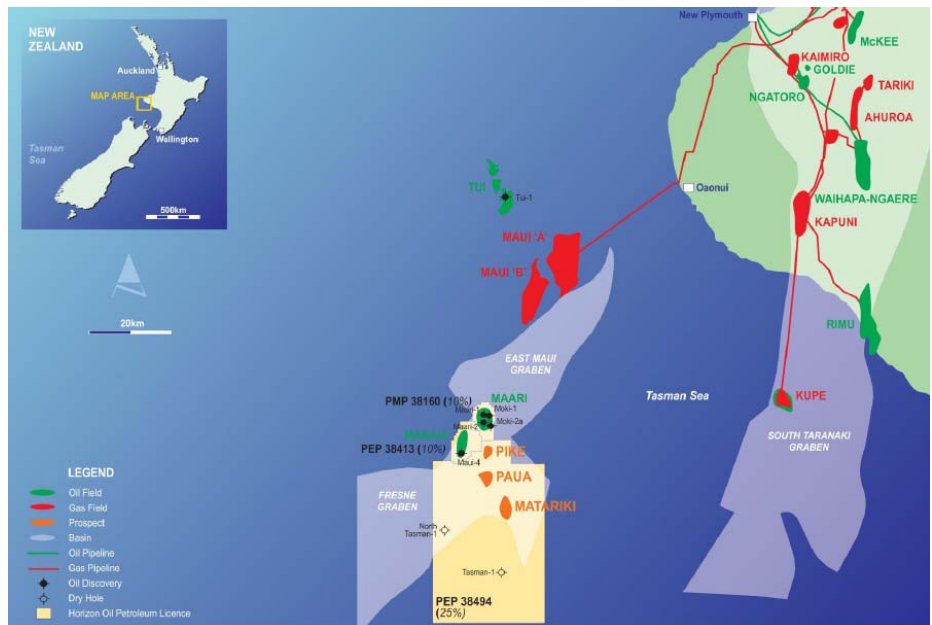
Good oil play, still undervalued

HZN is now an established oil producer

HZN has now established plateau production at Maari, currently exceeding the 35,000bopd design capacity. The constraining factor on the FPSO is the amount of gas associated with the oil, and as the gas-oil ratio is lower than expected, it can produce more oil, with daily rates up to 40,000 barrels. However, with the drilling and testing of Manaia and the M2A sandstone continuing, there will be some interruptions to the production, so the field will not be consistently producing above 35,000bopd until this work is completed, anticipated by the end of October. At 35,000bopd and an oil price of US\$70, HZN's 10% interest generates revenues of more than US\$7m/month.

The project facilities have been designed for the Maari oil field's Moki sandstone reservoir, which holds 140mb oil-in-place (OIP) with an estimated recovery rate around 40%. The JV holds a production license for 22 years, and if Manaia and the M2A oil reservoirs prove commercial, a longer production plateau and an extended life expectancy can be assumed. Manaia could hold 25mb recoverable reserves and M2A 15mb.

Figure 1 - NZ oil operations



Source: Company Data

Balance sheet moving into net cash

HZN has also just announced that its project finance facility for Maari had passed the final completion tests required by the lender BOS International. The company revealed that the effective interest rate is an attractive 2% on the remaining US\$36.6m debt facility, and that cash on hand is US\$33.6m as of 30 September. The net debt position of US\$3m will very quickly build to a net cash position, leaving ample room for new development expenditures.

