



**Breakaway
Research**

March 2012

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Company Information

ASX Code	TEX
Share Price	A\$0.11
Shares + con notes	327.5
Options	101.0m
Market Cap	A\$37.6m
Cash	A\$1.1m
Debt	A\$ 0
Enterprise Value	A\$36.5m

Directors

Chairman	Chris Rowe
Managing Director	Laurence Roe
Director	Graham Riley
Director	Stephen Mann
Chairman (TELA USA)	Ralph Kehle
Director (TELA USA)	Mike Martin

Substantial Shareholders

Investmet Ltd	16.1%
Graham Riley	3.7%
Chris Rowe	3.0%
Laurence Roe	2.2%
Stephen Mann	1.5%

Company Details

Address	6 Richardson St, Suite 5 West Perth, 6005, WA
Phone	+618 9476 9000
Web	www.targetenergy.com.au

1 Year Price Chart



Source: Bloomberg

Target Energy (TEX)

Increasing activity in the prolific Permian Basin

Recommendation: Speculative Buy

Key Points

- **Highly prospective licences in Texas and Louisiana, USA**
- **Established oil and gas production from three fields with additional nearby exploration potential**
- **Recent entry into prolific Permian Basin, West Texas**
- **Successful 'fracking' of first unconventional well at Fairway project**
- **A further 70 'Wolfberry' wells possible within Fairway licences**
- **At least 3 additional wells planned for 2012**

Target Energy is an oil and gas exploration company with modest production already established. A recent move to exploit the oil and gas rich shales within the Permian Basin has the potential to deliver significant resources and drive future cash flow.

Company Overview

Target Energy (ASX: TEX) is a junior petroleum exploration and production company with principle projects located in West Texas and Louisiana, USA. Current production is sourced from three onshore fields and production from a fourth field is likely in the coming weeks.

The Fairway project, located in the prolific Permian Basin, West Texas, has recently become a cornerstone project for the company. Although not yet producing, the project has the potential to yield significant hydrocarbons and become a 'company making' asset. Target Energy has a 60% interest in the Fairway project and aims to exploit the oil and gas rich 'Wolfberry' and deeper Fusselman carbonates via 'fracking' the various producing zones and co-mingling production.

Target Energy and its partners have drilled and completed the first Fairway well and have encountered hydrocarbons in all of its primary and secondary target reservoirs. The well is currently being de-watered before production and flow rates can be established.

Significant exploration upside also exists with a further 70 well locations (at 40 acre spacing) still technically possible within the Fairway project area. Target Energy is due to drill the next 'Wolfberry' well in April 2012 and a possible shallow well soon after, testing the shallow prospective zones identified in the first well. A further two Wolfberry wells are planned for Q3, 2012.

Additional exploration opportunities exist through possible up dip and down dip extensions to the already producing East Chalkley field, and a 10.3% interest in the Shepard's Channel prospect.



Investment Review

Annualised production of 102,565mmcf gas and 19,700bbls oil

Target Energy's oil and gas production is currently sourced from seven wells located in West Texas and Louisiana. On a current annualised basis, Target Energy's share of total production equates to 102,565mcf of gas and ~19,700bbls of oil per year. Assuming an approximate gas price of US\$2.50/mmbtu and US\$100/bbl oil, current production equates to ~US\$1.6m p.a.

5 upcoming wells planned for drilling and appraisal

A number of production increasing opportunities exist during 2012 with five wells targeted for drilling or appraisal work. Target Energy's first 'Fairway Project' well, located in Howard County, West Texas, was drilled and completed in late 2011. The well (BOA 12 #1) was targeting the highly prospective 'Wolfberry' section and the deeper Fusselman formation. The pre-drill recoverable volumes from the well were estimated at 180,000boe (barrels of oil equivalent) at an expected initial flow rate of 100-200bopd (barrels of oil per day). The well was recently fracture stimulated and the operators are now recovering 'frac' water from the well before representative flow rates and production can be established. Further opportunity exists in the deeper Fusselman formation where wireline logs interpreted a prospective 5m oil pay zone. Testing of the Fusselman flowed both oil and water. Production from this zone will be later tied in with the Wolfberry producing zones.

Highly prospective 'Wolfberry' play

Fusselman provides bonus upside

Target Energy anticipates drilling a further four wells in 2012 within the highly prospective Fairway Project area, with the first due to spud in April. The company is also assessing the potential drilling of a well to test the shallow prospective zones identified by the first well. A further two Wolfberry wells are planned for Q3, 2012.

