

Friday 14th September, 2012

Target Energy – oil flow success as predicted in Darwin-1 well in Texas, USA

In our previous coverage of **Target Energy (ASX: TEX, Share Price: \$0.098, Market Cap: \$34m)** in early September, the company was trading at around \$0.063 and senior management comprising Chairman Chris Rowe and the MD Laurence Roe were out and about on a promotional road-show to draw attention to both the company's undervalued status and its busy work program on its USA petroleum acreage.

In my note on September 4 I highlighted the prospectivity of the company's current Darwin-1 well, where flow-test results were imminent. I'm pleased to say that target has today announced highly encouraging flow-test results from the well, which have led to a more than 50% jump in its share price in today's trade.



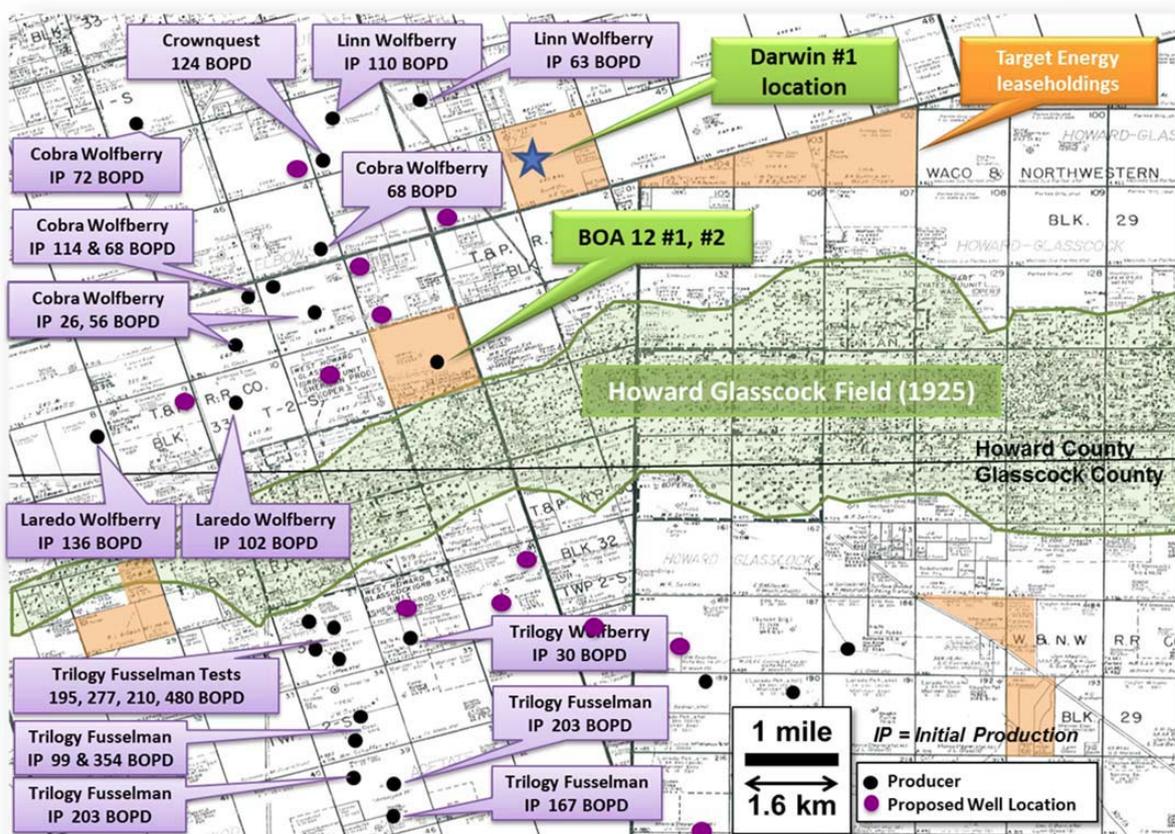
Target has announced that oil has flowed to surface from the Fusselman formation within the Darwin #1 well in West Texas at rates in excess of 240 barrels of oil per day (BOPD). The well, which targeted both

highly prospective Wolfberry and Fusselman sections, was perforated in the Fusselman section. Following acid stimulation, the well commenced flowing oil through a 10/64 inch choke at rates equivalent to over 240 BOPD, with associated gas and importantly with no water. The well has now been shut-in for a pressure buildup survey and will re-commence flow testing over the weekend.

Locally, the Fusselman interval is an extremely attractive target with wells just 8km south of Darwin #1 producing at rates up to 480 BOPD. Importantly it's not just the Fusselman formation that looks attractive, with the Wolfberry section also worthy of testing at a later stage, with nearby Wolfberry wells producing at flow-rates of up to 136 BOPD. Typical Wolfberry wells in the region have the potential to contain up to 130,000 barrels of oil equivalent, with very long lives.

The Darwin #1 well is the second well in Target's Fairway project in Howard County, Texas and lies just 3km northeast of Target's BOA wells, which we'll discuss in a moment.

