

Company Spotlight

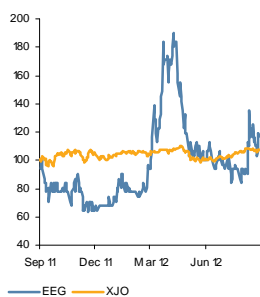
EEG120925

RBS Morgans Refiner

Price (close 10-Sep)	A\$0.18
3M high/low	A\$0.21 / 0.13
Market cap	A\$55.63m
Av (12M) turnover	A\$0.14m
Freefloat	79%
Reuters	EEG.AX
Bloomberg	EEG.AU
Net debt (cash)	A\$49.64m
3yr EPS CAGR	N/A

Source: Capital IQ, Bloomberg

ASX200 Index comp



Source: IRESS

Reported Reserves

1P Reserves	10.23 mmbob
2P Reserves	12.6 mmbob
3P Reserves	12.71 mmbob

Source: Company data

Analysts

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Empire Energy Group

Upside wrapped in red tape

Empire Energy Group (EEG) is an Australian-based oil and gas company with operations in the US and Australia. The company has producing assets in the Appalachian Basin (gas) and Central Kansas Uplift Region (oil), and prospective assets in the Utica and Marcellus areas of New York. Furthermore, EEG holds a significant frontier shale play in the MacArthur Basin, Australia. These assets present significant upside potential, but EEG must overcome legislative and regulatory hurdles before commencing work. In the US, it is unclear when/if New York will lift its moratorium on fracking; and in Australia EEG is still negotiating with the Traditional Land Owners. In our view, many shareholders are waiting for the lifting of the moratorium as a catalyst; as such patience by investors could be required (depending on the timing). In our view, patient investors could be rewarded if all approvals are given resulting in a potential valuation of \$0.34ps based on risked \$/ac values.

Company description:

Empire Energy Group (EEG) engages in the acquisition, exploration, and production of oil and natural gas. It holds interests in oil and gas fields located in Appalachia and Central Kansas Uplift, USA. In addition, it undertakes an exploration and development program of unconventional oil and gas opportunities in New York and Pennsylvania (USA) as well as the Northern Territory (Australia); and participates in a joint venture seeking conventional oil reservoirs in the Williston Basin, North Dakota. EEG is based in Sydney, Australia.

Investment view:

EEG's current producing assets are attractively hedged and provide some support to the share price. However, we see the value and upside as being tied to the regulatory decision in New York (NY) and the negotiations with traditional landowners in the Northern Territory (NT) coming to a conclusion. If the moratorium on hydraulic fracture stimulation is lifted in the NY counties of interest that EEG holds acreage in, then we see value on its oil window holdings of ~100,000 acres. We think that this would potentially be worth \$0.12/sh in the near term. With some drilling and derisking, this could potentially move toward \$1500/ac or \$0.46/sh. However prior to drilling, testing of wells to optimize completion techniques will be required. Valuing the NY Marcellus gas shale acreage and Utica holdings remains challenging at this time without more information on flow rates (as they may not be commercial in this gas price environment). If EEG's flow rates are commercial we could see further upside. Currently, Australian acreage in the NT has not been highly valued by the market. However, if negotiations with traditional landowners are finalised, we see the potential for it to be valued at \$2.50/acre. In turn this would value EEG's interest at \$0.11ps when negotiations are completed. We do note that EEG's current debt of ~\$0.15/sh may increase if development of the NY Marcellus or Utica shales commences.

Key financials

year to Jun	FY09A	FY10A	FY11A	FY12F	FY13F
Revenue (A\$m)	1.3	26.5	31.5	N/A	N/A
EBITDA (A\$m)	0.1	7.5	11.6	N/A	N/A
Net Income (A\$m)	6.2	(0.3)	(1.5)	N/A	N/A
Cash & Equivalents (A\$m)	8.4	2.7	4.4	N/A	N/A
Total Assets (A\$m)	17	114	120	N/A	N/A
Total Liabilities (A\$m)	3	83	71	N/A	N/A

1. Pre non-recurring items and post preference dividends
Accounting standard: IFRS

Source: Company data, S&P and CIQ Estimates

Empire Energy Group (EEG)

Recent Newsflow

Date	Announcement
21/08/2012	Response to ASX Price Query
31/07/2012	Quarterly Activities Report
31/07/2012	Quarterly Cash flow Report

Source: ASX

Empire Energy Group (EEG) is an oil and gas producer with operations in Appalachia (New York and Pennsylvania) and the Central Kansas Uplift (Kansas), USA. The company also has interests in significant prospective assets, including 400,000 acres of Marcellus and Utica shale formations in New York State, USA, and expansive frontier shale gas acreage in the McArthur Basin, Australia. We see significant upside in EEG's unconventional plays; but the company must overcome significant regulatory hurdles before commencing work. Empire Energy operates approximately 1,800 gas wells and 256 oil wells. Current production is ~1,400 Boe/d (36% oil).

