

## Initial Production Exceeds Expectations

### Investment Highlights

- The Newest Eagle Ford Producer.** AZZ yesterday reported initial production rates from the Frances Dilworth No. 2H of 790bopd and 0.9mmscf/d, equating to 15.4mmscfe/d on an 18:1 basis. This exceeds production guidance provided by NuTech's fracture stimulation modelling which suggested an IP of 11.4mmscfe/d on an 18:1 basis. The initial result is a tremendous success on a number of fronts; firstly de-risking AZZ by confirming that the company's acreage is across a highly productive shale, secondly confirming production above expectations and thirdly indicating that the acreage has a higher liquids content than anticipated.
- Production test significantly oilier than anticipated.** The production test produced significantly higher liquids levels than the modelled rate, at 850bbls/mmscf compared to 50bbls/mmscf. From an economic perspective there is no doubt that the result is an improvement on the predicted rates and on a technical front the result can be explained by 1) conservatism of the model, 2) AZZ's up-dip position and 3) it is worth noting the emerging stage of the play and that the results will help define trends across the shale.
- We have upgraded our recommendation from speculative to a BUY with an increased price target of \$1.03/sh.** We have increased our Yellow Rose valuation, moving from a 20% to 25% risking to mark progress towards booking reserves and de-risking the modelled 2C resource. Our valuation utilises a full field development based on the NuTech modelled rates but will look to readdress this as more production data becomes available.
- AZZ to push ahead.** AZZ's forward program has potential to unlock substantial value with a further 9 wells planned for 2010 and the results from the first 3 wells (subject to timing) to be included in its reserves assessment at the end of March Q. AZZ had \$1.7m as at the Dec Q following \$9.3m in expenditure on the well, gas trunkline and fracc pond. Costs for the 2 upcoming wells in the March Q are ~US\$10m. While we modelled additional equity of A\$50m into our valuation over 2010/2011, we would anticipate debt drawdown and or small capital raising shortly, to meet immediate requirements.

2 February 2010

12mth Rating		BUY
Price	A\$	0.65
Target Price	A\$	1.03
12m Total Return	%	59.8
RIC: <b>AZZ.AX</b>		BBG: <b>AZZ AU</b>
Shares o/s	m	246.4
Free Float	%	100.0
Market Cap.	A\$m	158.9
Net Debt (Cash)	A\$m	13.3
Net Debt/Equity	%	530.1
3m Av. D. T'over	A\$m	0.36
52wk High/Low	A\$	0.74/0.04
2yr adj. beta		0.98

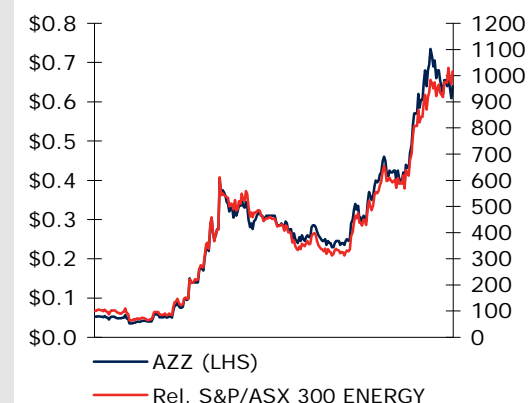
#### Valuation:

Methodology		DCF
Value per share	A\$	1.03

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*Disclosure: Patersons Securities was the Lead Manager to the \$10m Institutional Placement and \$4.2m SPP in August 2009. It was paid a fee for these services.*

#### 12 Month Share Price Performance



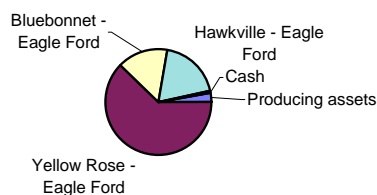
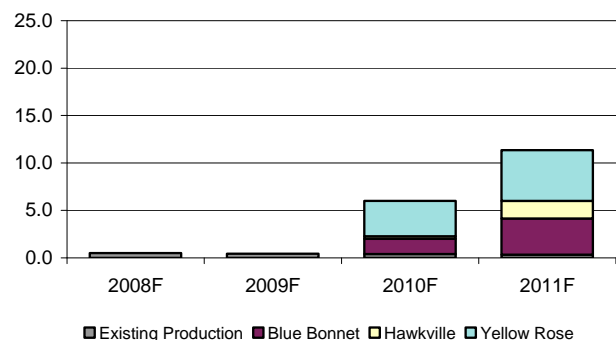
Performance %	1mth	3mth	12mth
Absolute	5.2	42.1	694.1
Rel. S&P/ASX 300	7.2	39.5	500.3

