

This Week
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Reminder:

For every friend or colleague who signs up to StockAnalysis and quotes you as a referee, we will add two months to your subscription, free of charge.

Indices & Prices

All Ordinaries	4,788.90
Energy Index	16,475.40
Brent AU\$/bbl	108.46
AUS\$/US\$	1.0668

As at Close May 31st, 2011

In this Issue

Cooper Basin Dries Out: COE & BPT drill for 'sizeable' oil pool.

Carnarvon Drilling: Oilex's duster dulls Cue's shine

Media Madness: Bad dives out good

All Ords: Recovered to 4800, but still in down trend

China!: Beware the Marco Polo Syndrome

Buru: Ready to drill

Antares: A go out of business value of 62 cps

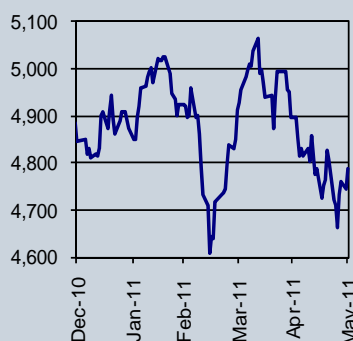
Market Moves

Cooper Energy (COE) and **Beach Energy (BPT)** have commenced drilling at Turton-1, targeting a P50 resource of 4.6 million barrels of oil. **Success at this level would be worth 11 cps to Cooper**, which has a 25% interest in PEL-92 and would reverse a run of outs with projects at Menzel Horr in Tunisia and its most recent Cooper Basin wells at Parham and Stenhouse.

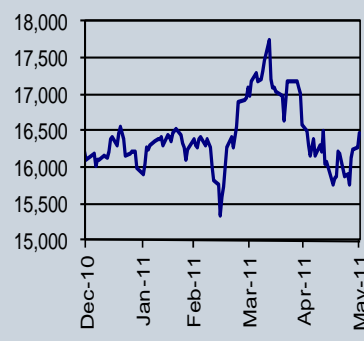
Cue Energy (CUE) received a market drubbing following drilling of the **La Rocca** duster by Apache last week. Even though Cue was not involved, its partnership with Woodside in neighbouring WA-389-P relies on an anomalous trend identified by seismic data which runs from WA-388-P into Cue's ground. La Rocca had an AVO seismic signature which looked similar to that seen by Apache at its Julimar and Brunello gas fields but the AVO bright spots here may have been the result of exceptionally high porosity in the target zone, which is unusual at a depth of greater than 4,500 metres. While no hydrocarbons were present at La Rocca, the discovery of such good reservoir characteristics would be fantastic if it were found to be full of gas at another location. Next door, Woodside has been active, acquiring additional seismic data, with the aim of drilling in early 2012. No doubt the results from La Rocca will be factored in to Woodside's decision making process, but StockAnalysis would be surprised if the La Rocca result kills the WA-389-P venture. There are several play types in the permits, ranging from structural to stratigraphic. Drilling by Apache and Oilex was limited by the operating water depth of its rig, so my guess is that Apache will be back for another attempt in deeper water next year, once it gets the right gear with which to drill. Meanwhile, Cue is interpreting new seismic data over prospects in the Taranaki Basin, south of its Maari oilfield. The company is also progressing with expansion of its 15% held Indonesian oil and gas production. **Cue's price is underpinned by about 27 cents per share of value for net cash and its producing oil & gas assets, so there is currently very little value registering for exploration upside and it remains a speculative buy.**

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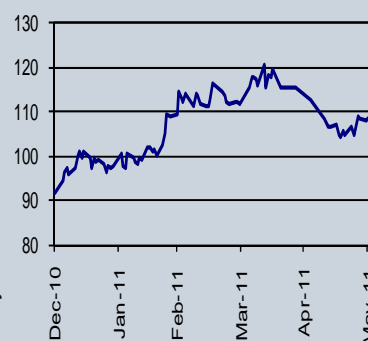
All Ordinaries



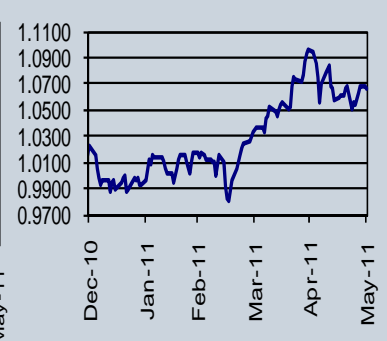
S&P ASX 200 Energy Index



Brent Crude Oil \$A/barrel



A\$/US\$



Media Madness is rising to a fever pitch in Australia as **Gresham's Law** shows its power. Sixteenth Century economist Sir Thomas Gresham, was one of many who observed that bad money drives out good and this 'law' can also be applied loosely to morals and ethics. The theory goes that if there are two coins or currencies of equal face value, but one unit (the good) has a higher intrinsic value by dint of its higher metal content for instance, then the 'bad' coin will prevail as the 'good' coin is withdrawn by hoarders. This rule might be seen to apply to the US dollar, which is widely used despite its lack of any real value, while gold is withdrawn and held by those seeking a currency of real and sustainable value.

