

Horizon Oil Limited

March 2010 quarterly: China and PNG activity increasing



Wilson HTM
INVESTMENT GROUP

3 May 2010

\$0.36

BUY

John Young

+61 3 9640 3846

john.young@wilsonhtm.com.au

Charmaine Cornford

+61 3 9640 3897

charmaine.cornford@wilsonhtm.com.au

Price Performance



Security/Capital Details

ASX Code	HZN
Market Cap (dil)	\$415 M
Issued Shares (dil)	1,169.8 M
Avg Mth T'over	81.55 M
12 Mth High – Low	\$0.40 - \$0.12

Key Data/Ratios – FY 2010

EBITDA / Sales	68.9%
EBIT / Sales	53.8%
Debt / Equity	27.5%
Interest Cover	8.0 x
ROE	-0.2%
EPS Growth	97.8%
DCF	\$0.41
12 Mth Price Target	\$0.46

Recommendation

Maari gross oil production averaged 16 kbd, providing net sales of 163 kbbbl and revenue of \$US12.2m. Production was lower than design capability of 35 kbd due to downhole pump problems which should be rectified in the coming quarter. We expect a revised reserve assessment around end CY10 following some production history on the M2A well, to be tied-in this quarter. Preparations are well advanced for drilling in PNG commencing in the September quarter and a final investment decision on the Block 22/12 oil project in China is expected in 2HCY10. We retain our Buy recommendation; price target revised to \$A0.46 /sh (prev \$A0.47).

Key Points

	Units	Mar-10	% vs pcp	Comment
Forex	\$US/\$A	0.91	-0.5	
Oil price	\$US/bbl	79.38	2.9	Tapis
Oil price	\$A/bbl	87.66	3.5	Tapis
Production	mmbbl	0.14	-21.4	unplanned shut in of MR5 & MR3, planned mtce.
Sales	mmbbl	0.16	0.0	
Sales revenue	M\$US	12.2		
Production costs	M\$US	2.2	106.2	
Other costs	M\$US	0.0	0.0	not reported
Unit sales	\$US/bbl	74.8		
Unit opex	\$US/bbl	15.2	162.2	increased due to maintenance and lower production
Capex	M\$US	4.1	-43.5	mainly PNG, completed Manaia/ Maari appraisal
Cash @ period end	M\$US	26.0	-6.0	
Debt @ period end	M\$US	25.6	-17.7	

- New Zealand:** Electrical faults with two downhole pumps are believed to be related to repeated shutdowns and restarts during the drilling and well hook-up phase of development, which is essentially over. Tie-in of the MR9 well accessing the upper (M2A zone) should commence in May, to be followed by repair of failed pumps and modifications to increase water re-injection rates, after which we expect production rates to increase to ~30 kbd. Additional seismic acquisition and processing is underway to better define exploration targets for future drilling (in FY12).
- China:** Commercial negotiations with the Chinese partners continue for development of the Block 22/12 project. FID and the start of development work are expected in 2HCY10. First oil is planned for FY12.
- PNG:** Drilling of the Stanley-2 well (PRL4) is expected to commence in August 2010 to be followed by Elevala-2 (PRL5) in November. Tenders have been received from contractors for front end engineering and design work for the proposed Stanley condensate product and HZN is awaiting regulatory approval for a Production Development Licence.
- USA:** HZN has withdrawn from its Bayou Chocktaw leases.
- Balance sheet:** Cash \$US26.0m, plus ~\$US25m remaining of Talisman farm-in funding. Debt \$US26m.

