Conventional Oil & Gas: Explorer

# PANCONTINENTAL OIL AND GAS NL

## Early Mover Strategy Starting To Pay Off

Pancontinental Oil and Gas NL ("Pancontinental", "PCL", "Company") is on the verge of realisation of significant value from its strategy of early entry into oil prone frontier areas that have potential for world class (billion barrel+) prospects. By virtue of this strategy, the Company now has large exposure in two of the hottest emerging areas off the coast of Africa, Kenya and Namibia.

Drilling by PCL and others over the next 12-18 months has the potential to substantially re-rate the share price of the Company, which is already undervalued when compared to peers with similar resource potential. We expect strong share price appreciation in the lead up to these drilling events, which should kick-off towards the end of CY2011.

## Drilling on Giant Mbawa Prospect Could Result in 20X Uplift

On the L8 permit offshore Kenya, PCL will participate (on a free carried basis, 15% working interest) in the drilling of the giant, 1 billion barrel plus Mbawa structure, most likely in H1 2012. The Company recently farmed in successful African explorer, Tullow Oil Plc, to obtain a free carry in this well, which, if successful, could result in 20X uplift on the current share price. Operator, Apache Corporation, is completing interpretation of the seismic prior to finalising a drilling schedule.

Elsewhere in Kenya, the Company is in the process of farming out a 3D seismic program on its L6 permit (PCL 40%), located to the north of L8.

The Company, through its strong in-country relationships, was also recently awarded two additional permits (L10A/L10B, PCL 15%) in Joint Venture with industry heavy weights, BG Group, Premier Oil Plc and Cove Energy Plc. BG has indicated that it plans to "fast track" exploration on these permits and early work on existing seismic has already identified some large leads.

## Namibia Icing on the Cake – Peers Illustrate Value Potential

Pancontinental entered Namibia in 2007, prior to the recent upsurge in industry interest in the region, which has been spurred by interpreted geological similarities to the offshore areas of Brazil where multi-billion barrel oil discoveries have been made. The Company was recently awarded a large exploration licence, EL0037 (PCL 85%). Like Kenya, PCL selected the area for its potential for generation of oil as opposed to gas. Subsequently, oil slick analysis, undertaken by multi-billion dollar neighbour HRT Oil and Gas, has identified the largest concentration of oil slicks offshore Namibia directly over PCL's blocks.

Peers with permits in the region are trading on substantially higher valuation metrics than PCL. Up to 6 wells will be drilled offshore Namibia over the next 18 months, several of which will be nearby to PCL's blocks.

## Window of Opportunity Closing for Cheap Entry

The level of increased industry interest, combined with the upcoming drilling in both regions, means that, prior to any drilling events, PCL is unlikely to be any cheaper than its current price. This gives investors an opportunity to gain access to substantial leverage to possible drilling success but also to participate in the likely share price appreciation in the lead up to any drilling. This appreciation has already begun but we believe it has a long way to go yet, and view this as one of the lowest risk opportunities for positive investment returns in the sector.

We rate Pancontinental as a Speculative Buy with a 6 month price target of 20cps.

**PCL.asx**
**Speculative Buy**

3 Aug 2011

| | |
|---|---|
| **Share Price:** | $0.100 |
| **6mth Price Target:** | $0.20 |

**Brief Business Description:**
Frontier explorer with a knack for early entry into oil prone areas.

**Hartleys Brief Investment Conclusion**
Undervalued compared to international peers. Large exposure to drilling events over next 18 months.

**Chairman & CEO:**
Mr Henry David Kennedy (Chairman)
Mr Roy Barry Rushworth (CEO, Director)

**Top Shareholders:**
HENRY DAVID KENNEDY (23.5%)
INDAGO RESOURCES LIMITED (8.8%)
ROY BARRY RUSHWORTH (5.3%)

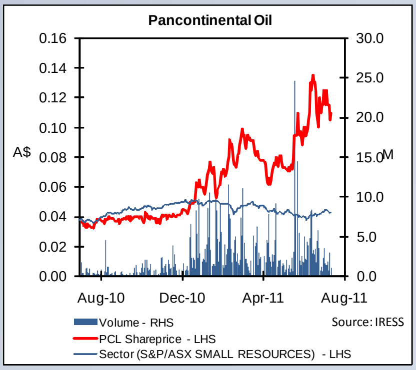
**Company Address:**
Ground Floor, 288 Stirling St
Perth, WA, 6000

| | |
|---|---|
| **Valuation:** | $0.32 |
| **Issued Capital:** | 660.8m |
| - fully diluted | 674.5m |
| **Market Cap:** | $66.1m |
| - fully diluted | $67.5m |
| **Cash Equiv (30 June '11):** | $5.7m |
| **Debt (30 June '11):** | $0.0m |

**Valuation Summary**

| Asset | Value ($m) | Value ($ps) | Unrisked Value ($ps) |
|---|---|---|---|
| L8 - Mbawa | 128.28 | 0.190 | 1.90 |
| EL0037 | 30.00 | 0.044 | 4.45 |
| 10A | 10.00 | 0.015 | 0.74 |
| 10B | 10.00 | 0.015 | 0.74 |
| Malta | 1.81 | 0.003 | 1.34 |
| L6 | 40.00 | 0.059 | 1.19 |
| Australia | 3.60 | 0.005 | 1.00 |
| Cash | 5.70 | 0.008 | 0.008 |
| Debt | 0.00 | 0.000 | 0.000 |
| Corp Admin | -11.33 | -0.017 | -0.017 |
| Options | 1.00 | 0.001 | 0.001 |
| **Total** | **219.06** | **0.325** | **11.35** |

Source: Hartleys Research





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# HIGHLIGHTS

*Early mover in oil prone areas with potential to hold multi billion barrel prospects.*

Pancontinental Oil and Gas NL is an ASX listed oil and gas explorer with core assets in Kenya and Namibia. It also has oil and gas assets in Malta and Australia, with a licence application pending in Morocco.

The Company's strategy has been to gain early access to areas that are more likely to be oil prone than gas prone and that have potential for high quality reservoir and structures capable of containing multi billion barrels.

Both Kenya in East Africa and Namibia in Southwest Africa meet these criteria and have consequently become the focus of a recent increase in interest by credible industry participants. This has occurred several years after PCL has identified the potential and gained its entry.

*Strategy starting to pay off with recognition by large, credible industry players.*

In Kenya, the Company is joint ventured though farmouts to Origin Energy Ltd, Apache Energy Ltd and Tullow Plc in one of its permits, L8, where drilling on the potential billion barrel plus Mbawa prospect is planned for next year. PCL's 15% interest could be worth >$2 per share if Mbawa is successful.

In other new Kenya permits (L10A & L10B) Pancontinental is joint ventured with major African oil players BG Group, Premier Oil Plc and Cove Energy Plc.

*>18,000km² net acreage in Kenya and Namibia where PCL will have direct and indirect exposure to 8 wells over the next 18 months.*

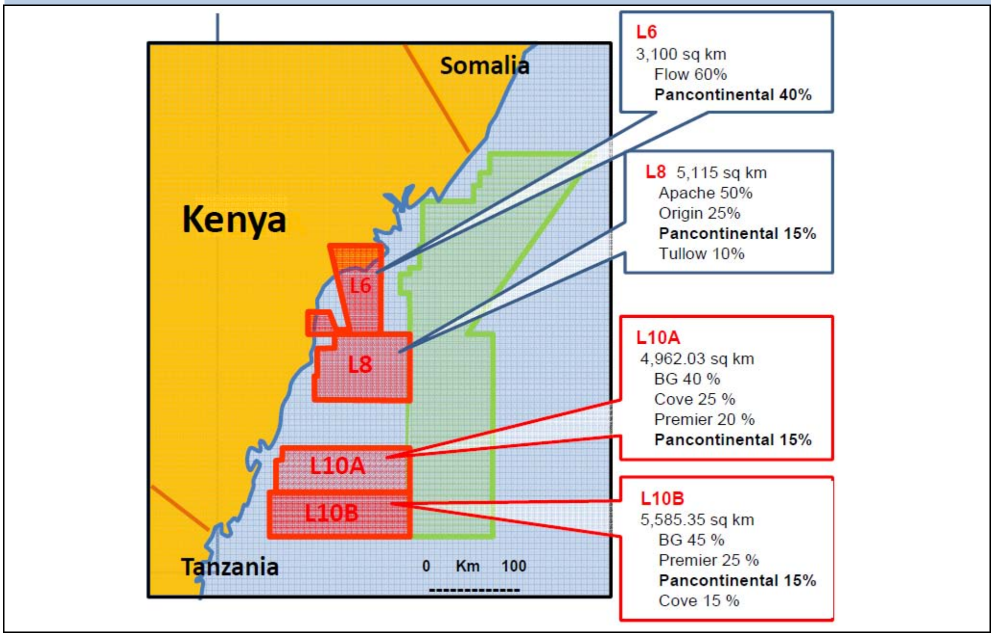
Offshore Namibia, Pancontinental was recently awarded a large licence (EL0037) which appears highly prospective despite being early stage. Activity by others, with up to 6 wells planned over the next 18 months, has already significantly upwardly re-rated this region.

## KENYA (PCL 15%-40%)

Pancontinental was one of the first companies in recent times to be awarded offshore acreage in Kenya, entering the country in 2002. PCL now has an interest in 4 permits, two of which are advanced, L8 and L6, with L8 containing the world-scale and drill-ready Mbawa prospect.

*Direct exposure is through drilling at the billion barrel+ Mbawa prospect, which will be drilled by Apache in Joint Venture with Origin, Tullow and PCL. Likely H1 2012.*

*Fig. 1: Four Permits Offshore Kenya*




Source: Pancontinental

*PCL initiated activity on L6, L8 and L10, with the larger partners entering later, validating the interpreted prospectivity.*

Significantly, PCL initiated activity on blocks L6, L8 and L10, with the major Joint Venture partners entering the fray later, confirming Pancontinental's interpretation of prospectivity.