Shepard's Channel encountered immediate gas show

In Louisiana, Target is earning a 10.3% interest in the Shepard's Channel prospect. Shepard's Channel was drilled by previous operators who (it is believed) overlooked a prospective hydrocarbon producing zone. Target Energy and its partners have re-entered the borehole and drilled down to a depth 3,923m where the drill pipe became stuck (95m from TD). The JV partners are currently working to free the drill pipe via the use of a larger drill rig. Although the drill pipe is currently stuck, **Breakaway is encouraged by the 'immediate gas show'** which was observed from the target zone. Once the drill pipe is free, analysis of the potential flow rates can be completed.

Up dip extension from producing field

The fifth well planned for 2012 is in the East Chalkley oil field, South West Louisiana. Target Energy has already had success from the oil field with the Pine Pasture #2 well, producing at 60bopd. Target Energy is testing a possible up dip extension to the oil field. This appraisal well has been earmarked for late 2012.

New technology causing a resurgence of activity

Breakaways view

The Wolfberry intersection is a highly prospective hydrocarbon bearing zone, however due to low porosity levels, previous operators have struggled to recover economic volumes of oil and gas. Advancements in drilling technology and 'fracking' have allowed this resource 'play' to become economically attractive paving the way for a resurgence of activity in the region. Indeed, one of the larger companies operating in the area, Pioneer Natural Resources, has plans to drill ~1,000 Wolfberry wells in 2012 alone.

BOA 12 #1 is a significant well for Target Energy as it is the first to target the Wolfberry (and deeper Fusselman) sections. Proof of viable flow rates would likely lead to many more Wolfberry wells being drilled at the Fairway project and ultimately lead to significant oil and gas production upgrades and a re-rating of the company valuation.



Target Energy - Project Summary

Project	Location	Interest	Well name	Comments
Exploration drilling				
Shepard's Channel	Lafourche Parish, Louisiana	10.33%		Large Gas and condensate potential - Previously drilled in the 1980's however absence of testing overlooked potential. Potential recoverable volumes of 200 Bcf / 12 mmBo (mmBo -million barrels of oil)
Buffalo Project	Jim Wells County, Texas	100%	Weldon #1	Drilled and 'fraced' mid 2011. Stabilised flow rates of 35 mcfgd and 2bopd. 240bwpd. Deemed uneconomic - well shut in
Fairway Project	Howard County, Texas	60%	BOA 12 #1	Targeting the Wolfberry section and the deeper Fusselman Formation. Multiple potential productive zones identified by log data. Frac complete and flow testing underway. Estimated recoverable volumes of 180,000boe at 100-200 bopd. Confirmation of 5m oil pay zone in deeper Fusselman Formation. Shallow San Andres formation may warrant additional shallow well. Potential for 70-140 further wells on Fairway acreage
Fairway Project	Howard/Glasscock County, Texas	60%	Fairway #2	Potential recoverable volumes of 180 - 220 mBo (mBo - thousand barrels of oil)
Fairway Project	Howard/Glasscock County, Texas	60%	Fairway #3, #4	Potential recoverable volumes of 180 - 220 mBo
Appraisal and Development				
East Chalkley	Cameron Parish, Louisiana	35%	Pine Pasture #3	Proposed up dip (from #1 and #2) development well
Production				
East Chalkley	Cameron Parish, Louisiana	35%	Pine Pasture #1	Shut in due to mechanical issues with salt water disposal well. Was producing 12-15 BOPD with 145 BWPD
East Chalkley	Cameron Parish, Louisiana	35%	Pine Pasture #2	Current production of ~60 BOPD plus 473 BWPD
Merta #1	Wharton County, Texas	25%	Merta #1	Fraced in Oct 2010 - Producing at ~ 0.3MMCFGD with 4 BOPD - Initial reserves estimated at 700 mmcrg (unaudited)
Snapper	St Martin Parish, Louisiana	25%	SML # A-1	Producing at ~0.25 MMCFG with associated condensate. Remaining proved and probable reserves are ~1.14BCF plus 55,000bbls oil
Snapper	St Martin Parish, Louisiana	25%	SML # A-2	Producing ~15 BOPD plus 50 mcfgd. Remaining proved and probable reserves are estimated at 0.03BCF plus 9,000bbls of oil
Snapper	St Martin Parish, Louisiana	25%	SML # A-3	Well recently re-completed. Producing at 100 BOPD with 400 mcfgd. No reserve estimate yet completed

Target Energy - Project Locations (Texas and Louisiana)



Source: Target Energy/Google



Project Review

Target Energy's projects are all located in Texas and Louisiana, USA. Both states have a rich heritage in oil and gas production with well-developed infrastructure and industry 'know-how'.

