

An Eventful June Q – More to Follow in 2H 2011

Investment Highlights

- Production up significantly in the June Q.** NEN successfully completed 2 x new development wells which came online in May at a combined IP of 700bopd before stabilising. This boosted the average production for the June Q to 590bopd. The company booked revenue of \$5.5m from an average sales price of US\$102.7/bbl, finishing with cash of \$25.8m after receiving ~\$13m in remaining proceeds from its capital raising.
- Completion of independent assessments for Blocks 102 & 105.** A key highlight for the June Q was the receipt of NSAI's independent prospective resource assessments for Blocks 105 and 120. Based on the assessment, NEN highlighted 2 x key prospects for drilling in the shallower Block 105 – the Cua Lo gas prospect (3.5tcf and 26.4mmbbls of prospective resource) and the Song Ca oil prospect (129.8mmbbls). In Block 120 NEN identified the Rua Bien prospect (611mmbbls) and the Ca Lang prospect (461mmbbls) as key targets for drilling.
- Farmout of Vietnam acreage underway.** NEN and KrisEnergy have commenced farm-out of both permits to target the drilling of 2 x wells in Block 105 and 1 x well in Block 120, commencing in the June Q 2012. Completion of the farmout will be a key catalyst.
- NEN to push ahead with Californian exploration and appraisal.** NEN will shortly commence drilling of the Paloma Deep prospect targeting 300mmboe in place across stacked objectives plus drill an additional 3 x wells in the Salinas Basin this quarter. A key highlight will be the drilling of the 1st of 3 horizontal wells at Paris, commencing in October. The well will trial cyclic steaming to determine if commercial production of the heavy oil is possible.
- We maintain our BUY recommendation with a price target of \$0.69/sh.** Key short term catalysts will include the farmout of Vietnam, drilling of Paloma deep, Paris Valley appraisal plus potential for new ventures. Results from Exxon's 3 x well Vietnam exploration program could also provide a positive impact which has reportedly commenced in the 3 x blocks to the North of NEN's 120.

27 July 2011

12mth Rating

BUY

Price	A\$	0.41
Target Price	A\$	0.69
12m Total Return	%	69.5

RIC: **NEN.AX**

BBG: **NEN AU**

Shares o/s	m	431.7
Free Float	%	100.0
Market Cap.	A\$m	177.0
Net Debt (Cash)	A\$m	-25.8
Net Debt/Equity	%	na
3m Av. D. T'over	A\$m	0.37
52wk High/Low	A\$	0.46/0.10
2yr adj. beta		1.65

Valuation:

Methodology		DCF
Value per share	A\$	0.69

Analyst:

Scott Simpson

Phone:

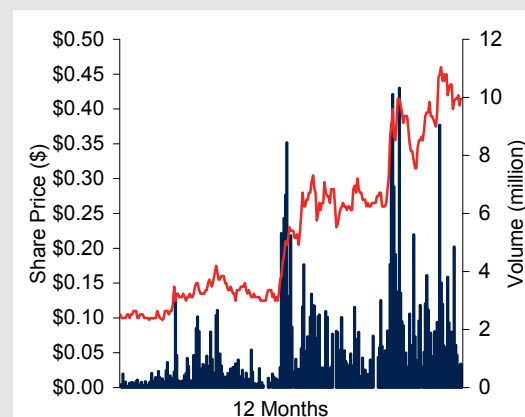
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Disclosure: In November 2009 Patersons Securities Limited was mandated to place 42m shares at A\$0.135 per share, raising a total of \$5.7m. Patersons received a fee for these services.

12 Month Share Price Performance



Performance %	1mth	3mth	12mth
Absolute	19.6	24.1	179.2
Rel. S&P/ASX 300	30.7	25.4	152.2

Year End June 30	2009A	2010A	2011F	2012F	2013F
Reported NPAT (\$m)	(10.9)	(4.0)	(3.3)	5.0	3.9
Recurrent NPAT (\$m)	(10.9)	(2.3)	1.4	5.0	3.9
Recurrent EPS (cents)	(4.2)	(0.7)	0.3	1.1	0.9
EPS Growth (%)	na	na	na	242.9	(21.1)
PER (x)	(9.7)	(62.2)	129.2	37.7	47.7
EBITDA (\$m)	(7.7)	(0.9)	3.3	7.9	6.8
EV/EBITDA (x)	(13.1)	(162.2)	48.1	20.4	23.1
Capex (\$m)	8.3	2.5	3.9	4.9	2.1
Free Cashflow	(1.5)	(7.4)	(6.2)	(0.3)	4.7
FCFPS (cents)	(0.6)	(2.1)	(1.4)	(0.1)	1.0
PFCF (x)	(70.4)	(19.2)	(29.8)	(556.0)	39.5
DPS (cents)	0.0	0.0	0.0	0.0	0.0
Yield (%)	0.0	0.0	0.0	0.0	0.0
Franking (%)	0.0	0.0	0.0	0.0	0.0