Year to June	NPAT (Rep) \$M	NPAT (PSig) \$M	EPS (PSig) c	EPS Growth %	PER x	CFPS c	P/CF x	DPS c	Div Yld %	Franking %
2009a	-7.9	-7.9	-0.9	57.9	-14.5	0.4	48.6	0.0	0.0	0
2010e	93.2	-0.2	0.0	97.8	-	2.1	17.1	0.0	0.0	0
2011e	31.6	32.3	2.8	13,900.0	11.5	4.5	8.0	0.0	0.0	0
2012e	58.1	35.6	3.0	10.1	10.0	3.5	10.1	0.0	0.0	0

Project status

Project	%	Key points
Maari Field, PMP 38160, PEL 38413, offshore Taranaki Basin, NZ	10	<ul style="list-style-type: none"> 0.14 mmbbl net Mar 2010 quarter. Cumulative oil production to 28 Apr 2010 was 7.6 mmbbl (gross). Production affected by MR3 & MR5 which were shut in for remedial mechanical work. Field was also shut in from 8-28 Jan 2010 for planned inspection and maintenance of the FPSO Raroa. MR9 well drilled in M2A sandstone – Production tested in early March and flowed 4kbd oil. Crude quality similar to Moki zone. MN1 well (Manaia Mangahewa zone) – Tie-in & hook-up scheduled to be completed in Apr/ May 2010. Subsurface evaluation and reservoir modelling of primary producing zone at Maari, the Moki sandstone, Maari M2A sandstone and the Manaia Mangahewa zone are continuing. Reserves update expected in 2HCY10. JV submitted application on 8 March 2010 for a petroleum mining permit in respect of Manaia field to the NZ Crown Minerals Group. The application seeks an expansion of PMP 38160 to encompass the Manaia field.
PEP 51313, offshore Taranaki Basin, NZ	30	<ul style="list-style-type: none"> Technical work confirmed high prospectivity of the permit with mature prospects Pike, Matariki, Te Whatu and Pukeko. Reprocessing of existing 2D & 3D seismic underway. Existing 3D provides continuous coverage over Maari, Manaia, Pike & Paua prospects. New 204 km² 3D began on 12 April 2010 and will continue the coverage from Paua to south of Matariki prospect. At the completion of 3D survey, 2 further lines totalling 80 km will be acquired to provide advance coverage on critical elements of the Te Whatu and Pukeko Prospects. New seismic in the Te Whatu area planned for 2HCY10/ 1HCY11. First well to drill in 2HCY11/ 1HCY12.
Block 22/12 (China)	30→ 14.7	<ul style="list-style-type: none"> Overall Development Plan (ODP) involves two stages. First phase involves development of Wei 6-12, Wei 6-12S and Wei 12-8W. The development concept involves two lightweight remote platforms, 6 wells per platform, tied back to CNOOC's Wei12-1A facilities. Will use existing water injection and gas processing. Technical section of ODP for Wei 6-12 and 12-8W combined development completed on 20 Dec 2009. Integrated development concept utilising an auxiliary platform (PUQB) to the existing CNOOC platforms. First oil expected CY12. Commercial negotiations with CNOOC on shared use of facilities expected to conclude by end of April. Completion of the economic section of the ODP is expected shortly to be followed by formal Chinese Govt approvals, FID and start of development work in 2HCY10. Exploration prospects adjacent to Wei 6-12S are to be tested at the time of development drilling and included in development if successful. A second development phase involving Wei 12-8E and Wei 12-3 is anticipated after production from the first phase.
PRL 4, Stanley Field, PNG	50	<ul style="list-style-type: none"> Stanley-2 – Well site has been cleared and civil work to commence in 2QCY10. Drilling rig negotiations underway with drilling to commence in Aug 2010. Further wells, Stanley-3 and -4, likely. Application for a PDL for the Stanley Field is progressing and lodged with PNG Govt. Negotiations on gas agreement (as part of the PDL application) with the DPE are also continuing. Tenders have been received for FEED of a gas processing plant to be constructed in well Stanley-4 location.
PRL 5, Elevela/ Ketu, PNG	50	<ul style="list-style-type: none"> Elevela-2 appraisal well – Progressing in parallel with Stanley-2. As a result of new mapping, decided to acquire ~60 km of new seismic before final decision is made. Seismic to be located in area between Elevela and Tingu to define the structure. Expect to drill in Nov 2010. Likely to be followed with Ketu-2.

