Burleson Energy (BUR)

Horizontal well set to significantly expand existing production and reserves

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Grant Craighead | Research Manager
gcraighead@breakawayinvestmentgroup.com

Andrew McLeod | Research Analyst
amcleod@breakawayinvestmentgroup.com

Company Information

ASX Code	BUR
Share Price	A$0.034
Ord Shares	420.8m
listed options (BUROA)	138.8m
Market Cap	**A$14.3m**
Cash (Aug 12)	A$3.0m
Total Debt	A$0m
Enterprise Value	**A$11.3m**

Directors

Chairman	Norman Zillman
Managing Director	Michael Sandy
Executive Director	Alex Sundich
Non-Executive Director	Andrew Kugler
Non-Executive Director	Khib Kugler

Directors hold ~12.5% of issued capital

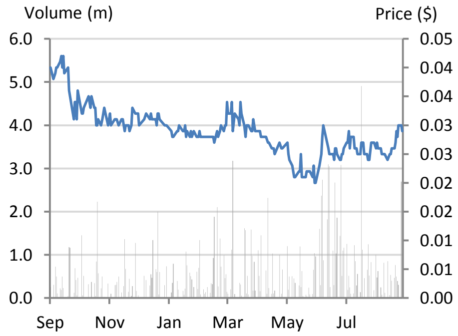
Substantial Shareholders

Norman Zillman	4.6%
UBS Nominees	1.9%
Pine Street	1.9%
Allan Christie	1.7%
Harrison Jedel	1.6%

Company Details

Address	Level 6, 9 Barrack Street Sydney NSW 2000
Phone	+612 8252 6177
Web	www.burlesonenergyltd.com

1 Year Price Chart



Source: Bloomberg

***Recommendation: Speculative* BUY**

Key Points

- ***2P Reserves of 2.9mmboe net to Burleson***
- ***Production from four wells, with a fifth well currently being drilled***
- ***Fully funded horizontal well targeting proven hydrocarbon bearing sandstone***
- ***Significant opportunity to increase production in coming weeks***
- ***Successful horizontal well will pave the way for a 'roll-out' of the strategy with 10-15 additional sites identified***
- ***Breakaway has a 'base case' valuation of 5.5c/share with upside potential of 11.5cents/share***

Burleson Energy has four producing vertical wells and has commenced drilling its first horizontal well in the Heintschel field in South Texas, targeting the proven hydrocarbon bearing Wilcox sandstone. Expectations are this well could produce at several times the rate of the existing wells. Successful implementation of the horizontal well will see this strategy rolled out over 10-15 additional sites within the Heintschel, significantly boosting production.

Company Overview

Burleson Energy (ASX: BUR) is a junior oil and gas company with its principle projects located onshore, in the Gulf Coast region of Texas, USA.

The company has a working interest in ~26,000 acres of exploration licences within the Colorado and Wharton counties in South Texas. The most advanced project in the portfolio is the ~4,400 acre Heintschel oil and gas field which was discovered in April 2010. Following the discovery of the field, Burleson and the joint venture partners completed a further two vertical appraisal wells with all three wells producing from the Wilcox formation. A fourth vertical well, Joann #1, on the neighbouring Joann field, augments total current production of 460,000mcf and 22,000bbls of condensate per annum.

Within the Heintschel field, a fully funded horizontal well is currently in progress aimed at increasing production from the tight Wilcox sandstone. The vertical section has already reached target depth, intersecting a hydrocarbon charged reservoir with 36m of net sands. The horizontal section and six stage 'frac' will be completed in the coming weeks.

The horizontal well, if successful, will significantly increase production from the field, boosting company cash flow and provide a short-term opportunity for a share price re-rating. A roll out of the 'horizontal well strategy' across the 10-15 sites within the Heintschel field provides a longer term pipeline to further increase production, supported by established infrastructure.

Investment Review

4 producing wells

Burleson Energy has a 38% Working Interest (WI) and a ~30% Net Revenue Interest (NRI) in the Heintschel oil and gas field, located onshore in the Gulf Coast region of Texas. The field currently hosts three producing wells with a fourth producing well (Joann #1) on the adjacent Joann field.

Revenue of ~US$1.4m p.a.

On a 100% basis, these four wells produced ~460,000mcf (thousand cubic feet) and ~22,000bbls of condensate in 2012, which generated revenue of ~US$1.4M, net to Burleson.