Production at NSA Significantly Increased

During the quarter NEN completed the drilling of the Lombardi 20-27H and 21-27H wells at its North San Ardo project. The wells were drilled into the southern lobe of the field using 1000ft horizontal sections into the oil column to maximise well recoveries. The wells were a great success, coming online at a combined rate of 700bopd, boosting the overall field rate to over 1000bopd for a short duration. At a cost of \$650k per well, payback is less than 1 month.

The net result of the wells was a short term boost to cash flow and a higher average quarterly rate of 590bopd (467bopd average for the March Q) which together with an average realised oil price of \$102.7/bbl boosted revenue to \$5.5m. The success of development wells and the ongoing trials of cyclic steaming are important in maintaining a solid performance at NSA. At current oil prices the cash flow not only supports day to day operations but assists in the funding of early exploration endeavours.

Competent Persons Reports Received

During the Quarter the key highlight was the receipt of independent assessments for both Blocks 105 and 120 in Vietnam. The reports were the culmination of NEN's extensive background work, farmout of the permits to KrisEnergy for the completion of 2D seismic acquisition, processing and interpretation. The independent assessments were completed by industry renowned experts Netherland Sewell & Associates which provides verification as to the prospectivity of the acreage.

Block 105

The independent assessment for Block 105 was based on a review of the top 7 leads identified by NEN. While the block is largely prospective for gas, the report identified the potential for an oil fairway on the western side of the block up against a hinge line fault system. As a result NSAI presented alternative oil estimates for three of the leads located on this western side. The estimates are summarised below:

Figure 1: Prospective Resource Estimates

PRIMARY CASE							
Lead	Interval	Low Estimate		Best Estimate		High Estimate	
		Gas (BCF)	Condensate (MMBBL)	Gas (BCF)	Condensate (MMBBL)	Gas (BCF)	Condensate (MMBBL)
Lead 1	4.0 Ma	17.9	0.1	60.9	0.4	163.5	1.5
Lead 1	5.5 Ma	71.2	0.4	242.8	1.7	737.5	5.7
Lead 1	16.5 Ma	54.7	0.3	232.6	1.6	712.8	6.4
Lead 2	4.0 Ma	15.2	0.1	49.1	0.4	133.4	1.1
Lead 3	4.0 Ma	12.1	0.1	41.6	0.3	118.6	1.1
Lead 4	4.0 Ma	930.9	5.2	3,463.3	26.4	12,655.2	104.2
Lead 4	5.5 Ma	129.8	0.7	429.5	3.0	1,314.4	11.0
Lead 5	5.5 Ma	35.2	0.2	128.0	0.9	443.3	3.7
Lead 5	6.5 Ma	100.4	0.6	362.7	2.7	1,178.9	10.2
Lead 5	9.2 Ma	81.7	0.4	296.0	2.1	917.4	7.2
Lead 6	5.0 Ma	91.2	0.5	283.7	2.0	801.9	6.9
Lead 7	7.0 Ma	175.7	1.0	678.6	4.8	2,243.1	18.6
Total		1,716.0	9.7	6,268.9	46.3	21,420.0	177.9