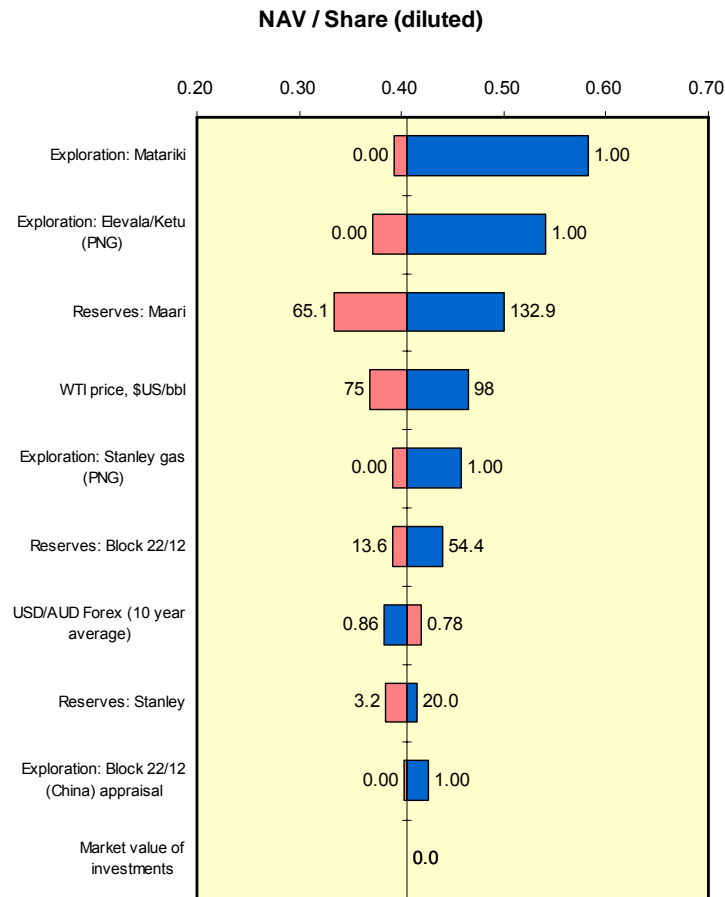


Modelling changes

Key changes to our model are as follows:

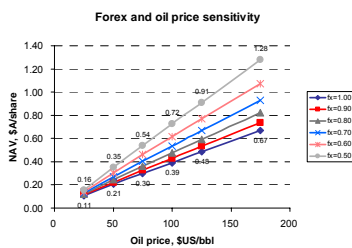
- Downward revision to Maari June half 2010 production due to downhole pump issues.
- Increase in Block 22/12 capex (~\$US250 gross -> ~\$US300 gross).

Sensitivity analysis



Source: Wilson HTM

The Tornado chart shows the impact of changes in individual variables on the valuation. Variables are ranked from highest to lowest impact on the valuation and are centred on the expected (i.e. the mean) outcome. The ends of each bar correspond to the P90 (red bar) and P10 (blue bar) probability level of the variable concerned (where P90 indicates a 90 % probability of the value being above a given level). The values at the end of each bar are the values of the variable concerned at the P90 and P10 probability levels.



