PetroNeft Resources

Oil & Gas
United Kingdom
12 September 2007

Initiating Coverage: Just getting started

BUY

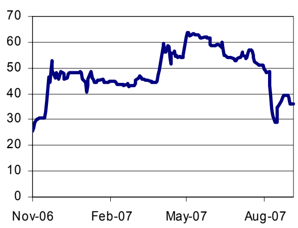
Current Price
36p

Target Price
82p
(Previous: n/a)

Basic data

TIDM	PTR.L
Shares (000)	191,771
Market cap. (£000)	104,036
Relative performance:(1m)	+5.3
(3m)	+3.3
(12m)	n/a
12 month high / low (p)	64 / 21
Reserves (mmboe)	70
Est. NAV (p/share)	64

Share price performance



■ **Following the discovery of the West Lineynoye field earlier this year, we believe PetroNeft's proved and probable reserves are likely to have more or less doubled to around 67 mmbbl. On this basis, we estimate the company has a core net asset value of 69p/share. Meanwhile, the proposed drilling campaign for next winter includes two exploration wells that will target prospects with reserves potential of 53 mmbbl between them. If both of those were successful, we believe they would be worth a further 53p/share, and, in our view, giving the company credit for one-quarter of that now does not seem unreasonable. Hence, we are initiating coverage of PetroNeft Resources with a target price of 82p/share, which is more than double the current level, and a Buy rating.**

■ PetroNeft holds 100% of Licence 61, which extends over an area of 4,991 square kilometres in the eastern portion of the West Siberian basin. The area is under-explored and under-exploited because the multi-billion barrel oil fields located elsewhere in the region were the priority for early development during the Soviet era. At the time of PetroNeft's flotation on AIM in September 2006, consultants Ryder Scott estimated it had proved and probable reserves of 34 mmbbl in two distinct oil fields – Lineynoye and Tungolskoye. More recently, the third and final well in the company's 2007 drilling programme established that the West Lineynoye structure also contains oil.

■ PetroNeft continues to boast a substantial inventory of exploration prospects on Licence 61. Most of these are deemed to be relatively low risk and, between them, PetroNeft estimates that they could contain recoverable reserves of a further 310 mmbbl. If this was to prove to be the case – and we should point out that the nature of oil and gas exploration is such that it almost certainly will not – then we estimate they could add perhaps another $1.2 billion or over 300p/share to PetroNeft's net asset value.

■ PetroNeft has a strong management team led by Dennis Francis who spent 30 years with Marathon Oil, much of it as USSR/FSU task force manager. In that capacity, he represented Marathon on the board of Sakhalin Energy Investment Company (SEIC). Similarly, David Golder and David Sanders, PetroNeft's non-executive chairman and vice president, respectively, also held senior positions with SEIC whilst on secondment from Marathon. PetroNeft's other non-executive directors include the chief financial officer of Tullow Oil and the general director of a drilling company operating in Western Siberia.

Year End 31/12	Net Income ($000)	P/E Ratio	Cash Flow ($000)	P/CF Ratio	Dividend (p)
2006a	-993	n/a	-1239	n/a	0.0
2007e	-1728	n/a	-1227	n/a	0.0
2008e	-3870	n/a	-3170	n/a	0.0
2009e	13071	10.7	15301	9.2	0.0

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DISCLOSURES ARE LOCATED ON PAGE 16 OF THIS REPORT

INVESTMENT SUMMARY

PLENTY MORE TO COME

PetroNeft was established in 2003 as an oil and gas investment and consultancy company focused principally on the Russian market. However, in May 2005 it bought Stimul-T, a Russian company that held the rights to Licence Area 61 in the Tomsk region of Western Siberia. Covering an area of nearly 5,000 square kilometres, at that time this block contained two known oil fields – Lineynoye and Tungolskoye – as well as numerous prospects and leads that had already been identified by seismic surveys. Lineynoye and Tungolskoye were discovered in the early 1970s but were considered too small to be of interest at a time when very large oil fields were being discovered elsewhere in the West Siberian oil and gas basin.

Subsequently, in September 2006 PetroNeft joined London's Alternative Investment Market (AIM) and issued 41.5 million new shares at just under 20p each to raise £7.5 million net of expenses. In the Competent Persons Report in the accompanying admission document, Ryder Scott attributed proved and probable reserves of 34 mmbbl to the company's existing discoveries with a further 37 mmbbl categorised as possible. Moreover, in excess of 350 mmbbl of prospective resources were identified on an unrisked basis and, after adjusting for the estimated chance of exploration success, almost 160 mmbl on a risked basis.

Since acquiring Stimul-T, PetroNeft has reprocessed almost 2,700 kilometres of old seismic and shot more than 1,000 kilometres of new data. Armed with this information, since the start of 2007, the company has drilled three wells on Licence 61. Two of those were appraisals designed to delineate Lineynoye and Tungolskoye prior to PetroNeft proceeding with the full development of those fields. The third targeted the much larger West Lineynoye prospect that, pre-drill, was thought to have the potential to more or less triple PetroNeft's reserves. In the event, it failed to encounter as much oil as hoped but the group still estimates the new field contains more than 30 mmbbl. Hence, it seems reasonable to assume that PetroNeft's proved and probable reserves are, in fact, around 67 mmbbl with continuing upside potential of over 300 mmbbl.

PetroNeft is led by Dennis Francis who spent 30 years with Marathon Oil, much of it as USSR/FSU task force manager. In that capacity, he managed the purchase of the Khanty Mansiysk Oil Company and represented Marathon on the board of Sakhalin Energy Investment Company (SEIC). Similarly, David Sanders, PetroNeft's vice president, also held senior positions with SEIC whilst on secondment from Marathon. The executive team is completed by Desmond Burke and Paul Dowling. The former has over 30 years experience in natural resources industries whilst the latter was recently appointed chief financial officer and will join the company at the beginning of October. The equally impressive non-executive team consists of David Golder, who is also a veteran of Marathon's Russian business, Tom Hickey, who is chief financial officer of Tullow Oil, and Vakha Sobraliev, who is general director of a drilling and services company operating in Western Siberia.