2P reserves of 2.9mmboe

A reserves audit carried out by Degolyer and MacNaughton (D&M) in late 2011 estimated 2P reserves of 2.5mmbls of hydrocarbon liquids (condensate + Natural Gas Liquids (NGL's)) and 30 Bcf of dry gas attributable to the three producing vertical wells on the Heintschel field. This equates to **2P Reserves of ~2.9mmboe net to Burleson's 38% working interest** and ~2.3mmboe net to BUR's 30% NRI. No assessment was undertaken on the neighbouring Joann field.

For the purpose of estimating the value of the three producing Heintschel wells, Breakaway has split the reserves into the three recovered hydrocarbon components (as per the Degolyer and MacNaughton reserves report) and assigned a nominal 'value per unit'. The 'values per unit' for each of the hydrocarbon groups are in line with industry peer valuations, however, Breakaway views them as conservative given current commodity pricing.

Breakaway values 2P reserves at A$0.055/share

Base Case - Breakaway valuation estimate based on 2P Reserves

Current 2P Reserves (per D&M):	Total Volume	Recovery Factor	BUR Share (30% NRI)	Value per unit	Total Value (US$m)
Oil & Condensate (MMBBls)	0.96	100%	0.29	$25.00	7.2
NGLs (MMBBls)	1.51	100%	0.45	$15.00	6.8
Natural Gas (Bcf)	30.00	100%	9.00	$0.70	6.3
Total Reserves Value					20.3
Current Cash Holding					3.0
Total Value					23.3
Value per Share					**$0.055**

Source: Breakaway Research

No value attributed to producing Joann well or upcoming horizontal well or exploration potential

Based on Breakaway's valuation metrics, the three producing Heintschel wells have a 'base case' nominal valuation of US$23m (A$0.055/share). This is before considering any value for the producing Joann well, the upcoming horizontal well or the company's significant exploration acreage.

Upcoming horizontal well

Vertical section complete

Significant opportunity exists to increase production (and revenue) in the coming months with the drilling of the Truchard #2H horizontal well (BUR: WI 50%, NRI 39.2%). The well is targeting production from the same reservoir formation (the Wilcox) as the existing producing wells.

Possible production by October 2012

The T#2H well spudded on the 8th June and will be completed in three stages:

- Vertical section to 11,500 feet (~3,500m) – Completed
- Horizontal section 2,300 feet (700m) – Due to commence by mid- September
- 6 stage frac program and completion – First production possible by mid October

IPT estimate the T#2H well could produce at several times the rate of existing wells

IPT (consulting petroleum engineers) have estimated the T#2H well could produce ~7Bcf of wet gas ('wet' gas sells at an approximate 50% premium to dry gas; e.g. currently ~US4.50/mcf vs. quoted 'dry' gas price of ~US$ 3.00/mcf) and ~0.2mmbls of condensate (~US$100/bbl). **At current pricing, this equates to total revenue of ~US$ 53m.** The total estimated cost for the T#2H well is ~US $6.3m, which has already been pre-paid and high front end production rates suggest a 6-9 month well 'payback' period.

Roll out of strategy

Success paves the way for a roll-out of the strategy

The significance of the upcoming horizontal well should not be underestimated. Assuming the well is a 'success', being that it performs as modelled by IPT, it paves the way for a roll out of the 'horizontal well strategy' across the rest of the Heintschel field.

10-15 sites identified for horizontal wells

Degolyer and MacNaughton have estimated total 'In-Place' hydrocarbons of 3.6mmbls and 125 Bcf of wet gas within the Heintschel field. Assuming a 60% recovery, Burleson's share of this would be in excess of 6mmboe. The JV partners have identified a further 10-15 possible drill locations which will be assessed following completion of the T#2H well. These wells will likely be financed through cash flow and some level of project debt.

