

Share Price:	\$0.073
12mth Price Target:	\$0.13

CUE ENERGY LTD (CUE)

The parts are moving in the right direction

We continue to like the outlook for Cue Energy Ltd (CUE). The Maari Growth Project is starting to yield meaningful results and the underlying price of oil has remained stable since the beginning of May. In Indonesia the strategy remains production growth plus exploration including an onshore well on the Mahakam Hilir PSC in 4Q CY15. CUE has also made a relative low cost and low risk entry into a US onshore conventional oil play (with production). Other potential catalysts include a farm-down of CUE's key W.A blocks – WA-409P and WA-359P (CUE 100%). We maintain our Speculative Buy recommendation on the stock with a price target of 13c.

US onshore acquisition

In June CUE acquired 80% of the Pine Mills project in Wood County, Texas. CUE has paid US\$2m in cash plus a commitment to carry the JV partner (Gale Force Petroleum) for US\$1m of operating and capital expenses over the next 4 years. The Pine Mills project consists of 2,200 acres (gross) with 14 producing (vertical, conventional) wells, 2 injection wells and 13 inactive wells. Current production from the field is 90b/d with 300kbbbl of 2P reserves. CUE's initial strategy will be to increase production through the workover of producing and inactive wells. Longer term CUE will look to acquire additional acreage in order to improve overall field economics.

We think this is a sensible entry into the US onshore oil market. Acquiring relatively cheap (US\$10 / bbl 2P reserves), conventional production assets in a proven oil province is a relatively low risk strategy. CUE also has the advantage of being able to fund the acquisition from cash reserves in an environment where alternative funding sources are increasingly difficult to find or are prohibitively expensive. Should the oil price recovery sufficiently then CUE also has the option to exploit the unconventional potential of the Woodbine formation.

Maari Growth project

The Maari growth project currently being completed by OMV (operator of the Maari Field) is designed to increase production and extend the life of the field. In May, production from the MR7A development well was successfully brought on line with provisional production rates of 1,500-2,000 b/d. This brings to 15,000b/d, the gross daily production from the Maari Field (compared to 14,000b/d in March). The Ensco 107 rig has since been completed with results pending. CUE holds a 5% stake in the Maari Field with OMV as the operator (69% interest).

Valuation and recommendation

We value CUE at 13.2 cps of which Maari contributes 4.8cps and Indonesian production 2.6cps. The balance of our valuation is exploration assets (2.1cps) and cash (4.7cps). The obvious risk (and benefit) to our investment thesis is ongoing volatility of the price of oil. The next catalyst for the stock is likely to be the release of the FY15 results. Investors should be aware that a General Meeting will be held on the 29th of July to consider resolutions to remove Geoffrey King and Andrew Young as Directors.

Brief Business Description:

CUE is a conventional oil and gas explorer/developer with projects in PNG, Indonesia, Australia and New Zealand

Hartleys Brief Investment Conclusion

CUE should be able to grow production in FY16 from the Maari Growth Project and higher Indonesian Gas Production.

Chairman & CEO:

Mr Geoffrey King (Non Exec Chairman)
Mr David Biggs (Chief Executive Officer)

Top Shareholders:

New Zealand Oil & Gas	48%
Petrochina	16%

Company Address:

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Melbourne, VIC, 3000

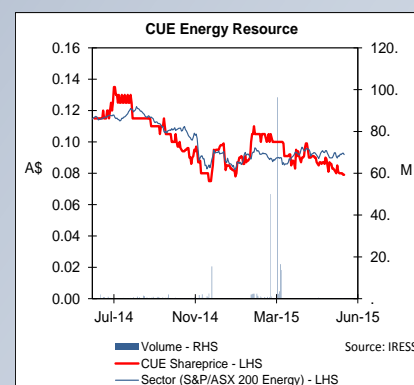
Issued Capital:	698m
- fully diluted	698m
Market Cap:	\$51.0m
- fully diluted	\$51.0m
Current Debt	\$0.0m
Current Cash	\$28.0m

2P Reserve (mmbbl)	4.70
EV / 2P Reserve	\$4.89

	FY14A	FY15F	FY16F
Prodn (boe)	677,278	808,991	808,060
Op Cash Flw	\$6m	\$11m	\$12m
Free Cash Flw	-\$19m	-\$16m	-\$3m
NPAT* (A\$m)	-\$5m	\$3m	\$4m
EPS (\$, bas)*	-0.8x	0.5x	0.5x
P/E (basic)*	-9.3x	15.5x	13.6x
EV / EBIT	-6.9x	4.9x	4.3x
EV / EBITDA	3.8x	1.8x	1.7x
N.D. / equity	-15%	-2%	0%
Interest Cover	na	na	na
Net Cash End	\$40.6m	\$24.3m	\$21.5m