In the eleven months they have been listed, PetroNeft's shares have performed very well, increasing in price by over 80%. Nonetheless, they continue to trade at little more than one-half of our estimate of their core net asset value, which is 69p/share. Moreover, the current price does not appear to reflect any of the $1.2 billion of potential value we estimate is offered by the exploration leads and prospects on the block. In addition, the group is hoping to add further value for its shareholders by exploiting both the expertise and the contacts of its management team in the pursuit of acquisitions. All-in-all, then, we believe PetroNeft shares represent a low cost means of participating in the exciting investment opportunity that is the Russian upstream oil and gas industry. We are initiating coverage with a Buy rating and a target price of 82p/share.

VALUATION

NET ASSET VALUE

PetroNeft's core value is a function of three discoveries located on Licence 61 in Russia's West Siberian basin, which are believed to contain recoverable reserves of approximately 67 mmbbl in total. Overall, we estimate these fields are worth $259 million and that the group will exit this year with approximately $10 million of net cash. The next table shows a breakdown of our assessment of PetroNeft's net asset value, which was calculated using the following key assumptions:

- An average Urals blend oil price of $65.94 per barrel in 2007, $70.03 in 2008, $68.52 in 2009, $67.28 in 2010, $66.31 in 2011, $60.19 in 2012, and $44.68 flat real thereafter. These figures represent the futures curve as of Tuesday, 11 September 2007, followed by a long-term average crude price.

- One-third of output is exported at the Urals blend price with the other two-thirds sold domestically at a price equivalent to 55% of that.

- An inflation rate of 2% per annum.

- A discount rate of 8% per annum, which we believe to be a figure that is commonly used by oil and gas exploration and production companies to evaluate potential acquisitions.

PETRONEFT ESTIMATED NET ASSET VALUE

Asset	Value ($m)	Value (p/share)
Block 61	259	66
Pro forma net cash	10	3
Total	**269**	**69**

Source: Natixis Bleichroeder estimates

Because we have assumed that PetroNeft sells the bulk of its production domestically and the Russian fiscal regime treats sales to the local market rather more benignly than it does exports, this means that PetroNeft's valuation remains sensitive to oil price movements. Indeed, as is shown in the next table, a 10% rise in oil prices would cause our estimate of the company's net asset value to increase by 14%. Of course, the reverse is also true and, in the event oil prices lost 10%, there would be a 14% decline in our valuation. In addition, the table shows the impact of different discount rates on our core net asset valuation.

PETRONEFT NAV SENSITIVITY (P/SHARE)

Oil price → Discount rate ↓	-20%	-10%	0%	+10%	+20%
5%	66	79	91	103	115
8%	50	60	**69**	79	88
10%	42	50	58	66	75
12%	36	43	50	57	64

Source: Natixis Bleichroeder estimates

Importantly, PetroNeft boasts excellent upside potential over and above its core net asset value, in our view. This is a function of the large number of exploration prospects and leads that have already been identified on Block 61. Most of these are deemed to be relatively low risk and, between them, PetroNeft estimates that they could contain recoverable reserves of a further 310 mmbbl. If this was to be the case – and the nature of oil and gas exploration is such that it almost certainly will not be – then it could add perhaps another $1.2 billion or 303p/share to PetroNeft's net asset value. Some further details of the company's prospect inventory can be found in the following table.

LICENCE 61 EXPLORATION PROSPECTS AND LEADS

Prospects and Leads	Risk	Size (mmboe)	Est. potential value ($m)	Est. potential value (p/share)
South Lineynoye	Low	2.9	11.0	2.9
Low Lineynoye	Low	3.3	12.5	3.3
Korchegskaya	Low	43.0	162.0	42.0
West Korchegskaya	Low	10.4	39.1	10.1
Varyakhskaya	Low	19.1	72.0	18.7
North Varyakhskaya	Low	6.0	22.4	5.8
Upper Varyakhskaya	Low	2.6	9.7	2.5
Emtorskaya Crown	Low	14.3	54.0	14.0
Emtorskaya North	Medium	13.8	51.9	13.5
Sigayevskaya	Low	17.4	65.7	17.0
East Sigayevskaya	Low	1.9	7.2	1.9
Kulikovskaya	Low	9.1	34.3	8.9
Kulikovskaya North	Low	8.9	33.4	8.7
Kusinskiy	Medium	5.2	19.4	5.0
Tuganskaya	Medium	10.8	40.5	10.5
Krillovskaya	Medium	20.4	77.0	20.0
Sibkrayevskaya Crown	Medium	23.3	87.9	22.8
Sibkrayevskaya East	Medium	17.2	64.8	16.8
Tungolskoye East	Medium	11.8	44.6	11.6
Sobachya	Medium	36.0	135.7	35.2
North Bakinskaya	Medium	19.9	75.1	19.5
West Bakinskaya	Medium	13.0	48.8	12.7
Total	**n/a**	**310.3**	**1169.2**	**303.1**

Source: PetroNeft, Natixis Bleichroeder estimates

Furthermore, we understand that last winter's seismic programme in the southern and western part of the block resulted in the identification of six additional prospects. Ryder Scott is currently updating its reserves report for Licence 61 based on this new data and will include these prospects in its assessment.

TARGET PRICE (82P/SHARE)

Our net asset value calculation of 69p/share is the starting point for our estimate of PetroNeft's target price. On top of this figure, we need to capture some of the exploration upside potential in the group's portfolio. Given that we believe this amounts to more than $1 billion, it could be argued that investors should be giving the company substantial credit for oil that it might find in the future. However, we would be inclined to be more conservative and prefer not to look beyond next winter's drilling campaign, when two exploration wells will target prospects with reserves potential of 53 mmbbl. If both of those were successful, we estimate they would add 53p/share to PetroNeft's net asset value, and giving the company credit for one-quarter of this seems both reasonable, and, in our opinion, leaves the balance between risk and reward in favour of shareholders.

RISK FACTORS

PetroNeft's future revenues, profitability and cash flow will depend substantially upon the prices and demand for oil. The market for this commodity is volatile and even a relatively modest drop in prices can significantly affect an upstream oil company's financial results and impede its growth. Prices for oil and natural gas fluctuate widely in response to a variety of factors beyond the control of an individual company, including relatively minor changes in supply and/or demand.

Estimating oil and gas reserves is complex and inherently imprecise. Actual future production, oil and natural gas prices, revenues, taxes, development expenditures, operating expenses and quantities of recoverable oil and gas reserves is likely to vary from estimates, perhaps significantly. In addition, PetroNeft may adjust estimates of proven and probable reserves to reflect production history, results of exploration and development, prevailing oil and natural gas prices and other factors, many of which are beyond its control.