*Recently awarded L10A and L10B with BG, Premier and Cove, all of which are industry heavy weights with successful exploration in Africa.*

Two additional permits were awarded recently, L10A and L10B, where PCL was part of a winning consortium with BG, Premier and Cove.

In early 2009, Origin Energy Ltd farmed-in for 75% of the L8 permit in exchange for acquiring $10m of 3D seismic. Subsequent to processing and interpretation of the seismic, PCL was able to secure a deal with Tullow Oil Plc to cover its share of costs for the drilling of a well, which may spud in H1 2012.

There have been 4 offshore wells drilled in Kenya, three of which have measured gas shows in the Tertiary / Cretaceous (1978-1985). The most recent well, drilled by Woodside Petroleum Ltd in 2007, Pomboo-1, was dry.

## Block L8 (PCL 15%)

*Free carried through drilling at Mbawa by Tullow after recent farm-out by PCL.*

PCL is free carried by Tullow through the drilling of a well on the permit, most likely on the giant Mbawa prospect. Tullow may also elect to earn an additional 5% interest by paying for Pancontinental's share of a second well. Apache Energy Ltd recently became operator of the permit after closing a deal with Origin.

The participation of both Tullow and Apache is a testament to the quality of work done to date on the permit and to the quality of the prospects generated by this work. There have also been 8 discoveries off the East Coast of Africa in the last 18 months, significantly increasing industry interest and drilling activity in the region.

*East Africa has had a strong run of exploration success in the last 18 months, resulting in a significant increase in industry interest and activity.*

Pancontinental believes that it has unlocked an economically significant world-scale oil play, rather than a gas play, in the East Africa region.

*Fig. 2: Regional Discovery History – 8 in last 18 months*

| Well/Field | Company | Location | Date | Description |
|---|---|---|---|---|
| Songo Songo | AGIP | Tanzania | 1974 | Offshore 1tcf gas |
| Multiple | Tullow | Uganda | 06-> | Onshore >1b barrels discovered, significant remaining potential |
| Windjammer / Barquentine / Lagosta | Anadarko | Mozambique | 2/10-11/10 | Offshore – large enough to justify LNG development >5tcf? |
| Ironclad | Anadarko | Mozambique | 8/10 | 38m net oil and gas pay, first liquids discovery offshore East Africa |
| Pweza-1 | Ophir/BG | Tanzania | 10/10 | Offshore gas, 60m gas column |
| Chewa-1 | Ophir/BG | Tanzania | 12/10 | Offshore gas, significant discovery |
| Tubarao | Anadarko | Mozambique | 2/11 | Offshore gas - 110ft net gas pay, 15,000 acre closure ~2-3tcf? |
| Chaza-1 | Ophir/BG | Tanzania | 2/11 | Offshore gas |

Source: Hartleys

*Substantial work by all joint venture partners has been done over the Mbawa prospect, with final interpretation and drill location to be finalised shortly.*

*Huge, world class potential has been identified of up to 4.9 billion barrels of oil in place. Could be worth 445cps to PCL in a high success case.*

*Double DHIs on the seismic could indicate gas/oil contact over an oil/water contact.*

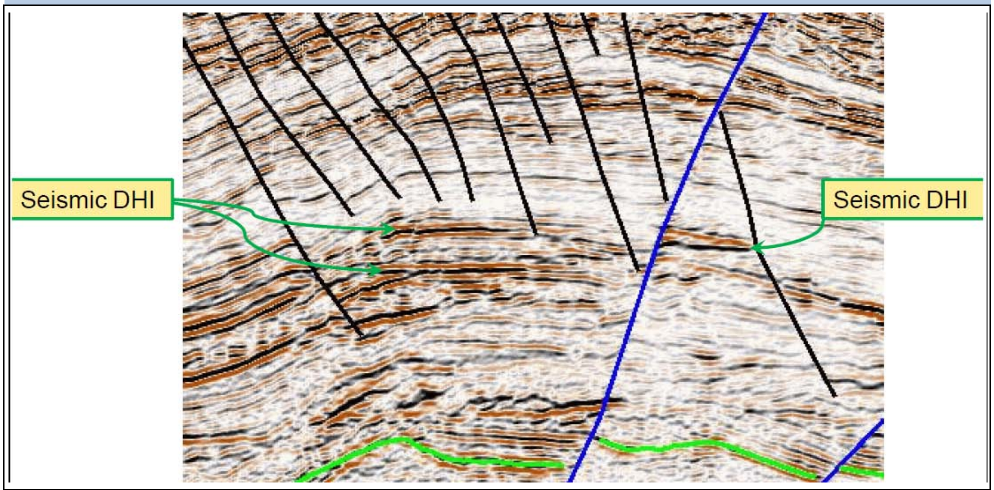
*Oil seeps evident on flanks of Mbawa structure, coincident with sea floor pock marks.*

## Mbawa

The Mbawa Prospect is the largest and most prospective of the targets identified on the L8 permit. It is supported by double Direct Hydrocarbon Indicators ("DHIs") on the 3D seismic that may be indicative of a gas/oil contact above an oil/water contact. Additionally, oil slicks on the flanks of the structure have been identified. These have likely escaped from pockmarks that can be seen on the sea floor.

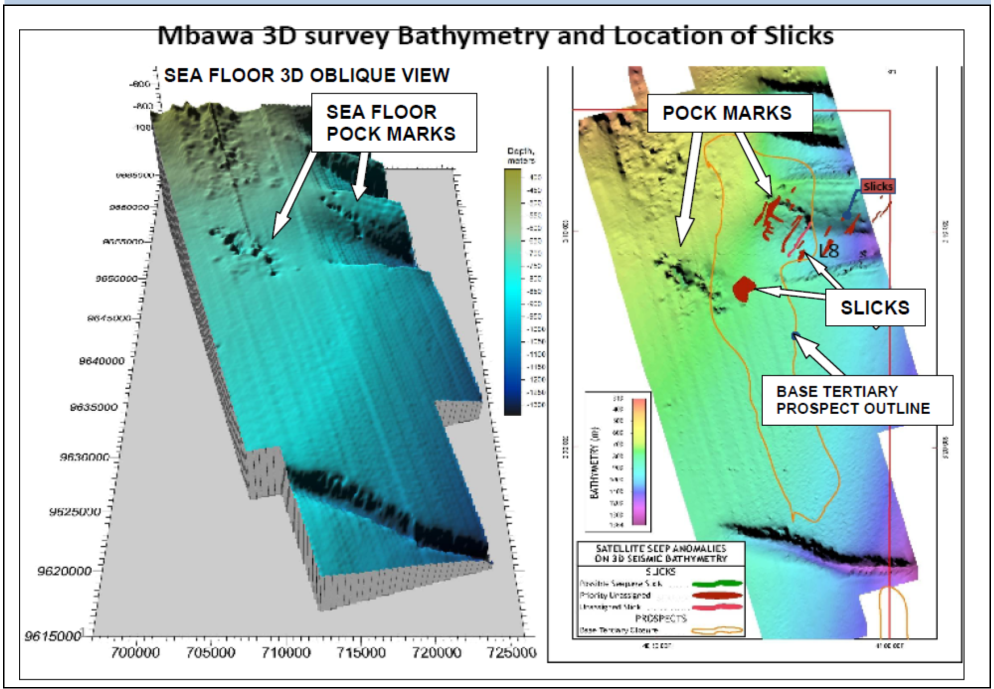
Based on initial interpretation of the seismic, the volumetric potential from two reservoir horizons is 2.1-5.2 billion barrels of oil in place (Pmean – P10). This implies potential recoverable volumes, net to PCL, of 128-312 million barrels of oil (assuming 40% recovery and 15% working interest). Using NPV per barrel of $10 results in notional value potential of $1.3b-$3.1b, or 190-445cps.

*Fig. 3: Mbawa – Large, Robust Structure with DHIs*




Source: Pancontinental

*Fig. 4: Pockmarks, Coincident Oil Slicks on Flanks of Structure*




Source: Pancontinental

The two figures above illustrate "flat spots" (or DHIs) and oil slicks with coincident pockmarks (expulsion craters) on the seabed.

*Drilling at Mbawa likely mid 2012. Drilling schedule to by finalised by Apache.*

Mbawa is located in water depth of 800m, with the primary reservoir of Tertiary / Cretaceous age, located at 1,800-2,200m with a deeper target in the Jurassic at 2,700-3,400m. We estimate that cost of drilling to be US$65m, on a dry hole basis.

The drilling schedule for Mbawa has not been finalised; however, it is possible that it is drilled in H1 2012, most likely towards the middle of the year.

*Several large followup prospects exist on L8, if Mbawa is successful.*

If drilling at Mbawa is successful (technically or commercially), then PCL has exposure to several other large prospects on the permit as well as on its other 3 permits.

## Block L6 (PCL 40%)

*L6 also has large potential but requires 3D seismic to firm up drill ready prospects. Farmout process is underway.*

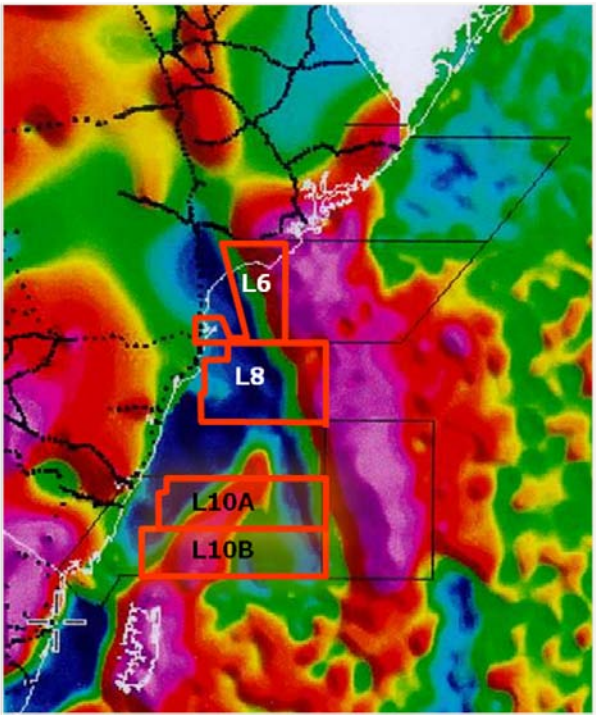
L6 is immediately to the north of L8 and contains several large, 2D defined prospects. The Joint Venture, with operator Flow Energy Ltd (60%), is currently seeking to farm-out the 3D seismic over the two most advanced prospects with a view to drilling in late 2012 / 2013.