Source: Hartleys Research

*normalised



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SUMMARY MODEL

CUE Energy Resources Limited CUE		Share Price \$0.073				
Key Market Information						
Share Price						
Market Capitalisation					\$51m	
52 Week High-Low					\$0.073 - \$0.135	
Issued Capital					698.1m	
Issued Capital (fully diluted inc. ITM options)					698.1m	
Cash est.					33.0m	
EV					\$18m	
Valuation					0.127	
12 Month Price Target					0.13	
Financial Performance						
Unit	2013A	2014A	2015F	2016F		
Net Revenue	A\$m	57.9	36.1	33.2	37.8	
Total Costs/Writeoffs	A\$m	(37.5)	(54.3)	(48.0)	(39.0)	
EBITDA	A\$m	33.3	6.0	12.6	13.8	
Depreciation/Amort	A\$m	(17.6)	(9.4)	(7.9)	(8.5)	
EBIT	A\$m	15.7	(3.3)	4.7	5.4	
Net Interest	A\$m	(0.0)	(0.0)	(0.0)	(0.0)	
Pre-Tax Profit	A\$m	19.4	(3.2)	4.7	5.4	
Tax Expense	A\$m	(2.0)	(2.2)	(1.4)	(1.6)	
NPAT	A\$m	17.4	(5.5)	3.3	3.8	
Abnormal Items	A\$m	(11.0)	(0.0)	8.7	-	
Reported Profit	A\$m	6.4	(5.5)	12.0	3.8	
Financial Position						
Unit	2013A	2014A	2015F	2016F		
Cash	A\$m	58.8	40.6	24.3	21.5	
Other Current Assets	A\$m	6.3	4.4	4.4	4.4	
Total Current Assets	A\$m	65.1	44.9	28.7	25.9	
Property, Plant & Equip.	A\$m	73.9	79.5	84.6	91.1	
Exploration	A\$m	36.9	54.1	68.4	68.4	
Investments/other	A\$m	0.3	0.2	0.2	0.2	
Tot Non-Curr. Assets	A\$m	111.2	133.7	153.2	159.8	
Total Assets	A\$m	176.2	178.7	181.9	185.7	
Accounts Payable	A\$m	12.0	21.2	21.2	21.2	
Other	A\$m	4.4	3.0	3.0	3.0	
Total Curr. Liabilities	A\$m	16.4	24.1	24.1	24.1	
Long Term Borrowings	A\$m	-	-	-	-	
Other	A\$m	28.2	25.1	25.1	25.1	
Total Non-Curr. Liabil.	A\$m	28.2	25.1	25.1	25.1	
Total Liabilities	A\$m	44.7	49.3	49.3	49.3	
Net Assets	A\$m	131.6	129.4	132.7	136.4	
Cashflow						
Unit	2013A	2014A	2015F	2016F		
EBITDA	A\$m	33.3	6.0	12.6	13.8	
Income Tax Paid	A\$m	-	-	(0.0)	(0.0)	
Interest & Other	A\$m	(2.0)	(2.2)	(1.4)	(1.6)	
Operating Activities	A\$m	32.7	5.6	11.2	12.2	
Property, Plant & Equip.	A\$m	(5.2)	(14.0)	(13.1)	-	
Exploration/Development	A\$m	(7.6)	(10.3)	(14.4)	(15.0)	
Investments	A\$m	1.9	(0.2)	-	-	
Investing Activities	A\$m	(10.9)	(24.4)	(27.5)	(15.0)	
Draw/Repay Borrowings	A\$m	-	-	-	-	
Equity	A\$m	-	-	-	-	
Financing Activities	A\$m	0.0	0.0	0.0	0.0	
Net Cashflow	A\$m	21.9	(18.8)	(16.2)	(2.8)	
Ratio Analysis						
Unit	2013A	2014A	2015F	2016F		
Cashflow Per Share	A¢	4.7	0.8	1.6	1.8	
Cashflow Multiple	X	1.6	9.1	4.5	4.2	
Earnings Per Share	A¢	2.5	(0.8)	0.5	0.5	
Price to Earnings Ratio	X	2.9	(9.3)	15.5	13.6	
EV / EBIT	X	1.1	(5.4)	3.8	3.3	
EV / EBITDA	X	0.5	3.0	1.4	1.3	
Interest Cover	X	na	na	na	na	
Net debt / Equity	%	na	na	na	na	
Directors						
Mr Geoffrey King (Non Exec Chairman)			Level 19, 357 Collins Street			
Mr Andrew Young (Non Exec Director)			Melbourne, VIC, 3000			
Mr Stuart Brown (Non Exec Director)			Tel: (03) 8610 4000			
Mr Peter Hazeldine (Non Exec Director)			Fax: (03) 9614 2142			
Mr Paul Foley (Non Exec Director)			Web: www.cuenrg.com.au			
Mr Brian Smith (Non Exec Director)						
Company Information						
Mr David Biggs (Chief Executive Officer)						
Mr Andrew Knox (Chief Financial Officer)						
Substantial Shareholders						
		m shares	%			
New Zealand Oil & Gas		335.9	48.1			
Petrochina		113.1	16.2			
Reserves (Net)						
		Unit	1P	2P		
<i>As at 1st January 2014</i>						
Oyong		mmbbl	0.01	0.03		
		bcf	0.67	2.83		
		mmboe	0.12	0.50		
Wortel		mmbbl	0.01	0.01		
		bcf	4.49	5.94		
		mmboe	0.76	1.00		
Maari		mmbbl	1.01	2.34		
Total		mmboe	1.88	3.85		
Production Summary						
		Unit	2013A	2014A	2015F	2016F
Oil		BBL	264,319	138,745	190,497	275,000
Gas		MCF	1,918	3,178	2,611	2,611
Total Production		BOE	1,042,436	677,278	618,315	710,098
Price Assumptions						
		Unit	2013A	2014A	2015F	2016F
Oil		JSD/bt	109.01	107.00	82.25	65.00
Gas		JD/MC	4.49	5.13	5.60	5.60
Exchange Rate		JD/US	0.97	0.92	0.83	0.77
Hedging						
		Unit	2013A	2014A	2015F	2016F
Total Forward Sales - Oil		mmbt	-	-	-	-
Forward Oil Price		A\$/bb	-	-	-	-
Share Price Valuation (NAV)						
		Weighting	\$m	\$/share		
EV/2P Reserves @ US\$15/bbl		30%	69.8	0.100		
EV/EBITDA target 5x		30%	93.5	0.134		
Sum of Parts		40%	99.4	0.142		
Weighted 12 Month Price Target				0.127		
Sum of Parts						
		\$m	\$/share			
Indonesia NPV		17.9	0.026			
New Zealand NPV		33.5	0.048			
Exploration & Development		15.0	0.021			
Net Cash		33.0	0.047			
<i>10% discount rate used for DCF</i>						
Analyst : Simon Andrew						
Phone: +61 8 9268 3020						
Last updated July 3, 2015						
Sources: IRESS, Company Information, Hartleys Research						