PetroNeft's oil and gas assets are located within a single licence in the Tomsk region of Russia. Since the dissolution of the Soviet Union in the early 1990s, Russia is undergoing rapid transformation. This has been marked by periods of significant economic, legal and political instability and uncertainty.

BACKGROUND

STRATEGY

PetroNeft's stated strategy is to develop an oil exploration, development and production business in Russia, using the combined skills, experience and resources of its directors and employees. Initially, the company intends to achieve this through a rigorous work programme on Licence 61, which will seek to bring three existing discoveries into production as rapidly as possible and also to exploit the additional opportunities already identified. In addition to operations on Licence 61, the company also continues to evaluate new projects for acquisition.

While the main focus for new acquisitions will be the Western Siberian Basin, PetroNeft will also consider projects in other areas within the Russian Federation. Initially at least, the group intends to target oil fields with reserves of less than 50 mmbbl, which are of limited interest to the major Russian oil and gas companies. PetroNeft will also evaluate opportunities with smaller companies that have assets they want to divest or jointly develop and which can provide near-term production growth. Finally, the group will participate in the Russian auction and tender process.

HISTORY

PetroNeft LLC was established in Texas in 2003 as an oil and gas investment and consultancy company focused principally on the Russian market. In May 2005, PetroNeft LLC acquired a Russian company, Stimul-T, which had acquired 100% of Licence 61 in the November 2004 Tomsk Licence Auction. In September 2005, PetroNeft Resources plc was incorporated in Ireland and, as part of a corporate reorganisation, acquired the principal assets and liabilities of PetroNeft LLC in November 2005. PetroNeft Resources plc was admitted to the London AIM and Dublin IEX Markets, in September 2006.

PETRONEFT RESOURCES TIMELINE

Date	Event
2003	PetroNeft LLC established in Texas
November 2004	Stimul-T acquires Licence 61 at auction
May 2005	PetroNeft LLC acquires Stimul-T
September 2005	PetroNeft Resources plc incorporated
November 2005	PetroNeft Resources plc acquires assets and liabilities of PetroNeft LLC
September 2006	PetroNeft Resources plc admitted to AIM

Source: PetroNeft Resources

OWNERSHIP STRUCTURE

PetroNeft has 192 million shares in issue of which 29% are held by the Directors and the remaining 71% are in public hands. The Directors participated in the initial public offering of September 2006 and bought further shares in the July 2007 fund raising. Apart from the Directors, the following shareholders own more that 3% of the company:

SUBSTANTIAL EXTERNAL SHAREHOLDERS

Name of Shareholder	Percentage	Shares (m)
RAB Octane Fund Limited	19.8%	37.9
Davycrest Nominees Limited	7.5%	14.3
JP Morgan Asset Mgt. (UK) Limited	3.9%	7.5

Source: PetroNeft Resources

OPERATIONAL REVIEW

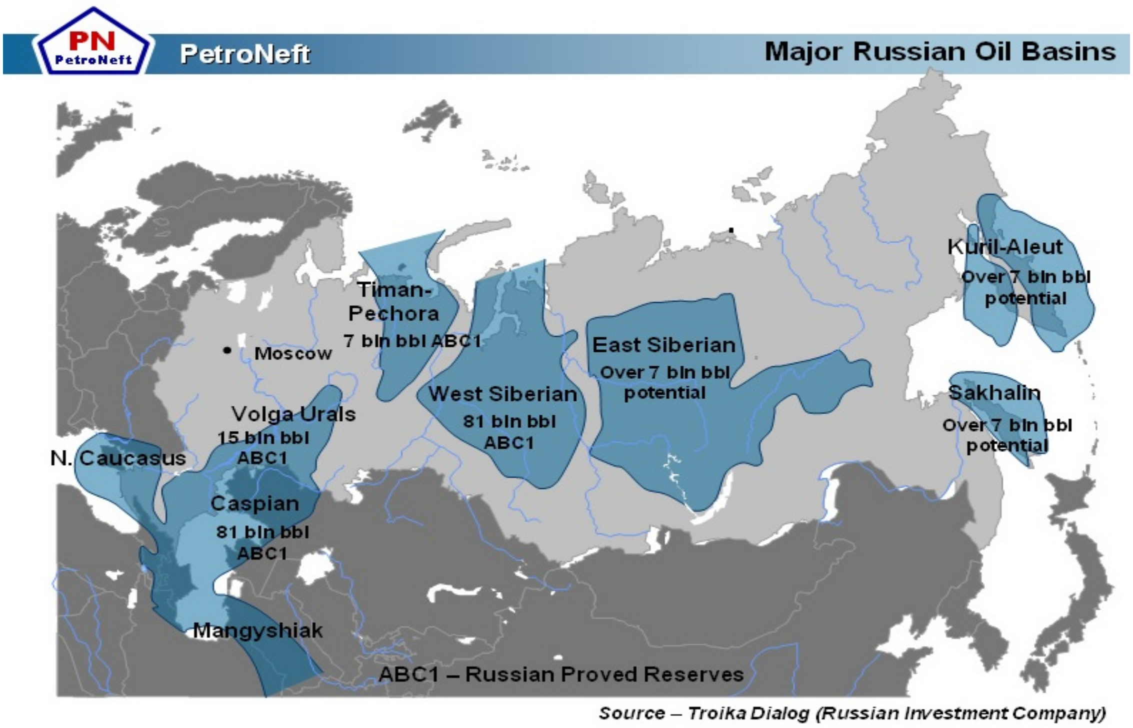
THE WEST SIBERIAN BASIN

The West Siberian basin occupies a large swampy plain between the Ural Mountains and the Yenisey River and extends offshore into the southern part of the Kara Sea. The permafrost is hundreds of meters thick in the northern onshore areas of the basin and gradually thins to zero north of the east-west segment of the Ob River. The basin, is about the same size as Saudi Arabia or Greenland, with an area of more than 2.2 million square kilometres of which almost 350,000 square kilometres is offshore. It is also the largest oil and gas producing region in the FSU, both in terms of physical size and the amount of recoverable oil and gas that it contains, and one of the largest petroleum-productive regions in the world.