Both L6 and L8 are located adjacent to a deep central graben, which is considered a likely source kitchen for generation of hydrocarbons. The oil slicks in the area support the interpretation that an active petroleum system is present. Oil migration modelling and seismic interpretation provides potential for nearby structures to be oil charged.

The dark blue area in Fig 5 is the deep central graben that Pancontinental interprets to hold mature oil source rocks as well as good reservoir rocks within and flanking the graben.

*Dark blue graben is interpreted to contain source rocks, with good reservoir also likely due to bounding regional high (mauve).*

*Fig. 5: High Quality Source Kitchen Interpreted*




Source: Pancontinental

*Kifaru is the largest identified prospect on L6, with potential ~1 billion barrels of oil.*

The Kifaru Prospect is the largest of the identified targets in Block L6 and is located in 80-100m water depth. We estimate the Kifaru may have potential for 1 billion barrels of oil, although 3D seismic is required before better volumetric estimates are known. Target reservoir is interpreted to be ~2,000m below the mudline and we estimate that a well may cost ~US$40m on a dry hole basis (not including mobilisation / demobilisation costs).

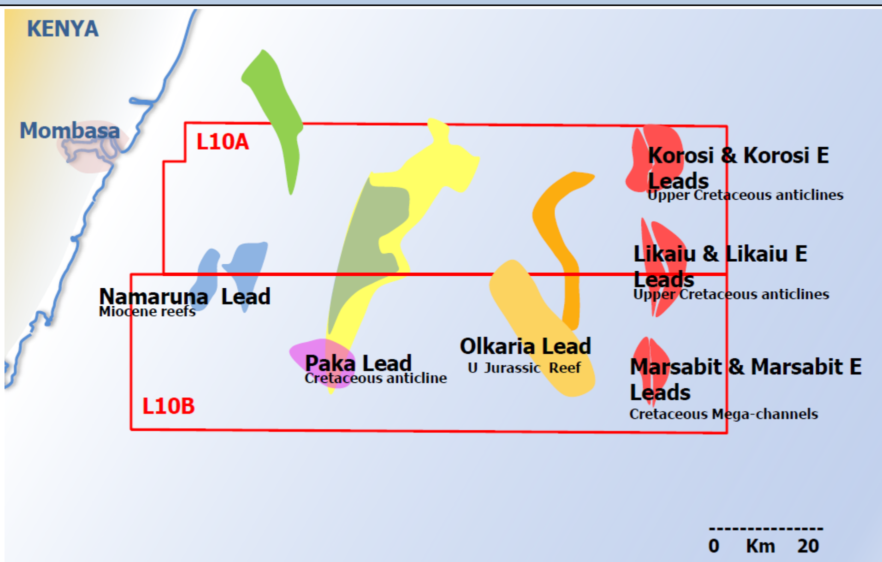
## Block L10A / L10B (PCL 15%)

*Recent award of blocks L10A and L10B with BG, Premier and Cove.*

PCL was recently awarded an interest in Blocks L10A and L10B as part of a bidding consortium with BG, Premier and Cove, following an early bid for the block by PCL. The two blocks will be operated by BG who has indicated that it plans to "fast track" exploration on the permits. Historic 2D seismic over the permits has indicated the potential for large structures. The potential for an active petroleum system is also supported by the geological model as well as oil seeps at Pemba Island, just across the border in Tanzania.

*Early work shows potential for large structures.*

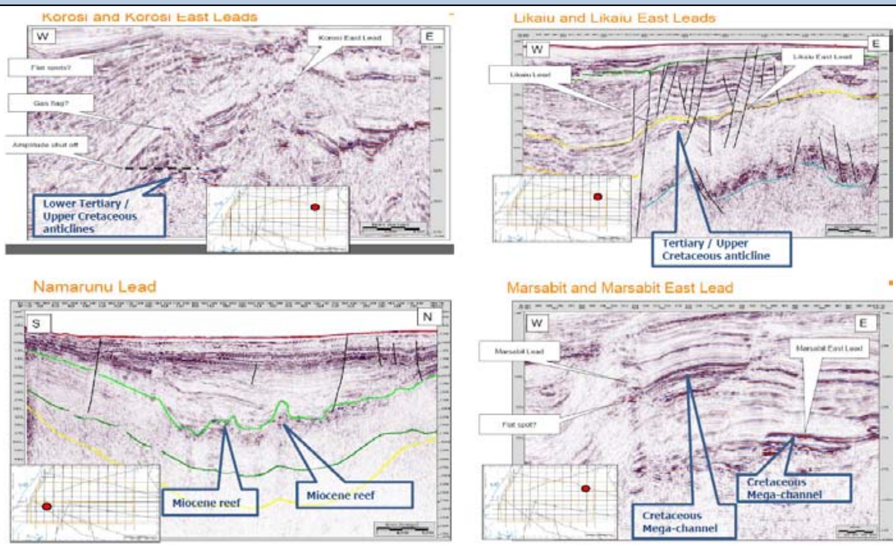
*Fig. 6: L10A / L10B Leads*




Source: Pancontinental

*Historic seismic shows possible DHIs. Modern seismic acquisition planned in the near term as part of fast tracked exploration program.*

*Fig. 7: Seismic Over L10A / L10B*




Source: Pancontinental

Possible DHIs identified over several leads on interpretation of vintage seismic. Fast tracked exploration program to shoot 2D seismic in 2011, 3D in 2012, with drilling possible in H1 2013.

## NAMIBIA EL0037 (PCL 85%)

*PCL recently secured a large exploration licence offshore Namibia. Similar to Kenya, the Company initiated activity on the permit several years before larger companies became interested.*

Namibia has recently experienced an upsurge in industry interest due to the geological similarities between it and that of offshore Brazil, where large multi billion barrel oil discoveries have been made in recent years. Namibia is also part of the West African Margin along which similarly large discoveries have been made offshore Nigeria and Angola.

Pancontinental entered Namibia in 2007 under a Reconnaissance Licence (RL-1). After studies over the region, the Company was invited by the government to select an area for a full Petroleum Agreement. Subsequently, PCL selected the EL0037 area, in Joint Venture with a local participant (Paragon), which was formally granted under a Petroleum Agreement and Exploration Licence in July 2011.

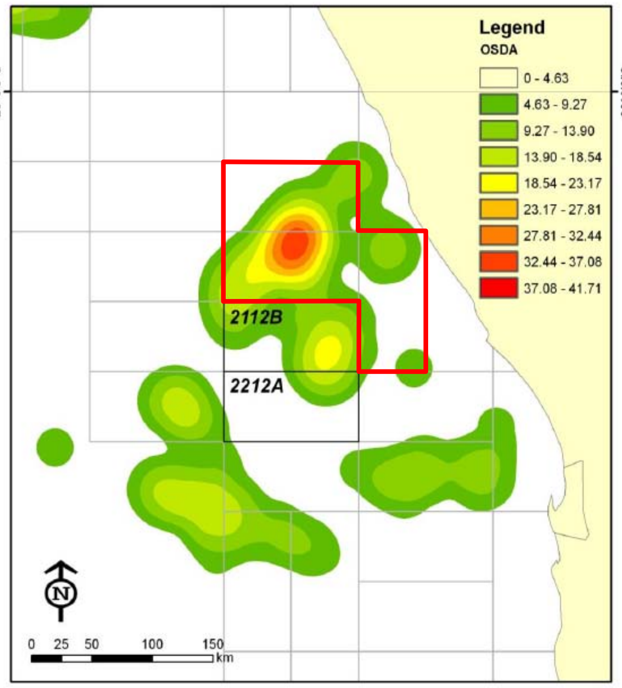
EL0037 is large, covering 3 blocks over 17,295km$^2$ in area. Significantly, the licensing procedure in Namibia has recently changed, making it more difficult to obtain permits in the region, especially for smaller companies.

*PCL's early studies indicated both the potential for oil and large structures.*

By virtue of its early entry into Namibia, PCL's blocks are located over a key prospective area in the Walvis Basin. Geological modelling in conjunction with oil seeps supports the likely presence of an active petroleum system. This is evidenced by work done by HRT Oil and Gas as shown in the figure below, which highlights the largest concentration of regional oil slicks, located directly over PCL's acreage (red outline). HRT recently concluded (July 19th) acquisition of 5,278km$^2$ of 3D seismic over its Walvis Basin acreage as a precursor to drilling in 2012.

*Oil slick analysis by HRT has confirmed the interpretation by PCL, with the largest concentration of slicks located on PCL's acreage.*

*Fig. 8: Oil Seep Density Analysis – Bullseye on PCL Blocks*



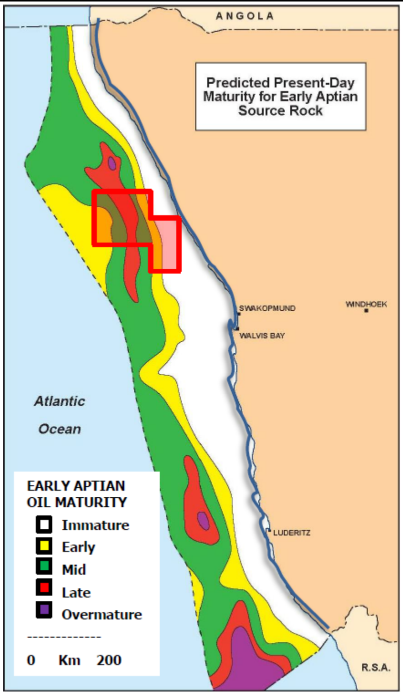

Source: HRT, Pancontinental

Oil seeps are further supported by source rock maturity analysis in Fig. 9 (below).