So it is with the mainstream media. Here, the often low-brow and hopelessly compromised commercial media machine is beholden to strong special interests, represented by the likes of industry lobby groups as well as the automobile, telecoms, grocery and the property development and construction industries that pay to use commercial media services. These powerful economic groups generate revenue for the likes of the Murdoch press which gives them primacy to influence the way the commercial press represents current events and political debates to the broader community. The commercial media's special pleading appeals to its own commercial interests and customers, who continue to generate revenue for their shareholders at the expense of more reasoned argument. It appears that there is no currency in reasoned argument and that the poorly thought out currency of a powerful elite prevails. Alternative voices, which we might portray as 'good', are too often excluded from access to the mass media and so struggle to get their voices heard, so Gresham's law applies as bad drives out good.

The blogosphere has similar characteristics, where often the 'signal' or idea is lost to the noise created by activists with special interests. This can be seen in the current debate on taxing carbon, where the idea is swamped by noise from special pleading to the detriment of the actual thrust of the idea.

In StockAnalysis' opinion, deregulation of Australia's media in the 1980s led to consolidation and a downward spiral in the quality of reporting. The infrastructure of mainstream media has become all powerful, but new media opens up alternative, though perhaps less well travelled channels. To paraphrase Marshal McLuhan, the medium has become the message.

A special case has erupted, where the Murdoch/Fox media is currently running a vendetta against Australia's public broadcaster, the ABC, and public broadcasters in general, including the BBC. The ABC does not have to pander to any special funding interests. The organisation has a board of management and operates under a charter to be fair and to offer balanced views. However, the ABC's move to provide a quality alternative to the trash dished up as news by most of the commercial media in a 24 hour news reporting service, threatens the commercial interests of News Corporation, which is desperately trying to weaken the ABC and force it to withdraw.

Let's see if bad drives out the good or if the Federal Government will cave to powerful sectional interests that would emasculate the ABC. I am hoping that the ABC will flourish and that new media, like StockAnalysis, will provide an alternative to Dr Who's 'Bad Wolf Company'.

"bad drives out good"

Alternative voices are too often excluded from access to the mass media

The medium has become the message

The ABC does not pander to any special funding interests



The Aussie market has recovered to meet its 200 day moving average trending up and the 30 day moving average on the way down in action reminiscent to May/June 2010. The 4,800 level on the All Ords has been influential and the market looks set to trade around that level, after which further weakness is expected and StockAnalysis recommends taking cash out of the market at this level.

China!

- **StockAnalysis** feels that rising interest rates in China and uncomfortably high food prices, raises a potential for increased social unrest, resulting in some sort of dislocation to its current economic growth path during 2012. The country is facing a severe drought, which will limit domestic food production in 2010, keeping the price of corn, wheat, rice and soybeans higher than previously expected. Water shortages in China go hand in hand with water and air pollution, which is going to impact not only on crop yields but also human health in China in coming decades.
- As China ramps up its global acquisition of assets to provide access to raw materials to feed its industry and agricultural lands to feed its people, global tensions are likely to rise. China will not follow the failed Japanese business model of the 1930s, but as it arms itself, it will exert more strategic power in the Pacific and beyond.

These days you only have to write the heading 'China' to get people's attention. There is no need to say any more, as the word China evokes a wide eyed response from investors, especially investors in Australia, which has effectively become China's southern province in the eyes of many. There is however what I call a **Marco Polo syndrome** when China is mentioned. The numbers involved when describing Chinese economic development are so huge that sometimes, rational thought processes are hard to follow and get distorted by the enormity of what China is accomplishing. In common with that 15th Century Venetian, people tend to get excited by the scale of Chinese events and forget to look at the underlying outcome and value.

Bentley Continental. Just the thing for a Shanghai commute!