Central Kansas Uplift – Producing Oil

EEG's landholding in the Central Kansas Uplift (CKU) is estimated to have 1P reserves of 3.6 million barrels (71% of which is proved, developed and producing) and 2P reserves of 4.3 million barrels. EEG has 254 operating well in CKU, producing 284,000 Bbl gross pa (184,000 Bbl Net pa). Well depths range from ~2,200ft-4,000ft. Historically, Kansas has been a very prolific oil and gas producing state with cumulative production exceeding 6.1 billion barrels of oil and 37.5 trillion cubic feet of gas. Current yearly production is approximately 33 million barrels of oil and 342 billion cubic feet of gas from over 60,000 wells.

The most prolific oil reservoirs are the Arbuckle (Ordovician) and Lansing-Kansas City (Pennsylvanian) formations, particularly from fields located on the CKU. Of the 31 counties in which the Arbuckle has been productive, over 70% of the production has come from 10 counties situated on the CKU in which EEG operates.

A 10 well drilling program is currently being undertaken, with the first 3 completed and producing to tank with the 4th well expected to be completed in the next 2 weeks. Approximate cost per completed well is US\$350,000. In wells drilled to date, the program has been to target the entire Arbuckle formation, as opposed to the first few feet of the formation. The concept is to get a better understanding of the geology of the Arbuckle formation and to identify closed, oil producing layers within the formation itself.

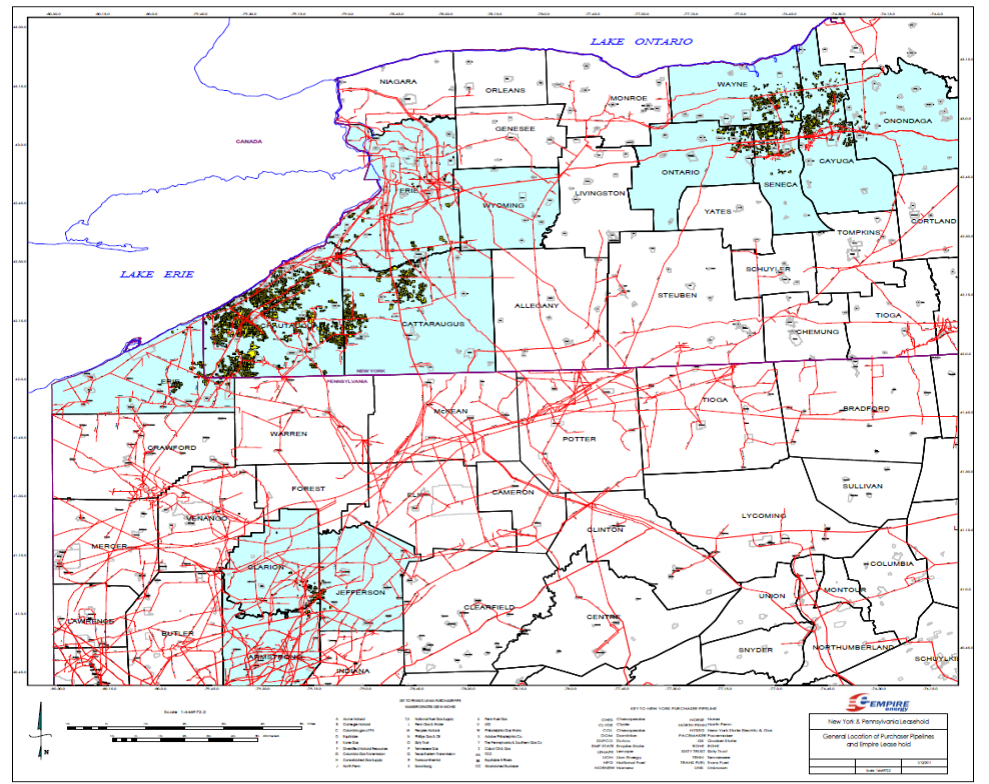
Appalachia – Producing Gas

EEG controls approximately 300,000 acres in Appalachia (Pennsylvania and New York), operating over 1,800 wells with depths ranging 3,200-4,000 feet. The assets are estimated to hold 2P reserves of 45.1 Bcf. Gross production from the assets is 2,525,000 Mcf pa (1,950,000 Mcf pa net), with net daily production for the last half at 5,340 Mcf/day. Field operations focused on reducing shrinkage from a current estimated 10% to 12% of production.