Upside Case – Assumes a 60% recovery of the Heintschel field Resources In Place

Breakaway values Heintschel field at $0.115

Current Resources in Place (per D&M):	Total Volume	Recovery Factor	BUR Share (30% NRI)	Value per unit	Total Value (US$m)
Oil & Condensate (MMBBls)	3.56	60%	0.64	$25.00	16.0
NGLs (MMBBls)	5.64	60%	1.01	$15.00	15.2
Natural Gas (Bcf)	111.00	60%	19.98	$0.70	14.0
Total Reserves Value					45.2
Current Cash Holding					3.0
Total Value					48.2
Value per Share					**$0.115**

Source: Breakaway Research

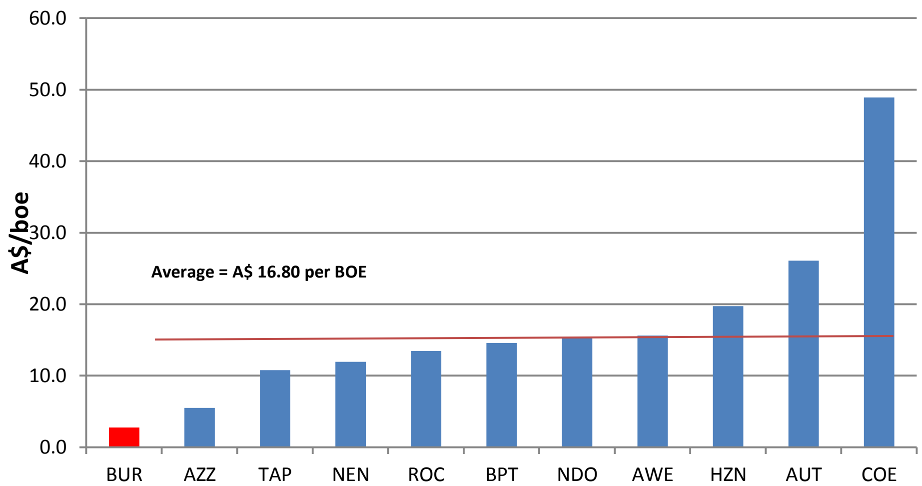
The table above highlights the potential upside case based on the Resources-In-Place as assessed by D&M. Assuming a 60% recovery and applying the same 'value per unit' metrics, Breakaway estimates the potential upside valuation for the Heintschel field at $45m (A$0.115/share). Additional upside exists through earlier stage prospects such as the Peikert prospect which currently attribute zero value to our upside case.

Peer Comparison

BUR appears cheap on a peer comparison

The chart below highlights the enterprise value of ASX listed 'oil and gas' peers relative to the respective 2P BOE Reserves. Based on the 11 companies considered, the average EV/2P BOE is ~A$16.80 while Burleson's EV/2P BOE multiple is significantly below this at A$2.70. Applying the average multiple to BUR's 2.9mmboe of 2P reserves implies an enterprise value of ~A$ 48m or A$0.11/share.

Enterprise Value per 2P Reserves BOE



**Data sourced during Aug 2012* *Source: Breakaway Research*

Breakaway's View

Low risk horizontal well underway

New strategy provides opportunity for increased flow rates

Burleson offers exposure to a relatively low risk oil and gas play with pre-existing production from 2P reserves. The fully funded horizontal well, currently underway, is targeting the Wilcox sandstone, a proven hydrocarbon bearing formation, and as such offers a lower risk opportunity for the company to increase production and reserves. The horizontal six stage 'frac' allows for greater surface area 'exposure' to the producing reservoir, providing the opportunity for increased flow rates and a step change in the company earnings. Assuming the well is a success, the 'horizontal well strategy' will be rolled out across 10-15 new locations within the Heintschel field, providing ample opportunity for a significant increase in revenue and a re-rating of the share price.

Step change in company earnings possible

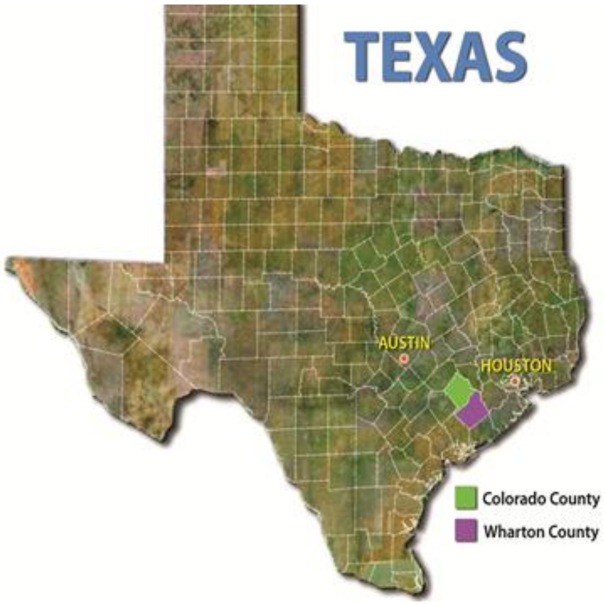
With an enterprise value of ~A$ 9.0m, Burleson already appears significantly undervalued relative to its peers. Production success with the T#2H well is likely to provide the impetus for a meaningful re-rating of the company valuation.