Pancontinental believes that its acreage is over an oil generating "Inner Graben", or geological trough shown in red in Fig 9. Pancontinental is exploring for ponded turbidites and channel sands close to the oil-mature source rocks in the graben.

*High quality reservoir and oil prone source rocks are also supported by the geological modelling.*

*Fig. 9: Source Rock Maturity Indicates Oil Likely*

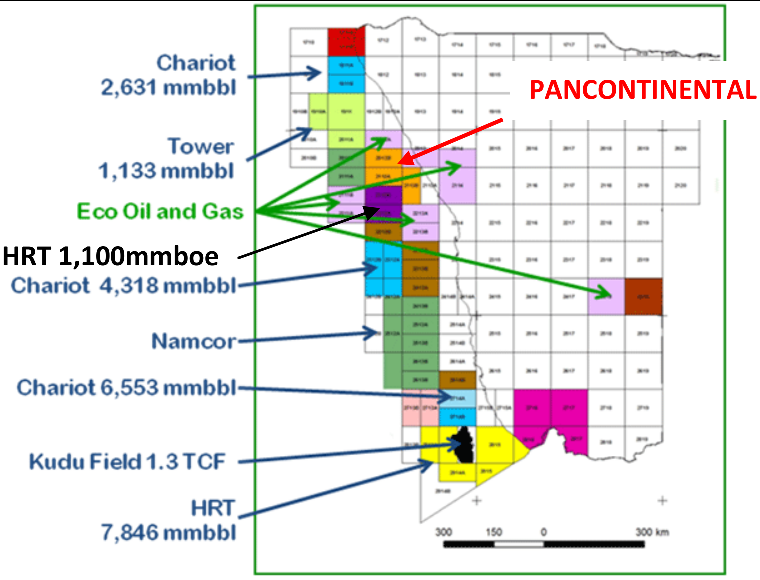



Source: Pancontinental

*Independent consultants have estimated large potential on neighbouring blocks. Similar potential is likely to be indicated on PCL's blocks with the reprocessing of vintage seismic and acquisition of additional modern seismic.*

Independent consultants, DeGolyer & MacNaughton has evaluated six prospects and two leads in parts of HRT's Walvis Basin blocks, resulting in mean estimate Pe-Adjusted prospective resources of 1.1 billion BOE. Further to the south, Chariot has identified (via independent work by Netherland Sewell and Associates) potential of 4.3 billion barrels on blocks straddling the Walvis and Luderitz basins.

*Fig. 10: Large Resource Estimates By Regional Peers*

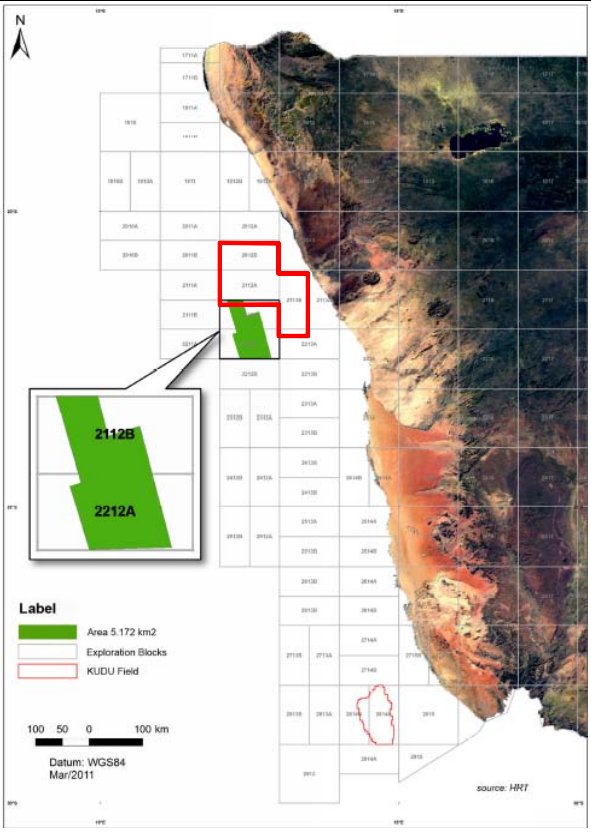



Source: Eco Oil and Gas Ltd, Pancontinental, Hartleys

*HRT has recently completed a large 3D seismic shoot on neighbouring blocks. This is the precursor to likely drilling in 2012, which could significantly re-rate PCL's acreage.*

An historic well exists on one of PCL's blocks, which encountered excellent quality reservoir and oil shows but had a poor trapping mechanism. Three other wells in the basin encountered good quality reservoir with oil shows. The offshore drilling history in Namibia is tabulated in Fig. 12.

*Fig. 11: 2011 3D Seismic Program by HRT Adjacent to PCL*




Source: HRT, Pancontinental

Intepretation of HRT's recently acquired seismic, shown above, may give further insight into the potential on PCL's acreage immediately adjacent to the north.

*Drilling history in Namibia provides encouragement with numerous oil and gas shows. Only 8 exploratory wells indicate that the area remains underexplored.*

*Fig. 12: Historic Results – Oil Shows and Reservoir Proven*

## RESERVOIR – Historical Exploration Results

Field & Lab 2010

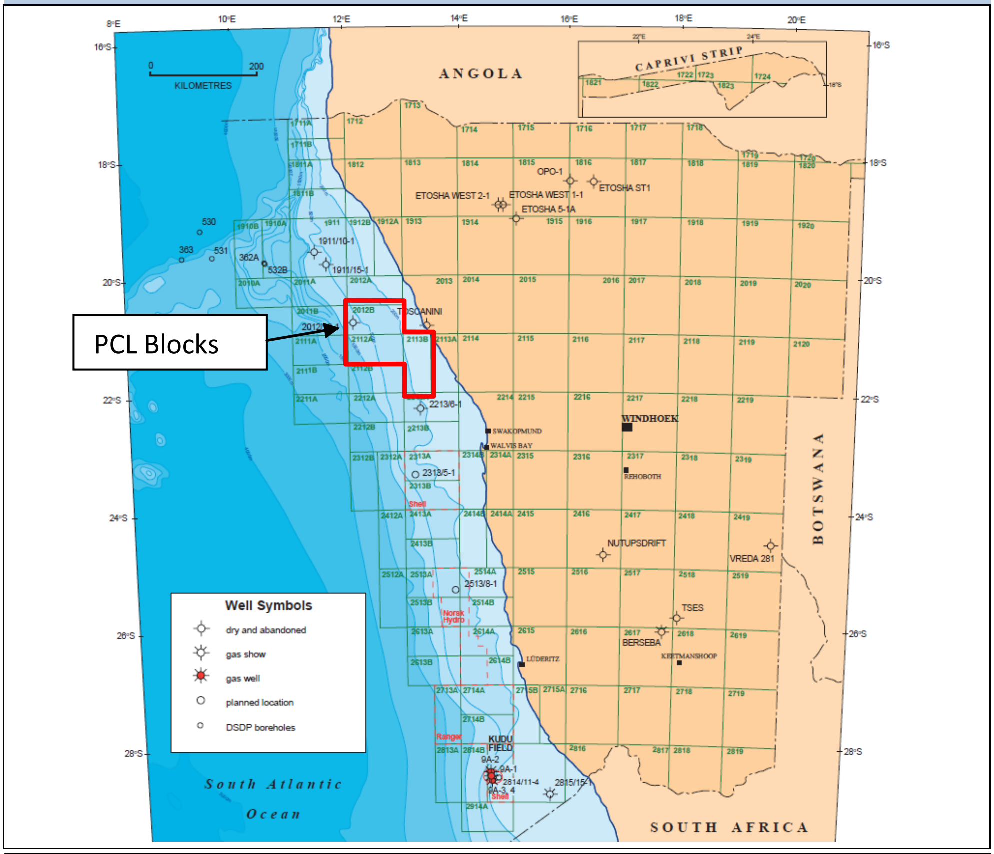
| Lab | Well ID | License area | Water depth Shallow waters | Operator | Year Drilled | Basin | Total Depth | Result shows | Reservoir | Source potential-migration pathways | Trap |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Kudu 9A-1 | (2814A) | 167m | Chevron | 1973 | Orange | 4536 mbKB | Gas & Oil shows | good sandstone | good | good |
| | Kudu 9A-2 Kudu 2 | (2814A) | 168m | Swakor | 1987 | Orange | 4505 mbKB | Gas & Oil shows | poor sandstone | good | stratigraphic poor |
| | Kudu 9A-3 Kudu 3 | (2814A) | 166m | Swakor | 1988 | Orange | 4522 mbKB | Gas & Oil shows | good sandstone | good | good |
| | Kudu - 4 | 2814A | 176 m (MSL) | Shell | 1996 | Orange | 4719 mbKB | Gas & Oil shows | good sandstone | good | good |
| | 2814/11-4 Kudu - 5 | 2814A | 162.9m (MSL) | Shell | 1998 | Orange | 4898 mbKB | Gas & Oil shows | good sandstone | good | good |
| | 2814/11-5 Kudu - 6 | 2814A | 171m (MSL) | Shell | 2002 | Orange | 4725 Mahbdf | Gas & Oil shows | good sandstone | good | stratigraphic poor |
| | 2814/7-2 Kudu - 7 | 2814A | 179 m (MSL) | Shell | 2002 | Orange | 5275 mbKB | Gas & Oil shows | good sandstone | good | stratigraphic poor |
| | Kudu - 8 | Kudu Production | 179 m | Tullow | 2007 | Orange | 4725m | Gas & Oil shows | good sandstone | good | stratigraphic poor |
| | 1911/15-1 | 1911 | 489 m (MSL) | Norsk Hydro | 1994 | Walvis | 4586 mbKB | Oil shows in core 4 | good carbonate | fair | poor |
| | 1911/10-1 | 1911 | 631m (MSL) | Norsk Hydro | 1996 | Walvis | 4185 mbKB | Oil shows | good sandstone | fair | poor |
| * | 2012/13-1 | 2012 | 650m (MSL) | Sasol | 1995 | Walvis | 3712 mbKB | Oil shows | good sandstone | good | poor |
| * | 2213/ 6-1 | 2213 | 240m (MSL) | Ranger Oil | 1995 | Walvis | 2627 mbKB | Oil shows | good sandstone | poor | poor |
| | 2313/ 5-1 Shark 1 | 2313 | ?? | Shell | 1998 | Luderitz | 2588 mbKB | Oil shows | good sandstone | poor | poor |
| | 2513/8-1 | 2513 | 243m | Norsk Hydro | 1998 | Luderitz | 2423 mbKB | Oil shows in core 1 | good sandstone | poor | poor |
| | 2815/15-1 | 2815 | 177m (MSL) | Chevron | 1996 | Orange | 4751 mbKB | Gas & Oil shows | tight sandstone | fair | stratigraphic poor |

