January 2012
UPDATE

Central Petroleum Limited

ASX: CTP

BAKERS Investment Group

Recommendation
Strong Buy

Volatility
High

Trading Price for the 18th January 2012
$0.059

Target Price in 12 Months:
$0.32

Price Performance

Industry Group: Energy
Market Cap: $63,324,986
Total Issue: 1,073,304,842
12m High/Low:
$0.084 / $0.042

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SUMMARY

This report is an update to the earlier report on Central Petroleum Limited (ASX: CTP) issued in July 2011 and should be read in conjunction with that report.

CTP is a junior exploration and production company with extensive granted and pending tenement acreage in Central Australia, predominately in the Northern Territory totalling over 70 million acres, almost entirely 100% net owned. Within this acreage large resources of oil, natural gas, helium and coal have been identified and/or inferred by independent geological assessment. These resources are located within four main geological structures; the Amadeus, Pedirka, South Georgina basins and the Lander Trough of the Wiso Basin.

On 11 January 2012, CTP announced significant oil flows from its Surprise-1 Re-entry H (S1REH) well. The oil flow from the S1REH was tested at 380 barrels per day of “light sweet crude” with an API Gravity averaging 40 Degrees, with some prospects for a further increase in flow-rate. This is the first horizontal well completion in Central Australia producing oil and the first onshore discovery well in the Northern Territory producing significant oil flow for more than fifty years. The company is seeking to finalise a sales agreement and within the next two to three months finalise the arrangements for an Extended Production Test. CTP is also considering its options for a second well and advancing its previously announced timetable.

The 11 January 2012 announcement significantly lowers the risk associated with CTP’s initial projects demonstrating not only the presence of oil in its target areas, but also the company’s ability to bring oil to market in accordance with its strategic plans.

We continue to rate CTP as a **STRONG BUY** with a twelve month target price of **$0.32** per share. This is based on a “sum of parts” assessment of Central Petroleum’s short time-to-commercialisation projects, and the company as a whole, including factoring in the risks faced in bringing these projects to an operational phase. The value per share of $0.0858 for the Surprise-1 project alone exceeds the current market price per share. Whilst undervalued, CTP has consistently outperformed the ASX300 energy stocks over the last twelve months.

The reduction in the twelve month target price compared to the previous report reflects, in part, a stronger Australian Dollar and a softening in global oil prices. Further, CTP has increased its operational expenditure as a result of its drilling. Increased operational expenditure from further drilling and then operation of its wells will be increasingly offset as CTP receives revenue from oil sales.

Although significantly higher than current trading price, this valuation continues to reflect a heavily risked and realistic assessment of the value of CTP’s quick-to-market projects for which CTP has development plans and development capital reserves. This valuation does not include any value potential from Central Petroleum’s longer term projects, such as

unconventional resources or coal monetisation, despite the company progressing plans for commercialisation of its coal assets through farmout arrangements which will add additional value to the company without distracting from its principal oil and gas focus.

SURPRISE-1

The Surprise-1 project is located in the Amadeus Basin within the EP 115 tenement. Initial drilling by the company in December 2010, produced a core sample from the Lower Stairway Sandstone zone which presented 100% fluorescence which was independently confirmed as due to the presence of oil. Further independent tests concluded that the zone from which the core came could produce between 500 and 1,000 barrels a day subject to confirmation by electronic logging and flow testing. Central Petroleum has now announced significant oil flows from its Surprise-1 Re-entry H (S1REH) well. The oil flow from the S1REH well is currently 380 barrels per day of “light sweet crude” with an API Gravity averaging 40 Degrees, with some prospects for a further increase in flow-rate.

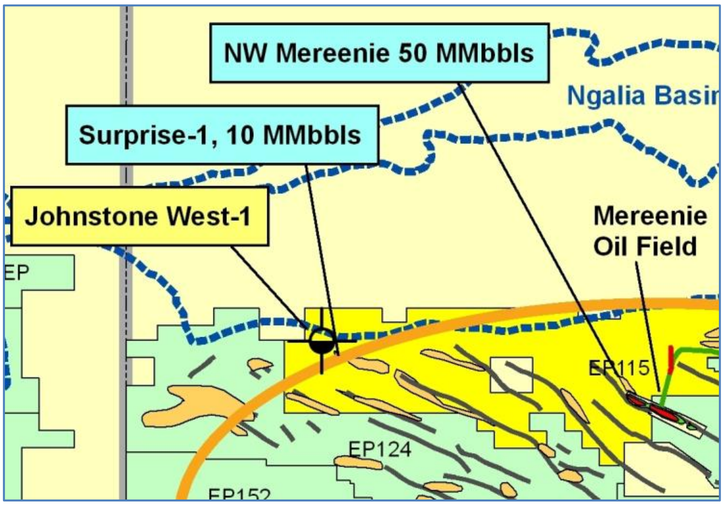

Figure 1 - Surprise-1 well in relation to the producing Mereenie Oil Field to the east (UOIIP – “best” estimate)

The company is looking to follow up success with up to three to four wells at Surprise within the next 6 to 18 months to finalise the extent of the deposit and/or to drill additional prospects in the near vicinity. These wells are anticipated to be designed with horizontal drilling to maximise potential production.

