

Horizon Oil Limited HZN (\$0.33)

Recommendation: BUY

PNG Development to Commence in August

Analyst: Scott Simpson

OUR VIEW

HZN is set for an eventful 2010 as it puts the final touches on Maari and kicks off projects in China and PNG. Following tie-in of the Manaia MN1 well in May and work-over of MR3 and MR5 in June, the field should be at capacity around mid-July. At full capacity the field provides free cash flow of US\$12m a quarter to pay down debt and fund development. Commercial negotiations concerning the Beibu Gulf development are nearing completion with Chinese government approval expected shortly, followed by FID and start of development works in H2 2010. Drilling will commence in August in PNG at the Stanley project site, followed by appraisal at Elevala. The 8mmbbls Stanley development is a high value project with potential development of the larger 26mmbbl Elevala/Ketu discovery providing further value. Appraisal of the fields 691bcf of gas (267bcf net) will provide a key catalyst for an aggregated gas development of the western province gas, led by partner Talisman Energy.

INVESTMENT HIGHLIGHTS

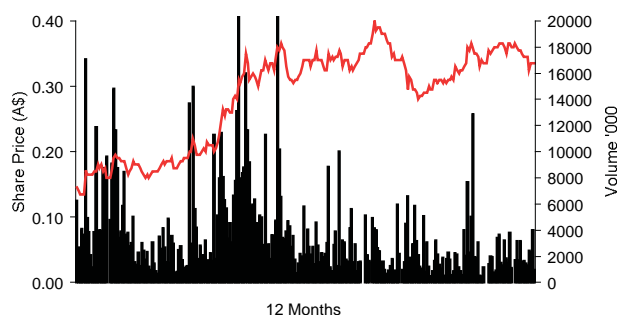
- **Lower production at Maari due to down-hole pump failures.** Production averaged around 15kbopd for the March quarter, down from the design rate of 35kbopd due to a shut in of the MR3 and MR5 wells and scheduled field shut-in. Despite the lower output, HZN booked revenue of US\$12.17m and finished the period in a net cash position with US\$25.96m in cash and debt of US\$25.62m.
- **Full ramp-up delayed at Maari.** While we had anticipated full production by the end of March, repairs to 2 x wells will be required prior to achieving this goal. Commissioning of a work-over unit, installed on the platform, is nearing completion and following this a number of works will be conducted including repairs to the down-hole pumps in the MR3 and MR5 wells, perforation of the two injection wells and completion of the Manaia MN1 well for production. Subsurface evaluation of the field is continuing and HZN expects to be able to estimate additional reserves as a result of the Manaia and M2A appraisal wells in H2 2010. Planning has also commenced on a full field development of the 'Greater Maari complex'.
- **Beibu Gulf development nearing approval.** Commercial negotiations should be near complete and will be followed by FID and commencement of development works in H2 2010, for a first oil target of 2012.
- **Preparations in PNG on schedule.** Negotiations for a rig are nearing completion to commence drilling in August, with the firm program to include Stanley-2 and Elevala-2, likely followed by Ketu-2, Stanley-3 and Stanley-4. The project is a high value staged approach with initial condensate stripping followed by the potential for gas commercialisation at both a local level and possibly aggregated into a larger liquids project. Partner Talisman Energy has amassed interest in a large gas resource (5-6 tcf) which it aims to develop as a stand alone LNG facility or potentially tie-in to the existing PNG LNG project.
- **We maintain our BUY recommendation with a price target of \$0.42/sh.** HZN is well positioned with solid cash flows from Maari, a free-carry on US\$30m of works in PNG and a pipeline of projects to grow the business going forward. Ramp-up at Maari, Beibu Gulf FID and PNG drilling/testing will provide short term catalysts.