The company has modest production sourced from seven onshore wells, four of which are located in Louisiana and three in Texas. The table below summarises the average daily production (during the Dec11 quarter) for both oil and gas.

Oil and Gas production summary

Well	TEX Interest	Average daily gas production (mcf/d)	Average daily oil production (bopd)
Snapper #A-1	25%	179	0
Snapper #A-2	25%	69	12.5
Snapper #A-3	25%	512	105.2
Pine Pasture #1	35%	0	0
Pine Pasture #2	35%	43	44
Merta #1	25%	254	3.7
*BOA 12 #1	60%	20	13.1
Total		1,077	179
Total net to TEX		281	54

Total production net to TEX is 281Mcf/d gas and 54bopd oil

Source: Target Energy

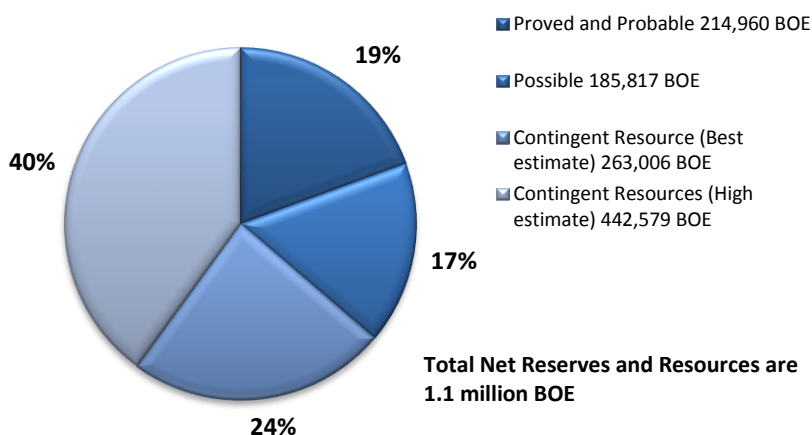
*BOA 12 #1 still on test. Flow rates are conservatively estimated as ~10,000 bbls of water still need to be recovered before flow rates can be observed

Assuming steady state flow rates as indicated in the table above (i.e. no natural decline in production), and assuming no new wells come on stream, current annual production equates to 102,565mcf of gas and ~ 19,700bbls of oil per year.

Reserves and Resources

Target Energy's total net reserves and resources as at the 30/06/11 are ~1.1m BOE (Barrels of Oil Equivalent)

Targets total reserves and resources are 1.1m BOE



Total Net Reserves and Resources are 1.1 million BOE

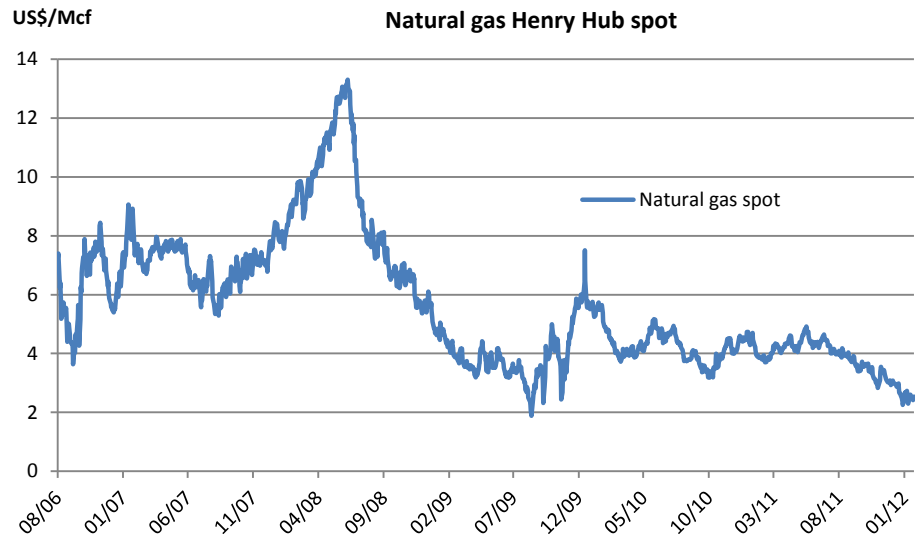
Source: Target Energy

East Chalkley: Audited by Risc Pty
SML 1,2,3: Audited by Mike Harper and ass.
Merta #1: Target Energy internal estimate



Current gas prices are currently ~US\$2.50/Btu, significantly below from the highs witnessed in 2008. Incremental increases in the gas price from these low levels would have a relatively marginal bearing on company cashflow as in excess 90% of revenue is generated from oil sales.