Project Review

Burleson Energy has a working interest in ~26,000 acres (119 square miles) of exploration ground in the Colorado and Wharton Counties, Texas, USA.

Large acreage position in Texas

Colorado County Location



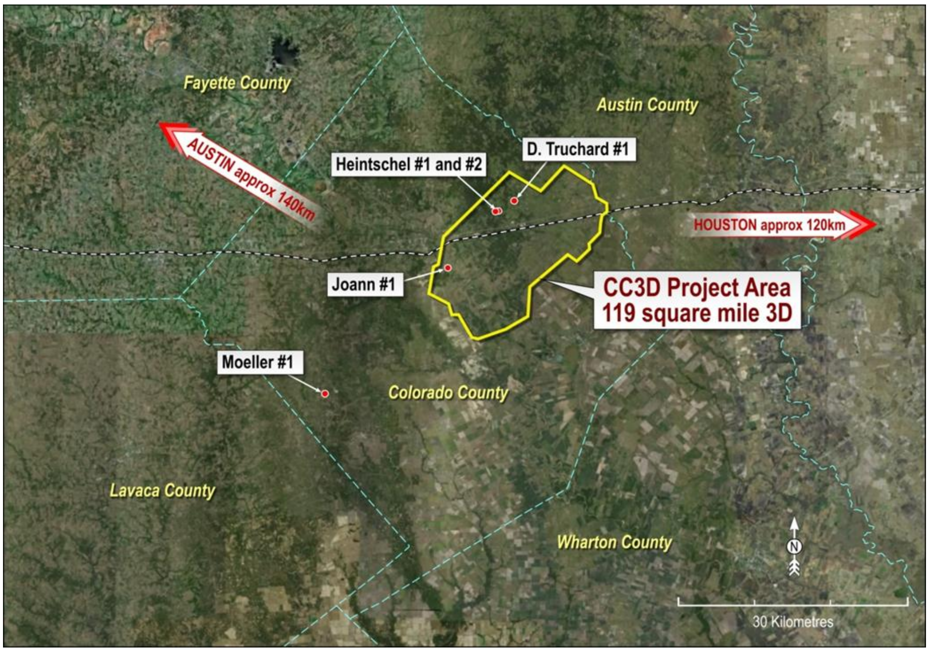
Source: Burleson Energy

3D seismic de-risks exploration targets

Between 2009 and 2010, the company carried out a detailed 3D seismic survey over 119 square miles in Colorado County. A drilling program targeting the tight Wilcox sandstone formation soon followed with the company encountering early success in the Heintschel #1 well. During late 2010 - early 2011, Burleson subsequently drilled another two vertical appraisal wells (Heintschel #2 and D Truchard #1) with all three wells fracture stimulated (fracc'ed) and completed for production. A fourth well (Joann #1) was also drilled on the neighbouring Joann field which did not require fraccing.