**The main risks:** in Walvis and Luderitz the main risk is Charge (maturation and pathways); while in Orange it is trap (stratigraphic) . The proximity of the pod of geration is critical and the concentration of migration pathways.

Source: UNX

*One of the 8 exploratory wells drilled is on PCL's acreage but deemed to be off structure. Oil shows and excellent reservoir were encountered..*

*Fig. 13: Historic Wells*




Source: Namcor

The two preceding figures detail the historic drilling offshore Namibia. Note the low number of wells (8 outside of the Kudu Gas Field) and the incidence of oil and gas shows. With the aid of modern 3D seismic and more drilling, the likelihood of commercial discoveries in the region is considered high. Up to six wells are planned in the Walvis and Orange basins over the next 18 months.

A number of these wells are expected in the region of Pancontinental's acreage.

## MALTA (PCL 80% - PENDING)

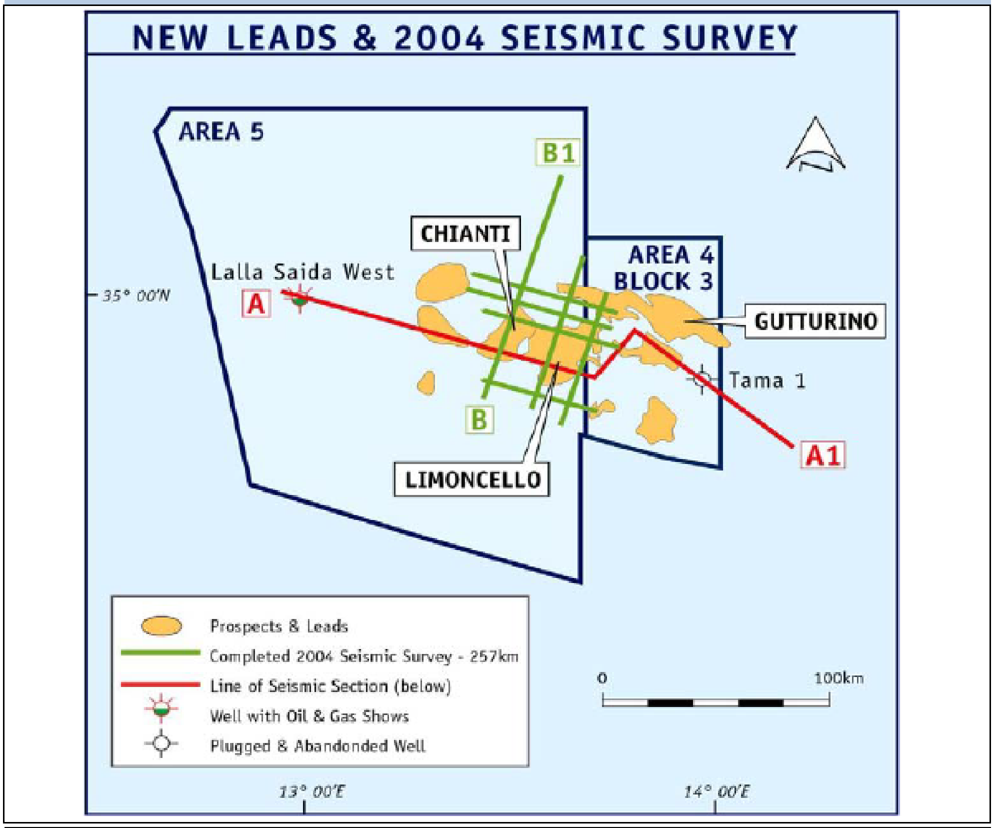
*Huge potential in Malta remains in limbo pending reactivation of exploration activity, which was suspended due to a territorial dispute. Talks remain positive; however, timing is uncertain.*

Pancontinental entered Malta in early 2001, after identifying large potential with similar geology to nearby producing fields in both Libya and Tunisia. This was confirmed by 2D seismic acquired in 2004. The prospectivity of the acreage was enough to attract Anadarko to farm-in in June 2005. Unfortunately, a portion of the two blocks are part of a territorial dispute and Anardarko walked away in December 2008 after a lack of progress on resolution of the dispute.

PCL continues to negotiate with the Maltese government to reactivate exploration on the licenses, which officially lapsed in August 2008 (although force majeure would likely apply). Talks are positive; however, timing of resolution is unclear.

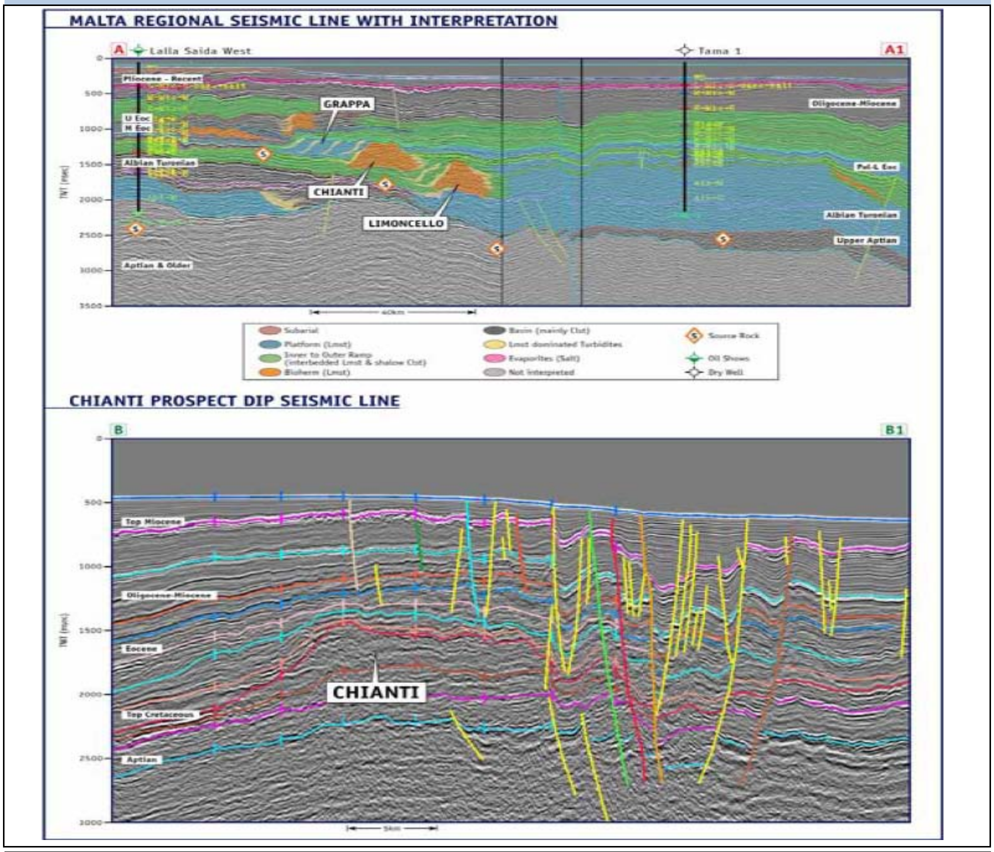
The two largest leads on the permit, Chianti and Limoncello, have potential for 453 and 968 million barrels of oil (mean recoverable potential) and are considered analogous to nearby producing fields offshore Libya. Significantly, the Chianti prospect is interpreted to lie outside of the disputed areas.

*Fig. 14: Malta Blocks*




Source: Pancontinental

*Fig. 15: Seismic Over Chianti and Limoncello*




Source: Pancontinental

## OTHER ASSETS (PCL VARIOUS INTERESTS)

Pancontinental has various interests in several permits in Western Australia, which are described briefly below.

*Fig. 16:* *Australian Assets*

| Permit | Working Interest | Description |
|---|---|---|
| EP110 / EP424 | 38.5% | Onshore / offshore Barrow Dampier Sub-basin. Largest prospect, Baniyas, may contain up to 34 million barrels of oil. Drilling possible within 12 months pending farmout. |
| EP406 | 5% | Carnarvon Basin – offshore Merlinleigh Sub-basin. Large early stage permit. |
| EP104 / R1 | 10% | Canning Basin – onshore Lennard Shelf. Large prospective permit. Significant appraisal work at Stokes Bay-1 resulted in recovery of saline water. Retained until late 2015. |
| L15 | 12% | Canning Basin – onshore Lennard Shelf. Production licence over West Kora-1 oil discovery. Aim to restore production from West Kora, which historically produced 20,000 barrels of oil after being drilled in 1984. |

Source: Pancontinental

PCL also has a Reconnaissance Licence pending offshore Morocco; however, a territorial waters dispute between Morocco and Spain is delaying the issue of the licence.