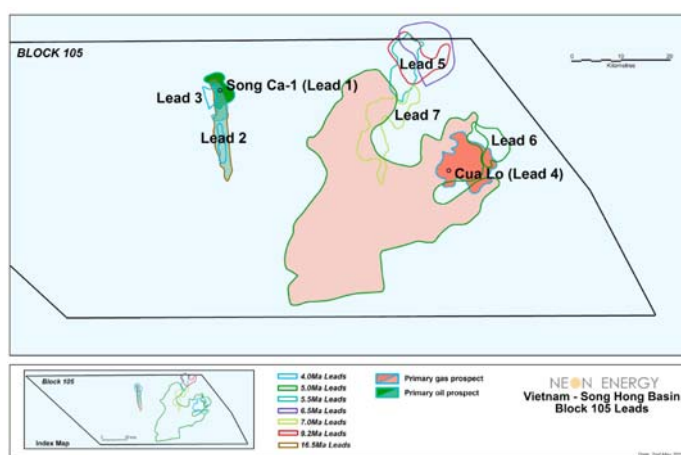
ALTERNATE CASE							
Lead	Interval	Low Estimate		Best Estimate		High Estimate	
		Gas (BCF)	Oil ⁽¹⁾ (MMBBL)	Gas (BCF)	Oil ⁽¹⁾ (MMBBL)	Gas (BCF)	Oil ⁽¹⁾ (MMBBL)
Lead 1	4.0 Ma	-	3.9	-	16.3	-	50.5
Lead 1	5.5 Ma	-	9.1	-	42.8	-	133.4
Lead 1	16.5 Ma	-	13.6	-	70.7	-	224.7
Lead 2	4.0 Ma	-	2.5	-	13.4	-	40.5
Lead 3	4.0 Ma	-	2.5	-	12.3	-	38.7
Lead 4	4.0 Ma	930.9	5.2	3,463.3	26.4	12,655.2	104.2
Lead 4	5.5 Ma	129.8	0.7	429.5	3.0	1,314.4	11.0
Lead 5	5.5 Ma	35.2	0.2	128.0	0.9	443.3	3.7
Lead 5	6.5 Ma	100.4	0.6	362.7	2.7	1,178.9	10.2
Lead 5	9.2 Ma	81.7	0.4	296.0	2.1	917.4	7.2
Lead 6	5.0 Ma	91.2	0.5	283.7	2.0	801.9	6.9
Lead 7	7.0 Ma	175.7	1.0	678.6	4.8	2,243.1	18.6
Total		1,544.9	40.3	5,641.9	197.4	19,554.1	649.7

Totals may not add because of rounding.

⁽¹⁾ The oil volumes shown include both crude oil and condensate.

Source: NEN Release 9th May 2011

Figure 2: Lead Map



Source: NEN Release 9th May 2011

Based on the results NEN identified two priority targets for drilling, the Cua Lo gas prospect (Lead 4) and the Song CA-1 oil prospect (Lead 1). Key risks/challenges to Block 105 include the current low gas prices in Vietnam, lack of immediate onshore gas infrastructure and the risk of high CO₂, given its occurrence in a number of nearby fields. However the shallow water would provide for low development costs should a significant discovery be made and potential CO₂ could be managed/engineered around. Although there is minimal gas infrastructure in place and a historically low gas price in the South of Vietnam, there is a growing demand for gas and a plan to import LNG which suggests that domestic gas production could command a strong gas price and/or be readily used for power generation. Despite the challenges, any gas discovery would certainly provide upside for NEN. Discovery of oil in shallow water would be more readily developed. We have assumed that the JV will farm-out 1/3 of its interest in Block 105 with NEN retaining a 33% stake, targeting a free/maximum carry on its share of a 2 well drilling program (est. cost of \$17m dry-hole).

Block 120

The independent assessment for Block 120 was based on a review of the top 12 leads identified by NEN. The results are provided in the table below:

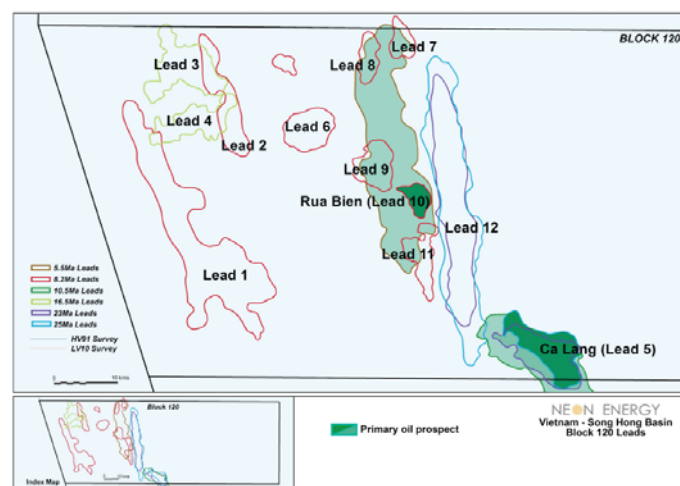
Figure 3: Prospective Resource Estimates