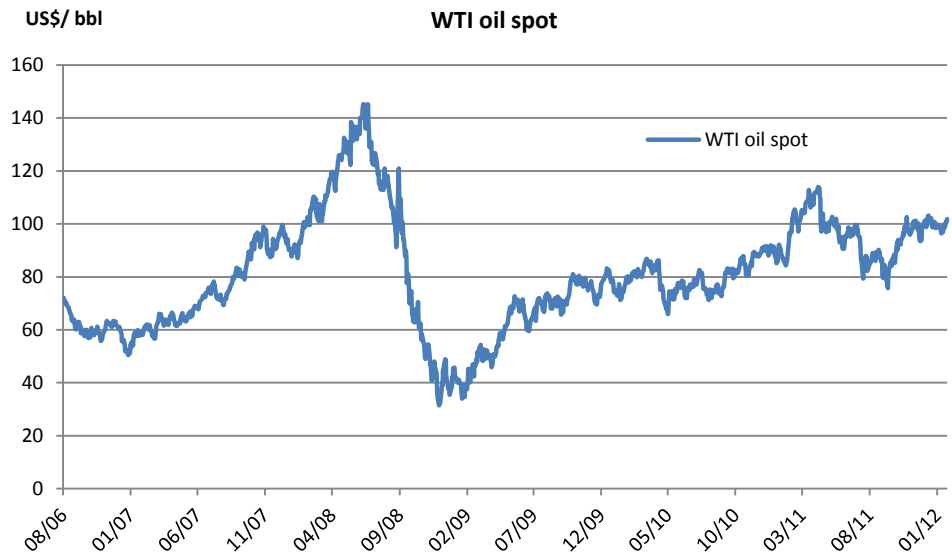
Gas price currently
~US\$ 2.50/Mcf



Source: Bloomberg

Oil prices have been trading above US\$100/bbl in recent times. Current production net to Target is ~19,700bbls per annum and forms the bulk of production revenue. At US\$100/bbl, expected revenue is ~US\$1.9m.

Oil price currently
~US\$100/bbl



Source: Bloomberg

Total net revenue from both gas and oil projects is around US\$ 2mpa however Target Energy hold a number of opportunities to increase production in both oil and gas through currently underway and upcoming drill campaigns.