But in China, the music is well and truly still playing and the dancers are all up and out of their seats. At the recent Shanghai motor show, Roll Royce sold 60 of its Bentley Continentals at an estimated A\$211,000 each in the UK and A\$375,000 in Australia (see alongside) and this is over and above the 302 vehicles sold into China in the March quarter alone. The company was bowled over with this outcome, since it had only ever sold a handful of vehicles at its previous best effort.

Several presentations at last week's **Stockbrokers conference** in Sydney focused on the outlook for China. This was particularly pertinent following the release of China's 13th 5-year development plan last month. The **latest 5-plan** aims to improve the quality of life for Chinese. It focuses on income redistribution, putting in place social security safety nets, cleaning up the environment, continuing to urbanise 20 million people per year and refocusing

the economy towards domestic led growth, through home-grown consumption and away from export led growth. The nation aims to increase its welfare backup, building 35 million new affordable housing units over 5 years.

Structural **inflation** has become a big issue for China. Wages have been growing strongly and remarkably, the country has a shortage of labour! Wages are growing so rapidly that in order to keep pace with inflation, the minimum wage is now set every six months. The days of cheap Chinese labour are rapidly coming to an end, forcing some Chinese entrepreneurs to look towards Sri Lanka, Bangladesh or Vietnam for skilled workers.

(Continued on page 4)

China is working to establish its currency the **Yuan** as a widely used unit for settlement of trade flows and it expects that outbound investment will continue to rise from its current rate of about US\$59 billion pa. This rate of outbound investment has increased 25 fold in 10 years as fiscal surpluses grow. China has established huge financial reserves of about \$3 trillion, only 2% of which is represented by **gold**. If China wanted to raise its gold holdings towards the average of 15% it would need to buy all the gold mined for a whole year, which leads many to remain bullish on the gold price.

Clear **risks** for China will be an inevitable decline in domestic savings as consumption is boosted and rising inflation, which is likely to see additional hikes in interest rates by the Chinese Central Bank as 2011 rolls on. Higher interest rates combined with Central Bank and government initiatives are aimed at pulling economic growth back towards 8%. The Chinese property market is also overheated in large coastal cities.

The Chinese economy will refocus towards expanding its **service sector** while boosting high-tech sectors, including automated manufacturing (good for German tool and machine makers), construction, information technology, biotech, new and renewable energy initiatives and advanced materials development. Presently, Chinese have limited avenues to hold savings beyond cash and gold. A more sophisticated financial services sector will be established, opening up plenty of opportunities for scammers and charlatans to rock the boat.

China's demand for electric power is growing at a rate of ~96GW pa and already has at least a 7GW shortage of generating capacity for current market demand. It will commission 1,000 MW of coal fired power generation every week for the foreseeable future. Each 1,000 MW plant consumes about 5 mt pa of coal, so China needs an additional 250 million tonnes of thermal coal each year.

China is putting a lot of effort into establishing a **shale gas** industry and its **renewable** sector already has over 103 GW of standing capacity, compared with about 60 GW of renewables in the USA. In China, on average a new 1MW wind turbine is being erected every 90 minutes, while there is increased focus on LNG and other sources of gas as well as a huge and unstoppable expansion in **nuclear power** generation capacity. China is manufacturing more solar PV components and broadly spending more on clean-energy investments than any other nation. Surveys have shown that China led all nations in 2010 with US\$54.4 billion in clean-energy investment, compared to US\$34 billion of investment in the U.S.A.