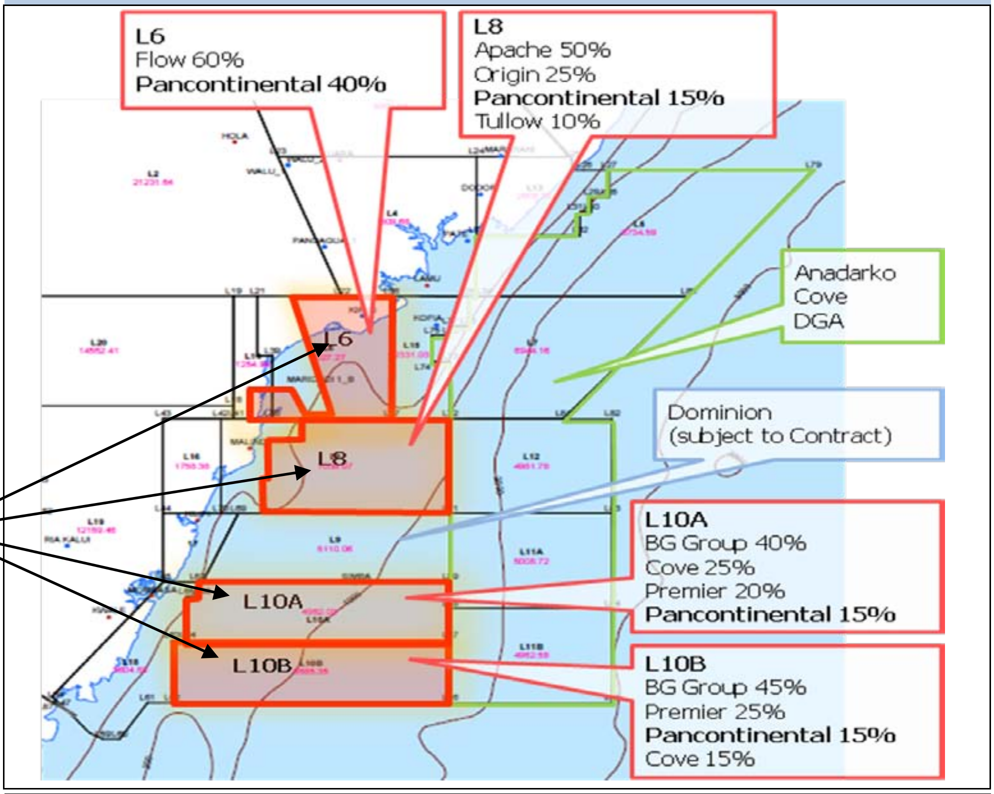
## Peer Analysis – Undervalued in "Hot" Regions

The figure below shows PCL in Joint Venture on blocks L8, L6, L10A and L10B and illustrates that offshore Kenya is now predominantly the playground of much larger companies.

**Market Cap of Neighbours***

| | |
|---|---|
| Apache Market Cap = | A$47.4b |
| Origin Market Cap = | A$15.6b |
| Premier Market Cap = | A$2.9b |
| Tullow Market Cap = | A$16.5b |
| BG Market Cap = | A$73.3b |
| Cove Market Cap = | A$655m |
| Anadarko Market Cap = | A$40b |
| Dominion Market Cap = | A$115m |
| **PCL Market Cap =** | **A$70m** |
| DGA & Flow (private) | |

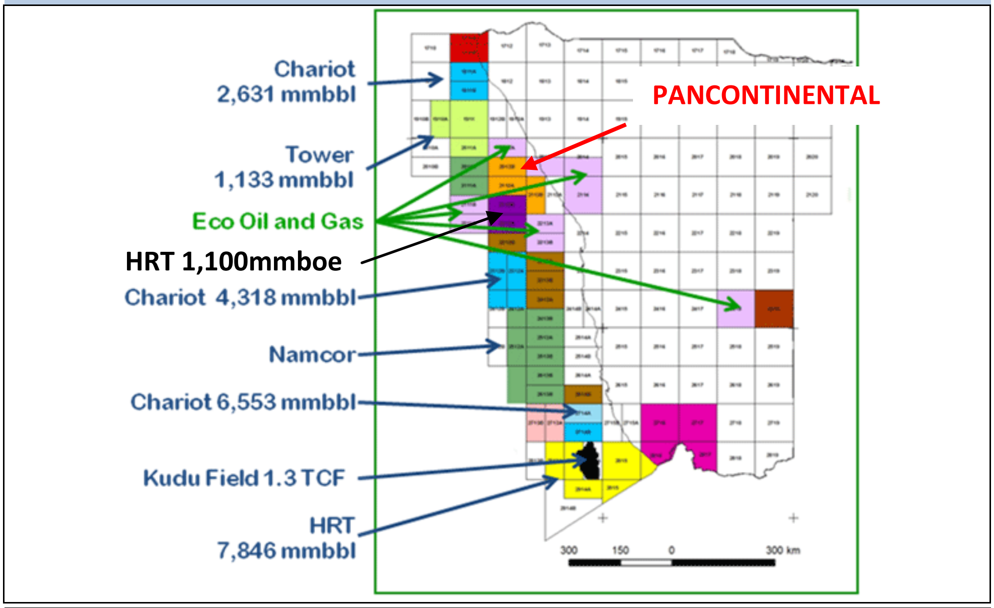
*Fig. 17: PCL in 4 Permits Offshore Kenya*




Source: Pancontinental, Hartleys

Initial work by PCL on its Namibian acreage indicates potential for large structures, similar to nearby peers. The likelihood of oil rather than gas is also supported.

*Fig. 18: Large Resource Estimates By Regional Peers*




Source: Eco Oil and Gas Ltd, Pancontinental, Hartleys

**Market Cap of Neighbours***

Ophir Market Cap = A$1.2b

HRT Market Cap = A$4.8b

Premier Market Cap = A$2.9b

Chariot Market Cap = A$450m

Hyperdynamics

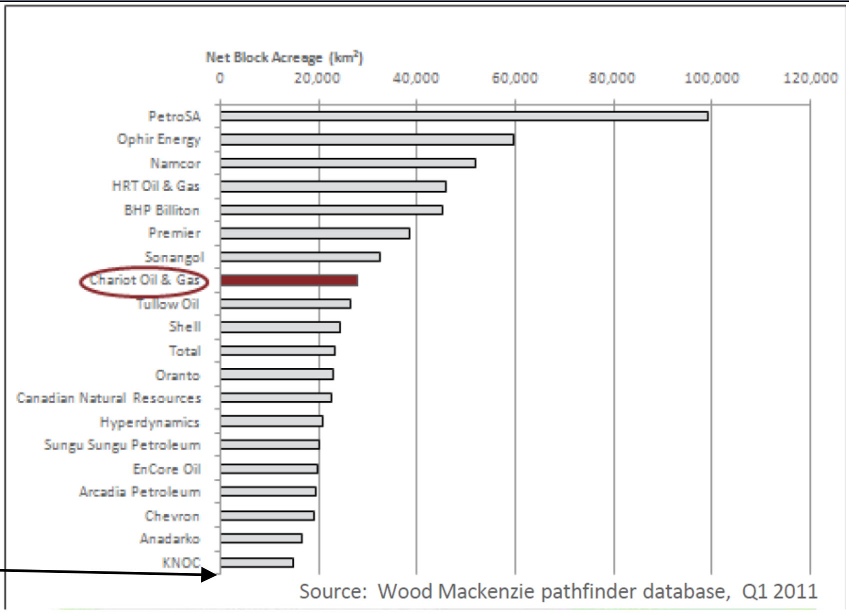
Market Cap = A$800m

Encore Market Cap = A$260m

**PCL (Namibia only)**

**Market Cap = A$70m**

*Fig. 19: West Africa Acreage Holders*




Source: Chariot, Hartleys,*does not take into account value of non West African assets

The figure above does not take into account many factors, such as: the potential value of assets located outside of West Africa, where the assets in West Africa are or how advanced work is on those assets. Despite this, it illustrates the uplift potential possible and that PCL has a large exposure. Some companies, like Chariot provide a more direct comparison as it only has assets offshore Namibia. The assets are more advanced and predominantly located in the Orange Basin; however, this shows that work planned by PCL on its Namibian assets is likely to result in significant share price appreciation if initial prospectivity is confirmed. This is in addition to PCL's significant Kenyan acreage portfolio.

The recent entry of larger companies into areas that PCL has been active for many years validates the Company's strategy and increases credibility associated with prospectivity. Both Namibia and Kenya are the focus of significantly increased activity, which will see up to 10 wells drilled offshore in these areas over the next 18 months. PCL will participate in at least one of these wells at Mbawa; however, as the Company has net acreage of 3,600km$^2$ in Kenya and 14,700km$^2$ in Namibia (total net 18,300km$^2$), success by others may be just as significant.

## INDUSTRY EXPOSURE

PCL has exposure to the oil and gas industry in Kenya, Namibia, Australia, Malta and Morocco.

The oil and gas industry in Africa is relatively mature but still evolving; however, we consider Kenya and Namibia to be stable and supportive of exploration efforts.

Malta and Morocco are both challenged by territorial disputes, with Northern Africa generally a more complex business environment, particularly in recent months.

Australia, historically considered as low risk has recently proposed changes to its taxation system. PCL has little exposure to any impact from these changes.

PCL's largest exposure is offshore Kenya and Namibia. Fiscal terms in both are considered favourable.

## GEOGRAPHIC EXPOSURE

PCL's main geographic exposure is offshore Kenya and Namibia. Weather conditions generally do not pose significant operational risk.

## PEERS AND COMPETITORS

See previous page.

