Conventional Oil & Gas: Explorer

Hartleys

PANCONTINENTAL OIL AND GAS NL

Bits are Spinning Nearby

Activity around Pancontinental Oil and Gas Limited's ("PCL", "Pancontinental", "Company") acreage in both Kenya and Namibia is heating up, with two wells currently being drilled.

In Kenya, Anadarko is drilling the Kiboko well in block L11B which is east of Pancontinental's L10A and L10B blocks. In Namibia, HRT is currently drilling the Wingat prospect (the first well in a three well program) which is immediately south of Pancontinental's Namibian acreage. Success in either of these wells has the ability to re-rate Pancontinental because the Company has similar play types across its own acreage.

The March quarterly shows Pancontinental has $35.3m in cash, which should be sufficient to meet exploration commitments for the next 12 to 18 months.

Plenty of catalysts to come out of Kenya in 2013

There are a number of catalysts to come from drilling and farmouts in Kenya.

BG plans to drill one well each in blocks L10A (PCL 15%) and L10B (PCL 15%) commencing in 4Q13. BG is targeting Miocene Reefs believed to contain oil (similar to the Kifaru prospect in the L6 block).

The L8 (15%) joint venture is due to decide on a second well following the Mbawa well. The decision to drill a second well will provide more confidence in the prospectivity of the block, especially if Tullow exercises its right to partly carry Pancontinental for another 5% interest (leaving PCL with 10%). We suspect that the joint venture parties may be waiting for the results of Anadarko's second well before deciding on drilling a second well in L8.

Pancontinental is seeking to farmout some of its interest in L6, though this may take some time while newly acquired 3D seismic is interpreted.

Speculative Buy – drilling nearby now with direct drilling later in the year

We maintain our Speculative Buy recommendation, with a price target of 24cps. Nearby drilling has already commenced in Kenya and Namibia. Despite proving a working oil system, the lack of commercial success at Anadarko's Kubwa well has possibly caused some downward pressure on Pancontinental's share price. As such, success in the second well could see a bounce but a failure may have little impact.

Direct drilling (drilling in permits where Pancontinental has an interest) will commence near the end of the year which is when we expect a material uplift in share price. Buying now ensures maximum exposure to potential upside in the lead up to drilling, with the additional potential impact of nearby success, farmout of L6 or Namibia and a decision to drill a second well in L8.

PCL.asx
Speculative Buy

8 May 2013

Share Price:	$0.073
12mth Price Target:	$0.24

Brief Business Description:
Large acreage position across 4 permits offshore Kenya inlcudes the Mbawa discovery. Also huge oil potential offshore Namibia.

Hartleys Brief Investment Conclusion
Buying early for the next phase of the exploration program

Key Personnel
Mr David Kennedy (Chairman)
Mr Barry Rushworth (CEO, Director)
Mr Ernest Myers (Finance Director)

Top Shareholders:
SUNDOWNER INTERNATIONAL LIMITED (11.5%)
HSBC CUSTODY NOMINEES (13.5%)

Company Address:
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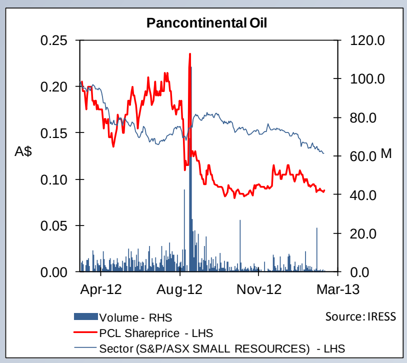
Valuation:	$0.49
Issued Capital:	1151.0m
- fully diluted	1151.0m
Market Cap:	$85.2m
- fully diluted	$85.2m
Cash Equiv (Mar '13):	$35.3m
Debt (Mar '13):	$0.0m

Valuation Summary

Asset	Value ($m)	Value ($ps)	Unrisked Value ($ps)
L8 - Mbawa	52.50	0.046	0.07
L8 - Other	75.00	0.065	0.33
EL0037	78.00	0.068	3.39
10A	75.00	0.065	0.33
10B	75.00	0.065	0.33
L6	179.54	0.156	0.78
Australia	3.60	0.003	0.06
Cash	35.30	0.031	0.031
Debt	0.00	0.000	0.000
Corp Admin	-11.33	-0.010	-0.010
Options	1.00	0.001	0.001
Total	**563.61**	**0.490**	**5.30**

Source: Hartleys Research



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Hartleys has completed capital raisings in the past 12 months for Pancontinental Oil & Gas NL, for which it has earned fees. Hartleys has provided corporate advice within the past 12 months and continues to provide corporate advice to Pancontinental, for which it has earned fees and continues to earn fees. See back page for details

KEY ASSUMPTIONS / RISKS

Our valuation methodology is based on risked value of resource potential using notional in ground valuation and conservative estimates for probability of success. This methodology results in Net Asset Value of 49cps.