In Appalachia the focus has been based around declining natural gas prices, and implementing processes to reduce operating costs, while at the same time improving production from existing operating wells.

Current operations in Central Kansas and Appalachia may be valued at between \$0.16 and \$0.27ps based on \$/boe metrics. EEG has net debt and corporate costs of \$0.16ps on our numbers.

Chart 1 : Appalachia

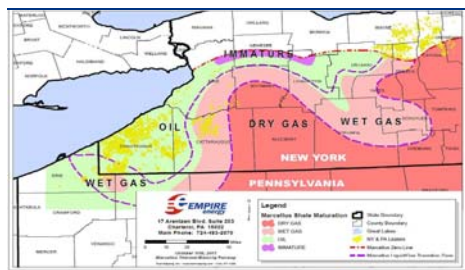


Source: Company Data

Contingent Unconventional Plays – Playing the Politics

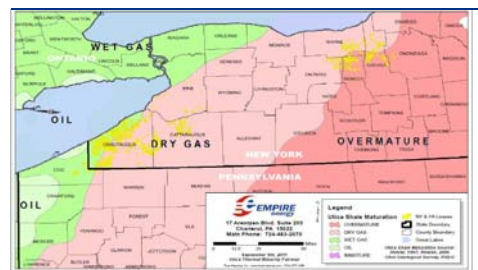
EEG is undertaking a detailed geological and engineering review of its 300,000+ acres held in western New York and north western Pennsylvania. The acreage covers a number of oil and gas bearing formations. In both States recent horizontal wells targeting liquid rich shales have been successful and recent announcements by third parties confirm the development of further gas processing plants. Geologists estimate that the entire Marcellus Shale formation may contain up to 489 trillion cubic feet of natural gas throughout its entire extent. It is not yet known how much gas will be commercially recoverable from the Marcellus in New York.

Chart 2 : Marcellus Shale



Source: Company presentation

Chart 3 : Utica Shale



Source: Company presentation

Questions have been raised about possible environmental and community impacts. Most concerns are related to water use and management, and the composition of the fluids used for fracturing the shale. A moratorium has blocked fracking in New York since 2008, and Governor Andrew Cuomo’s administration is expected to announce before the end of this year whether drilling can proceed. EEG has recently employed an experienced landman to commence

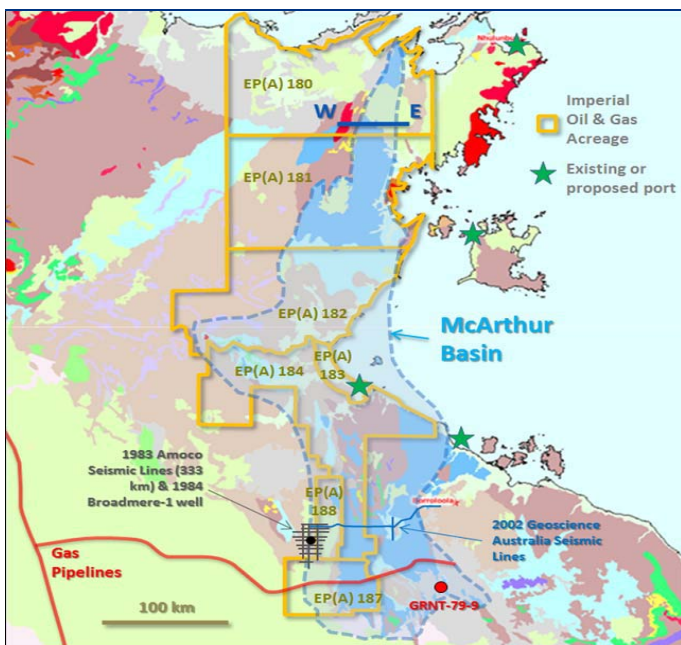
management of the Group's extensive New York land holdings in expectation of the lifting of the fracking moratorium.

In our view, the acreage in the oil window is the valued acreage in the near term. EEG has 100,000 acres in the potential oil window. Other plays have gone from \$200/ac to \$2000/ac after some drilling and derisking has taken place. Once production has been established, significant further increases occur on acreage valuations. At \$400/ac, EEG's oil window acreage could be worth \$0.12/ac and at \$2000/ac, it could be worth \$0.61ps.

Closer to home - McArthur Basin Shale Gas Play

In early 2010 EEG identified the McArthur Basin as having attractive potential for shale oil and gas, and secured 7 exploration licence applications in the McArthur Basin, Northern Territory. Imperial Oil & Gas (a wholly owned subsidiary of EEG) holds a 100% interest in 14 million acres of prospective shale gas exploration acreage in the Proterozoic McArthur Basin (Exploration Permit Applications EP (A) 180 – 188). All the permits constitute high risk/high return frontier plays at very low historic exploration maturity.