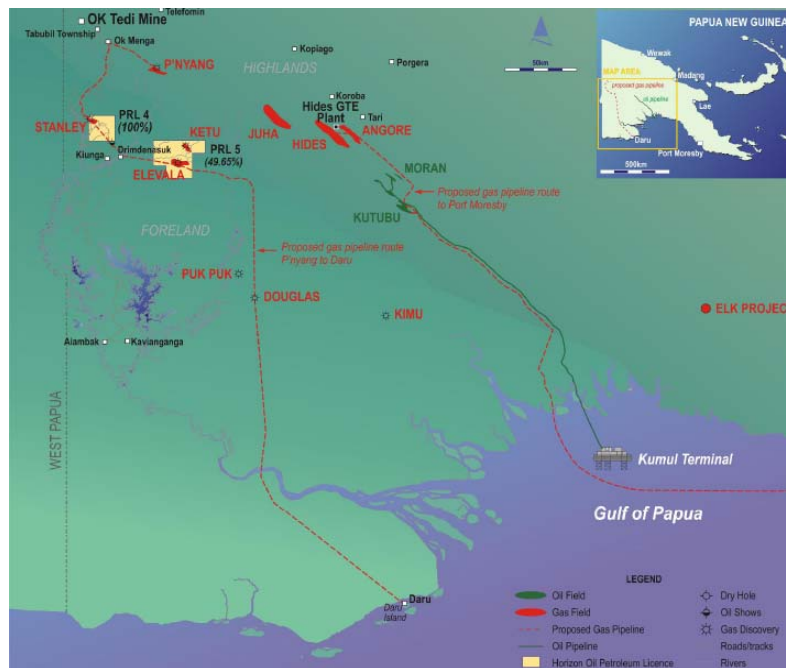
PNG development(s) now more likely

Talisman Energy has bought 50% of PRL4, which contains the Stanley gas discovery in western PNG for US\$60m. US\$30m has already been paid, and the remaining US\$30m will be as a carry on the initial development capex. Gross capex on the Stanley liquids stripping project has been estimated at US\$100-120m, so HZN is essentially fully funded for its 50% share of the project, with first production in 2011. Output of 4,000b condensate/day is anticipated from gas production of 140 million cubic feet/day (mmcf), reflecting a liquids yield of 30 barrels/mmcf.

However, Talisman has not bought 50% of Stanley just for the liquids project. As discussed in our HZN note of 31 August, Talisman paid US\$180m for Rift Oil & Gas Plc so now owns the Puk Puk and Douglas dry gas fields in western PNG, as well as 48% of the offshore Pandora gas discovery. Talisman has also paid US\$20m for Santos' 50% in PRL5, which contains the Ketu and Elevela gas discoveries, in which HZN holds 50% too. It is clear that Talisman's strategy is to aggregate enough gas fields in the region in order to justify a larger scale gas development which will most probably be through a Floating LNG concept in the Gulf of Papua.

Our valuation approach for HZN remains conservative, as we essentially focus on the liquids reserves at Stanley. If HZN's gas fields at Stanley, Ketu and Elevela (all 50/50 with Talisman) can be commercialised as part of a larger LNG project, additional value of \$0.10-\$0.20/share could be attributed to HZN. This upside potential remains speculative until we get better clarity on the scale, timeframe and costs of the project.

Figure 2 - PNG gas developments



Source: Company Data

Beibu Gulf oil development next

HZN is also a 30% partner in the Beibu Gulf oil project offshore China with Roc Oil. This +25m barrel oil complex is likely to be approved for development by CNOOC, the local Chinese operator in the next few months. This would dilute HZN's equity stake to 14.7%, as CNOOC has the rights to take 51% equity. Gross capex is estimated at US\$300m (net US\$44m to HZN), with first production in the June half of 2012.

Still scope for share price performance

We have been recommending a Buy on HZN from \$0.12, and the recent performance is particularly pleasing. The combination of an oil price recovery, successful commissioning of the Maari oil project, the Talisman deal on Stanley, and entry of HZN to the ASX300 Index have all contributed to the improved market rating.

We believe there is further upside potential in the share price, and the following table highlights our valuation, and sensitivities. The key difference to our previous valuation of \$0.36 is the improved net debt position as of 30 September.

Figure 3 - HZN valuation

Valuation						
Oil reserves	Gross	Net	Mboe	A\$m	\$/share	NPV/boe
New Zealand Maari (mb)	57.0	5.7	5.7	238.1	0.23	\$41.78
China Wei South (mb)	25.0	3.7	3.7	67.9	0.07	\$18.48
US Bayou Choctaw (mb)	1.3	0.2	0.2	0.5	0.00	\$2.02
PNG Stanley cond/LPG (mb)	10.0	3.9	3.9	74.6	0.07	\$18.96
		13.6	13.6	381.2	0.37	\$28.11
Other resources						
Maari/Manaia upside (mb)	25.0	2.5	2.5	12.5	\$0.01	\$5.00
Wei upside (mb)	15.0	2.2	2.2	11.0	\$0.01	\$5.00
PNG Stanley upside (mb)	12.0	4.7	4.7	23.5	\$0.02	\$5.00
PNG Elevala gas (PJ)	300.0	117.8	19.6	9.8	\$0.01	\$0.50
PNG Ketu gas (PJ)	200.0	78.5	13.1	6.5	\$0.01	\$0.50
Cash (Net debt)				-3.4	\$0.00	
Corporate overheads				-25.0	-\$0.02	
TOTAL				416.1	\$0.41	
Sensitivities						
Valuation on LT oil price from 2012				A\$m	A\$/share	
Base case		US\$80		416	\$0.41	
Low case		US\$50		204	\$0.20	
High case		US\$100		553	\$0.54	
Discount rate						
Base case		10.0%		416	\$0.41	
Lower case		12.0%		381	\$0.37	
Conservative case		14.0%		349	\$0.34	
EPS sensitivity				2010	2011	2012
Base case				1.6¢	3.5¢	6.9¢
US\$50 case				1.1¢	1.5¢	2.7¢
US\$100 case				2.6¢	4.4¢	9.8¢