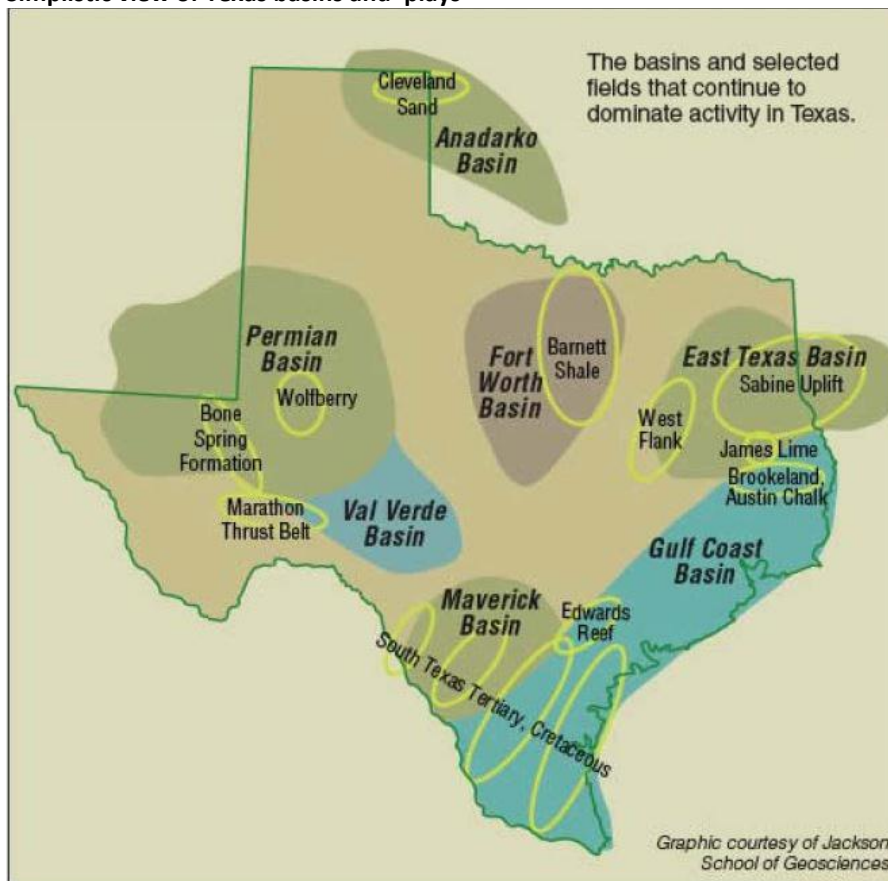
Exploration Potential

Geological Setting

Permian basin is prolific for oil and gas production

The Permian basin is principally located in western Texas and is the second largest producing oil and gas region in the US. The basin hosts multiple producing formations, however the two formations of particular interest are the Spraberry and Wolfcamp trends.

Simplistic view of Texas basins and 'plays'



Source: Blacksands Petroleum

New technology allows production from multiple target zones

The term "Wolfberry" is used to characterise the completion method of perforating, fracture stimulating and comingling for production the various Spraberry and Wolfcamp intervals and, more recently, the deeper Mississippian intervals.

Within the Permian basin, the Spraberry trend hosts the largest oil and gas reserves and is ranked third in the US by total proved reserves and seventh in total production.

The Wolfcamp, lies stratigraphically below the Spraberry, is also a major producer within the Permian Basin. The Wolfcamp trend is however, also well known for its low permeability. Advancements in completion methods have made it possible to combine production from the Spraberry and Wolfcamp zones in areas that were previously uneconomic on a standalone basis, achieving robust economic results. Drilling depths of typical 'Wolfberry' wells are between 7,000ft and 10,500ft and would include 8-12 fracture stimulations beginning at the bottommost formation.



Current Exploration Drill Schedule

2 wells awaiting appraisal

3 further wells planned in 2012

Estimated Timing	Prospect	Location	TEX working interest	Potential recoverable volumes
Currently flow testing	BOA 12 #1 Frac	Howard County, Texas	60%	180-220 mBo
Currently drilling	Shepard's Channel	Lafourche Parish, Louisiana	10.30%	200Bcf /12mmBo
Q2 2012	Fairway #2	Howard/Glasscock County, Texas	60%	180-220 mBo
Q3 2012	Fairway #3, #4	Howard/Glasscock County, Texas	60%	180-220 mBo
2012	East Chalkley PP#3	Cameron Parish, Louisiana	35%	250 - 450 mBo

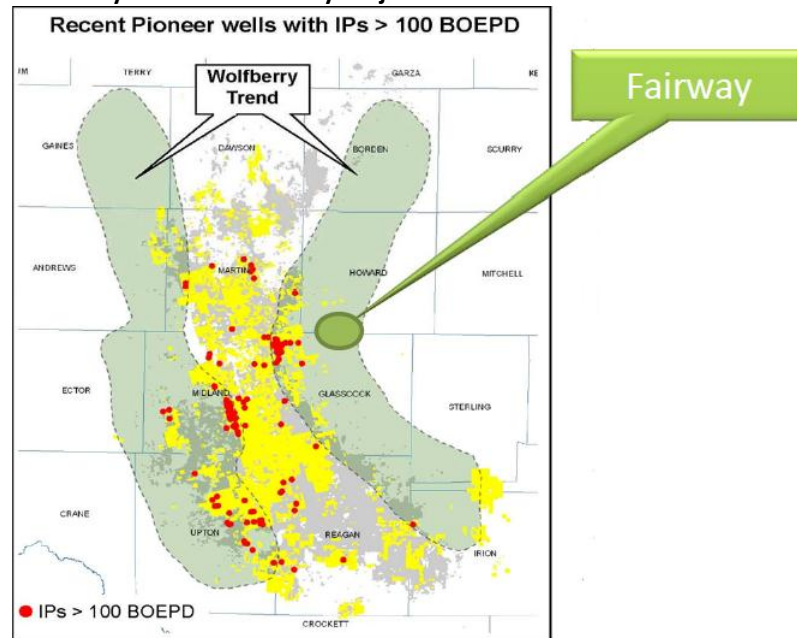
Source: Target Energy mmBo-Million barrels of oil. Mbo-Thousand barrels of oil