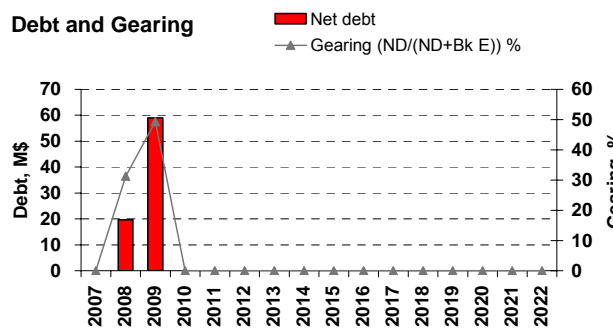
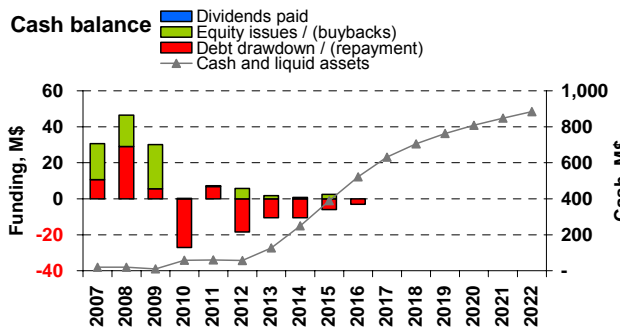
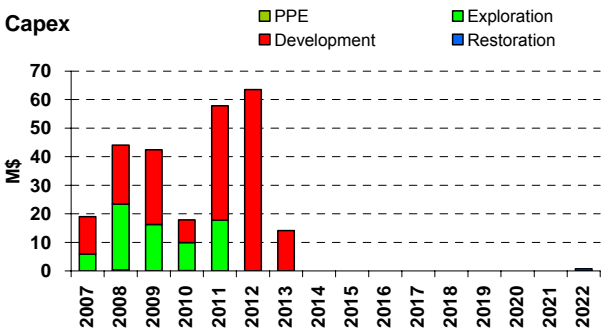
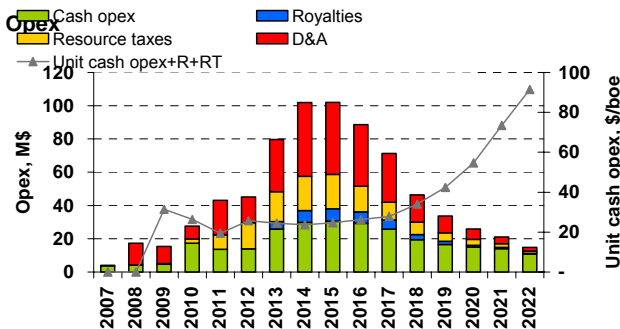
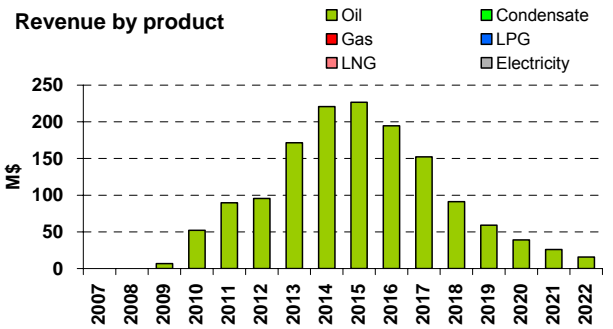
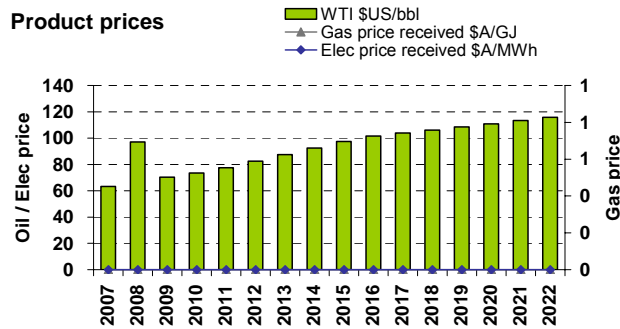
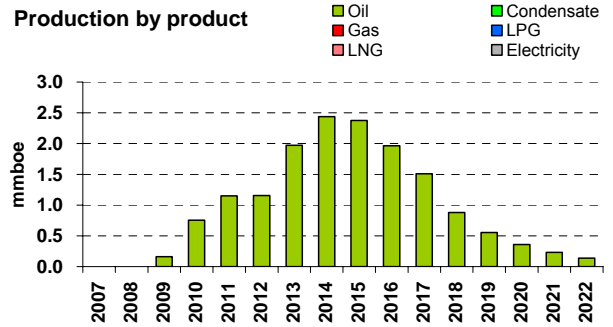
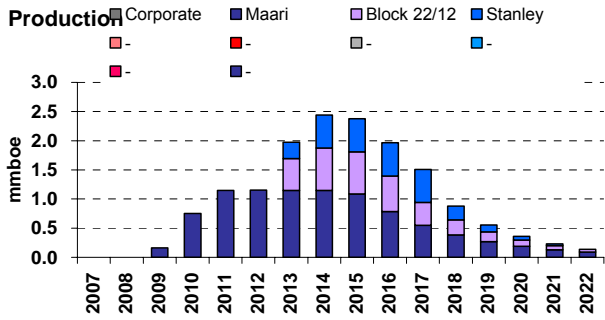
Share price sensitivity to oil price and exchange rate