In 2003, the US Geological Survey estimated volumes of discovered hydrocarbons in the basin at 144 billion barrels of oil and more that 1,300 trillion cubic feet of gas. The first hydrocarbon discovery was made in 1953, when a well tested gas on the western edge of the basin, and most of the giant fields that contain the bulk of the basin's reserves were discovered during the 1960s and 1970s. In the following years, the sizes of newly discovered fields gradually diminished. Large-scale production began in the early 1970s, and presently the basin produces about 70% of Russia's oil and gas. In spite of large volumes of drilling and seismic surveys, the basin remains only moderately explored, especially in its northern regions.

Topographically the basin is one of the world's largest areas of unbroken terrain. The region is characterized by water logged soils, shallow lakes and extensive swamps. Winters are severe and last seven to nine months of the year with mean temperatures ranging from about -15º C to -30º C. These winter conditions support better access to the fields, particularly in newer areas of development that have negligible infrastructure. Winter roads, which are maintained when the ground is sufficiently frozen to support heavy loads, or barge access in the brief summer if waterways exist, are the easiest and least expensive way to ship goods and people to producing fields.

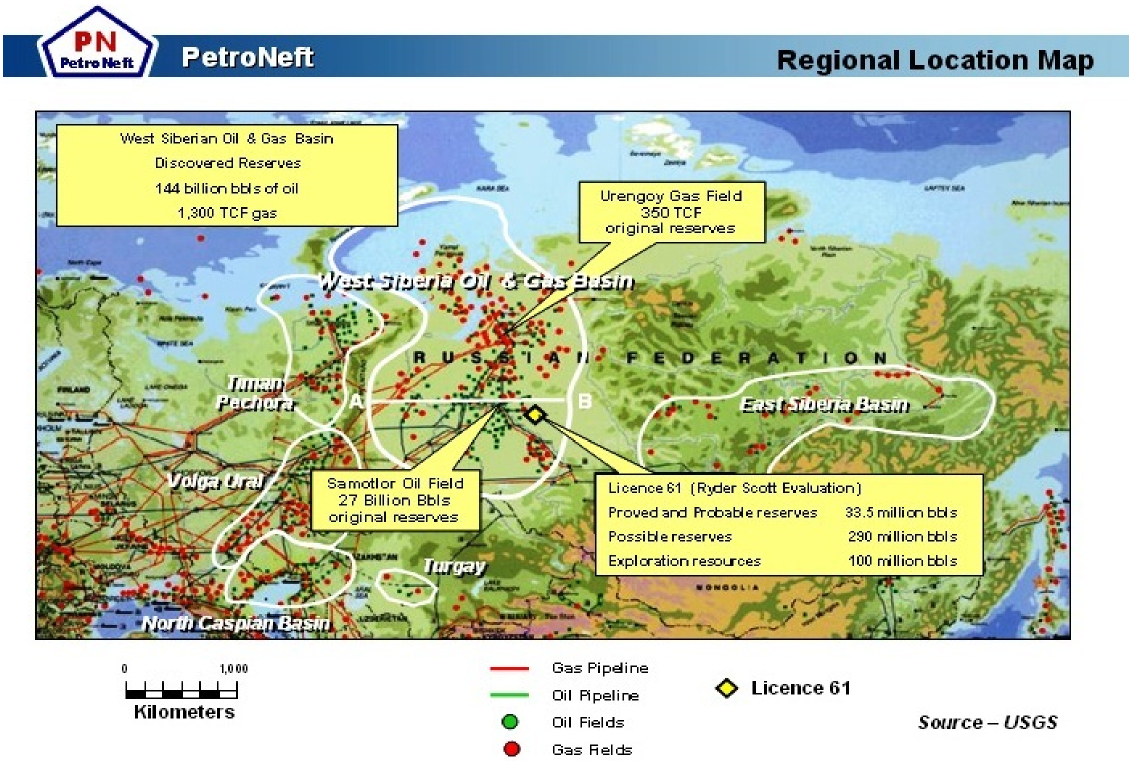
MAJOR RUSSIAN OIL BASINS



Source: PetroNeft Resources

LICENCE 61

LICENCE 61 – REGIONAL LOCATION MAP



Source: PetroNeft Resources

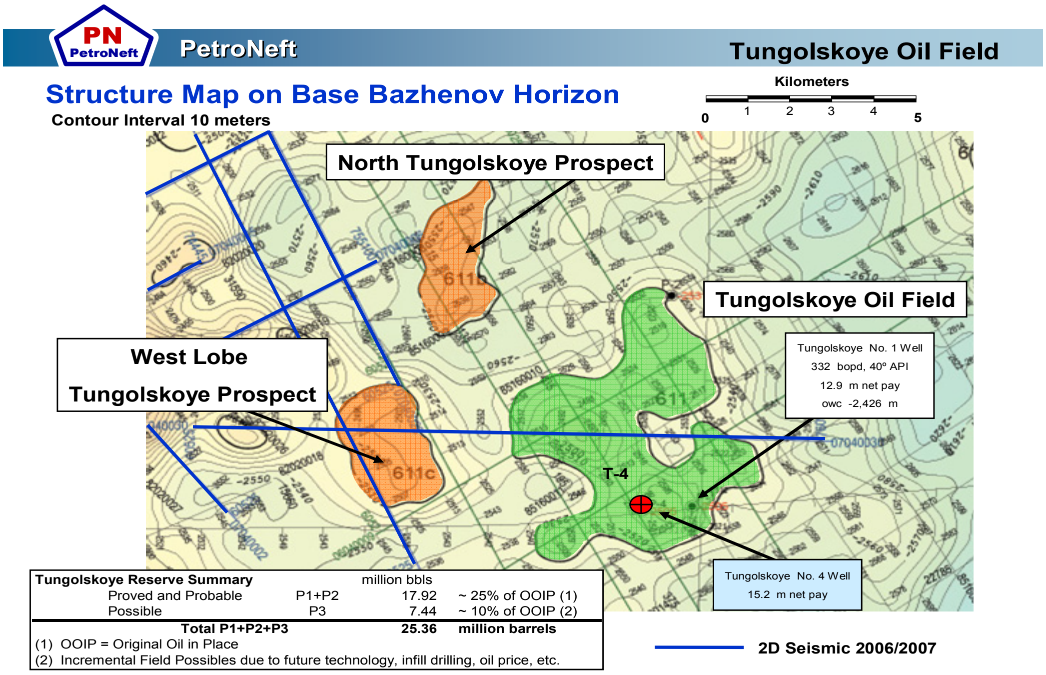
Existing oil fields

Licence 61 extends over an area of 4,991 square kilometres in the eastern portion of the West Siberian basin. The area is under-explored and under-exploited because the multi-billion barrel oil fields located elsewhere in the region were the priority for early development. At the time of PetroNeft's flotation on AIM in September 2006, consultants Ryder Scott estimated that it contained proved and probable reserves of 34 mmbbl in two distinct oil fields – Lineynoye and Tungolskoye.