The Fairway Project – Target Energy 60%, Trilogly Operating 30%, Avalon Oil 10%

The 'Wolfberry' trend hosts several hundred drillable locations and has Expectant Ultimate Recoveries (EUR's) of ~120- 150mmboe

Highly prospective licences

Wolfberry Trend and Fairway Project Location



Source: Pioneer Natural Resources and Target Energy

Target Energy is earning a 60% interest in the 2,873 acre 'Fairway Project' which straddles the Howard and the Glasscock county border. The Howard/Glasscock field was first discovered in 1925 and since then, has produced over 410M barrels of oil.

Operators recovering 'frac' water before flow testing

Target Energy's first 'Fairway' well (BOA 12 #1) was drilled and reached target depth (~10,000ft) in October 2011. The well encountered a 1,080m interval in the 'Wolfberry' section which exhibited numerous oil shows. Wireline logging confirmed the well encountered oil and gas pay zones and the well was completed for production. The operators of the well are currently recovering 'frac' water, a necessary process before representative oil flow rates can be established.

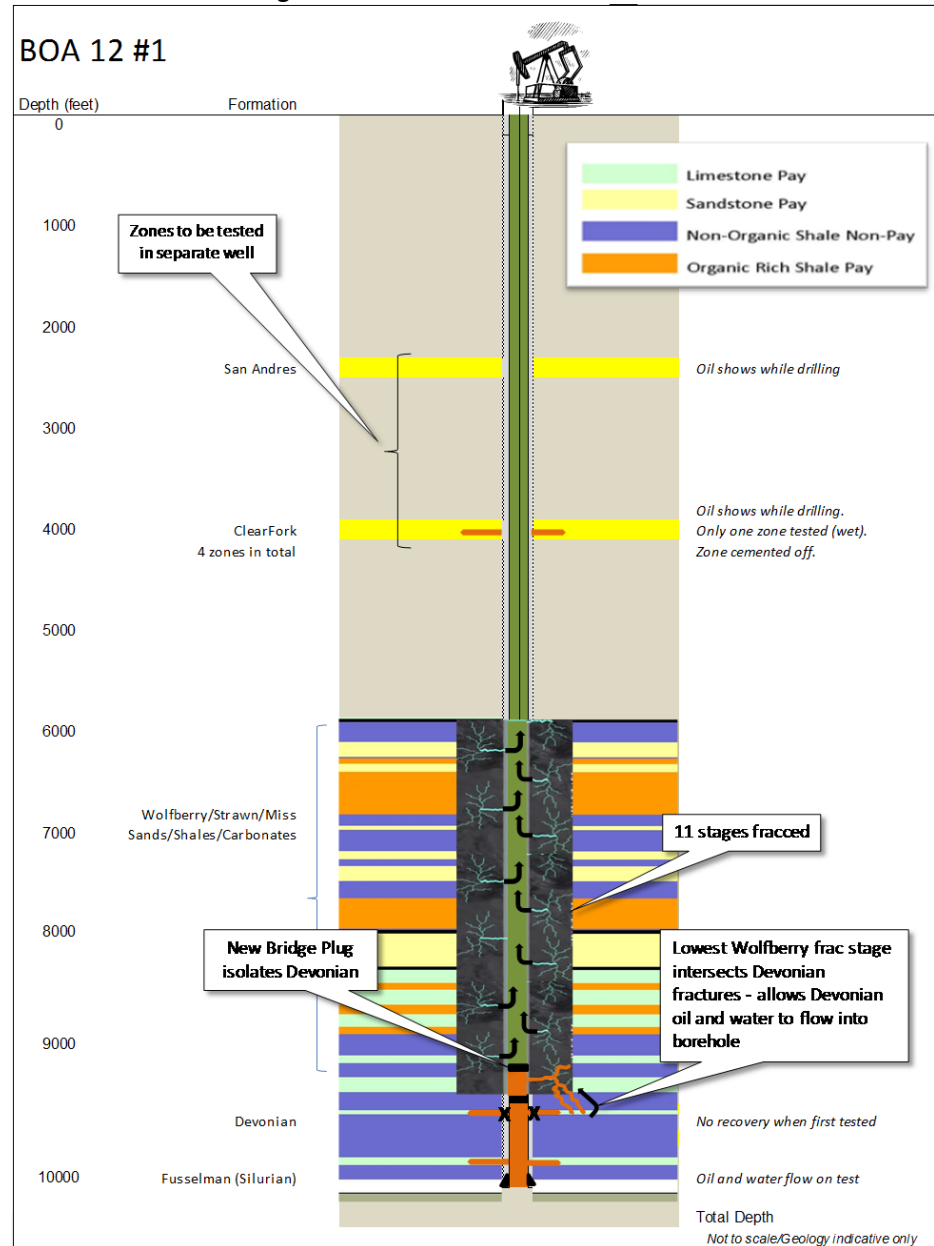
Bonus production from Devonian likely

Analysis of fluid recovered from the well suggests it may have encountered an unexpected additional oil producing zone from the deeper Devonian section (see image on next page). Should this be confirmed, and subject to the drilling of a water disposal well, this new Devonian hydrocarbon zone can be later comingled with 'Wolfberry' production.



Additional opportunity lies with a possible second well which will 'twin' BOA 12#1 to independently test the potentially productive Clear Fork and San Andres sections.

BOA 12#1 schematic diagram



Operators may 'twin' current well with a second shallow well to target San Andres and Clear Fork

BOA 12#1 proves concept

3 further wells planned

Source: Target Energy

Three further wells are now planned within the Fairway project area, targeting the same 'Wolfberry' intervals. The first well, Fairway #2, is planned to spud in April 2012 with the following two wells, Fairway #3 and #4 expected to spud in Q3 2012.