NAV Sensitivity table	\$A/share					
	\$US/\$A forex		Real oil price, \$US/bbl			
	25	50	75	100	125	175
fx= 1.00	0.11	0.21	0.30	0.39	0.48	0.67
fx=0.90	0.11	0.22	0.33	0.43	0.53	0.74
fx=0.80	0.12	0.24	0.36	0.48	0.59	0.82
fx=0.70	0.13	0.27	0.40	0.53	0.67	0.93
fx=0.60	0.14	0.30	0.46	0.61	0.77	1.07
fx=0.50	0.16	0.35	0.54	0.72	0.91	1.28



Horizon Oil Limited (HZN)

\$US currency unless otherwise noted. Nominal \$ basis. Year ending June.



Valuation summary: HZN

Field / Well	Expected Interest %	Risk factor %	Oil volume mmbbl	Gas volume PJ	NPV value \$US/boe	EMV risked M\$A	EMV risked \$A/sh	EMV unrisks \$A/sh	EMV risked %
DCF modelled projects									
Maari	10.0	90	84	-	32.40	301	0.26	0.29	62.7
Block 22/12	14.0	40	27	-	25.80	50	0.04	0.10	10.3
Stanley	38.8	40	8	-	20.30	25	0.02	0.06	5.1
-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-
Total (attributable, risked)			10	0		375	0.32	0.45	78.2
Exploration / Appraisal									
-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-
Block 22/12 (China) appraisal	14.7	10	15	-	9.70	3	0.00	0.02	0.5
-	-	-	-	-	-	-	-	-	-
Stanley gas (PNG)	38.8	20	-	306	3.30	16	0.01	0.07	3.3
Elevala/Ketu (PNG)	38.8	20	26	441	4.30	40	0.03	0.17	8.3
-	-	-	-	-	-	-	-	-	-
Pike	30.0	-	-	-	-	-	-	-	-
Matariki	30.0	10	112	-	5.60	15	0.01	0.19	3.2
Te Whatu	30.0	-	-	-	-	-	-	-	-
Paua	30.0	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-
Total (attributable, risked)			6	58		73	0.06	0.45	15.3
Other items (corporate, cash, debt, etc)									
Total Other						26	0.02	0.02	5.3
Total DCF Valuation (diluted)			16	58		474	0.41	0.92	100.0
Assumptions									
Forex (10 year average)	USD/AUD	0.81				M\$A	\$A/sh	TSR, %	Dividend \$A/sh
Discount rate (nominal, after tax)	%	11.5				Current market	400	0.36	-
Number of shares (undiluted)	-	1,126.6				Valuation: base	474	0.41	15.5
Number of shares (diluted)	-	1,169.8				low	-	-	-
Valuation reference date		Jun-10				high	-	-	-
		@ \$US85/bbl real & 0.93 fx				spot	421	0.36	1.4
		20 Apr 2010 Nymex strip				futures	468	0.40	12.7
		0% discount to forward NPV				Price target	538	0.46	29.6
									0.00