THE COMPANY

Central Petroleum has significant resources in Central Australia, predominately in the Northern Territory, with a range of resources on its tenements. The company’s strategy is to identify and monetise a select few liquids-focused projects based on existing geological data which present the lowest risk and the shortest time to production. Using these short term projects as a base, the company plans to investigate and develop its longer term assets. This strategy has led the company to identify three main projects as short term priorities and CTP has developed capital programs to bring them online as quickly as possible.

Short Term Priority Projects

Central Petroleum has a stated goal[1] of developing its oil and natural gas prospects, bringing them to production as quickly as possible. The three priority projects are the Surprise-1 and Madigan Prospect oil projects, and the Mount Kitty condensate, natural gas and helium project.

Longer Term Assets

Due to its significant tenement holdings, Central Petroleum has a large portfolio of assets which it could exploit through a number of methods in the long term. Given Central Petroleum's stated focus on its short term liquids-focused projects, the details on how and when these long term assets will be utilised have not yet been sufficiently finalised. Central Petroleum continues to source funding and partners to develop its potential coal assets through a number of projects through farmout arrangements.

Corporate

Central Petroleum is continuing its corporate strategy of developing a handful of select projects which have an expected shortest time to production, which will then be leveraged to further develop the company's other longer term assets.

Central Petroleum was founded in 1998, as Merlin Synergy NL, by Mr John Heugh and Mr Richard Faull with the stated "countercyclical strategy aimed at securing large acreage tracts with very large targets in prospective areas of strategically well placed parts of central Australia[2]". The company listed in 2006 and has since grown through the application for new tenements and permits and the acquisition of other unlisted permit holders within the target basins, to become one of the largest exploration acreage holders in Australia.

Directors and Management

Central Petroleum is governed by an experienced board supported by a skilled senior management team. The Board is made up of

- Dr Henry Askin (Non-Executive Chairman)
- Mr John Heugh (Managing Director & Co-founder)
- Mr Richard Faull (Non-Executive Director & Co-founder)
- Mr William Dunmore (Non-Executive Director)

[1] ASX Announcements, as recently as 24 April 2011
[2] Company website - accessed 18 July 2011

The Board has long-term experience in the petroleum and mineral exploration industries with large multinationals including Shell, Esso, Santos, BHP Petroleum and Chevron-Texaco. The Board is supported by the senior management team made up of experienced geologists, exploration managers and energy professionals, including recently recruited members, with key management experience in unconventional resource exploration and recovery in North America.

VALUATION

This valuation updates our previous valuation of July 2011 and this assessment should be considered in conjunction with that report. As before, we only considered those projects which are likely to become operational, or have capital expended on them, within the next 12 to 24 months. Therefore, the company's valuation is based upon Central Petroleum's short-term projects: the Surprise-1 and Madigan Prospects oil projects and the Mount Kitty natural gas and helium project. The change to the valuation in this report is solely due to the reported oil flows to surface from the Surprise-1 Re-entry H (S1REH) well.

As before, this valuation does not include any value potential from Central Petroleum's longer term projects, such as unconventional resources or coal monetisation, which will add additional value to the company as the development plans for these are finalised.

Central Petroleum was valued using a discounted cash-flow method (DCF) for each short term project, based on publicly available information such as Annual Reports and Operational Updates as well operational data and geological reports provided by the company, and those reports prepared by independent third parties. The DCF method was selected due to its greater accuracy compared to other valuation methods given the availability of predicted cash-flows and the lack of suitable peers in the Australian market.

The DCF modelling values cash flows from predicted operations for a period of 15 years for each project, with no terminal value. It is believed that 15 years of cash flow is reasonable for valuing each project. However, given the nature of each project, it is likely that each project may exceed 15 years and that operating cash-flows beyond this period would provide additional value to that stated in the DCF model. The DCF method takes into consideration a number of risk factors, reflected in the Risk Adjustment Factor, which are discussed in the next section.