Lead	Interval	Unrisked Gross (100%) Prospective Resources (MMBBL)		
		Low Estimate	Best Estimate	High Estimate
Lead 1	8.2 Ma	82.7	361.8	1,074.5
Lead 2	8.2 Ma	20.7	100.7	310.4
Lead 3	16.5 Ma	52.7	215.9	628.1
Lead 4	16.5 Ma	26.7	110.5	323.1
Lead 5	10.5 Ma	87.5	269.7	702.5
Lead 5	23 Ma	16.1	80.3	255.5
Lead 5	25 Ma	22.1	110.6	353.1
Lead 6	8.2 Ma	7.8	38.0	117.3
Lead 7	8.2 Ma	6.0	29.0	89.3
Lead 8	8.2 Ma	10.7	51.9	160.3
Lead 9	8.2 Ma	10.0	48.4	147.8
Lead 10	5.5 Ma	152.6	575.0	1,613.1
Lead 10	6.5 Ma	3.7	18.2	55.8
Lead 10	8.2 Ma	3.8	18.0	55.3
Lead 11	8.2 Ma	11.4	55.0	169.7
Lead 12	23 Ma	37.0	187.4	599.2
Lead 12	25 Ma	81.3	403.3	1,291.9
Arithmetic Sum		632.8	2,673.5	7,947.0

Totals may not add because of rounding

Source: NEN Release 19th May 2011

Figure 4: Lead Map



Source: NEN Release 19th May 2011

Based on the results NEN identified the two high ranking leads for drilling as the Rua Bien and the Ca Lang prospects which NSAI provided best unrisked prospective resource estimates of 611mmbbls and 461mmbbls, respectively. Overall the report highlighted significant potential in Block 120 with the size of the prospects certainly sufficient to justify semi-submersible drilling at an estimated well cost of ~\$25m per well. In our valuation we have assumed that the JV will farmout 50% of the permit with NEN maintaining a 25% interest in the permit for a free carry on the drilling of the first well.

Paris Valley Appraisal to Commence in October

NEN will commence the drilling of the 1st of 3 possible wells in the Central Paris Valley (CPV) area in October. The Central part of the field is well delineated with over 30 wells drilled and 9.1mmbbls of 2P reserves certified across the area from +100mmbbls of oil in place. NEN had previously drilled a vertical well on the northern part of the field, which when steamed, failed to deliver commercial rates. The upcoming well will trial the use of a horizontal well to steam a much greater volumes of reservoir in order to potentially deliver a higher production rate. With +100mmbbls in place a commercial flow rate that delivered as low as 10-15% recovery would be a very material outcome for NEN.

Figure 5: Paris Valley

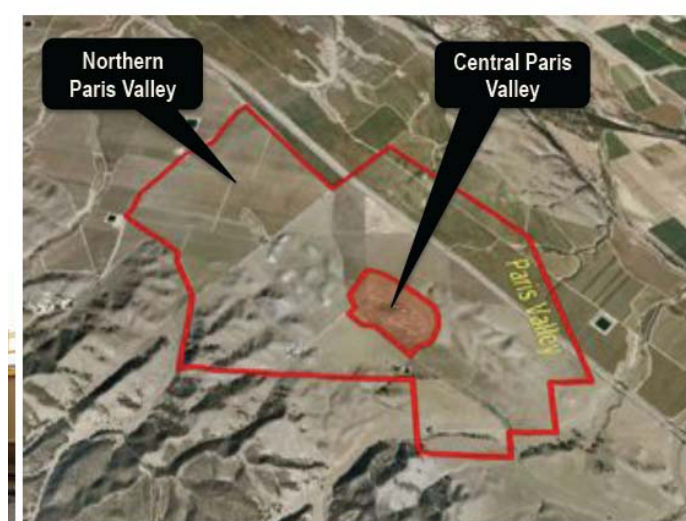
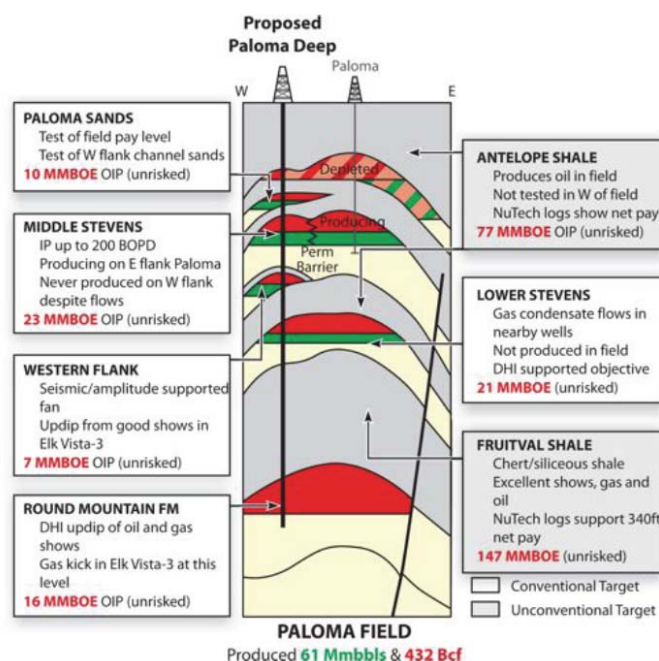