As a reminder, Target is a modestly-priced junior oil play with a flagship project in West Texas called the Fairway project, which comprises a sizeable acreage package of 3,492 acres - 3,012 acres of which are under lease with a commitment for a further 480 acres. Target holds a substantial 60% working interest in the project, with other participants comprising Trilogy Operating (30%) and Avalon Oil (10%). Although not yet producing, the project has potential to yield significant hydrocarbons and become a company-maker.



The first well in Target's Fairway project, the BOA 12#1 well, encountered a 1,080-metre interval in the "Wolfberry" section, which exhibited numerous oil shows while drilling, in particular in the Wolfcamp, Strawn and Mississippian formations. Shows were also noted in the shallower San Andres and Clear Fork Formations and the deeper Fusselman Formation. The well was later fraced in the Wolfberry section.

During the testing phase, oil and water from the deeper Devonian section migrated into a number of the frac stages, inhibiting the flow from the Wolfberry. Isolating these zones eliminated the flow of the Devonian water and oil along with the bulk of the gas. There was a persistence of the water-flow and the upper three Wolfcamp frac stages were also isolated via a cement squeeze.

Following the isolation of the upper Wolfcamp and deeper Devonian sections, BOA 12 #1 continued to flow oil, but was also accompanied by large volumes of water. Off-site disposal of the water is uneconomic in the long-term and the well was shut-in on 13 July awaiting the conversion of BOA 12 #2 to a salt-water disposal well (SWD). Using the SWD well will significantly reduce water-handling costs and allow the acceleration of the water recovery from the Wolfberry section and addition of the Devonian and Fusselman zones back into production.

A jet-pump, capable of pumping fluid at rates of up to 2,000 barrels per day (compared to the existing 275 BPD capacity) has been sourced and will replace the existing pump. When BOA 12 #1 is back on line, production will initially recommence from the Wolfberry section and the Devonian/Fusselman sections will be included later on.

The company's second well - BOA 12 #2 – was unsuccessful in terms of producing hydrocarbons, but the bore-hole has been converted to a salt-water disposal well that will allow the acceleration of water recovery from the Wolfberry section in the adjacent BOA 12-1 well and allow the Devonian and Fusselman zones to be returned into production.

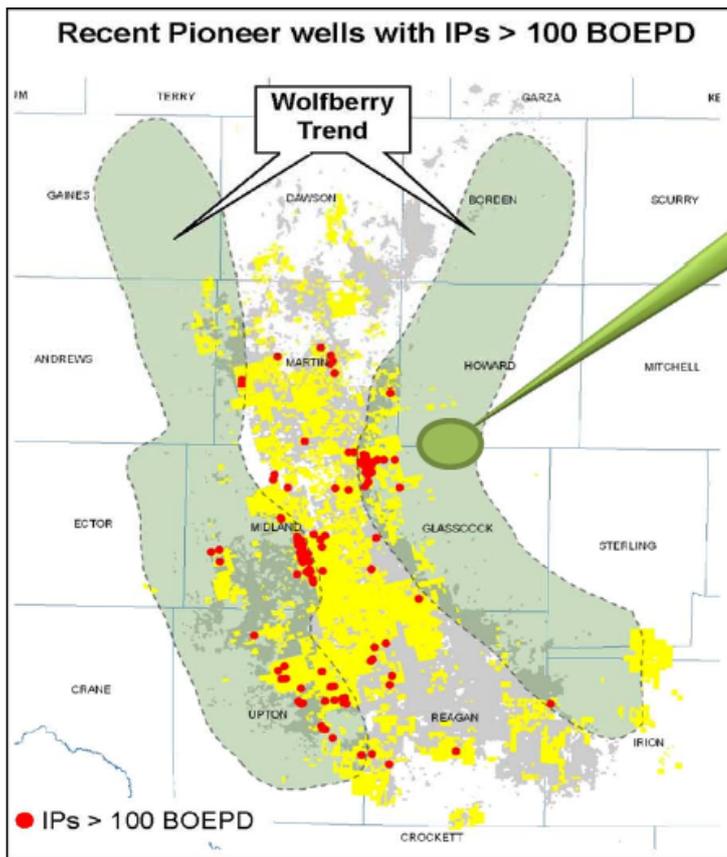
As I've previously outlined, the key attraction of the company's Fairway Project is that it's hosted within the Permian Basin, which boasts an outstanding oil discovery success rate. Located principally in western Texas, the Permian Basin is one of the most prolific oil-producing basins in North America. Not surprisingly, this has led to the area being targeted by many of the USA's leading petroleum companies.

The primary targets within the current well comprise the Wolfberry interval, along with the deeper Fusselman Formation. The Wolfberry is the primary target, as it is considered to have the potential to be a company-maker. Importantly, there are up to 75 drilling locations within the Fairway project area on a 40-acre spacing, each with potential recoverable reserves estimated at up to 180,000 barrels of oil equivalent.

The Wolfberry play, originally named because of the combination of hydrocarbon production from the separate Wolfcamp and Spraberry Formations, is a major low-permeability oil play within the Permian

Basin. The Wolfcamp interval lies stratigraphically below the Spraberry Formation, and is in itself a significant producer within the Permian Basin.