Established infrastructure

Burleson Project Area – Colorado County



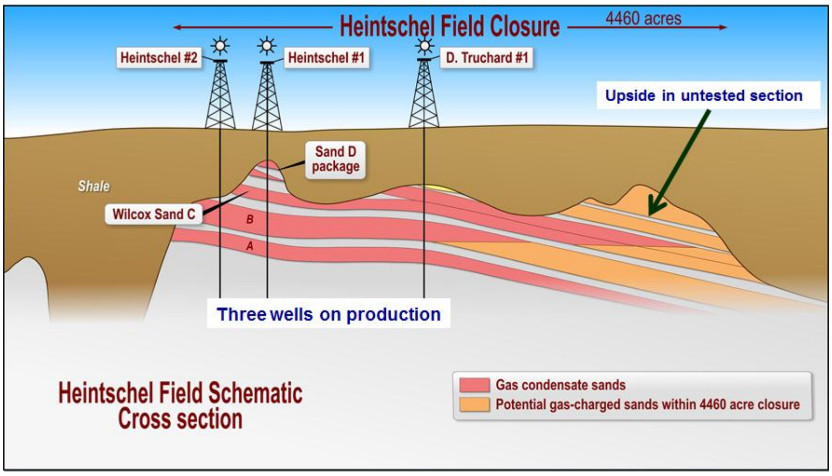
Source: Burleson Energy

Reserves and Production

The cross section diagram below shows the vertical Heintschel #1, #2 and D Truchard #1 wells in the Heintschel field, all of which produce from the tight Wilcox sandstone. The wells were treated with a reduced strength 'frac' to avoid perforating suspected water bearing sands located above the reservoir. Despite this sub-optimum frac; production from the wells has been encouraging indicating a productive reservoir rock.

Wilcox sandstone is a productive reservoir

Heintschel Field Cross Section



Source: Burleson Energy

Reserves audit from just the 3 producing Heintschel wells

In 2011, Degolyer and MacNaughton (D&M) undertook a reserves audit of the three producing wells and estimated **2P reserves** of 2.5mmbls of hydrocarbon liquids (condensate + Natural Gas Liquids (NGL's)) and 30 Bcf of dry gas. This equates to **~2.9mmboe net to Burleson's 38% working interest**.

Heintschel field estimated to hosts >6mmboe net to BUR

D&M has also highlighted significant upside potential for the Heintschel field indicating 'In-Place' hydrocarbons of 3.6mmbbls of condensate and 125Bcf of 'wet' (NGL rich) gas. Assuming a conservative 60% recovery, Burleson's share of this equates to > 6mmboe. Additional upside exists along strike (as indicated be the green arrow in the above diagram) which has not been included in the D&M 'In Place' estimate. JV partners, AKG, have estimated the 'in place' gas to be as high as 160Bcf + liquids.

Well Production Statistics – 100% Basis

		2011		2012	
Well (BUR Working Interest)	First Production	Gas (thousand cubic feet, mcf)	Condensate (barrels)	Gas (thousand cubic feet, mcf)	Condensate (barrels)
Brasher 1					
(WI 38%, NRI 29.7%)	Dec-10	71,566	-	-	-
Heintschel #1					
(WI 38%, NRI 29.6%)	Oct-10	196,068	7,942	83,934	2,165
Heintschel #2					
(WI 38%, NRI 29.6%)	Feb-11	146,718	4,256	143,856	3,394
D Truchard #1					
(WI 38%, NRI 29.7%)	Feb-11	72,354	4,169	99,875	5,160
Truchard #2H			**Currently Drilling**		
(WI 50%, NRI 39.2%)					
Joann #1					
(WI 39.4%, NRI 30.8%)	Apr-11	122,431	5,519	130,680	10,844
Total		**609,137**	**21,886**	**458,345**	**21,563**

Source: Burleson Energy

2012 production from the four producing wells provides total revenue (net to BUR) of ~A$1.2m p.a with the revenue derived from approximately 1/3 liquids, 2/3 gas. Breakaway is confident 2013 revenue will be significantly higher on the back of success with the upcoming horizontal well.

Revenue likely to increase for FY 2013

Horizontal Well Potential

Increased flow rates likely

'Integrated Petroleum Technologies' (IPT) were recently engaged to estimate the possible oil and gas recoveries from a horizontal well completion in the Heintschel field. **Analysis concluded a 'multi-stage frac' approach along the Wilcox sandstone would produce several times the rates and volumes of the vertical wells.** Over a 10 year period, IPT has estimated cumulative production of 7Bcf of liquids-rich gas and ~200,000bbls of condensate is achievable which, at current commodity prices, would deliver ~US$ 53m in revenue and pay back the cost of the well in 6 – 9 months.