Figure 6: Paloma Deep



Source: NEN Investor Presentation – July 2011

Source: NEN Operational Update– June 2010

Californian Exploration

The Sep Q will see 4 x exploration wells drilled by NEN in California. The first well to spud will be Paloma Deep, scheduled for August which will test 300mmbbls of oil and gas in place across multiple horizons. The objectives to be drilled include a number of conventional horizons which are known to be productive in other fields/offset wells and also include some non-conventional shale horizons. NEN will have a 75% interest in the well and partial carry in the US\$4.9m gross well cost. It is worth noting that although the well will be drilled through multiple objectives it will not be possible to test all the zones. We assume that all zones will be logged however follow-up wells will likely be required if more than 1 x zone is to be tested. However a positive result will still provide a catalyst for NEN and potential development project from a relatively low cost.

In the Salinas Basin NEN intends to drill 3 x exploration wells in the Sep Q. This includes the East San Ardo (100% WI) and Lombardi East (100% WI) prospects, with mean prospective resource estimates of 2.7mmbbls and 2.5mmbbls, respectively. In addition NEN will drill Deadman's Gulch (50% WI) estimated at 4mmbbls of prospective resource. Dry hole well costs are estimated at less than US\$0.5m.

Activity Schedule

NEN's upcoming activity schedule is provided below:

Figure 7: Activity Schedule



Source: NEN Investor Presentation – July 2011

Valuation

We maintain our BUY recommendation with an upgraded price target of \$0.69/sh. Our valuation is summarised below:

Figure 8: Base Case Valuation

Valuation	A\$m	A\$/sh
North San Ardo	69	0.15
Exploration & Appraisal	225	0.49
Other	7	0.02
Cash -est	26	0.06
Corporate	(9)	(0.02)
Debt	0	0.00
Total @ 10% Discount Rate	318	0.69
Price Target		0.69

Source: Patersons estimates

Our valuation is based on DCF analysis of NEN's remaining ~3mmbbls of 2P oil and its NSA field plus a risked assessment of its exploration and appraisal opportunities. Further detail is provided below:

Figure 9: Risked Valuation of Exploration and Appraisal Portfolio

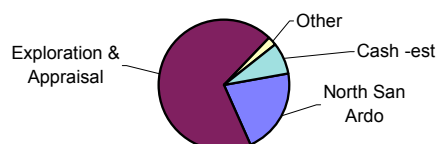
Permit	Prospect	Interest %	Gross Prospective Resource			Nominal NPV	Unrisked Value		Risking	Risked Value	
			(mmbbls)	(bcf)	(mmboe)		(A\$m)	(\$ ps)		(A\$m)	(\$ ps)
Block 105	Cua Lo	33.0%	26.4	3,463.5	621.9	\$10/bbl, \$0.50/mcf	658.6	1.44	7.5%	49.39	0.11
Block 105	Song Ca Oil	33.0%	129.8		129.8	\$10/bbl, \$0.50/mcf	428.3	0.94	7.5%	32.13	0.07
Block 120	Ca Lang	25.0%	460.0		460.0	\$10/bbl, \$0.50/mcf	1,150.0	2.51	7.5%	86.25	0.19
California	Paris Valley	100.0%	15.0		15.0	\$10/bbl, \$0.50/mcf	150.0	0.33	20.0%	30.00	0.07
California	Paloma Deep	60.0%			33.0	\$10/bbl, \$0.50/mcf	198.0	0.43	10.0%	19.80	0.04
California	Salinas Basin	100.0%	7.2		7.2	\$10/bbl, \$0.50/mcf	72.0	0.16	10.0%	7.20	0.02
	Subtotal		616	3,464	1,212		2,237	4.9		224.8	0.49