Year End Dec 31	2008A	2009F	2010F	2011F	2012F
Reported NPAT (\$m)	0.6	(0.9)	44.9	77.3	108.3
Recurrent NPAT (\$m)	0.6	(0.9)	44.9	77.3	108.3
Recurrent EPS (cents)	0.4	(0.5)	18.5	31.3	43.8
EPS Growth (%)	na	na	na	69.0	40.0
PER (x)	182.5	(128.3)	3.5	2.1	1.5
EBITDA (\$m)	4.7	2.4	46.8	95.5	159.9
EV/EBITDA (x)	26.0	53.3	3.4	1.4	0.7
Free Cashflow	(6.0)	(16.2)	(18.6)	16.7	20.1
FCFPS (cents)	(3.5)	(9.1)	(7.7)	6.7	8.1
PFCF (x)	(18.3)	(7.1)	(8.4)	9.6	7.9
DPS (cents)	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	0.0	0.0	0.0

**Antares Energy Ltd****\$0.65**

Valuation	A\$m	A\$/sh
Producing assets	11	0.03
Yellow Rose - Eagle Ford	240	0.69
Bluebonnet - Eagle Ford	60	0.17
Hawtkville - Eagle Ford	73	0.21
Exploration and Appraisal	3	0.01
Cash (est)	2	0.00
Debt	(15)	(0.04)
Corporate	(15)	(0.04)
Other	0	0.00
<b>Total @ 10% Discount Rate</b>	<b>358</b>	<b>1.03</b>
<b>Price Target</b>		<b>1.03</b>

Price Target Sensitivity	-10%	0%	+10%
Gas Price Sensitivity (A\$/sh)	0.93	1.03	1.13
Oil Price Sensitivity (A\$/sh)	0.95	1.03	1.11
Exchange Rate Sensitivity (A\$/sh)	1.15	1.03	0.93

**Valuation Summary of Operating Assets****Production Summary****Reserves & Resources**

Reserves	Oil/Cond (mmbbl)	Gas (bcf)	Total (mboe)
2P Reserves as at Dec 2008	0.04	3.26	0.58

**Directors**

Name	Position
James Cruickshank	Chairman & Chief Executive Officer
Matthew Gentry	Director & Chief Operating Officer
Gregory Shoemaker	Director & Chief Scientist
Vicky McAppion	Director & Company Secretary
Mark Clohessy	Non-Executive Director

**Substantial Shareholders**

	Shares (m)	%
HEP Oil GP, L.L.C	24.0	9.9
Yandal Investments Pty Ltd	12.2	5.1

Commodity Assumptions	Year End December 31			
	2008A	2009F	2010F	2011F
A\$:US\$	0.85	0.75	0.82	0.80
Crude Oil - WTI (USD/bbl)	99.61	56.71	77.50	86.06
Gas Price - Base Case (US\$/GJ)	5.00	5.17	5.04	5.14

Production Summary	2008A	2009F	2010F	2011F
<b>Gas (bcf)</b>				
Yellow Rose	0.00	0.00	2.88	4.13
Blue Bonnet	0.00	0.00	1.22	2.94
Hawtkville	0.00	0.00	0.20	1.41
Oyster Creek	0.00	0.64	0.61	0.57
West Wharton	0.00	0.14	0.12	0.11
<b>Total Gas (bcf)</b>	<b>0.00</b>	<b>0.78</b>	<b>5.03</b>	<b>9.16</b>
<b>Liquids (mmbbl)</b>				
Yellow Rose	0.00	0.00	0.14	0.21
Blue Bonnet	0.00	0.00	0.06	0.15
Hawtkville	0.00	0.00	0.01	0.07
Oyster Creek	0.00	0.04	0.05	0.03
West Wharton	0.00	0.01	0.01	0.01
Total Liquids (mmbbl)	0.00	0.05	0.27	0.46
<b>Total (bcfe)</b>	<b>0.50</b>	<b>0.43</b>	<b>6.00</b>	<b>11.35</b>
<b>Total (mmbbl)</b>	<b>0.09</b>	<b>0.07</b>	<b>1.00</b>	<b>1.89</b>