Lineynoye is located in the north-west of the block and was discovered by a well drilled in the eastern part of the structure in 1972. This tested 264 b/d of light oil and led to the State Committee for Reserves attributing reserves of 18 mmbbl to the field that year. Subsequently, detailed seismic surveys were carried out in the mid-1980s and PetroNeft has reprocessed this and acquired over 515 kilometres of new data over the block. This enabled the company to reinterpret the Lineynoye structure and led to a small downgrade in reserves, with Ryder Scott estimating the proved and probable number at 16 mmbbl. However, following the drilling of the Lineynoye-6 appraisal well this year, which established that the field's oil-water contact is lower than previously thought, there appears to be some scope for that figure to be increased once more.

Tungolskoye is located in the central part of Licence 61 and initially the structure was delineated by seismic data in the late 1960s. Additional seismic data was obtained in 1970 and 1971 before the field was discovered by Tungolskaya-1 well in 1973. This produced a result similar to that achieved at Lineynoye a year earlier, testing 332 b/d of light oil. As with Lineynoye, since it became the operator of Licence 61, PetroNeft has reinterpreted the historic seismic for Tungolskoye, including some from the 1980s and 1990s, and acquired a certain amount of new data. This led to Ryder Scott estimating the field's reserves at 18 mmbbl and PetroNeft recently announced that the initial results from the Tungolskoye-4 well, which is still operating, appear to confirm this interpretation.

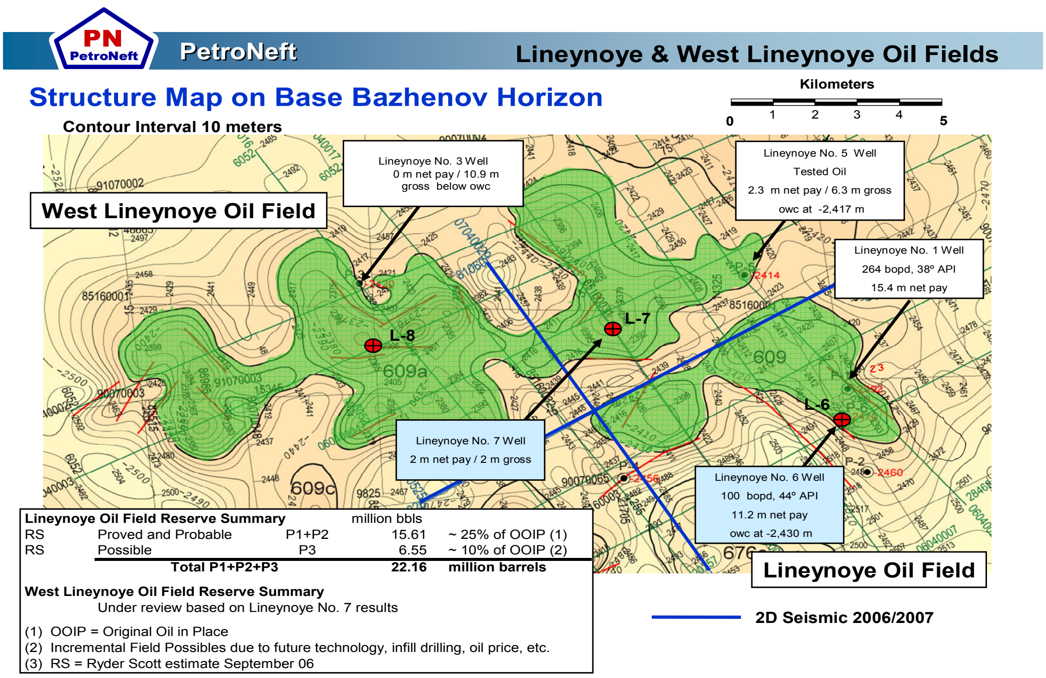
TUNGOLSKOYE OIL FIELD



Source: PetroNeft Resources

The latest field to be discovered on Block 61 is also the largest. Known as West Lineynoye, it is adjacent to the Lineynoye field and was identified by PetroNeft. Ryder Scott deemed the prospect to be low risk, with a chance of success in excess of 80%, and attributed possible reserves of 67 mmbbl to it as a result. Following the success of Lineynoye-7, which was the third and final well in this year's drilling programme and encountered net pay of 2 metres within a gross oil column of 22 metres, it now seems likely that over 30 mmbbl will be transferred into the proved and probable categories.