Source: Patersons Estimates

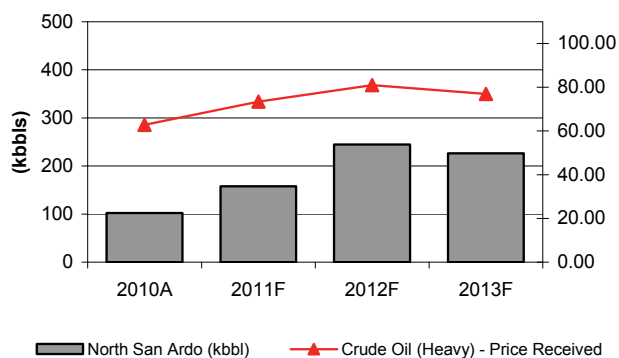
Our valuation for Blocks 105 and 120 are based on an assumed farmout requirement for a free carry on a targeted well campaign, a conservative NPV value plus a risking to reflect a conservative geological risk plus risking for completion of farmout/funding. We will look to de-risk these prospects as the targeted farmout is progressed. While it is not expected that all of the short term objectives are discovered in line with our assumptions, the unrisked value reflects the potential for material upside.

Neon Energy Limited (NEN)		\$0.41	
Valuation	A\$m	A\$/sh	
North San Ardo	69	0.15	
Exploration & Appraisal	225	0.49	
Other	7	0.02	
Cash -est	26	0.06	
Corporate	(9)	(0.02)	
Debt	0	0.00	
Total @ 10% Discount Rate	318	0.69	
Price Target		0.69	
Valuation Sensitivity	-10%	0%	+10%
Oil Price Sensitivity (A\$/sh)	0.66	0.69	0.72
Exchange Rate Sensitivity (A\$/sh)	0.71	0.69	0.68

Valuation Summary of Operating Assets



Production Summary



Reserves & Resources

Reserves - Net NEN as at June 2010	Oil/Cond (mmbbl)	Gas (bcf)	Total (mboe)
2P Reserves			
North San Ardo	3.8	0.0	3.8
Paris Valley	9.1		9.1
Total Group	13.0	0.0	13.0

Directors

Name	Position
Alan Stein	Non-Executive Chairman
Ken Charsinsky	Managing Director
John Lander	Non-Executive Director

Substantial Shareholders

	Shares (m)	%
BlueGold Global Fund	28.9	15.0

Commodity Assumptions	Year End June 30			
	2010A	2011F	2012F	2013F
A\$:US\$	0.89	0.99	1.05	1.00
Crude Oil - WTI (USD/bbl)	75.43	91.72	101.25	96.18
Crude Oil (Heavy) - Price Receive	62.81	73.37	81.00	76.95

Production Summary	2010A	2011F	2012F	2013F
North San Ardo (kbbbl)	103	158	245	226
Other				
Total (kbbbl)	103	158	245	226
North San Ardo (bbl/day)	281.29	431.88	670.25	620.01
Other				
Total (bbl/day)	281	432	670	620

Profit & Loss (A\$m)	2010A	2011F	2012F	2013F
Sales Revenue	7.4	13.6	18.8	17.4
Other Income	0.2	0.0	0.0	0.0
Operating Costs	2.6	2.5	3.5	3.5
Exploration Exp.	0.0	0.3	0.0	0.0
Corporate/Admin	4.3	4.5	3.2	3.3
Royalty	1.5	3.0	4.1	3.8
EBITDA	(0.9)	3.3	7.9	6.8
Depn & Amort	1.4	1.9	3.0	2.9
EBIT	(2.3)	1.4	5.0	3.9
Interest	0.0	0.0	0.0	0.0
Operating Profit	(2.3)	1.4	5.0	3.9
Tax expense	0.0	0.0	0.0	0.0
Minorities	0.0	0.0	0.0	0.0
FX Adjustment	(1.7)	(4.7)	0.0	0.0
NPAT	(4.0)	(3.3)	5.0	3.9