## KEY SUPPLIERS & CUSTOMERS

PCL is partnered with several industry heavy weights offshore Kenya, including: Origin Energy Ltd, Apache Oil Corporation, Tullow Oil Plc, BG Group Plc, Premier Oil Plc and Cove Energy Plc. The market capitalisations of these companies can be seen in the Peer Comparison section. All are of high quality and in particular are renowned for the exploration acumen in frontier areas.

In Namibia, PCL has a local partner, consistent with government policy in many African nations, which required local participation.

# MANAGEMENT AND DIRECTORS

The following excerpt has been sourced from the PCL website.

***Mr Henry David Kennedy***

BA (Geology), MA (Geology), Member of SME, SEG, PESA, AIG
Chairman

Mr Kennedy has had a long association with Australian and New Zealand resource companies. As a technical director he has been instrumental in the formation and/or development of a number of successful listed companies. These include Pan Pacific Petroleum NL, New Zealand Oil and Gas Limited (NZOG), Mineral Resources (NZ) Ltd and Otter Exploration NL.

During his term as Executive Director of Pan Pacific, NZOG and Otter, these companies were involved in the discovery of a number of oil and gas fields. These included the Tubridgi gas field and South Pepper, North Herald and Chervil oil fields in Western Australia and the Kupe South and Rua oil/gas condensate fields in New Zealand.

He is also a director of Norwest Energy NL.

***Mr Roy Barry Rushworth***

BSc, Member of AAPG and PESGB, Chief Executive Officer and Executive Director

Mr Rushworth has more than 25 years experience in petroleum exploration. His experience extends from wellsite geology and seismic acquisition to company administrative and management functions. He was previously General Manager and Director of Afrex Limited where he was responsible for negotiating the company's international projects that are now held by Pancontinental.

***Mr Ernest Anthony Myers***

CPA, Finance Director

Ernie Myers has over 30 years experience in the resources industry. He is an accountant (CPA) who has held senior management and executive roles within a number of ASX listed companies. Ernie joined Pancontinental in March 2004 as Company Secretary and was appointed Finance Director in January 2009. He brings corporate and operational experience in a variety of fields including project development, feasibility studies and both equity and debt financing. Prior to his appointment with Pancontinental, he was CFO and Company Secretary of Dragon Mining Limited for a period of six years during its transition from explorer to gold producer in Sweden. Ernie has extensive experience in exploration and operational issues particularly in Kenya, Tanzania, Namibia and Eritrea.

***Mr Anthony Robert Frederick Maslin***

Non-Executive Director

Mr Maslin is a stockbroker with corporate experience in both management and promotion, along with an extensive understanding of financial markets. Mr Maslin has been instrumental in the capital raisings and promotion of several resource development companies.

***Mrs Vesna Petrovic***

Company Secretary

Mrs Petrovic has an accounting background with a Bachelor of Commerce, Major in Accounting & Business Law, she is a Certified Practicing Accountant and has completed the Graduate Diploma in Applied Corporate Governance from Chartered Secretaries Australia Ltd. Mrs Petrovic has experience in the resources sector, particularly with companies involved in Africa.

*Fig. 20: Financial Exposure of Board and Management*

| Name | Position | Options | Ord Shares | Total |
|---|---|---|---|---|
| **Directors** | | | | |
| Henry David Kennedy | Chairman Executive | 1,500,000 | 155,301,968 | 156,801,968 |
| Roy Barry Rushworth | CEO, Executive Director | 3,000,000 | 34,764,181 | 37,764,181 |
| Ernest Anthony Myers | Finance Director | 1,000,000 | | 1,000,000 |
| Anthony Maslin | Non-Executive Director | | 0 | 0 |

Source: Pancontinental

Source: Pancontinental

# MAJOR SHAREHOLDERS

*Fig. 21: Major Shareholders*

| Entity / Person(s) | Amount | Percentage | Relationship |
|---|---|---|---|
| Henry David Kennedy | 155m | 23.5% | Chairman |
| Indago Resources Ltd | 58.2m | 8.8% | Investment Fund |
| Roy Barry Rushworth | 34.8m | 5.3% | CEO |
| Total | 248 | 37.6% | |

Source: Pancontinental

# FINANCIALS

## PRODUCTION / PROFIT & LOSS

### Company guidance

As the Company's assets are currently not in the development phase, there is no guidance for profit.

### Hartleys Forecasts

We have not calculated on forecast financials; however, have modelled notional net present value for different success scenarios. These are the basis for our valuation.

## BALANCE SHEET

The Company had cash of $5.7m at end of June 2011, with no debt.

### Debt

The Company is currently debt free.

### Hedging

There are no hedges in place.

## CASH FLOW

### Capex requirements

In Kenya, the Company's share of 2D / 3D at L10A / L10B is estimated at $3m. It is free carried by Tullow Plc through the drilling of Mbawa and is seeking a farmout to cover seismic costs on its L6 permit.

In Namibia, initial work consists of re-processing old seismic. Acquisition of additional seismic is possible towards the end of CY2011; however, the Company has several years to do this.

## EQUITY ISSUANCE

PCL recently issued 68,493,151 shares at 7.3cps to raise $5m (April 2011).

The Company has 660.8m shares on issue with 13.75m options (9.25m strike 9.6cps, expiry 28 November 2011, 4.5m strike 5.9c, expiry 28 November 2012).

## SENSITIVITIES

As the Company has no production, sensitivities are less quantitative; however, as a general observation, higher oil and gas prices result in increased exploration activity and interest in frontier areas.

### Commodity Price Exposure

As implied above, PCL will benefit from increased oil and gas prices, which will improve the value of its permits as the higher prices offset the risk associated with frontier exploration.

# VALUATION CONSIDERATIONS AND PRICE TARGET METHODOLOGY

## VALUATION

Valuation of exploration in frontier areas is subject to quantitative measures such as potential size of prospects as indicated by seismic and also qualitative measures such as probability of success ("POS"). Global average frontier exploration success rate pre-2000 is ~10%; however, since 2000, advances in technology have increased this to almost 20%.

A substantial amount of work has been done, particularly over the Mbawa Prospect, including modern 3D seismic with advanced processing and interpretation techniques. The recent farm-ins by Tullow and Apache, both of whom have an excellent exploration track record, indicates that there is a high level of prospectivity.

We have adjusted our assumed POS based on work done to date to de-risk the prospects as well as other factors, including risk related to granting of permits (in the case of Malta). We have taken a conservative line on POS by comparison to global success rates. This means that there is potential for future valuation increases depending on de-risking activity by PCL or others operating nearby.

We have used a notional value per barrel of A$10, except in Australia where we have used A$15 per barrel. Volumetric assumptions for Mbawa and Chianti are from the Company, the remainder are our own estimations. We have also made assumptions regarding post farm-out working interest on each of the permits where farmouts are pending.

The result is a risked valuation of 33cps, with unrisked upside potential of 1,047cps. This does not include any followup potential at other prospects / leads in each block.

*Fig. 1: Exploration Valuation*

| Permit / Prospect / Interest | Net Recoverable Potential | NPV per Unit (A$) | POS | Risked Value (A$m) | Risked Value (cps) | Un-risked Value (cps) |
|---|---|---|---|---|---|---|
| L8-Mbawa (15%) | 128 million barrels | A$10 per bbl | 10% | A$128m | 19.0cps | 190cps |
| L6 (20%) | 80 million barrels | A$10 per bbl | 5% | A$40m | 5.9cps | 119cps |
| EL0037 (30%) | 300 million barrels | A$10 per bbl | 1% | A$30m | 4.5cps | 445cps |
| 10A (10%) | 50 million barrels | A$10 per bbl | 2% | A$10m | 1.5cps | 74cps |
| 10B (10%) | 50 million barrels | A$10 per bbl | 2% | A$10m | 1.5cps | 74cps |
| Malta-Chianti (20%) | 91 million barrels | A$10 per bbl | 0.2% | A$2m | 0.3cps | 134cps |
| Aus-Baniyas (20%) | 5 million barrels | A$15 per bbl | 5% | $3.6m | 0.5cps | 11cps |
| Total | 703 million barrels | | | A$224m | 33cps | 1,047cps |

Source: Hartleys

## PRICE TARGET

Based on our experience with other junior oil and gas explorers and their historical market performance versus speculative resource potential, we believe our valuation is reasonable. If PCL can gain recognition in capital markets outside of Australia, we believe that our valuation of 33cps may be achieved prior to the drilling of a well. The Company; however, needs to achieve certain milestones before a valuation of this magnitude is achieved.

Consequently, our price target is a 40% discount to valuation, which takes into account size and liquidity discounts that are common to all smaller companies. This results in a 6-month price target of 20cps.

# RECOMENDATION & RISKS

## INVESTMENT THESIS & RECOMMENDATION

Pancontinental's strategy of early entry into oil prone frontier areas is starting to be given recognition in the market; however, we believe that this is only the beginning. Industry interest typically precedes the stock market by 12 months or so and we have seen a strong increase in industry interest in PCL's main core areas, offshore Kenya and Namibia in recent times.

In Kenya, PCL has farmed-in arguably the best African explorer of the last decade, Tullow Oil Plc, and will be free carried through drilling of the 1 billion barrel plus Mbawa prospect. Timing has not been finalised but we believe that operator, Apache, is contemplating drilling in H1 2012. The value uplift for PCL, in a success case, exceeds 20 times return on investment. It is likely that share price appreciation will occur in the lead up to the drilling, given the upside potential.

In Namibia, the Company has recently been awarded a large Exploration Licence in an area that is deemed prospective based on studies done by PCL and also by regional neighbours. Overseas markets are valuing explorers in Namibia on high multiples despite no wells being drilled. This is due to interpreted geological similarities between Namibia and Brazil, where large discoveries have recently been made. Drilling of up to 6 wells over the next 18 months, starting late 2011, could re-rate PCL's acreage significantly.