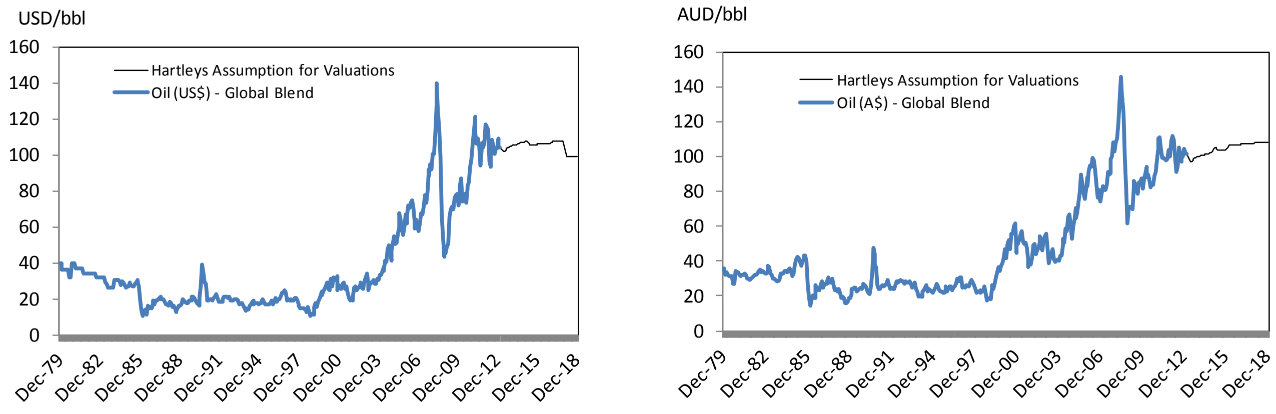
Our price target is a qualitative discount to our valuation based on market cap, liquidity and takeover premium. In PCL's case, this discount has been estimated at 50% resulting in a price target of 24cps.

Fig. 1: Exploration Valuation

Permit / Interest*	Country	Operator	Net Recoverable Potential	NPV per Unit ($)	POS	Risked Value ($)	(cps)	Unrisked Value (cps)
L8 (10%)	Kenya	Apache	600 bcf	$0.75	28%	127.5	11.1	39.1
L6 (10%)	Kenya	FAR	2,138 bcf	$0.5	20%	213.8	18.6	92.9
L10A (15%)	Kenya	BG	750 bcf	$0.5	20%	75	6.5	32.6
L10B (15%)	Kenya	BG	750 bcf	$0.5	20%	75	6.5	32.6
EL 0037 (30%)	Namibia	PCL	390 mmbbls	$10.0	2%	78	6.8	338.8
Baniyas (20%)	Australia	Strike	5 mmbbls	$15.0	5%	3.6	0.3	6.3
Total			**4,238 bcf 395 mmbbls**			**573**	**50**	**542**

Source: Hartleys, *post farm-out

Fig. 2: Commodity price assumptions



Source: Hartleys, Bloomberg

Fig. 3: Key assumptions and risks for valuation

Assumption	Risk of not realising assumption	Downside risk to valuation if assumption is incorrect	Comment
Exploration Risk	Moderate	Moderate-High	The recent success at Mbawa has significantly de-risked our valuation for PCL and increased the likelihood of further discoveries on its acreage.
Schedule Risk	Low	Low-Moderate	Now that there has been a discovery, we predict that drilling activity will significantly increase offshore Kenya, with at least 4 wells expected in 2013.
Funding Risk	Low	Low-Moderate	PCL has $35m in cash and is fully funded for the foreseeable future.
Valuation Risk	Low	Low-Moderate	Our exploration valuation includes a risked metric based on prospect sizes. It assumes that the market will recognise a portion of potential value before the results of a well are known. In most cases, we include ~10% of potential prospect value in our valuations. However, this may increase or decrease depending on the type of well drilled and confidence in the prospect
Conclusion	*We believe the assumptions we have used have a low-moderate risk of not being achieved, which would have a moderate impact on our risked valuation.*		

Source: Hartleys

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Note: personal email addresses of company employees are structured in the following manner: firstname_lastname@hartleys.com.au

Hartleys Recommendation Categories

Buy	Share price appreciation anticipated.
Accumulate	Share price appreciation anticipated but the risk/reward is not as attractive as a "Buy". Alternatively, for the share price to rise it may be contingent on the outcome of an uncertain or distant event. Analyst will often indicate a price level at which it may become a "Buy".
Neutral	Take no action. Upside & downside risk/reward is evenly balanced.
Reduce / Take profits	It is anticipated to be unlikely that there will be gains over the investment time horizon but there is a possibility of some price weakness over that period.
Sell	Significant price depreciation anticipated.
No Rating	No recommendation.
Speculative Buy	Share price could be volatile. While it is anticipated that, on a risk/reward basis, an investment is attractive, there is at least one identifiable risk that has a meaningful possibility of occurring, which, if it did occur, could lead to significant share price reduction. Consequently, the investment is considered high risk.

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