The largest accumulation of oil and gas reserves within the Permian Basin is found within the Spraberry trend, which encompasses an overall area of ~2,500 square miles and covers large sections of six counties. The Spraberry trend ranks third in the USA in terms of total proved reserves and seventh in terms of total petroleum production.



Fairway

The biggest game-changer for companies wanting to exploit these prospective petroleum-bearing horizons has been the overall advancement in completion methods, which have made it possible to combine production from the Spraberry and Wolfcamp zones in areas that were previously uneconomic on a standalone basis.

Several senior oil and gas producers such as Concho Resources, St. Mary Land and Exploration, Pioneer Natural Resources, Oxy USA, ExL Petroleum, Mariner Energy and Cambrian Management, are actively developing the Wolfberry. In fact more than 2,000 wells have been drilled since late 2007, which is when the play type first began to be exploited.

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 has confirmed the Wolfberry strategy and highlights the prospectivity of the region. The Fairway project comprises 2,873 acres with up to 75 possible well locations, with well potential recoveries up to ~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.

Target advised the market back in July that it had agreed terms with its largest shareholder, Investmet Limited, to secure additional funding of \$2.5 million. The funds will be applied to the drilling and testing of Darwin #1 well and two further Fairway wells over the course of the next two quarters.

Estimated Timing	Prospect	Location	Target Working Interest	Potential Recoverable Volumes*
Shut in	BOA 12 #1 Frac	Howard Co, Tx	60%	180 – 220 mBO
Now flow-testing	Shepard’s Channel	Lafourche Parish, La	15.3%	200 Bcf / 12 mmBO
Underway, Converting to SWD	BOA 12 #2 (Shallow)	Howard Co, Tx	60%	N/A
July 2012	Darwin #1 (Fairway)	Howard Co, Tx	60%	180 – 220 mBO
Q4 2012	Fairway #3, #4	Howard/Glasscock Co	60%	180 – 220 mBO
Q1 2013	East Chalkley / PP#3	Cameron Parish, La	35%	250 – 450 mBO

We’ll be monitoring progress on Target Energy’s BOA 12-1 well closely. The company’s modest market value of just \$37 million in combination with relatively low-cost but high-impact wells, means the company offers the appropriate risk-reward balance for investors. The recent share price pull-back on the back of technical delays and share market nervousness has provided a nice near-term entry point for investors. Accordingly, we will look to introduce the stock to our Portfolio within the very near future.

Fairway - Permian Basin Wolfberry Oil Resource Play

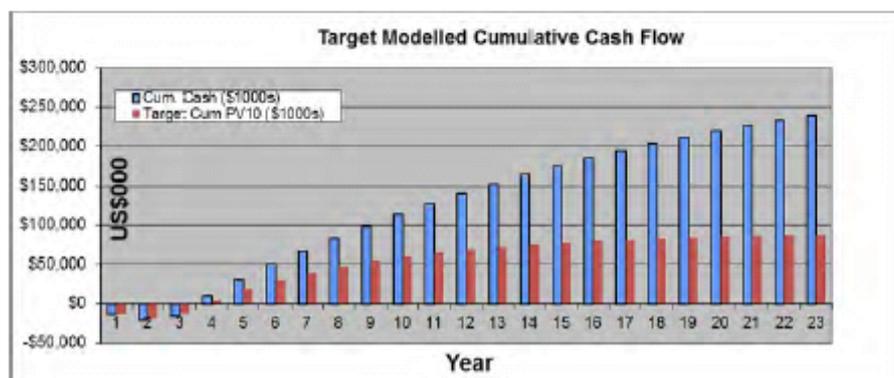
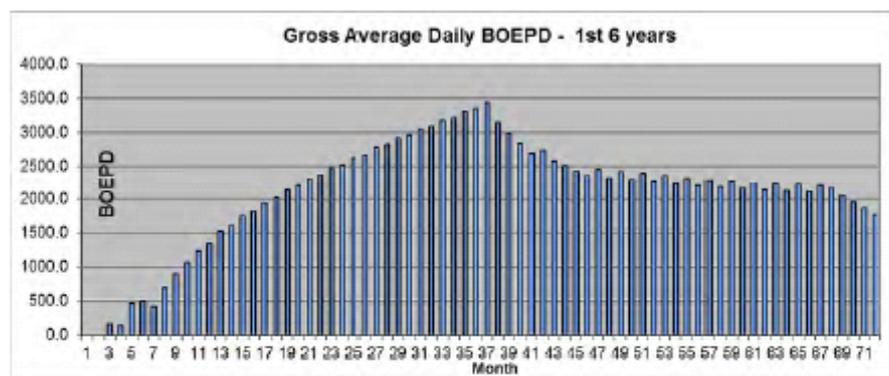
64 Well Program (model)

Production peaks at >3,437 BOE/D in 37 months

The 64 well model indicates up to 11.46 mmBOE prodn in 23 years; could generate >\$240m in cash for TEX (undiscounted), \$87m NPV10.

Model assumes all 64 wells successful and match Wolfberry Type well with 16 successful in Fusselman as well. Fairway wells may not match Type well and may produce more oil and gas (or less).

US\$75/bbl oil escalated at \$5/bbl/yr to \$100/bbl, then flat.



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