LINEYNOYE AND WEST LINEYNOYE OIL FIELDS NEED TO UPDATE THIS SLIDE



Source: PetroNeft Resources

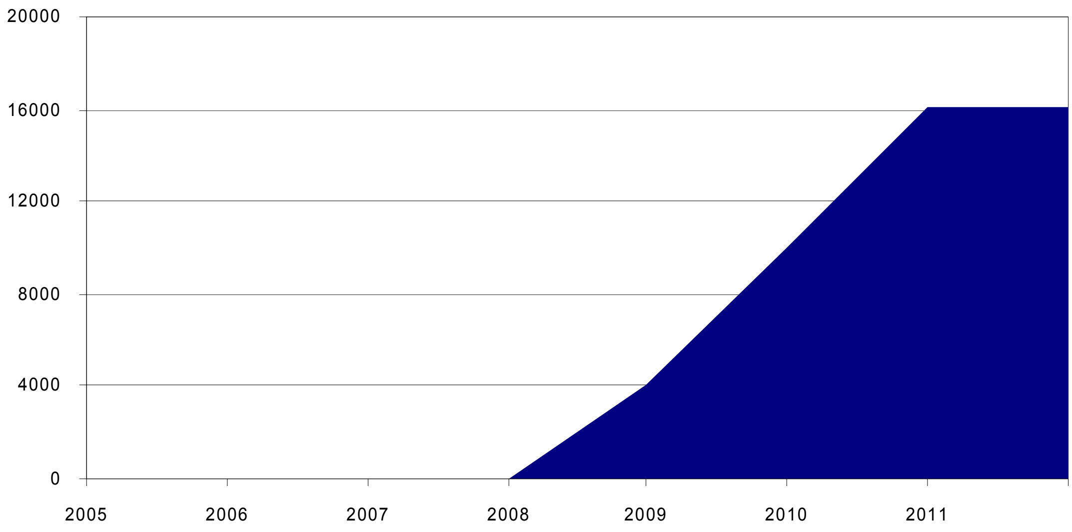
Hence, we believe PetroNeft's reserves are now in the region of 67 mmbbl on a pro forma basis and expect the group to proceed to establish production from Block 61. To this end, it has engaged the State Unitary Enterprise, Siberian Scientific Research Institute, to prepare a detailed feasibility study for the development of Licence 61. The scope of this includes full field reservoir modelling to determine the optimal recovery plan as well as designing proposed production facilities and export pipelines. Once complete, it will provide the basis for PetroNeft to seek development approval from the Russian authorities and enable it to start the process of securing project finance. Additionally, in May the group engaged ETC Service to design and then gain regulatory approval for an export pipeline from Licence 61 to Transneft's Raskino pumping station.

PETRONEFT PRO FORMA OIL AND GAS RESERVES

	Proved	Probable	Total
Tungolskoye (31/12/2006)	2.7 mmbbl	15.3 mmbbl	18.0 mmbbl
Lineynoye (31/12/2006)	2.2 mmbbl	13.4 mmbbl	15.6 mmbbl
West Lineynoye (est.)	Not disclosed	Not disclosed	34.0 mmbbl
Reserves	**n/a**	**n/a**	**67.6 mmboe**

Source: PetroNeft Resources, Natixis Bleichroeder estimates

PETRONEFT PRODUCTION PROFILE (BOE/D)



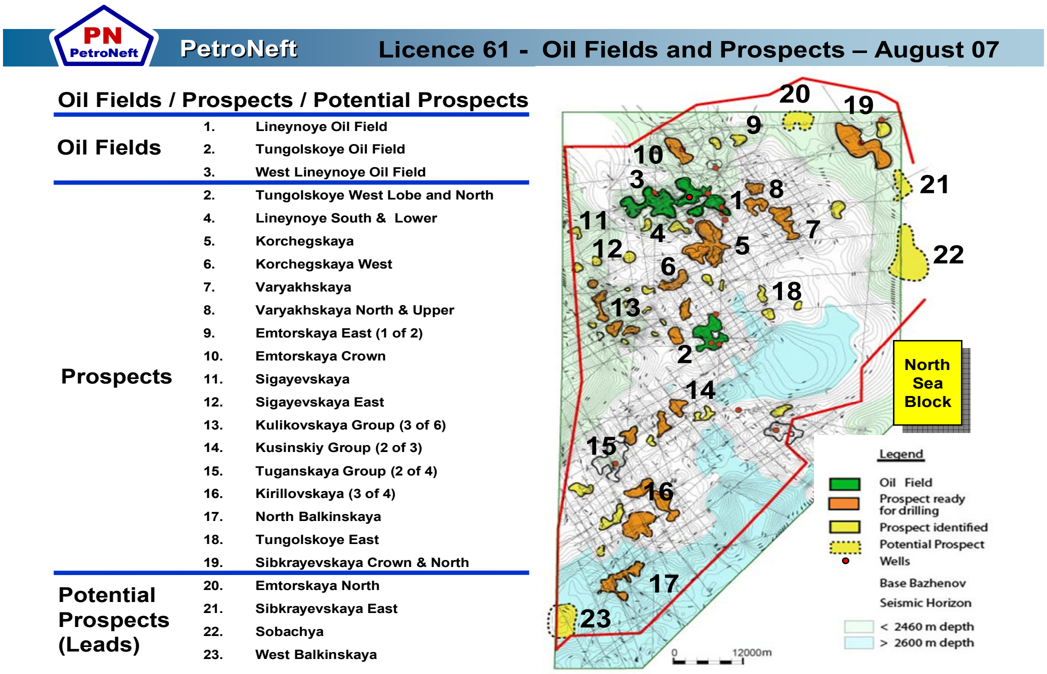
Source: Natixis Bleichroeder estimates

Exploration upside

In June 2005, PetroNeft executed an agreement with Tomskaya Geophysical Company for the reprocessing and interpretation of 1,392 kilometres of seismic data covering the northern half of Licence 61. Nine months later, a similar contract was signed for 1,262 kilometres of data located in the southern part of the block. The projects resulted in the company having a consistent database that is superior in quality to anything covering the licence previously. In addition, 515 kilometres of new seismic was acquired during the 2005/06 winter season and a further 540 kilometres last winter. As a result, the group had dispensed its obligation to shoot at least 1,000 kilometres of new seismic during the first three years of the licence term. PetroNeft has also reprocessed the data from the 14 wells previously drilled on the acreage.

Combined with the results of this year's drilling programme, PetroNeft has used this data to de-risk and select the drilling locations for next winter. PetroNeft has chosen two exploration targets, Korchegskaya and West Korchegskaya, which are located in the same fairway as Tungolskoye and Lineynoye. These prospects could add more than 50 mmbbl to PetroNeft's reserves and (we estimate) 53p/share to its net asset value between them. The company also plans to drill an additional delineation well on the West Lineynoye Oil Field to assist in the development planning. The following table and map detail the current inventory of oil fields, exploration prospects and leads. In total, these could add over 300 mmbbl or more than quintuple PetroNeft's current reserves. Clearly, the economics of any future discoveries are likely to be enhanced by the existence of the infrastructure used to develop the three existing fields whilst the distribution of these prospects and leads could allow PetroNeft to conduct farm-outs should it wish to do so in the future.