Profit & Loss (A\$m)	2008A	2009F	2010F	2011F
<b>Sales Revenue</b>	<b>8.1</b>	<b>3.6</b>	<b>51.9</b>	<b>103.8</b>
Other Income	1.4	0.1	0.5	1.3
Operating Costs	0.9	0.3	4.0	7.6
Exploration Exp.	1.7	0.0	0.0	0.0
Royalties	0.0	0.0	0.0	0.0
Corporate/Admin	2.2	1.0	1.7	2.0
<b>EBITDA</b>	<b>4.7</b>	<b>2.4</b>	<b>46.8</b>	<b>95.5</b>
Depn & Amort	1.6	1.6	0.4	1.4
<b>EBIT</b>	<b>3.1</b>	<b>0.8</b>	<b>46.4</b>	<b>94.1</b>
Interest	2.5	1.7	1.5	1.4
<b>Operating Profit</b>	<b>0.6</b>	<b>(0.9)</b>	<b>44.9</b>	<b>92.6</b>
Tax expense	0.0	0.0	0.0	15.3
Minorities	0.0	0.0	0.0	0.0
Discontinued Operations	0.0	0.0	0.0	0.0
<b>NPAT</b>	<b>0.6</b>	<b>(0.9)</b>	<b>44.9</b>	<b>77.3</b>
<b>Normalised NPAT</b>	<b>0.6</b>	<b>(0.9)</b>	<b>44.9</b>	<b>77.3</b>

Cash Flow (A\$m)	2008A	2009F	2010F	2011F
Adjusted Net Profit	0.6	(0.9)	44.9	77.3
+ Interest/Tax/Expl Exp	4.2	1.7	1.5	16.8
- Interest/Tax/Expl Inc	11.7	9.2	1.5	16.8
+ Depn/Amort	1.6	1.6	0.4	1.4
+/- Other	(0.7)	(0.0)	0.0	0.0
<b>Operating Cashflow</b>	<b>(6.0)</b>	<b>(6.9)</b>	<b>45.3</b>	<b>78.8</b>
- Capex (+asset sales)	0.0	9.3	63.9	62.1
- Working Capital Increase	0.0	0.0	0.0	0.0
<b>Free Cashflow</b>	<b>(6.0)</b>	<b>(16.2)</b>	<b>(18.6)</b>	<b>16.7</b>
- Dividends (ords & pref)	0.0	0.0	0.0	0.0
+ Equity raised	2.5	14.7	30.0	10.0
+ Debt drawdown (repaid)	(1.0)	(3.2)	0.0	0.0
+ Other	0.0	1.7	0.0	0.0
<b>Net Change in Cash</b>	<b>(4.5)</b>	<b>(3.0)</b>	<b>11.4</b>	<b>26.7</b>
Exchange rate effects	1.1	(0.9)	0.0	0.0
Cash at End Period	5.6	1.7	13.1	39.7
Net Cash/(Debt)	(13.0)	(13.4)	(2.0)	24.7

Balance Sheet (A\$m)	2008A	2009F	2010F	2011F
Cash	5.6	1.7	13.1	39.7
Total Assets	22.1	33.3	112.2	199.5
Total Debt	18.6	15.1	15.1	15.0
Total Liabilities	19.6	31.6	65.6	75.6
Shareholders Funds	2.5	1.6	46.6	123.9

Ratios	2008A	2009F	2010F	2011F
Net Debt/Equity (%)	518.6	826.8	4.4	na
Interest Cover (x)	1.2	na	na	na
Return on Equity (%)	23.9	na	96.5	62.4

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