

ICON ENERGY LIMITED (ICN)

Cracking the Nappamerri Code...

The next six months shapes up as an important period for Icon Energy (ICN) as the company embarks on the next stage of exploration of its Cooper Basin acreage. ICN and its JV partners hope to firm up a 28Tcf (P50) prospective resource on ATP 855 via a four well fracture stimulation program. The initial flow rates from this program represent a significant share price catalyst in 1H FY15. Recent corporate activity associated with Cooper Basin acreage (Ambassador offer from Drillsearch) may also provide a boost for Cooper Basin explorers such as ICN. We maintain our Speculative Buy on the stock with a target price of 23cps.

ATP 855 - 28 Tcf (P50) prospective resources

ICN and its JV partners in ATP 855 have announced a best estimate (P50) of 28Tcf of Gross Unconventional Prospective Raw Natural Gas Resource, of which ICN's net position is 10Tcf. The P50 estimate puts ICN on track to achieve 2P reserves of 2Tcf (net). It should be remembered that prospective estimates have no certainty of discovery or commercial viability. We are encouraged by these results which provide useful insight into the field; however the true tell of the potential commerciality will be in the stimulation program.

Set for a stimulating second half...

ICN along with partners Beach Energy (Operator) and Chevron will conduct a four well stimulation campaign at ATP 855. Expected to begin in Q1 FY15, the program will test various target zones within the Hervey-1, Geoffrey-1, Redland-1 and ETTY-1 wells. The priority will be optimising recoveries by determining the most productive zones within each well. The release of initial flow rates after each well has been stimulated could be a significant catalyst for the stock price. We estimate the cost net to ICN will be A\$10m (paying 35.1%). The success or failure of this program will then lead into a decision by Chevron to proceed to Phase 2 of the farm-in. This will involve a payment of A\$36m to BPT for an additional 18%.

Valuation and recommendation

A very simplistic valuation of ICN involves the look through value of ATP 855 based on the recent farm-in agreements. Beach Energy paid ICN US\$18m for a 4.9% stake in the block in June 2013. Based on this transaction ICN remaining 35.1% interest in the block has a look through value of A\$135m or 23c/share.

The current takeover battle for Ambassador Oil and Gas (AQO) provides a read through the value of ICN's stake in ATP 855. The current takeover offer implies A\$5.5m/Tcf which values ICN's 35.1% interest in ATP 855 at A\$52m or 8.4cps. This is a base case valuation given that ATP 855 is significantly more de-risked than PEL 570 (Albeit in the gas prone part of the Cooper Basin). Alternatively, if we assign a 25% probability of success to 3.5Tcf (Gross) at 50c/GJ, we arrive at a value of 26cps. We maintain our Speculative Buy on the stock with a target price of 23cps.

23 Jun 2014

Share Price:	\$0.135
Price Target:	\$0.230

Brief Business Description:

Exploration, appraisal and development of oil and gas properties both conventional and non-conventional.

Investment Summary:

ICN offers investors exposure to the developing Cooper Basin unconventional exploration story.

Chairman & CEO:

Mr. Stephen Barry (Chairman)
 Mr. Raymond James (Managing Director)

Top Shareholders:

HK Prosperous Technology Limited	13.0%
Citigroup Nominees Pty Limited	8.6%

Company Address:

4 Miami Key
 Broadbeach Waters, QLD, 4101

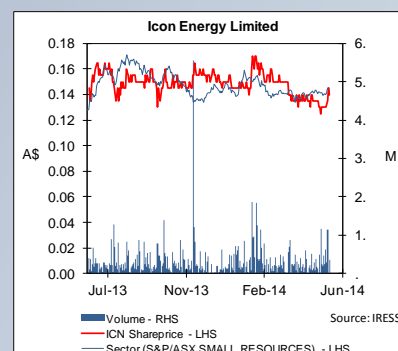
Issued Capital:	615.8m
- fully diluted	620.8m

Market Cap:	\$83.1m
- fully diluted	\$83.8m

Cash (Mar 14):	\$27.6m
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Debt (Mar 14):	\$0.0m
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Source: Hartleys Research