Truchard #2H – Horizontal Well (BUR: WI 50%, NRI 39.2%)

Increased NRI in the upcoming T2#H well

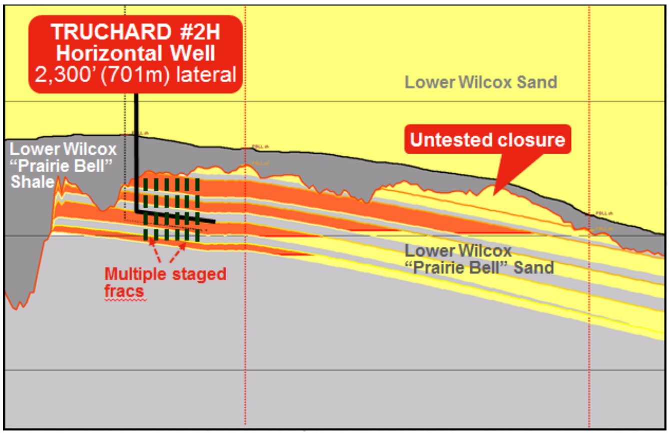
Following a 'non-consent' from some of the JV partners, Burleson increased their working interest in a 664 acre 'excised' unit (incorporating the proposed T#2H well) to 83.5%. Subsequently, farmout transactions were completed of 3.5% to a US private company and to 'Mogal Holdings' which acquired a 30% WI in the 664 acre unit for US$2.76m, reducing BUR's exposure to 50% working interest and 39.2% NRI.

Electronic logging confirms 36m hydrocarbon zone

On the 8th June 2012, the Truchard #2H well was spudded, ~785m from the producing Trunchard #1 well. The vertical component of the well has now been completed reaching a total depth of ~3,500m. **Electric logging has confirmed a 36m zone of hydrocarbon charged sands** highlighting the potential for the T2H well to be a substantial producer of oil and gas. Breakaway is further encouraged by the lower reservoir unit (the Prairie Bell 1 sand) which has been interpreted to be better developed than in Burleson's' previous three wells in the Heintschel field.

6 stage frac increases surface area to productive zone

Scematic of Truchard #2H



Source: Burleson Energy

T#2H well easily tied into existing infrastructure

Following the completion of the vertical section, a drill rig has now been contracted to drill the ~700m horizontal section and began drilling on the 12th September. Following completion of the horizontal section, a 'frac' unit will be used to undertake up to six frac's, significantly increasing the exposure to the productive reservoir. Should the well produce economic flow rates it will be brought into production, facilitated by nearby established infrastructure.

Assuming no unforeseen circumstances, the Truchard #2H could be in production by mid October 2012.

Additional Exploration

Heintschel Exploration Potential

Roll-out of strategy provides strong project pipeline

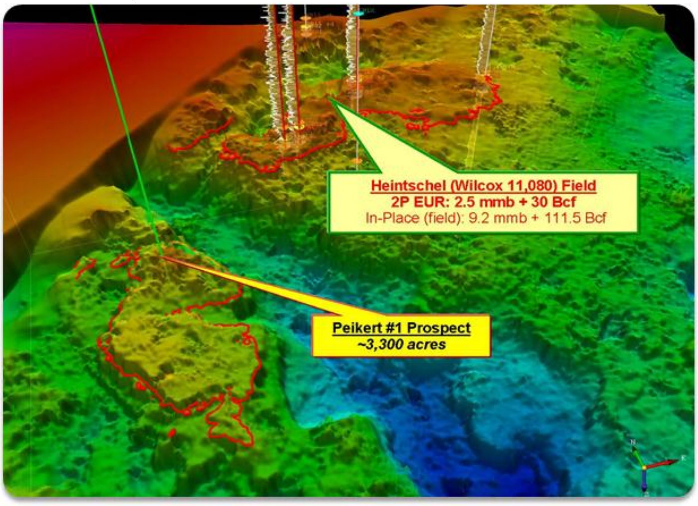
The outcome of the Truchard #2H will be significant for Burleson and the JV partners as it will dictate the strategy employed to develop the rest of the Heintschel field. Burleson has identified 10 – 15 additional sites suitable for horizontal well completions and a confirmation of the 'horizontal well strategy' would largely de-risk future wells targeting the same productive Wilcox formation.

Peikert prospect

Of particular interest to Breakaway is the Peikert prospect which appears to be a Heintschel "look-alike". The prospect is located in the Colorado County 3D seismic area, adjacent to the Heintschel field, and has the potential for up to 57Bcf of gas and 1.6mmbls of condensate.

Peikert is a Heintschel 'look-alike'

Peikert Prospect – 3D Seismic



Obvious candidate for drilling program

Source: Burleson Energy

The Heintschel field, in the background of the above image, shows the three wells on production. The Peikert Prospect is ~3/4 the size of Heintschel and is an obvious candidate for drilling in due course.