LICENCE 61 EXPLORATION PROSPECT MAP



Source: PetroNeft Resources

LICENCE 61 EXPLORATION PROSPECTS AND LEADS

Prospects and Leads	Risk	Size (mmboe)	Est. potential value ($m)	Est. potential value (p/share)
South Lineynoye	Low	2.9	9.5	2.4
Low Lineynoye	Low	3.3	10.8	2.8
Korchegskaya	Low	43.0	139.7	36.1
West Korchegskaya	Low	10.4	33.8	8.7
Varyakhskaya	Low	19.1	62.1	16.0
North Varyakhskaya	Low	6.0	19.3	5.0
Upper Varyakhskaya	Low	2.6	8.3	2.2
Emtorskaya Crown	Low	14.3	46.6	12.0
Emtorskaya North	Medium	13.8	44.8	11.6
Sigayevskaya	Low	17.4	56.7	14.6
East Sigayevskaya	Low	1.9	6.2	1.6
Kulikovskaya	Low	9.1	29.6	7.6
Kulikovskaya North	Low	8.9	28.8	7.4
Kusinskiy	Medium	5.2	16.8	4.3
Tuganskaya	Medium	10.8	34.9	9.0
Krillovskaya	Medium	20.4	66.4	17.1
Sibkrayevskaya Crown	Medium	23.3	75.8	19.6
Sibkrayevskaya East	Medium	17.2	55.9	14.4
Tungolskoye East	Medium	11.8	38.4	9.9
Sobachya	Medium	36.0	117.0	30.2
North Bakinskaya	Medium	19.9	64.8	16.7
West Bakinskaya	Medium	13.0	42.1	10.9
Total	**n/a**	**310.3**	**1008.2**	**260.2**

Source: PetroNeft, Natixis Bleichroeder estimates

FINANCIAL REVIEW

PRODUCTION GROWTH WILL DRIVE EARNINGS

With PetroNeft only listing on AIM and the Irish Stock Exchange in the second half of last year, its income statement for the 12 months to the end of 2006 was fairly meaningless. Moreover, with the company unlikely to produce any oil until sometime in 2009, the same is likely to be true for both 2007 and 2008. However, thereafter things are likely to get much more interesting and, assuming the group produces an average of 4,000 b/d from Licence 61, we expect it to generate sales of $70 million in 2009. All other things being equal, that figure should increase rapidly in 2010 and 2011 as the PetroNeft's output builds up to a plateau rate of 16,000 b/d. In the meantime, with management keeping a tight rein on general and administrative expenses, we expect the group to report relatively small losses this year and next before generating earnings of 6.8¢ in 2009.

PETRONEFT SUMMARY INCOME STATEMENT ($000)

Year-end June	2006a	2007e	2008e	2009e
Sales	25	0	0	70027
Operating profit	-1046	-2324	-2812	21779
Pre-tax profit	-993	-1728	-3870	17663
Net income	-993	-1728	-3870	13071
Earnings per share (¢)*	-0.7	-0.9	-2.0	6.8

Source: PetroNeft, Natixis Bleichroeder estimates

INVESTMENT WILL BE FUNDED BY DEBT AND EQUITY

Over the next couple of years, we expect PetroNeft's cash flow statement – and in particular the rate at which the group is spending the funds available to it – will be of greater interest to investors than the income statement. Without any production until 2009, PetroNeft will have to rely on a combination of its existing cash balances, debt, and further equity issues to fund its investment programme. Indeed, on an annual basis, we do not expect the company to be generating cash surpluses until 2010 at the earliest and we expect the total shortfall from the beginning of 2007 until the end of 2009 to be $87 million. Moreover, given that the company is unlikely to start production from Licence 61 until the second half of 2009, the peak cash deficit is likely to be slightly larger than that.

PETRONEFT SUMMARY CASH FLOW STATEMENT ($000)

Year-end June	2006a	2007e	2008e	2009e
Operating cash flow	-1292	-1823	-2112	21713
Interest & tax	53	597	-1058	-6411
Capital expenditure	-8412	-16000	-41000	-41000
Other	0	0	0	0
Surplus/deficit	-9651	-17227	-44170	-25699
Cash flow per share (¢)*	-0.9	-0.6	-1.7	8.0

* Fully diluted

Source: PetroNeft, Natixis Bleichroeder estimates

DRILLING SUCCESS SHOULD HELP FUNDING EFFORT

At the end of 2006, PetroNeft had almost $13 million in the bank and recently supplemented that when it placed 15 million new shares at a price of 50p each to raise more than $14 million net of expenses. As a result, after paying for this year's three well drilling programme and long lead items for next year's programme, we expect the company to exit 2007 with a little more than $10 million of net cash. In the absence of further acquisitions, we estimate this would leave PetroNeft in need of perhaps another $80 million to get it to first production on Licence 61 and the company will probably want some headroom over and above this figure.

Once it has an approved development plan and certified reserves, we expect PetroNeft will be able to raise debt to meet much of this requirement. Nonetheless, it is still likely that the group will come back to the stock market for substantial additional funds in due course, especially if it wants to accelerate its exploration effort. This process of raising further equity should, of course, be rendered much simpler if the group's bankers have already agreed to provide significant funds for the project and if the 2007/08 drilling programme has already met with some success.

PETRONEFT SUMMARY BALANCE SHEET ($000)

Year-end June	2006a	2007e	2008e	2009e
Fixed assets	10968	26735	67487	102448
Net current assets	12489	12472	12272	18628
Long-term liabilities	3689	611	-43810	-72056
Shareholders funds	27146	39818	35948	49019
Net debt	12872	10045	-34125	-59823
Gearing (%)	n/a	n/a	94.9%	122.0%

Source: PetroNeft, Natixis Bleichroeder estimates

THE TEAM

BOARD MEMBERS

David Golder, Non-Executive Chairman, is aged 58 and has 36 years experience in the petroleum industry. He was formerly a Senior Vice President of Marathon Oil and, after being seconded from that company, also performed at executive and director level for Sakhalin Energy Investment Company from 1996 to 1999. During that time, he was based in Moscow and managed the development of the Sakhalin II Project. Additionally, Mr. Golder managed the planning and implementation of the US$650 million development of the Piltun-Astokhskoye oil field and associated infrastructure. Mr. Golder is a member of the Society of Petroleum Engineers and has a degree in Petroleum & Natural Gas Engineering from Pennsylvania State University.