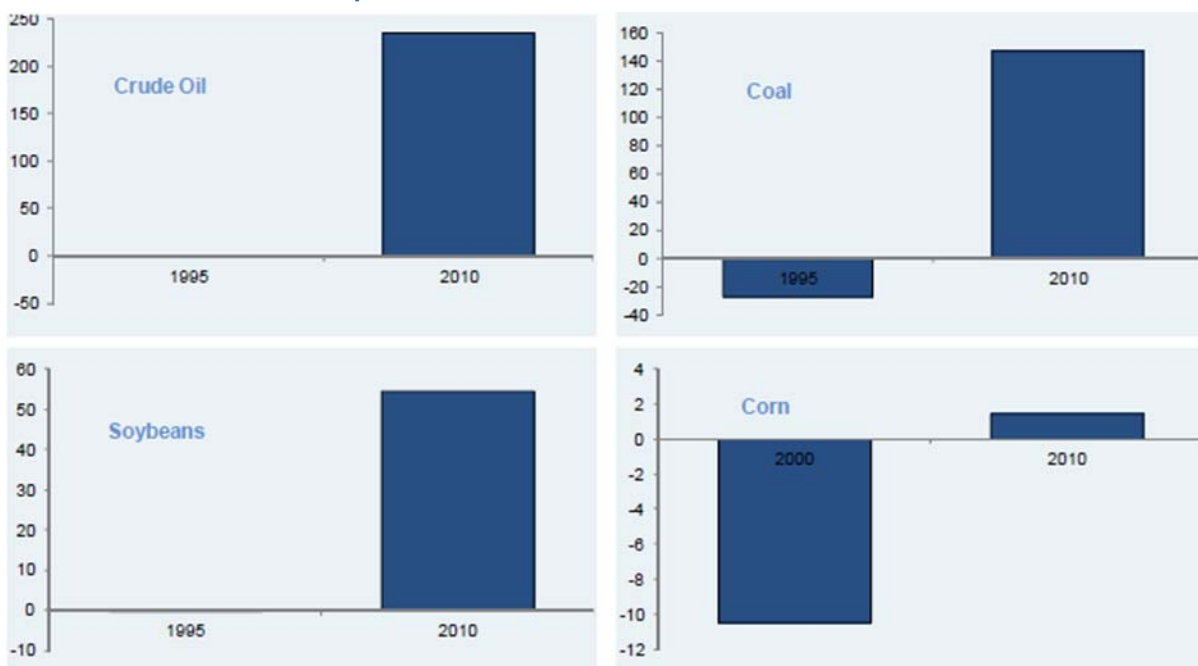
China is also a very dry country overall. A drought currently affecting China's grain growing areas is severe. China has only recently become a net importer of corn, largely used for animal feed and it will increasingly rely on imported food. Imports of soybean have shown 18% pa growth in recent years. An underlying lack of water and desertification, which sees an area of 1,000 km², equivalent to the whole of Melbourne's metropolitan area turning to desert each year, represents a huge risk for China. Government response has been to crank up acquisition of agricultural land in places such as Ethiopia, Brazil and Australia. As far as I know, there is no foreign register of Australian **agricultural land**, but my feeling is that a list would be very interesting and somewhat concerning.

Companies such as **Australian Agriculture** (AAC) and **PrimeAg** (PAG) will certainly be on the radar for foreign sovereign wealth funds from Asia and the Middle East, as they seek to secure food for their growing populations. This represents a massive threat to Australia, whose own food security is threatened by a population which has been growing at the fastest rate of any OECD nation. Recent rains on Australia's east coast have relieved a long period of drought. Wetter weather on the east coast ensures favourable cropping conditions for one or two years, but the west coast remains in drought and eventually dryer weather will return to the east.

Power shortages are exacerbated by low hydro-power options and a shortage of coal, leading to an increased use of diesel to generate power, with a consequent rise in pollution along the Pearl River delta, impacting on China's ability to meet manufacturing output.

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Net Imports of Selected Commodities 1995 vs 2010



Source: CEIC

Remember also that **China plays by its own rules**. Firstly, its commercial systems are corrupt and its courts act as organs of the Central government, doing the bidding of the Party. Microsoft is being robbed blind in China by widespread pirating of its intellectual property, for which China takes scarce regard. Foreign businessmen are routinely entrapped into dodgy practices by local contacts until such time as their business represents a threat to the locals, at which time the trap is sprung, the foreigner is charged and given the opportunity to sit in jail until he sees things in the same light as his captors, at which time he is put on a plane with his passport and must leave his business to be divided amongst erstwhile peers.

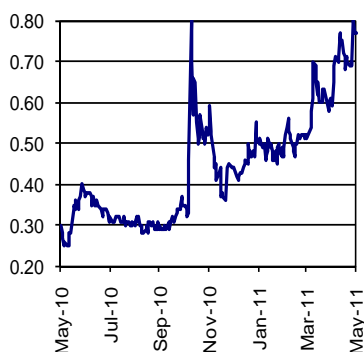
The jailing of Rio executive Stern Hu was clearly a response to a serious loss of 'face' by China in its dealing with Rio Tinto during the GFC. Mr Hu was unlikely to be operating in that iron ore market in a way which was different from any of his peers. China Inc felt that through its Chinalco deal, it had Rio backed into a corner and was badly bruised when the deal fell through. I know several senior executives who just do not want to go to China ever again. A persistent threat of being detained and having one's passport removed until certain financial arrangements are made can be a significant deterrent to transparent trade with China.