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SUMMARY MODEL

Icon Energy Limited ICN		Share Price \$0.140	Jun-14 Speculative Buy			
Key Market Information			Directors			
Share Price		\$0.140	Mr. Stephen Barry	Non Executive Chairman		
Market Capitalisation		\$86m	Mr. Raymond James	Managing Director		
Cash		\$27.6m	Dr. Kevin Jih	Chief Financial Officer		
Debt		0.0m	Mr. Derek Murphy	Non Executive Director		
Issued Capital		615.8m	Dr. Keith Hillless AM	Non Executive Director		
Unvested 2012-13 LTI Performance Rights		2.7m	Mr. Howard Lu	Non Executive Director		
Issued Capital (fully diluted performance rights)		618.5m				
Issued Capital (fully diluted all options)		620.8m				
EV		\$58.6m				
Valuation		\$0.23				
Projects			Substantial Shareholders			
Projects	Interest	Major Partners	Net acres	m shs	%	
ATP-855	35.1%	Beach Energy	145,314	HK Prosperous Technology Limited	80	13.0%
ATP-549	33.3%	Drillsearch	303,168	Citigroup Nominees Pty Limited	53	8.6%
ATP-560	50.0%	Lake Oil	37,956	Ray James	22	3.6%
ATP-626	100.0%		549,562	Howard Lu	16	2.6%
ATP794	16.0%	Victoria Petroleum	210,138	Taiwan Fructose Co Limited	9	1.5%
PEL218*	33.3%	Beach Energy	131,941			
PEP170	100.0%		198,672			
*Post-Permian Section Only			Investment Summary			
			Icon Energy's activities include the exploration, appraisal and development of oil and gas properties focused primarily on the Cooper Basin. Over the next 12 months the work program on the ATP-855 block will dominate new s flow for ICN.			
			Quarterly Cash Burn (A\$k)			
			Corporate Overheads	Capex	Other	Total Cash Burn
Sep-12			-1,288	-734	65	-1,957
Dec-12			-2,315	-1,703	17,605	13,587
Mar-13			-1,312	-113	2,806	1,381
Jun-13			-923	-4,651	19,005	13,431
Sep-13			-1,064	-6,731	546	-7,249
Dec-13			-2,045	-4,044	15,756	9,667
Mar-14			-1,847	-424	-5,755	-8,026
Forecast						
Jun-14			-1,400	-7,500	0	-8,900
Analyst: Simon Andrew Phone: 618 9286 3020			Last Updated: 23/06/2014			
Sources: IRESS, Company Information, Hartleys Research						

VALUATION

The look through value of recent farm outs values ICN's 35.1% stake in the ATP-855 at 23c/share

ICN is fully funded for the CY14 exploration program on the ATP-855

We have assumed total field capex in CY2014 of A\$60m. This would equate to a capex budget for ICN of A\$21m for CY14.

As a rule of thumb, around half of the capital costs of an LNG project are revenues available to suppliers with local operations. The other half is likely to be sourced internationally

VALUATION

The simplest way to value ICN is the look through value of the ATP-855 given the two recent farm-in agreements. In June Beach paid ICN US\$18m for a 4.9% stake in the block. This values ICN's 35.1% stake at US\$128m (A\$122m) or 23c/share. The Beach farm-down to Chevron values ICN's stake at 24c/share.

An assessment of the in ground hydrocarbon value is a far more difficult proposition. Given the JV is still in the early stage of assessing a 6 well drill program any resource estimates will need to be aggressively discounted.

The current takeover battle for Ambassador Oil and Gas (AQO) provides a read through the value of ICN's stake in ATP 855. The current takeover offer implies A\$5.5m/Tcf which values ICN's 35.1% interest in ATP 855 at A\$52m or 8.4cps. This is a base case valuation given that ATP 855 is significantly more de-risked than PEL 570. Alternatively, if we assign a 25% probability of success to 3.5Tcf (Gross) at 50c/GJ, we arrive at a value of 26cps. We maintain our Speculative Buy on the stock with a target price of 23cps.

INVESTMENT CONCLUSION

ICN offers investors exposure to the developing Cooper Basin unconventional exploration story. The company has managed to farm-down to two strong partners in Beach Energy (Operator) and Chevron. As with any exploration story there is significant uncertainty until the flow testing is complete and an assessment of commercial viability is complete.

RISKS

The risks to our investment thesis are both specific to ICN but also to the macro in nature.

By definition exploration is risky. Even within known gas bearing zones commercial flow rates may not be achieved because of poor reservoir quality governed by localised geology.

The cost of drilling and limited infrastructure mean the hurdle to achieve a commercial gas project is much higher in Australia than in other parts of the world. This means gas producers are at risk even from a modest fall in the domestic gas price.

The unconventional assets do not have a long term production history; as such decline curves and long term production rates are not as well understood as conventional wells. The general nature of unconventional wells in the US is an aggressive production decline curve. This results in operators having to maintain an aggressive drill program in order to replenish lost production.

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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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