Source: Bell Potter Securities

Recommendation

We consider our valuation conservative at \$0.41, with further upside from a future LNG development in PNG, and with good leverage to higher oil prices. The company's first oil development at Maari is rapidly strengthening the balance sheet, which will enable funding for the next two developments at Stanley liquids stripping, and Beibu Gulf. We maintain the Buy recommendation

Horizon Oil Ltd (HZN)						Share price: \$0.310					
As at 5/10/2009						Market cap: \$315.7m					
US\$ reporting						Recommendation: Buy					
Income Statement						Valuation Data					
Year end June 30	2008A	2009A	2010F	2011F	2012F	Year end June 30	2008A	2009A	2010F	2011F	2012F
Revenue	0.5	8.7	71.8	102.1	164.2	Adjusted NPAT (A\$)	-12.6	-2.7	18.9	40.5	79.3
EBITDA	-3.9	3.5	44.2	66.8	110.7	Adjusted EPS (A\$)	-1.6c	-0.3c	1.6c	3.5c	6.9c
DD&A	0.0	-2.9	-12.0	-15.2	-24.6	EPS growth	N/A	N/A	N/A	119%	97%
Exploration write-off	-13.0	-0.9	-4.0	-4.4	-4.9	P/E ratio	N/A	N/A	19.4x	8.9x	4.5x
EBIT	-16.9	-0.3	28.2	47.1	81.1	OpCFPS (excl. abnormals)	-0.3c	0.4c	2.9c	4.8c	8.3c
Net interest	0.7	-2.6	-5.2	2.1	3.9	Price/OpCFPS	N/A	82.4x	10.7x	6.4x	3.7x
Abnormals	0.0	-6.0	0.0	0.0	0.0	DPS (A\$)	0.0c	0.0c	0.0c	0.0c	0.0c
Pre-tax profit	-16.2	-8.9	23.0	49.2	85.0	Yield	0.0%	0.0%	0.0%	0.0%	0.0%
Tax	0.0	1.5	-8.1	-16.1	-27.0	EV/EBITDA	N/A	83.4x	6.1x	4.2x	1.7x
Minority interests	0.0	0.0	0.0	0.0	0.0	Profitability Ratios					
Reported net profit	-16.2	-7.5	14.9	33.1	58.0	Year end June 30	2008A	2009A	2010F	2011F	2012F
Adjusted net profit	-11.4	-2.0	16.1	34.5	59.5	EBITDA/sales	N/A	41%	62%	65%	67%
(adjusted net profit = pre-tax profit before abnormals minus tax at marginal rate)						EBIT/sales	N/A	N/A	39%	46%	49%
Cashflow						Return on assets (avg.)	-15%	-2%	10%	15%	21%
Year end June 30	2008A	2009A	2010F	2011F	2012F	Return on equity (avg.)	-26%	-4%	17%	24%	32%
Reconciliation						Dividend cover	N/A	N/A	N/A	N/A	N/A
Net profit US\$	-\$16.2m	-\$7.5m	\$14.9m	\$33.1m	\$58.0m	Effective tax rate	0%	17%	35%	33%	32%
Exploration write-off	13.0	0.9	4.0	4.4	4.9	Liquidity & Leverage					
Depreciation	0.0	2.9	12.0	15.2	24.6	Year end June 30	2008A	2009A	2010F	2011F	2012F
Change in working capital	0.6	-3.4	2.7	3.2	8.5	Net debt	\$19.4m	\$59.0m	\$2.7m	\$11.0m	-\$48.8m
Other	0.0	10.2	0.0	0.0	0.0	Net debt/equity	45%	97%	2%	7%	-22%
Net operating cashflow	-2.6	3.1	33.6	56.0	96.1	Interest cover	5.6x	1.3x	8.5x	-31.7x	-28.6x
Investing cashflow						Assumptions					
Capex on PPE	-21.0	-26.3	-19.5	-55.4	-28.4	Year end June 30	2008A	2009A	2010F	2011F	2012F
Exploration	-23.1	-16.2	-8.1	-8.9	-9.8	Maari production (bopd)	0	3,297	30,247	32,482	26,311
Other	0.0	0.0	38.0	22.0	0.0	Wei South production (bopd)	0	0	0	0	7,500
Net investing cash flow	-44.1	-42.5	10.4	-42.3	-38.2	Stanley production (bopd)	0	0	0	1,033	4,230
Financing activities						Total Production (Mboe)	0.0	0.1	1.1	1.5	2.6
Issue of shares	17.3	24.6	0.1	0.0	2.0	Net total production (boepd)	0	330	3,033	4,092	7,098