Notes

- 1) This table summarizes the sum-of-the-parts DCF valuation derived from the main financial model.
- 2) Expected interest = expected average equity interest in project based on modelled reserves and production
- 3) Risk = Project risk factor. This is the product of geological chance of success and commercial maturity.
Typical risk values are ~10% for exploration, ~30-60% for appraisal, ~60-80% for development & 90-100% for production.
- 4) Oil volume = 2P (proved & probable) oil & condensate reserves where data are available or P50 recoverable resource.
- 5) NPV value = estimated NPV multiple per 2P reserves derived from the DCF model of the project or a project analogue.
- 6) EMV = Expected Monetary Value (= project NPV * company share * risk factor).
- 7) EMV/sh = EMV/fully diluted share. Dilution includes assumed future capital raisings in addition to existing options, etc.
- 8) unrisks = company share of project NPV assuming full success (i.e. no risk factor applied).
- 9) The "Low" and "High" valuation estimates are derived from Monte Carlo simulation (@ 90% and 10% probability levels).
- 10) TSR = total shareholder return = (12 month share price appreciation + dividends) / current share price.

Horizon Oil Limited (HZN : \$0.36)

PRODUCTION

Yr Ending June	2008A	2009A	2010E	2011E	2012E
Liquids, mmbbl	0.0	0.2	0.8	1.1	1.2
Gas, PJ	0	0	0	0	0
Electricity, TWh	0.0	0.0	0.0	0.0	0.0
Total, mmbob	0.0	0.2	0.8	1.1	1.2

PRICES

Yr Ending June	2008A	2009A	2010E	2011E	2012E
\$/US\$/A forex	0.90	0.75	0.89	0.89	0.86
WTI, \$US/bbl	97	70	74	78	83
Gas received, \$A/GJ	-	-	-	-	-
Electricity rec'd, \$A/MWh	0	0	0	0	0

INVESTMENT & VALUATION FUNDAMENTALS

Yr Ending June	2008A	2009A	2010E	2011E	2012E
EPS Before Abs (c)	-2.1	-0.9	0.0	2.8	3.0
EPS Growth (%)	N/A	57.9%	97.8%	13,900.0	10.1%
PER (x)	-17.0	-14.5	-1,580.5	11.5	10.0
CFPS (c)	-0.4	0.4	2.1	4.5	3.5
P/CF (x)	-112.9	48.6	17.1	8.0	10.1
EV/EBITDA (x)	-71.8	60.8	10.1	4.7	4.0
DPS (c)	0.0	0.0	0.0	0.0	0.0
Yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%
Franking (%)	0%	0%	0%	0%	0%

DCF VALUATION

	@ 11.5%		@ 10.0%	
	A\$m	A\$ps	A\$m	A\$ps
Production	301	0.26	317	0.27
Development	0	0.00	0	0.00
Appraisal	132	0.11	159	0.14
Exploration	15	0.01	24	0.02
Corporate costs	-29	-0.02	-32	-0.03
Hedge book	0	0.00	0	0.00
Interests - other entities	0	0.00	0	0.00
Franking credits (@ 50 %)	0	0.00	0	0.00
Cash	65	0.06	65	0.06
Debt + Conv. Notes	-46	-0.04	-46	-0.04
Minorities / Other	27	0.02	39	0.03
Additional Capital - Dilution	10	0.01	10	0.01
Total Valuation - Fully Diluted	474	0.41	536	0.46

Valuation as of 30th June 2010

PROFITABILITY RATIOS

Yr Ending June	2008A	2009A	2010E	2011E	2012E
EBIT / Sales (%)	-	-82.7%	53.8%	61.1%	69.3%
ROA (%)	N/A	-6.6%	18.7%	30.0%	29.2%
ROE (%)	N/A	-15.3%	-0.2%	19.1%	16.4%
ROFE (%)	N/A	-7.4%	21.5%	35.4%	33.5%