Moeller #2

BUR will likely farm out interests in Moeller

Moeller #1 was drilled the south west of the CC3D area in May 2010. Testing indicated gas shows, however the well was deemed uneconomic based on the water produced from the high porosity sand reservoir. Analysis determined that this reservoir would likely flow gas in commercial quantities if found in an up-dip location with higher gas saturations. The Moeller #2 drill location is ~475m up-dip and 53m 'higher' than Moeller #1. Burleson and the joint venture partners have an exploration target of 10.4Bcf gas and 0.24mmbbls of condensate. Burleson anticipate farming out interests in this prospect to reduce the exposure to exploration costs.

Woppa

Large gas exploration 'play'

The 'Woppa' prospect is a very large (350Bcf), deep gas prospect which lies beneath the Heintschel field. The prospect is on trend from the 600Bcf producing 'Word' field. Wells targeting this play would be expensive (due to depth) and BUR is looking for a farm-out partner to share in the drilling costs. This prospect is a 'dry' gas prospect and would most likely require a sustained increase in the US gas price to be economic.

Directors & Management

Non - Executive *Chairman*

Norman Zillman

Norman Zillman was a founder and the inaugural managing director of Queensland Gas Company Limited, responsible for the acquisition of all of the company's coal bed methane (CBM) areas in the Surat Basin in Queensland and the discovery of its first CBM gas field with Arqyle No 1 well flowing CBM at more than 1 million cubic feet per day. He was also responsible for the successful IPO of the company, raising $12 million. Norm was also a founder and non-executive chairman of Great Artesian Oil and Gas Limited, Blue Energy Limited, Hot Rock Limited and China Yunnan Copper Australia Limited; a founder and non-executive director of Planet Gas Limited and a founder and significant shareholder of Bandanna Energy Limited. With 40 years' experience, Norm is non-executive co-chairman of Chinalco Yunnan Copper Resources Limited and a non-executive director of Earth Heat Resources Limited (ASX: EHR).

Managing Director

Michael Sandy

Michael Sandy is a geologist with more than 35 years' experience in the resources industry. He is the principal of consultants MJSA, which provides services to energy companies. He commenced his career as a minerals geologist with various mining exploration companies as well as the Australian research organisation, CSIRO. In 1982 he moved into petroleum geology, initially with the PNG government and later with Oil Search and as a consultant to various oil and gas exploration companies. He was involved in setting up Novus Petrolium in 1994/95 (still the largest oil and gas IPO) and held senior positions until Novus was taken over in 2005. He is a non-executive director of three ASX-listed energy companies, Caspian Oil & Gas Limited (ASX: CIG), Tap Oil Limited (ASX: TAP) and Hot Rock Limited (ASX: HRL).

Executive Director

Alex Sundich

Alex Sundich is a chartered accountant and company director. He previously worked as a banker for Credit Suisse First Boston (1990 to 2000) and Goldman Sachs (2001 to 2003), where he was responsible for advising oil and gas and mining companies on mergers and acquisitions and capital raisings, including for an extended period in the United States. From 2003 to 2006, Alex was the Chief Financial Officer of Record Investments Limited, an ASX-listed investment company. He also served as a Non-Executive Director of Eastern Star Gas, an ASX-listed oil and gas company, from 2007 until its takeover in 2011 for approximately $900 million.

Non - Executive Director

Andrew Kugler

Dr **Andrew Kugler** Jr is a geologist and geophysicist with more than 40 years of experience in the oil and gas industry. He holds a Bachelor of Science Geology from Yale University (USA), a PhD in Geology from University of Tasmania and is a member of the American Association of Petroleum Geologists, and a registered Certified Petroleum Geologist (#4912). Andrew is currently the President and CEO of AKG Oil Company, AKG Operating Company and a General Partner of AKG Energy, L.P. all of which are involved in oil and gas exploration, development and operations in Texas.

Non - Executive Director

Khib Kugler

Khib Kugler has more than 30 years of geological and geophysical experience both internationally and in the US, including eight years with Texaco. In 2001, Khib joined AKG as Vice President of Geology and Geophysics.

**Director CV's taken from company website*

Analyst Verification

We, Grant Craighead 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 Burleson 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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Breakaway Investment Group
AFSL 290093 ABN 84127962387
T+61292621363
F+61292792727
PO Box H116 Australia Square
Sydney, NSW 2001
Suite 505, 35 Lime Street,
Sydney, NSW 2000