Buy backs	0.0	0.0	0.0	0.0	0.0	Oil price (US\$/barrel)	93.69	70.11	65.00	75.00	80.00
Dividends paid	0.0	0.0	0.0	0.0	0.0	PNG Gas price (US\$/GJ)	0.00	0.00	0.00	0.00	0.00
Debt	29.1	5.6	0.0	0.0	-10.0	Exchange rate (A\$/US\$)	0.899	0.748	0.850	0.850	0.750
Others	0.0	0.0	0.0	0.0	0.0	Valuation					
Net financing cash flow	46.4	30.2	0.1	0.0	-8.0	Reserves	Gross	Net	Mboe	A\$m	\$/share
FX impact	0.0	-0.4	0.0	0.0	0.0	New Zealand Maari (mb)	57.0	5.7	5.7	238.1	0.23
Net change in cash held	-0.2	-9.6	44.1	13.7	49.8	China Wei South (mb)	25.0	3.7	3.7	67.9	0.07
Balance Sheet						US Bayou Choctaw (mb)	1.3	0.2	0.2	0.5	0.00
Year end June 30	2008A	2009A	2010F	2011F	2012F	PNG Stanley cond/LPG (mb)	10.0	3.9	3.9	74.6	0.07
Assets						Sub-total			13.6	381.2	0.37
Cash assets US\$	\$19.6m	\$10.0m	\$54.2m	\$67.9m	\$117.7m	Other resources					
Receivables	0.9	0.8	0.0	0.0	0.1	Maari/Manaia upside (mb)	25	2.5	2.5	12.5	0.01
Inventories	0.0	0.1	0.0	0.0	0.0	Wei upside (mb)	15	2.2	2.2	11.0	0.01
Other	0.1	0.2	0.0	0.1	0.1	PNG Stanley upside (mb)	12	5	4.7	23.5	0.02
Total current assets	20.6	11.1	54.2	68.0	117.9	PNG Elevala gas (PJ)	300	118	19.6	9.8	0.01
Plant and equipment	40.8	92.7	100.2	140.4	144.2	PNG Ketu gas (PJ)	200	79	13.1	6.5	0.01
Investment	0.0	0.0	0.0	0.0	0.0	Cash (Net debt)				-3.4	0.00
Intangible assets	33.2	34.5	38.6	43.0	47.9	Corporate overheads				-25.0	-0.02
Deferred tax assets	0.0	1.8	1.8	1.8	1.8	TOTAL				416.1	0.41
Other	0.0	0.0	0.0	0.0	0.0	Sensitivities					
Total non-current assets	74.0	129.1	140.6	185.2	193.9	Valuation on LT oil price from 2012					
Total assets	94.7	140.2	194.8	253.2	311.8	Base case	US\$80			416	0.41
Liabilities						Low case	US\$50			204	0.20
Debt	18.7	34.2	22.0	44.0	34.0	High case	US\$100			553	0.54
Payables	9.9	6.5	1.0	1.1	1.5	Discount rate					
Deferred revenue	0.0	0.0	7.2	10.2	16.4	Base case	10%			416	0.41
Current tax liabilities	0.0	0.0	0.2	0.5	0.8	Lower case	12%			381	0.37
Provisions	0.2	0.2	0.0	0.0	1.6	Conservative case	14%			349	0.34
Total current liabilities	28.9	40.9	30.5	55.8	54.3	EPS sensitivity					
Debt	20.2	34.8	34.8	34.8	34.8	Base case			2010	2011	2012
Other	0.6	0.5	0.5	0.5	0.5	US\$50 oil			1.6¢	3.5¢	6.9¢
Provisions	1.8	3.3	3.3	3.3	3.3	US\$100 oil			1.1¢	1.5¢	2.7¢
Total non-current liabilities	22.6	38.6	38.6	38.6	38.6	Peer group reserves comparison					
Total liabilities	51.4	79.5	69.1	94.4	93.0		EV	2P	3P	EV/2P	EV/3P
Net assets	43.2	60.6	125.7	158.8	218.8		\$m	Mboe	Mboe	\$/boe	\$/boe
Equity						AWE	1,182	69.0	112.9	\$17.14	\$10.48
Contributed equity	100.3	124.9	168.5	168.5	170.5	BPT	788	63.1	80.0	\$12.50	\$9.85
Reserves & outside equity	2.2	3.0	3.0	3.0	3.0	CVN	205	16.6	46.1	\$12.33	\$4.44
Retained earnings	-59.2	-67.3	-45.8	-12.7	45.3	ROC	624	48.0	132.2	\$13.01	\$4.72
Total equity	43.2	60.6	125.7	158.8	218.8	TAP	166	7.0	17.3	\$23.61	\$9.60
Diluted shares on issue	798.5	1156.9	1156.9	1156.9	1181.7	Peer group average				\$15.72	\$7.82
W'd ave diluted shares	761.3	834.1	1156.9	1156.9	1156.9	HZN	319	13.6	55.7	\$23.54	\$5.73