INTERIMS (US\$m)

Half Yr	Dec 08	Jun 09	Dec 09	Jun 10	Dec 10
Yr Ending June	1H A	2H A	1H A	2H E	1H E
Sales Revenue	0.0	8.1	24.4	26.5	43.8
EBIT	-9.4	2.6	14.8	12.7	26.4
Net Profit	-10.0	2.1	58.4	34.8	16.0
EPS	-1.2	0.2	0.4	-0.4	1.4

BALANCE SHEET (US\$m)

Yr Ending June	2008A	2009A	2010E	2011E	2012E
Cash	19.6	10.0	58.8	60.3	57.3
Total Assets	94.7	140.2	222.1	262.5	308.1
Debt	39.2	69.0	42.1	48.9	30.4
Total Liabilities	51.4	79.5	69.3	77.8	59.5
Total Shareholders Equity	43.2	60.6	152.8	184.7	248.6
Total Funds Employed	62.9	119.6	136.1	173.4	221.7

LIQUIDITY & LEVERAGE RATIOS

Yr Ending June	2008A	2009A	2010E	2011E	2012E
Debt / Equity (%)	90.7%	113.9%	27.5%	26.5%	12.2%
Gearing (%) ¹	47.6%	53.3%	21.6%	20.9%	10.9%
Interest Cover (x)	25.1	-2.9	9.7	532.1	-247.5
Debt / CashFlow (x)	-14.4	22.0	1.7	0.9	0.7
(Debt+CNNotes) / CashFlow	-11.1	57.1	2.1	0.9	0.7

PROFIT & LOSS (US\$m)

Yr Ending June	2008A	2009A	2010E	2011E	2012E
Sales Revenue	0.5	7.9	51.0	89.7	95.7
EBITDA	-3.8	3.3	35.1	75.6	81.8
Depn and Amortisation	13.1	10.3	7.7	20.8	15.5
EBIT	-16.9	-7.0	27.4	54.8	66.3
Net Interest Expense	-0.7	2.4	2.8	0.1	-0.3
Pre-tax Profit	-16.2	-9.4	24.6	54.7	66.6
Tax	0.0	-1.5	24.8	22.5	31.0
Tax rate (%)	0.0%	15.7%	100.8%	41.0%	46.6%
Minorities / pref divs	0.0	0.0	0.0	0.0	0.0
Equity accounted NPAT	0.0	0.0	0.0	0.0	0.0
Net Profit	-16.2	-7.9	-0.2	32.3	35.6
Abnormals	0.0	0.0	93.4	-0.6	22.5
Reported Net Profit	-16.2	-7.9	93.2	31.6	58.1

CASHFLOW (US\$m)

Yr Ending June	2008A	2009A	2010E	2011E	2012E
Operating Cash Flow	-2.7	3.1	24.2	52.1	41.1
Capital Expenditure	-21.0	-26.3	-8.1	-40.1	-63.5
Expln, Develop, Evaln	-23.1	-16.2	-9.8	-17.8	0.0
Asset Sales/Acquisitions	0.0	0.0	69.3	0.0	32.2
Other	0.0	0.0	0.0	0.0	0.0
Investing Cash Flow	-44.1	-42.5	51.4	-57.8	-31.3
Share Issues/(Buybacks)	17.9	25.5	0.3	0.4	5.8
Debt Drawdown (Repay)	29.1	5.6	-27.1	6.9	-18.5
Dividends Paid	0.0	0.0	0.0	0.0	0.0
Other Fin. Flows	-0.5	-0.9	-0.1	0.0	0.0
Financing Cash Flow	46.4	30.2	-26.9	7.2	-12.7
Cash Increase (Decrease)	-0.4	-9.2	48.8	1.5	-2.9