Investment Summary

Year End June 30	2009A	2010F	2011F	2012F
A\$				
Reported NPAT (\$m)	(2.7)	(50.8)	32.1	45.6
Recurrent NPAT (\$m)	(2.7)	10.0	32.1	45.6
Recurrent EPS (cents)	(0.2)	0.9	2.9	4.0
EPS Growth (%)	na	na	230.6	37.2
PER (x)	(140.1)	37.6	11.6	8.2
EBITDA (\$m)				
EBITDA (\$m)	3.3	41.4	67.4	107.3
EV/EBITDA (x)	142.0	11.0	6.3	3.5
Capex (\$m)	35.1	10.3	92.0	11.8
Free Cashflow	(52.6)	4.9	(46.0)	57.8
FCFPS (cents)	(4.5)	0.4	(4.1)	5.1
PFCF (x)	(7.3)	76.6	(8.1)	6.4
DPS (cents)				
DPS (cents)	0.0	0.0	0.0	0.0
Yield (%)				
Yield (%)	0.0	0.0	0.0	0.0
Franking (%)				
Franking (%)	0.0	0.0	0.0	0.0

Company Statistics & Performance

Shares on issue (m)	1126.0	3mth ADT (\$m)	0.79
Market Cap. (\$m)	371.6	Debt est (\$m)	28.2
52 week range	\$0.14 - \$0.40	Cash est (\$m)	28.5



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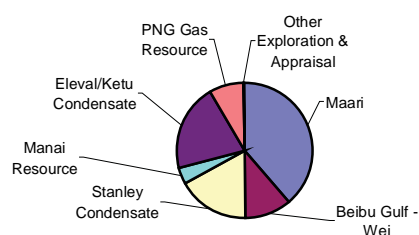
\$0.33

Year End June 30

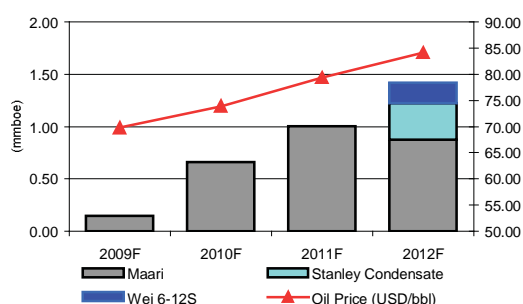
Valuation	A\$m	A\$/sh
Maari	190	0.17
Beibu Gulf - Wei	55	0.05
Stanley Condensate	84	0.08
Manai Resource	20	0.02
Eleva/Ketu Condensate	102	0.09
PNG Gas Resource	40	0.04
Other Exploration & Appraisal	1	0.00
Corporate	(23)	(0.02)
Cash	29	0.03
Debt	(28)	(0.03)
Total @ 10% Discount Rate	469	0.42
Price Target		0.42

Valuation Sensitivity	-10%	0%	+10%
Oil Price Sensitivity (A\$/sh)	0.38	0.42	0.45
Exchange Rate Sensitivity (A\$/sh)	0.46	0.42	0.38

Valuation Summary of Operating Assets



Production Summary



Reserves & Resources

Reserves - Net HZN	Oil/Cond (mmbbl)	Gas (bcf)	Total (mboe)
2P Reserves			
Maari	6	0	6
Wei 6-12	4	0	4
Wei 12-8	4	0	4
Total Group	14	0	14

Directors

Name	Position
Fraser Ainsworth	Chariman
Brent Emmett	Managing Director & CEO
Paul Nimmo	Non-Executive Director
Michael Sheridan	Company Secretary & CFO
John Humphrey	Non-Executive Director
Robert Laws	Non-Executive Director
Gerrit J de Nys	Non-Executive Director

Substantial Shareholders	Shares (m)	%
Austral-Asia Energy Pty Ltd	129.8	11.5
Ward Ferry Management Ltd	57.1	5.1
Acorn Capital Ltd	56.9	5.1

Commodity Assumptions	2009A	2010F	2011F	2012F
A\$:US\$	0.75	0.89	0.91	0.88
Crude Oil - WTI (USD/bbl)	69.78	73.91	79.38	84.17
Long Term Oil Price of US\$85/bbl				