BELL POTTER OFFICES

www.bellpotter.com.au

info@bellpotter.com.au

TOLL FREE 133 788

ABN 25 006 390 772

AFS Licence No. 243480

ADELAIDE

LEVEL 6, DA COSTA BUILDING
68 GRENFELL STREET
ADELAIDE SA 5000
TEL: 08 8224 2722
FAX: 08 8224 2799

BRISBANE

LEVEL 17, 10 EAGLE STREET
BRISBANE QLD 4000
TEL: 07 3295 2600
FAX: 07 3295 2688

CAIRNS

CNR SPENCE & MCLEOD STREETS
CAIRNS QLD 4870
TEL: 07 4047 4188
FAX: 07 4047 4199

GEELONG

LEVEL 1, 122 YARRA STREET
GEELONG VIC 3220
TEL: 03 5227 7000
FAX: 03 5227 7099

GOLD COAST

LEVEL 8, 50 CAVILL AVENUE
SURFERS PARADISE QLD 4217
TEL: 07 5554 4333
FAX: 07 5554 4399

HOBART

LEVEL 9, AMP BUILDING
86 COLLINS STREET
HOBART TAS 7000
TEL: 03 6231 1677
FAX: 03 6231 3744

MACKAY

CITY COURT, 78 VICTORIA STREET
MACKAY QLD 4740
TEL: 07 4957 6996
FAX: 07 4951 4114

MELBOURNE

LEVEL 29, 101 COLLINS STREET
MELBOURNE VIC 3000
TEL: 03 9256 8700
FAX: 03 9256 8787

MORNINGTON

SUITE 1, 330 MAIN STREET
MORNINGTON VIC 3931
TEL: 03 5970 0101
FAX: 03 5970 0199

PERTH

LEVEL 37, EXCHANGE PLAZA
2 THE ESPLANADE
PERTH WA 6000
TEL: 08 9326 7666
FAX: 08 9326 7676

SYDNEY

LEVEL 33, 225 GEORGE STREET
SYDNEY NSW 2000
TEL: 02 9255 7200
FAX: 02 9255 7227

TOOWOOMBA

3 DUGGAN STREET
TOOWOOMBA QLD 4350
TEL: 07 4638 5988
FAX: 07 4639 2608

Important Disclaimer—This may affect your legal rights: Because this document has been prepared without consideration of any specific client's financial situation, particular needs and investment objectives, a Bell Potter Securities Limited investment adviser (or the financial services licensee, or the proper authority of such licensee, who has provided you with this report by arrangement with Bell Potter Securities Limited) should be consulted before any investment decision is made. While this document is based on the information from sources which are considered reliable, Bell Potter Securities Limited, its directors, employees and consultants do not represent, warrant or guarantee, expressly or impliedly, that the information contained in this document is complete or accurate. Nor does Bell Potter Securities Limited accept any responsibility to inform you of any matter that subsequently comes to its notice, which may affect any of the information contained in this document. This document is a private communication to clients and is not intended for public circulation or for the use of any third party, without the prior approval of Bell Potter Securities Limited. This is general investment advice only and does not constitute advice to any person.

Disclosure of Interest: Bell Potter Securities Limited receives commission from dealing in securities and its authorised representatives, or introducers of business, may directly share in this commission. Bell Potter Securities and its associates may hold shares in the companies recommended.

Additional Disclosures:

The analyst and/or related parties own or have interests in securities issued by Horizon Oil.