EARNINGS SENSITIVITIES - % CHANGE

Yr Ending June	2008A	2009A	2010E	2011E	2012E
+10% forex					
+10% oil price					
+10% gas price					
+10% electricity price					

1. Gearing = (Debt + CNotes) / (Debt + CNotes + Equity)



Recommendation Structure

BUY: Total return +10% or more over a 12 month period

HOLD: Total return expected to be between +10% to -10% over a 12-month period

SELL: Total return expected to be -10% or more over a 12 month period

TOTAL RETURN OR TSR = capital growth in share price + expected dividend yield in that period

Other definitions

CS Coverage Suspended. Wilson HTM Ltd has suspended coverage of this company.

NR Not Rated. The recommendation has been suspended temporarily. Such suspension is in line with Wilson HTM Investment Group Ltd policies in circumstances where Wilson HTM Corporate Finance Ltd is acting in an advisory capacity in a merger or strategic transaction involving the company and in certain other situations.

Disclaimer

Whilst Wilson HTM Ltd believes the information contained in this communication is based on reliable information, no warranty is given as to its accuracy and persons relying on this information do so at their own risk. To the extent permitted by law Wilson HTM Ltd disclaims all liability to any person relying on the information contained in this communication in respect of any loss or damage (including consequential loss or damage) however caused, which may be suffered or arise directly or indirectly in respect of such information. Any projections contained in this communication are estimates only. Such projections are subject to market influences and contingent upon matters outside the control of Wilson HTM Ltd and therefore may not be realised in the future.

The advice contained in this document is general advice. It has been prepared without taking account of any person's objectives, financial situation or needs and because of that, any person should, before acting on the advice, consider the appropriateness of the advice, having regard to the client's objectives, financial situation and needs. Those acting upon such information without first consulting one of Wilson HTM Ltd investment advisors do so entirely at their own risk. This report does not constitute an offer or invitation to purchase any securities and should not be relied upon in connection with any contract or commitment whatsoever. If the advice relates to the acquisition, or possible acquisition, of a particular financial product – the client should obtain a Product Disclosure Statement relating to the product and consider the Statement before making any decision about whether to acquire the product. This communication is not to be disclosed in whole or part or used by any other party without Wilson HTM Ltd's prior written consent.

Disclosure of Interest. Horizon Oil Limited

The Directors of Wilson HTM Ltd advise that at the date of this report they and their associates have relevant interests in Horizon Oil Limited. They also advise that Wilson HTM Ltd and Wilson HTM Corporate Finance Ltd A.B.N. 65 057 547 323 and their associates have received and may receive commissions or fees from Horizon Oil Limited in relation to advice or dealings in securities. Some or all of Wilson HTM Ltd authorised representatives may be remunerated wholly or partly by way of commission.

In producing research reports, members of Wilson HTM Ltd Research may attend site visits and other meetings hosted by the issuers the subject of its research reports. In some instances the costs of such site visits or meetings may be met in part or in whole by the issuers concerned if Wilson HTM Ltd considers it is appropriate and reasonable in the specific circumstances relating to the site visit or meeting.

BRISBANE
Ph: 07 3212 1333
Fax: 07 3212 1399

SYDNEY
Ph: 02 8247 6600
Fax: 02 8247 6601

MELBOURNE
Ph: 03 9640 3888
Fax: 03 9640 3800

GOLD COAST
Ph: 07 5509 5500
Fax: 07 5509 5599

DALBY
Ph: 07 4660 8000
Fax: 07 4660 4169

HERVEY BAY
Ph: 07 4197 1600
Fax: 07 4197 1699

TOWNSVILLE
Ph: 07 4725 5787
Fax: 07 4725 5104

GEELONG
Ph: 03 5225 1500
Fax: 03 5225 1599

Our web site: www.wilsonhtm.com.au