Normalised NPAT	(4.0)	(3.3)	5.0	3.9
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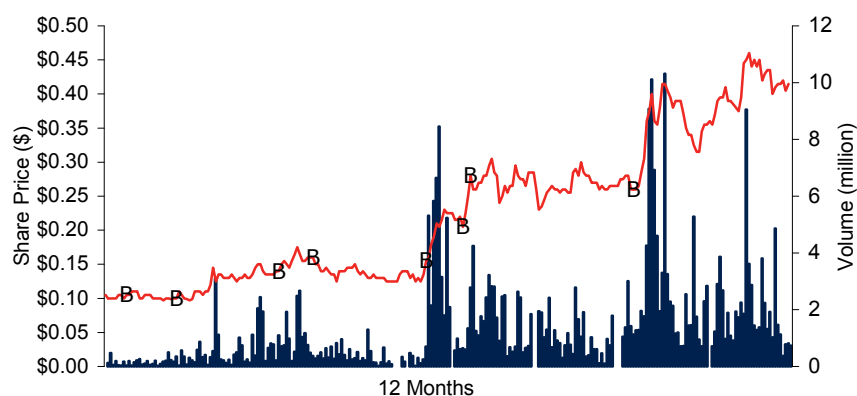
Cash Flow (A\$m)	2010A	2011F	2012F	2013F
Adjusted Net Profit	(1.5)	1.4	5.0	3.9
+ Interest/Tax/Expl Exp	0.0	0.3	0.0	0.0
- Interest/Tax/Expl Inc	1.3	4.9	3.4	0.0
+ Depn/Amort	1.4	1.9	3.0	2.9
+/- Other	(1.4)	(1.1)	0.0	0.0
Operating Cashflow	(2.8)	(2.4)	4.5	6.8
- Capex (+asset sales)	2.5	3.9	4.9	2.1
- Working Capital Increase	0.0	0.0	0.0	0.0
Free Cashflow	(5.3)	(6.3)	(0.3)	4.7
- Dividends (ords & pref)	0.0	0.0	0.0	0.0
+ Equity raised	5.3	24.7	0.0	0.0
+ Debt drawdown (repaid)	(0.1)	0.0	0.0	0.0
+ Other	(1.5)	5.6	0.0	0.0
Net Change in Cash	(1.6)	24.1	(0.3)	4.7
Cash at End Period	1.8	25.8	25.5	30.2
Net Cash/(Debt)	1.8	25.3	25.5	30.2

Balance Sheet (A\$m)	2010A	2011F	2012F	2013F
Cash	1.8	25.8	25.5	30.2
Total Assets	46.8	68.8	73.7	77.6
Total Debt	0.0	0.5	0.0	0.0
Total Liabilities	5.2	5.5	5.5	5.4
Shareholders Funds	41.6	63.3	68.2	72.2

Ratios

Net Debt/Equity (%)	na	na	na	na
Interest Cover (x)	na	na	na	na
Return on Equity (%)	na	na	7.3	5.4

Recommendation History



Date	Type	Target Price	Share Price	Recommendation	Return
06 Aug 10	Research Note	0.26	0.10	B	
02 Sep 10	Research Note	0.26	0.10	B	
27 Oct 10	Research Note	0.26	0.13	B	30.0%
15 Nov 10	Oil and Gas Review	0.26	0.16	B	23.1%
13 Jan 11	Research Note	0.26	0.16	B	
02 Feb 11	Research Note	0.31	0.21	B	31.3%
07 Feb 11	Research Note	0.43	0.26	B	23.8%
04 May 11	Research Note	0.42	0.26	B	
	Current Share Price		0.41		57.7%

Stock recommendations: Investment ratings are a function of Patersons expectation of total return (forecast price appreciation plus dividend yield) within the next 12 months. The investment ratings are Buy (expected total return of 10% or more), Hold (-10% to +10% total return) and Sell (> 10% negative total return). In addition we have a Speculative Buy rating covering higher risk stocks that may not be of investment grade due to low market capitalisation, high debt levels, or significant risks in the business model. Investment ratings are determined at the time of initiation of coverage, or a change in target price. At other times the expected total return may fall outside of these ranges because of price movements and/or volatility. Such interim deviations from specified ranges will be permitted but will become subject to review by Research Management. This Document is not to be passed on to any third party without our prior written consent.

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#1 Stock picker in Real Estate - Jonathan Kriska

#1 Stock picker in the Metals and Mining - Josh Welch

#2 Stock picker in Energy - Andrew Harrington

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