Breakaways View

Up to 64 further wells could technically be drilled

The calibre of the Permian Basin as a proven oil producing region is not to be underestimated. BOA 12 #1 is a significant well for the company as it confirms the Wolfberry strategy and highlights the prospectivity of the region. The Fairway project is 2,873 acres with up to 70 wells possible well locations (at 40 acre intervals) with well potential recoveries upto ~180,000bbls. There is scope to double the number of wells within the Fairway project should the Texas regulator agree to change the minimum spacing from 40 to 20 acres. This would significantly increase the exploration potential and the overall value of the project.



Shepards Channel Prospect:

Lafourche Parish, Louisiana – 10.3% Working Interest

Target is earning a 10.3% working interest in the Shepard’s Channel Prospect by paying its share of acreage costs and the cost of re-entering an existing cased borehole.

Previous operators overlooked a prospective zone

The operators who originally drilled the well, drilled through a particular channel sand zone that (at the time) was not thought to be prospective for hydrocarbons. Detailed analysis of historical wire line log data suggests the potential of this channel sand ‘zone’ was overlooked due to suppressed data and that it could in fact hold up to 200 Bcf of recoverable gas and 12 million barrels of oil.

Drill pipe currently stuck

Work commenced on re-entering the borehole on the 10th December 2011 and it has been re-drilled down to a depth of 3,923m into the target channel sand zone. The operators immediately encountered gas shows however the drill pipe has become stuck 95m from total depth.

Immediate gas shows encountered

Breakaway views the presence of ‘immediate gas shows’ from the target zone as encouraging. Once the drill pipe has been freed, more comprehensive test of possible gas flow can commence. The partnership has also identified an 8m thick channel sand at 4,005m, below the main area of interest, which may augment hydrocarbons from the targeted zone.