Production Summary	2009A	2010F	2011F	2012F
Maari				
Oil/Condensate (mmbbl)	0.1	0.7	1.0	0.9
Gas (PJ)	0.0	0.0	0.0	1.0
Total (mmboe)	0.1	0.7	1.0	1.0
Wei 6-12S				
Oil/Condensate (mmbbl)	0.0	0.0	0.0	0.2
Gas (PJ)	0.0	0.0	0.0	1.0
Total (mmboe)	0.0	0.0	0.0	0.2
Stanley Condensate				
Oil/Condensate (mmbbl)	0.0	0.0	0.0	0.4
Gas (PJ)	0.0	0.0	0.0	1.0
Total (mmboe)	0.0	0.0	0.0	0.5
Total (mmboe)	0.1	0.7	1.0	1.8
Total (mboepd)	0.40	1.82	2.74	4.83

Profit & Loss (US\$m)	2009A	2010F	2011F	2012F
Sales Revenue	8.2	45.5	79.4	119.0
Other Income	0.2	1.0	1.2	(0.1)
Operating Costs	0.6	5.1	15.4	19.4
Royalties	0.0	0.0	0.0	1.3
Exploration Exp.	0.9	0.1	0.0	0.0
Corporate/Admin	4.3	4.6	4.2	4.3
EBITDA	2.5	36.8	61.0	93.9
Depn & Amort	2.9	11.5	16.6	25.1
EBIT	(0.4)	25.3	44.4	68.8
Financing Cost	2.9	3.2	2.8	1.5
Operating Profit	(3.4)	22.1	41.5	67.3
Abnormals - Pre Tax	0.0	54.1	0.0	0.0
Tax expense	(1.3)	13.2	12.5	27.4
Minorities	0.0	0.0	0.0	0.0
Abnormals - Post Tax	(6.0)	0.0	0.0	1.0
NPAT	(8.1)	63.0	29.1	40.9
Normalised NPAT	(2.0)	25.3	29.1	39.9

Unit Revenue / Costs	2009A	2010F	2011F	2012F
Sales Revenue / boe (\$/boe)	55.9	68.7	79.4	83.9
Cash OPEX / boe (\$/boe)	4.1	7.6	15.4	13.6
Non-cash OPEX / boe (\$/boe)	56.1	24.4	20.8	21.7
EBIT / boe (\$/boe)	(2.9)	38.1	44.3	48.5
NPAT / boe (\$/boe)	(55.3)	95.3	29.1	28.1

Cash Flow (US\$m)	2009A	2010F	2011F	2012F
Adjusted Net Profit	(2.0)	63.1	29.1	39.9
+ Interest/Tax/Expl Exp	2.5	16.4	15.3	28.9
- Interest/Tax/Expl Inc	17.2	17.8	19.3	32.9
+ Depn/Amort	2.9	11.5	16.6	25.1
+/- Other	0.8	(59.8)	0.0	0.0
Operating Cashflow	(13.0)	13.5	41.7	60.9
- Capex (+asset sales)	26.2	9.2	83.3	10.3
- Working Capital Increase	0.0	0.0	0.0	0.0
Free Cashflow	(39.3)	4.4	(41.6)	50.6
- Dividends (ords & pref)	0.0	0.0	0.0	0.0
+ Equity raised	24.6	0.2	0.0	0.0
+ Debt drawdown (repaid)	5.6	5.9	(16.0)	(36.6)
+ Other	(0.1)	29.9	0.0	0.0
Net Change in Cash	(9.2)	40.4	(57.6)	14.1
Cash at End Period	10.0	48.4	(9.2)	4.9
Net Cash/(Debt)	(35.8)	(3.2)	(44.8)	1.0

Balance Sheet (US\$m)	2009A	2010F	2011F	2012F
Cash	10.0	48.4	-9.2	4.9
Total Assets	140.2	218.2	231.3	234.6
Total Debt	69.0	71.0	47.7	3.8
Total Liabilities	79.5	93.7	72.9	36.3
Shareholders Funds	60.6	124.5	153.6	193.5

Ratios	2009A	2010F	2011F	2012F
Net Debt/Equity (%)	59.0	2.6	29.2	na
Interest Cover (x)	na	8.0	15.6	45.4
Return on Equity (%)	na	50.6	18.9	21.1