The valuation of Central Petroleum's short-term projects, predicted corporate overhead expenses and net assets including current cash in bank is shown in Table 1 below. These valuations were calculated using a weighted cost of capital (WACC) of 10% and highly conservative risk adjustment factors which assume a low chance of successful development to production, except for the S1REH well. For more information on how the risks were assessed and the rationale behind them, please see the "Risks" section of this report.

Element	Risk Adjustment Factor[3]	Risk-Adjusted Value Per Share @ 10% WACC
Projects		
Surprise-1	59.05%	$0.0858
Madigan Prospect	16.03%	$0.2271
Mount Kitty	13.36%	$0.0734
Other		
Corporate Overhead[4]	-	-$0.0899
Net Assets	-	$0.0241
TOTAL		**$0.3205**

Table 1- Valuation of Short-Term Projects

The corporate overhead including drilling and exploration expenses have significantly risen compared to the previous report, as the company has moved towards first production. However, the anticipated revenues offset much of the additional operational costs with the company expecting to be cash-flow positive after the proposed second well is brought into production.

RISKS

External risk factors, including Political, Technology, Tenement, and Financing risks, may impact on the execution of each of Central Petroleum's short term projects and long term assets, and affect the ability of these projects to generate the operating cash flows that have been forecast by the DCF model. These risks as they relate to Central Petroleum's projects are outlined below. The valuation takes into consideration an appropriate discount given the likely impact each of these risks may have on the outcome of the forecast cash flows and consolidates them into a single risk factor. As each project advances, and associated risks of achieving forecast cash flows are reduced, the model may be adjusted to incorporate the new reduced level of risk. This would increase the forecast shareholder value of the DCF Model as certainty towards achieving forecast cash flows is improved.

Country and Political Risk

Country and Political Risk includes the risks associated with the international and domestic geopolitical situation of the project country and/or state, the political and bureaucratic processes of the various levels of government, and the relevant legal systems.

We have given Central Petroleum's projects a minimal political risk rating due to Australia's mature and well defined mining industry, as well as the strong demonstrated interest by the Northern Territory government in development of its remote resources as a method of creating regional jobs. However, the political risk is not completely eliminated due to possible environmental and indigenous land-rights concerns which could be raised, particularly for any projects which are to be located on protected land. While measures can be taken to ensure adequate compliance with any concerns raised, such as environmental protection measures

[3] Calculated as the chance of successfully bringing the asset fully to market
[4] Corporate costs not attributed to individual projects

and engagement and involvement with local communities, these processes may delay project timelines. CTP has factored reasonable consideration of such risks into its development plans.

Tenement Risk

Tenement Risk includes risk to the project location such as securing tenement rights, access to the site, overlapping tenements, native title or heritage claims, and the impact to the site from them, as well as any geological risks of the site including any exploration risks.

Despite the remoteness of the three proposed short-term projects, tenement risk cannot be eliminated just because there is no traditional surface use such as farming or grazing over large portions of Central Petroleum's acreage. But we consider it a low risk, which can be managed within existing legal processes.

Technology Risk

Technology Risk is risk associated with the track record and effectiveness of the technology used, access to or protection of the intellectual property required, and the reliability of the equipment required, both in the development and production stages.

We originally gave the three short-term projects a moderate technology risk rating based on the some uncertainty of the geological structures that are to be drilled due to the early stage of the projects. This translates to a technology risk as it cannot be certain what methods of extraction will be required and whether the technology to enable the extraction will be available and suitable for task. With the proven significant oil flows to surface from the S1REH well, technology risk with respect to the Surprise-1 project has been lowered.

Financing Risk

Financing Risk is the probability of the project being able to be funded, either through equity or debt and the risk inherent to the timing of predicted cash flows.

We have given all three short-term projects a conservative financing risk rating due to the early stage of these projects and the current, though improving, economic environment in Australia. The timing of the cash flows has also been factored into the risk assessment, taking into consideration the effect on the valuation should the cash flows not eventuate when predicted or are smaller than predicted for any reason, including weaker than expected commodity prices or higher production costs. Central Petroleum's demonstrated success at Surprise-1 and the likely sales contract lowers the financing risk assigned to the Surprise-1 project. The company believes that with a second producing well planned for production within the next 6 months, it will become cash-flow positive which will further reduce financing risk.

CONCLUSION

Central Petroleum is a junior explorer in the oil and natural gas sector, with significant tenement acreage centred in the Northern Territory. Within its granted and pending acreage, the company has large indicated and probable resources of oil, natural gas, helium and coal which present the potential for significant value.

Central Petroleum continues to trade below its indicated valuation. The announcement of significant oil flows to surface at its Surprise-1 Re-entry H well and contingent plans to bring a second well into production over the next six months, supports an increased target price per share of **$0.32** and we continue to recommend CTP as a **Strong Buy**.