To quote Yogi Berra, "It's hard to make predictions, especially about the future". One thing is for sure, China will remain a point of focus for Australian companies and investors as its huge sovereign wealth fund of over \$3 trillion, scours the world for raw materials.

Buru Spins a Bit

BRU

BRU Price History



Recommendation: *Buru is a hold at its current elevated price, ahead of first results from Canning Basin exploration work. Positive test results from Yulleroo or discovery at new prospects would support the current price, which seems to face resistance at 90 cents and finds support at 68-70 cents.*

As Buru commences an ambitious and complex programme involving drilling of multiple wells, work-over of producing wells and seismic data acquisition, its share price has risen in anticipation that commercial flows can be demonstrated from several targets. The company has received independent confirmation of its resource target at Yulleroo, with estimated mean contingent reserves stated as 352 Pj of gas plus 13.4 mmbbls of liquids.

Buru - Capital Structure

Shares	182.8 m.
Options	24.3
	<u>207.1 m.</u>
Price	\$0.78
Market cap	\$ 142

Yulleroo Contingent Resource Targets

	1C	2C	3C	Mean
Ultimate Recoverable Sales Gas (PJ)	53	205	846	352
Ultimate Recoverable Associated Liquids (mmbbl)	1.9	7.8	32.3	13.4
Total Recoverable Hydrocarbons (mmbbl)	<u>10.8</u>	<u>42.0</u>	<u>173.3</u>	<u>72.0</u>
Total Recoverable Hydrocarbons - net to Buru (mmbbl)	<u>5.4</u>	<u>21.0</u>	<u>86.7</u>	<u>36.0</u>

Source: Buru

Drilling and well completion procedures at Yulleroo will be critical for demonstrating commercial reserves. Estimates of Contingent Reserves have a wide range between C1 and C3 numbers, indicating a high level of estimation uncertainty surrounding parameters such as permeability, porosity and water saturation. If a number like 350 Pj of gas can be established, this volume of gas would be sufficient to underpin development of the Great Northern gas pipeline to Karratha.

StockAnalysis estimates a risked target value for underlying assets of 81 cents per share with risked exploration upside to \$1.14 per share. The company will spend about \$11 to \$15 million on exploration and development activities this year, reducing liquid assets to about \$24 million after accounting for the exercise of options, which are now in the money. Buru is well supported by ongoing funding from Mitsubishi for exploration and development and its \$22 million loan from Alcoa will not be called if there is a strong likelihood that the project can deliver gas to Alcoa, so funding is secure for a year or two, ahead of serious spending on project development, following any commercial success.

Buru Valuation	\$ per Share	
	\$m	
Oil Producing Field	6	\$ 0.03
Yulleroo	137	\$ 0.66
Cash	47	\$ 0.23
NSE Investment	2.4	\$ 0.01
Alcoa loan	(22)	-\$ 0.10
Un-issued Equity	8	\$ 0.04
Corporate	(10)	-\$ 0.05
	<u>168</u>	<u>\$ 0.81</u>
Risked Exploration	68	\$ 0.33
	<u>236</u>	<u>\$ 1.14</u>

AZZ Price History



Antares - AZZ

Recommendation: *Risks associated with development of oil production from a new area to investors, will begin to be reduced over the coming months, so long as Antares delivers acceptable first oil production results from a suite of new wells being drilled at its Permian Basin assets. Early production results from the Harrison-3 well should be reported in June, further lifting AZZ's production towards 1,000 BOEPD by the end of June while operating income rises towards \$1.4 million per month. The stock remains a buy with an initial price target of 60 cents and a risked target valuation of over \$1.40 per share.*

AZZ - Capital Structure

Shares (est)	275.0 m.
Convertible notes	7.5 m.
Performance rights	10.8 m.
Total	293.3 m.
Net Cash (est) \$m.	18
Price	\$ 0.415
Market Cap \$m.	\$ 114 m.
EV \$m.	\$ 96

AZZ - Asset	Value \$m	\$ per Share	Comment
Gulf Coast production	12	0.04	Estimate
Permian Assets	74	0.26	at cost
EFS Term Assignment	16	0.05	25% of \$8K/acre
Cash (est)	45	0.16	Estimate
Tax Liability (est)	(12)	(0.04)	Estimate
Convertible note	(15)	(0.05)	
Other	(16)	(0.06)	Corporate
	103	0.36	
Exploration Value	319	1.11	Risk adj
Total Value	422	1.48	

Source: Strachan Corporate

Antares has expanded its recent mineral rights purchases over areas in the Permian Basin of north-western Texas, while clarifying and outlining expected development plans. The company's net holdings now comprise nearly 22,000 acres, with potential to yield over 74 million barrels of oil equivalent (mmBOE) for the company, based on regional comparisons where wells drilled on 40 acre centres produce about 130,000 barrels of oil equivalent (BOE). Early work by peers in the Basin indicates that development on 20 acre centres is possible, given the heavy endowment of petroleum found throughout 1,800 metres of down-hole column. If 20 acre sections are tested and proven possible on the permits held by Antares, total reserves could exceed 140 mmBOE or over \$1.75 per share to Antares if 33% of those reserves were classified as 2P. This is the speculative upside potential of the AZZ Permian assets.