Dennis Francis, Chief Executive Officer, is aged 57 and has 35 years experience in the petroleum industry, including 30 years with Marathon Oil. After holding various international positions, in 1990, Mr. Francis became the company's USSR/FSU task force manager responsible for developing new opportunities in Russia. Marathon and its partners subsequently won the first Russian competitive tender, which was to develop the Sakhalin II Project offshore Sakhalin Island. Mr. Francis managed the progression of this project within Marathon and represented it on the board of Sakhalin Energy Investment Company. In 2003, he also managed Marathon's acquisition of the Khanty Mansiysk Oil Company. Mr. Francis is a member of the American Association of Petroleum Geologists and of the Society of Exploration Geophysicists and he has degrees in geophysical engineering and in geology from the Colorado School of Mines.

David Sanders, Executive Director, is aged 57 and acts as PetroNeft's Company Secretary and General Legal Counsel. He is an attorney of law and has over 30 years experience in the petroleum industry, including 12 years doing business in Russia. Dr. Sanders joined Marathon in 1988 and was assigned to the negotiating team for the Sakhalin II Project in Russia three years in 1991. In 1994, he was seconded as an attorney to Sakhalin Energy Investment Company in Moscow and later became the lead negotiator for Russian projects in Marathon's Business Development-Commercial & Negotiations Group. Dr. Sanders has a degree in electronics from Pennsylvania Institute of Technology, a liberal arts degree from the University of Houston and a doctorate of jurisprudence from South Texas College of Law. He is a member of the State Bar of Texas and of the American Bar Association.

Desmond Burke, Executive Director of Planning and Investor Relations, is aged 59 and has more than 30 years of experience as an exploration geologist and as an executive of publicly quoted companies in Ireland, Canada and Australia. From 1983 to 1993, he was managing director of Burmin Exploration & Development, a company that was admitted to trading on the Exploration Securities Market (ESM) of the Irish Stock Exchange in 1987. Mr. Burke became a director of Sipa Resources NL, an Australian company, following its merger with Burmin in 1993. From 1995 to 2000, he was managing director of Ormonde Mining, which was admitted to the ESM in 1996 and to the Vancouver Stock Exchange in 1998. Mr. Burke has degrees in geology, botany, and zoology from University College Dublin and a degree in mineral exploration from Imperial College London.

Paul Dowling, Chief Financial Officer, is aged 35 and is due to take up his position at the beginning of October 2007. He has 16 years experience in the areas of banking, accounting, auditing, taxation, financial reporting, corporate restructuring, corporate finance, and acquisitions/dispositions. Most recently he was a Partner in LHM Casey McGrath, a firm of Chartered Certified Accountants located in Dublin. Mr. Dowling has worked in a number of industries but has good experience in Natural Resources. He is a fellow of the Association of Chartered Certified Accountants (ACCA) and a member of the Irish Taxation Institute. He currently represents the ACCA with the Consultative Committee of Accountancy Bodies – Ireland (CCAB-I).

Thomas Hickey, Non-Executive Director, is aged 38 and has been Chief Financial Officer and a director of Tullow Oil since 2000. During this time Tullow has grown via a number of significant acquisitions and the company now has daily production of about 70,000 boe/d and a market capitalisation of about £4 billion. Prior to joining Tullow, Mr. Hickey was an Associate Director of ABN AMRO Corporate Finance (Ireland) Limited. In this role, he advised public and private companies in a wide range of industry sectors on subjects, including fund raising, stock exchange requirements, mergers and acquisitions, and floatations. Mr. Hickey is a Commerce graduate of University College Dublin and a Fellow of the Irish Institute of Chartered Accountants.

Vakha A. Sobraliev, Non-Executive Director, is aged 51 and has over 30 years experience with energy service companies and state operating units exploring for and exploiting the oil resources of the West Siberian Basin. He is a shareholder in and General Director of Tomskburneftegaz, LLC, which operates in Western Siberia and owns 15 drilling rigs plus associated support equipment and mechanical repair facilities. From 1975 to 2000, Mr. Sobraliev worked for Tomskneft and Strezhevoy Drilling Boards in various operational and financial roles, including chief engineer and chief accountant. He has degrees in mining engineering from Tomsk Polytechnic Institute and in economics from Tomsk State University.

RUSSIAN MANAGEMENT

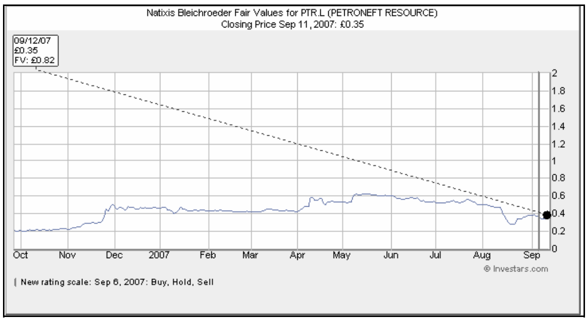
The board of PetroNeft views its Russian management team as a key differentiator for the company in terms of local credibility, access to equipment, and deal flow.

Alexey Balyasnikov, Managing Director of Stimul-T, is aged 60 and has 32 years experience in the Russian oil and gas industry. He was head of Marathon Oil’s representative office in Moscow, from 1990 to 2004. Prior to that, Mr. Balyasnikov was a senior geophysical researcher for the Moscow Research Institute. More recently he has worked as a consultant, including a stint as manager of a large due diligence project for TNK-BP in Western Siberia. Mr. Balyasnikov has a degree in geophysics from St. Petersburg University and speaks English fluently.

Alexander Frenovsky, Executive Director of Stimul-T, is aged 58 and a former general director and chief engineer of JSC Tomskneftegazgeologia. This Russian state enterprise discovered and delineated essentially all of the oil and gas fields in the Tomsk region. Mr. Frenovsky has over 34 years experience in the oil industry and has participated in the development of 15 of oil fields. He graduated from the Oil University in Ufa in 1971 with a specialisation in the drilling of oil and gas wells.

Nikolay Karapuzov, Chief Geologist and Geophysicist of Stimul-T, is aged 60 and was the chief geophysicist and geologist of JSC Tomskneftegazgeologia. He worked for this company for 35 years and directly participated in the discovery of 17 oil fields in the Tomsk region. Dr. Karapuzov graduated from Voronezh State University in 1970 with a specialisation in geophysical methods of prospecting and exploration of hydrocarbons.

TARGET PRICE HISTORY



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RATINGS DEFINITIONS (except as otherwise noted, expected performance within 12-month period from rating date):

Buy Greater than 20% increase in share price

Hold Price changes between +20% and -20%

Sell More than 20% decrease in share price

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