VALUATION

Our 12-month target price for CUE is 13cps

Our 12-month target price for CUE is 13cps. Our valuation is based on a combination of cash flow based valuation multiples and reserves based valuation.

Fig. 1: Valuation Table

Share Price Valuation (NAV)	Weighting	\$m	\$/share
EV/2P Reserves @ US\$15/bbl	30%	67.9	0.097
EV/EBITDA target 5x	30%	106.9	0.153
Sum of Parts	40%	99.4	0.142
Weighted 12 Month Price Target			0.132

Sum of Parts	\$m	\$/share
Indonesia NPV	17.9	0.026
New Zealand NPV	33.5	0.048
Exploration & Development	15.0	0.021
Net Cash	33.0	0.047

Source: Iress, Hartleys Research

RISKS

The key risks for CUE (like most oil & gas exploration and development companies) is making an economic discovery and obtaining the funding for ongoing exploration. Other risks include delays, key person risk, country/sovereign risk, weather, JV partner obligations, cost inflation. Investing in explorers is very risky given the exploration value of the company in essence assumes that the market will recognise a portion of potential value before the results of an exploration program are known, conscious that the ultimate chance of success is low (typically 1%-20%) and that failure is much more likely, in most cases. Other risks are earnings disappointments given the industry is volatile and earnings can disappoint due to cost overruns, project delays, cost inflation, environmental regulations, resource estimate errors and management performance and contract negotiation skills. High financial leverage (if it exists at that time) would add to the problem.

SIMPLE S.W.O.T. TABLE

Strengths	Large asset portfolio Experienced board and management. Close to infrastructure Existing producing assets/cash flow Strong balance sheet (cash and no debt)
Weaknesses	Uncertainty with exploration Sovereign risk in Indonesia and PNG.
Opportunities	Exploration upside Surplus cash providing acquisition and exploration potential.
Threats	Commodity price decline. Operating costs increase unexpectedly Exploration wells do not achieve current expectations

Source: Hartleys Research

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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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