This valuation does not value the company's long term assets, as they are not mature enough to be accurately valued. When development plans for these assets are finalised, they are likely to represent further value for the company.

BAKERS Investment Group

Central Petroleum Limited

ASX: CTP

SUMMARY

Overview

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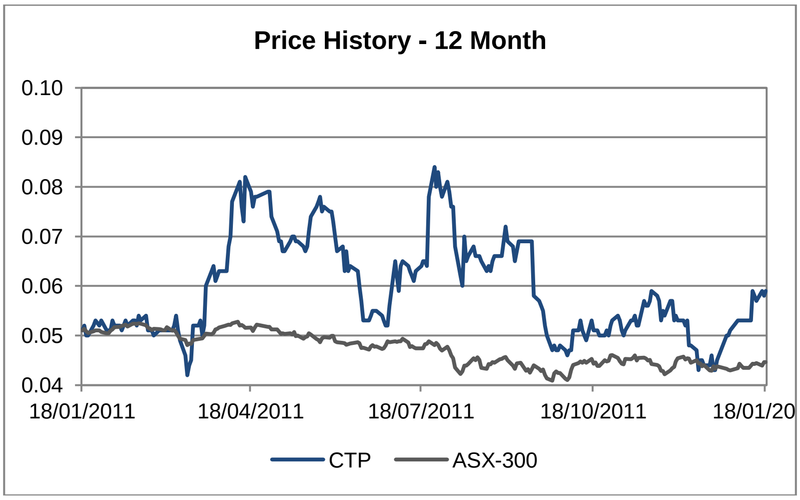
As at	18 January 2012
Name	Central Petroleum
Ticker (ASX)	CTP
Price	
Current	$0.059
12m High	$0.084
12m Low	$0.042
Shares on Issue	1,073,304,842
Mkt. Cap.	$63,324,986
Target Price	$0.32
Target Mkt. Cap.	$343,457,549

Price History



Valuation Breakdown

Valuation Break Down	Risk Adjustment Factor[5]	Risk-Adjusted Value Per Share
Projects		
Surprise-1	59.05%	$0.0858
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Other		
Corporate Overhead[6]	-	-$0.0899
Net Assets	-	$0.0241
TOTAL		**$0.3205**

Resources

Basin	Conventional Oil (P50 billions bbls)	Unconventional Oil (P50 billions bbls)	Natural Gas (P50 tcf)	Total (billions boe)
Amadeus	1.0	0.8	24.8	5.9
Southern Georgina	0.0	4.0	24.0	6.0
Pedirka	1.8	0.0	0.0	1.8
TOTAL	2.8	4.8	48.8	13.7

Top 10 Shareholders

Name	Shares Owned	% of Total Shares on Issue
Brighten International Pty Ltd	22,841,551	2.13%
National Nominees Limited	22,074,980	2.06%
Citicorp Nominees Limited	14,378,105	1.34%
Mr Mark Philip Shawcross	13,250,000	1.23%
Renlyn Bell Investments Pty Ltd	10,416,670	0.97%
JP Morgan Nominees Australia Limited	9,894,735	0.92%
RBJ Nominees Pty Ltd	9,375,000	0.87%
Franze Holdings Pty Ltd	9,360,000	0.87%
AMG International Pty Ltd	8,915,000	0.83%
Salavente Pty Ltd (GRB Superannuation Fund A/C)	8,625,000	0.80%

[5] Calculated as the chance of successfully bringing the asset fully to market
[6] Corporate costs not attributed to individual projects

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Absolute performance, long-term recommendation is based on implied upside/downside for the stock from the target price. A Buy/Sell implies upside/downside of 10% or more and a Hold less than 10%. The target price is the level the stock should currently trade at if the market accepted the analyst's view of the stock, provided the necessary catalysts are in place to effect the change in perception. If it is felt that the catalysts are not fully in place to effect a re-rating of the stock to its warranted value the target price will differ from 'fair' value. Given the volatility of share prices and our pre-disposition not to change recommendations frequently, these performance parameters should be interpreted flexibly. Performance in this context only reflects capital appreciation and the horizon is 12 months.

Each stock has been assigned a Volatility Rating to assist in assessing the risk of the security. The rating measures the volatility of the security's daily closing price data over the previous year relative to other stocks including in the S&P/ASX-300 Index. This rating is a quantitative (objective) measure provided as an additional resource and is independent of the qualitative research process undertaken by our research analysts.

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SUBJECT COMPANIES: ASX:CTP Central Petroleum Limited

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