Antares' Recent Permian Acquisitions & Retained EFS Interests

Permian Permits	Acres (est)	WI %	Net Acres	Value K\$/acre	Est Total Value A\$m.	AZZ \$/shr
Northern Star	12,400	100%	12,400	3.0	37	\$0.13
Big Star	8,500	75%	6,375	3.0	19	\$0.07
Southern Star	3,920	75.3%	3,109	19.9	62	\$0.22
EFS Permits	Acres	WI %	Net Acres	Value K\$/acre	Total Value A\$m.	NRI A\$m.
Petrohawk	8,558	T/A		8	16	\$0.05

Source: Antares

The company states its 2P Reserves as 27 mmBOE and 3P Reserves at 83 mmBOE, so with a market capitalisation of \$114 million, Antares can be bought for a price representing \$4.22 per barrel of 2P Reserves, when modelling by StockAnalysis indicates that oil in this location has an NPV of closer to \$11 per BOE. Ranking Antares with a market capitalisation of \$11 per barrel of its Permian Basin 2P oil reserves delivers a target share value of \$1.05 per share, prior to any adjustments for net cash or other assets.

On a going out of business case, assuming that Antares was to undertake an orderly sale of its current assets, StockAnalysis estimates that a pre-tax price equal to 70 cents per share could be achieved, which might be about 60 cps net to shareholders after tax.

(Continued on page 8)

AZZ - Risked Exploration & Development

Well	WI	Target		POS %	NPV Discovery Risked		AZZ to drill	Risked NPV
		Pj	mmbbl		Value	NPV		
					\$m	\$/share	\$m	\$m
West Warton	26%	16	0.0	50%	24	0.02	12	4.4
Oyster Ck	75%	5	0.4	50%	16	0.04	8	3.6
Big Kahuna *	30%	100	0.1	25%	151	0.16	38	3.0
Southern Star	75%	5.5	10	80%	80	0.11	64	30
Big Star	75%	11.0	20	70%	160	0.41	112	45
Northern Star	100%	27.2	32	70%	270	0.92	189	87
* post farmout								168

Source: Strachan Corporate Pty Ltd

The company holds small, largely gas prone exploration targets along the Texas Gulf Coast. These projects hold limited value while the US gas price lingers below US\$5 per mmBtu. Significant development appeal is held in AZZ's newly acquired oil prone Permian Basin Assets. Antares has acquired non-producing leases at prices which sit at about 20% of the price achieved by larger parcels of leases in recent sales. Demonstration of oil production by an ongoing drilling programme would further upgrade lease values.

Speculative Cash Flow Estimate

AZZ - Calendar Year	2011	2012
Cash Flow \$m.	June-Dec	CY
Opening cash at 1 June	45.0	10.0
Net Operating Income	9.5	54.0
Capital Spending		
<u>Oilfield Ops</u>		
Southern Star	(8.6)	(10.5)
Big Star	(7.5)	(16.5)
Northern Star	(11.5)	(9.2)
Corporate	(5.0)	(5.0)
Con Note repay		(15.0)
Taxation	(12.0)	(4.2)
Net Cash @ Year End	10.0	3.6

Source: Strachan Corporate Pty Ltd

StockAnalysis models cash flow which indicates that even if all convertible notes were repaid rather than rolled over, the company could support operations from retained cash and operating cash flow through until the end of 2012. Rising production towards 3,500 bbls per day in 2013 would support a \$50 million capital spending budget for drilling about 25 wells and leave over \$10 million of net cash by the end of 2013.

Importantly, the company maintains a share buyback programme, which has the effects of allowing weak and often small holders to exit their holdings thus simplifying the company's share register, while increasing the value of remaining shares for shareholders who remain. In addition, Directors of Antares have been consistent buyers of the stock at prices which are at or above the buyback prices paid, demonstrating their confidence in the company's ability to create wealth.

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