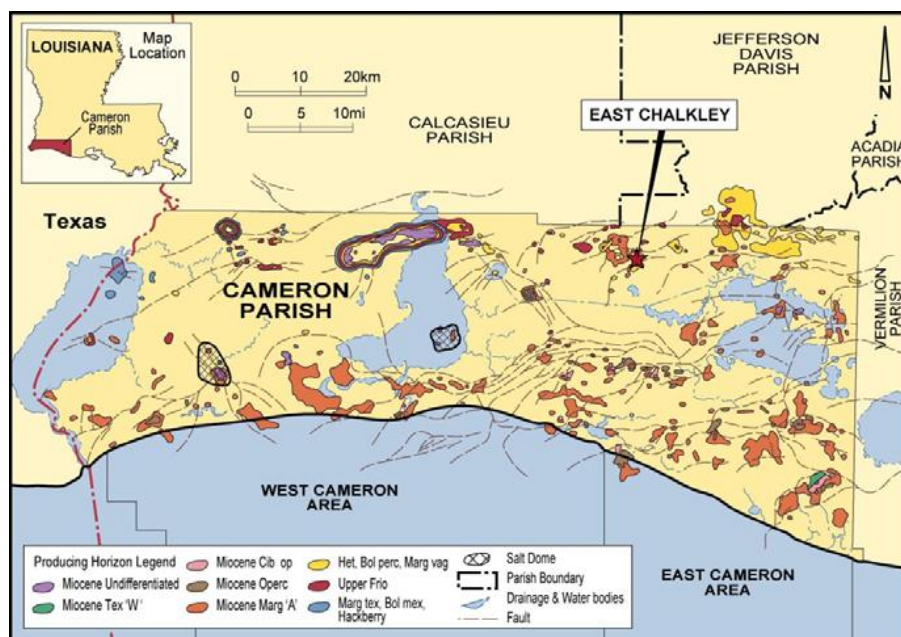
East Chalkley

Cameron Parish, Louisiana – 35% Working Interest

The East Chalkley project is an oil field and development program located 33km south east of the town of Lake Charles.

Up dip development well planned for already producing field

Target Energy and its joint venture partners already had success in the project area from the Pine Pasture #2 well (drilled in 2008) which is currently producing ~60bopd. The drilling of the proposed Pine Pasture #3 development well has been slated for the later part of 2012 although a definitive timetable is not yet in place.



Source: Target Energy



Directors

Chairman

Chris Rowe is a graduate of Cambridge University in Law and Economics. From 1979 to 1990, Chris was executive director of Cultus Petroleum where he participated in a number of commercial discoveries in Australia, New Zealand and the USA. Subsequently, Chris was Chairman of UTS Energy and International Oiltex, both of which are TSX listed. Chris is currently the Chairman of ASX listed Northern Star Resources and Hawkesbridge Private Equity fund.

Managing Director

Laurence Roe is a petroleum professional with over 30 years' experience gained in the industry both in Australian and internationally. He commenced his career with Santos Limited, subsequently taking a senior technical position with Magellan Petroleum Australia Limited, where he was later appointed Exploration Manager. While with Magellan, he had substantial involvement with US and other international projects. Mr Roe co-founded Target Energy in 2006.

Director

Graham Riley is a qualified legal practitioner and has been involved in the growth of a number of petroleum and mining companies. He is currently Chairman oil and gas exploration companies Buru Energy (ASX:BRU) and Entek Energy (ASX ETE). Mr Riley is also Chairman of Gaycoyne Resources (ASX: GCY) a diversified mineral exploration company. Mr Riley was formally a founding director if ARC Energy and a non-executive director of Adelphi Energy.

Director

Stephen Mann is a chartered accountant with over 30 years' of experience. Since 2003 he has acted as the chief financial officer and more recently as a consultant to the Nacap Asia Pacific Group which is a large Dutch group that specialises in oil and gas pipeline construction. He is also a Director of Investmet Limited (a significant shareholder in Target Energy), a non-executive Director of the ASX-listed company Pegasus Metals Ltd and a non-executive Director of Altus Renewables Ltd, an unlisted public company

TELA (USA)
(100% owed by
Target Energy)

Director

Prof Ralph Kehle has over 48 years' experience in the oil and gas sector and has to his credit the discovery and development of a +300Bcf extension to the Coleman North Gas Field in Alaberta, Canada, the discovery of the 200+ Bcf Guerra Field and the 15 million barrel Stockyard Oil Field, both in Texas. During his career he has served as CEO and Chairman of Hershey Oil Corp, Senior Vice President, Exploration of American Exploration Company (both publicly listed), and founded TKA Exploration and of OilTex International Ltd - now Enerplus, listed on the Toronto Exchange.

Director

Michael Martin is a practising geologist and has been actively involved with international resources industries for more than 30 years. Mr. Martin began his professional career in Kuwait and later the western Mediterranean offshore oil fields of Spain, prior to joining the North Sea oil boom in the early seventies. Following assignments in London with Atlantic Richfield and Cities Service, he joined Getty Oil in their Perth office. After his departure from Getty, Mr. Martin worked with the petroleum division of a major Australian Mining House.



Analyst Verification

We, Grant Craighead, Gavin Wendt and Andrew McLeod, as the Research Analysts, hereby certify that the views expressed in this research accurately reflect our personal views about the subject securities or issuers and no part of analyst compensation is directly or indirectly related to the inclusion of specific recommendations or views in this research.

Disclosure

Breakaway Investment Group (AFSL 290093) may receive corporate advisory fees, consultancy fees and commissions on sale and purchase of the shares of Target Energy and may hold direct and indirect shares in the company. It has also received a commission on the preparation of this research note.

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