PCL is undervalued on peer analysis and has significant drilling catalysts in the near-medium term. Given this, we believe that the current share price represents excellent value with high probability of achieving significant returns, although volatility is likely around high-risk drilling events.

We rate PCL as a Speculative Buy with a 6 month price target of 20cps.

## RISKS

The main risks associated with PCL concern high risk exploration drilling; however, as the first of these is not for at least six months, we believe risk to be low in the near term.

## SIMPLE S.W.O.T. TABLE

| | |
|---|---|
| Strengths | Early mover on strategy to secure oil prone acreage in frontier areas |
| | Technical capability highlighted by identification of multi-billion barrel prospects |
| Weaknesses | Exploration success rates in frontier areas are ~20% meaning that failure is more likely than success |
| Opportunities | Strong relationships in Africa mean that additional assets are likely to be acquired |
| Threats | Undervalued compared to peers and may be regarded as a potential takeover target |

Source: Hartleys Research

# HARTLEYS RESEARCH COVERAGE LIST

| Hartleys Research Coverage Name | Ticker | Last Price* | M. CAP (A$m) | Status | Hartleys Research Recommendation |
|---|---|---|---|---|---|
| **Resources** | | | | | |
| **Gold** | | | | | |
| 1. Intrepid Mines Limited | IAU | 1.72 | 895 | Explorer | Speculative Buy |
| 2. Beadell Resources Limited | BDR | 0.875 | 576 | Developer | Accumulate |
| 3. Integra Mining Limited | IGR | 0.495 | 417 | Producer | Accumulate |
| 4. Gold One International Limited | GDO | 0.510 | 412 | Producer | No Rating |
| 5. Silver Lake Resources Limited | SLR | 2.14 | 383 | Producer | Buy |
| 6. Tanami Gold NL | TAM | 0.970 | 253 | Producer | Accumulate |
| 7. Catalpa Resources Limited | CAH | 1.42 | 253 | Producer | Buy |
| 8. Focus Minerals Ltd | FML | 0.068 | 234 | Producer | Buy |
| 9. YTC Resources Limited | YTC | 0.670 | 166 | Developer | Buy |
| 10. Northern Star Resources Ltd | NST | 0.460 | 138 | Producer | Buy |
| 11. PMI Gold Corporation Limited | PVM | 0.650 | 129 | Developer | Speculative Buy |
| 12. Papillon Resources Limited | PIR | 0.555 | 113 | Explorer | Speculative Buy |
| 13. Emmerson Resources Limited | ERM | 0.150 | 34 | Explorer | Speculative Buy |
| 14. Cortona Resources Limited | CRC | 0.160 | 31 | Developer | Speculative Buy |
| 15. Ausquest Limited | AQD | 0.110 | 25 | Explorer | Speculative Buy |
| 16. Southern Gold Limited | SAU | 0.056 | 14 | Explorer | Speculative Buy |
| 17. Canyon Resources Limited | CAY | 0.325 | 13 | Explorer | Speculative Buy |
| 18. Geopacific Resources NL | GPR | 0.205 | 7 | Explorer | Speculative Buy |
| **Iron Ore** | | | | | |
| 19. Atlas Iron Limited | AGO | 3.82 | 2,087 | Producer | Buy |
| 20. Centaurus Metals Ltd | CTM | 0.081 | 69 | Explorer | Speculative Buy |
| **Coal** | | | | | |
| 21. Riversdale Mining Limited | RIV | 16.20 | 3,052 | Developer | No Rating |
| **Base Metals** | | | | | |
| 22. Independence Group NL | IGO | 5.740 | 1,163 | Gold, Ni, Zn, Cu | Buy |
| 23. Aviva Corporation Limited | AVA | 0.220 | 30 | Explorer | Speculative Buy |
| **Other metals** | | | | | |
| 24. Kasbah Resources Limited | KAS | 0.225 | 82 | Tin Developer | Buy |
| 25. Shaw River Resources Limited | SRR | 0.190 | 48 | Manganese: | Speculative Buy |
| 26. Hazelwood Resources Ltd | HAZ | 0.145 | 38 | Tungsten Developer | Speculative Buy |
| **Uranium** | | | | | |
| 27. Peninsula Energy Ltd | PEN | 0.073 | 153 | Developer | Buy |
| 28. Impact Minerals Limited | IPT | 0.065 | 8 | Explorer | Speculative Buy |
| | | Sub-Total | 10,822 | | |

| Name | Ticker | Last Price* | M. CAP (A$m) | Status | Hartleys Research Recommendation |
|---|---|---|---|---|---|
| **Oil & Gas** | | | | | |
| **Conventional Oil & Gas** | | | | | |
| 1. Woodside Petroleum Ltd | WPL | 40.68 | 31,736 | Major | Buy |
| 2. Nexus Energy Ltd | NXS | 0.31 | 292 | Developer / Explorer | No Rating |
| 3. Tap Oil Ltd | TAP | 0.84 | 201 | Producer / Explorer | Buy |
| 4. Carnarvon Petroleum Ltd | CVN | 0.21 | 141 | Producer / Explorer | Accumulate |
| 5. FAR Ltd | FAR | 0.11 | 131 | Explorer / Producer | Speculative Buy |
| 6. Cooper Energy Ltd | COE | 0.38 | 111 | Producer / Explorer | Buy |
| 7. Otto Energy Ltd | OEL | 0.09 | 98 | Explorer / Producer | Buy |
| 8. Amadeus Energy Ltd | AMU | 0.24 | 71 | Producer / Explorer | Neutral |
| 9. Hawkley Oil and Gas Ltd | HOG | 0.32 | 60 | Producer / Explorer | Buy |
| 10. WHL Energy Ltd | WHN | 0.03 | 25 | Explorer / Producer | Speculative Buy |
| 11. Sun Resources NL | SUR | 0.03 | 11 | Explorer / Producer | Neutral |
| **Non Conventional Oil & Gas** | | | | | |
| 12. Aurora Oil and Gas Ltd | AUT | 3.41 | 1,377 | Producer / Developer | Reduce |
| 13. Samson Oil & Gas Ltd | SSN | 0.130 | 225 | Developer / Producer | Buy |
| 14. Oilex Ltd | OEX | 0.37 | 92 | Explorer / Producer | Speculative Buy |
| 15. Transerv Energy Ltd | TSV | 0.03 | 88 | Developer | Buy |
| 16. European Gas Ltd | EPG | 0.37 | 74 | Producer / Explorer | Speculative Buy |
| 17. Strike Energy Ltd | STX | 0.20 | 66 | Explorer / Producer | Buy |
| 18. Entek Energy Ltd | ETE | 0.18 | 50 | Producer / Explorer | Speculative Buy |
| | | Sub-Total | 34,848 | | |
| **Industrials** | | | | | |
| **Resource Services - Capital Intensive** | | | | | |
| 1. Ausdrill Limited | ASL | 3.26 | 993 | Contract Drilling | Buy |
| 2. NRW Holdings Ltd | NWH | 2.74 | 768 | Contract mining | Accumulate |
| 3. Mermaid Marine Ltd | MRM | 3.27 | 697 | Oil & Gas Services | Accumulate |
| 4. Fleetwood Corporation | FWD | 11.35 | 650 | Accomodation | Neutral |
| 5. Matrix Composites & | MCE | 7.51 | 548 | Oil & Gas Services | Buy |
| 6. Imdex Ltd | IMD | 2.47 | 494 | Drilling Supplies | Buy |
| 7. Macmahon Holdings Limited | MAH | 0.58 | 426 | Contract mining | Neutral |
| 8. MACA Ltd | MLD | 2.42 | 363 | Contract mining | Buy |
| 9. Pacific Energy Ltd | PEA | 0.45 | 158 | Remote Power | Buy |
| 10. Swick Mining Services Ltd | SWK | 0.39 | 92 | Contract Drilling | Speculative Buy |
| **Resource Services - Labour Intensive** | | | | | |
| 11. Monadelphous Group Limited | MND | 18.99 | 1,634 | Construction | Buy |
| 12. Decmil Group Limited | DCG | 2.75 | 340 | Construction | Buy |
| 13. Lycopodium Limited | LYL | 6.56 | 254 | Engineer. & Constr. | Accumulate |
| 14. RCR Tomlinson Ltd | RCR | 1.65 | 218 | Engineer. & Constr. | Buy |
| 15. LogiCamms Limited | LCM | 1.11 | 74 | Engineer. & Constr. | Speculative Buy |
| 16. VDM Group Limited | VMG | 0.16 | 34 | Engineer. & Constr. | Speculative Buy |
| **Other Industrial Companies** | | | | | |
| 17. Seven West Media Limited | SWM | 4.10 | 3,160 | Media | Accumulate |
| 18. Austal Limited | ASB | 2.97 | 559 | Civil and Military | Buy |
| 19. iiNet Limited | IIN | 2.57 | 391 | Telecommunications | Buy |
| 20. Cash Converters Internat. | CCV | 0.75 | 300 | Unsecured Finance | Buy |
| 21. Amcom Telecommunications | AMM | 0.37 | 265 | Telecommunications | Buy |
| 22. RedHill Education Ltd | RDH | 0.16 | 4 | 'For profit' education | Neutral |
| | | Sub-Total | 12,420 | | |
| 68. | | GRAND TOTAL | 58,090 | | |

Source: IRESS, Hartleys Research. * 11 Jul 2011

# HARTLEYS CORPORATE DIRECTORY

## Research

| | | |
|---|---|---|
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| www.hartleys.com.au | info@hartleys.com.au |

*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. |

## Institutional Sales

| | |
|---|---|
| Carrick Ryan | +61 8 9268 2864 |
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| Simon van den Berg | +61 8 9268 2867 |
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Hartleys has provided corporate advice within the past 12 months and continues to provide corporate advice to Pancontinental Oil and Gas NL, for which it earned fees and continues to earn fees.

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