Chart 2 : McArthur Basin acreage



Source: Company Presentation

Chart 3 : GRNT-79-9 ignited for ~6 months



Source: Amour Energy

The McArthur Basin is a petroleum frontier basin at low exploration maturity and no prior shale gas activity. It is an inverted Proterozoic basin with thick carbon-rich black shale petroleum source rocks also mined for Pb-Zn. There are direct indications of oil & gas in the basin and existing gas pipelines. Analogue shale gas basins suggest Imperials acreage contains in the order of 24 Tcf of potential recoverable resources.

The target gas resource is in 1,640 million year old Palaeo-Proterozoic organic-rich black shales of the Barney Creek Formation and equivalents, proven gas-prone in the South McArthur Basin. In particular the 1979 mineral core hole GRNT-79-9 ignited and sustained a 6m high yellow smoky gas flare for approximately 6 months producing an estimated 0.5 Bcf at 6mmscf/d. Gas analysis revealed C1-C7. In addition oil bleeds are common in cores and hence shale oil offers secondary potential.

Consistent with a frontier basin the regional extent, quality, and thermal maturity of the Barney Creek & Velkerri Formation shales have yet to be adequately constrained due chiefly to past

focus on mineral exploitation from the former. Potential gas-prone sweet spots are yet to be delineated and hence strategy of acquiring a very large initial acreage position.

Landowner negotiations continue for the 14.5 million acres of shale formations secured onshore, in the MacArthur Basin, Northern Territory, Australia. It is expected that 3 licences will be finalised in the short term. EEG just received a 2 year extension on its holdings in order to continue negotiations. In May geological studies commenced on the above mentioned licence application areas to identify the most prospective areas for shale and gas drilling.

Large acreage positions in the northern territory have traded in the last year. AJQ operates in the area, as well as Hess/Falcon nearby. At \$2.50/ac, EEG's position would be valued at 0.11ps.

Hedging and Funding arrangements

EEG implemented a US\$100m credit facility with Macquarie Bank Limited in early 2008 for the sole purpose of acquiring and developing oil and gas assets in the USA. This facility has since been increased to US\$150m. The Group continues to negotiate potential acquisitions to identify additional upstream assets to integrate into existing operations and to reach a production milestone of +5,000 Boe/d. The EEG acquisition model metric is to target a 5 year debt repayment from project cash flows.

Due to the leverage growth model implemented by EEG, an aggressive hedging strategy is adopted to ensure commodity risk is eliminated over the period that a major portion of debt financing is repaid.

The portion of production hedged will be naturally reduced as drill bit production comes on line. The following table summarizes current hedging in place based on NYMEX – Henry Hub and WTI Contracts.

Chart 4 : EEG Hedging arrangements

Year	Est. Net mmBtu	Hedged mmBtu	%	Average \$/mmBtu	Est. Net Bbl	Hedged Bbl	%	Average \$/Bbl
2012	1,050,000	735,576	70.1%	\$6.07	124,081	59,340	47.8%	\$90.00
2013	2,000,000	1,398,716	69.9%	\$5.97	149,298	113,160	75.8%	\$90.00
2014	1,850,000	1,329,488	71.9%	\$5.91	141,058	105,120	74.5%	\$90.00
2015	1,650,000	1,272,488	77.1%	\$5.45	133,280	98,160	73.6%	\$90.00
2016	1,440,000	600,000	41.7%	\$4.49				
Total	7,990,000	5,336,268	66.8%	\$5.68	547,717	375,780	68.6%	\$90.00

Source: EEG

Investment view

EEG's current producing assets are attractively hedged and provide some support to the share price. However, we see the value and upside as being tied to the regulatory decision in New York (NY) and the negotiations with traditional landowners in the Northern Territory (NT) coming to a conclusion. If the moratorium on hydraulic fracture stimulation is lifted in the NY counties of interest that EEG holds acreage in, then we see value on its oil window holdings of ~100,000 acres. We think that this would potentially be worth \$0.12/sh in the near term. With some drilling and derisking, this could potentially move toward \$1500/ac or \$0.46/sh. However prior to drilling, testing of wells to optimize completion techniques will be required. Valuing the NY Marcellus gas shale acreage and Utica holdings remains challenging at this time without more information on flow rates (as they may not be commercial in this gas price environment). If EEG's flow rates are commercial we could see further upside.

Australian acreage in the NT has not been highly valued by the market. However, as negotiations continue with traditional landowners and are finalised, we see the potential for the EEG acreage to be valued at \$2.50/acre. In turn this would value EEG's interest at \$0.11ps when negotiations are completed. However, we do note that EEG's current debt of ~\$0.15/sh may increase if development of the NY Marcellus or Utica shales commences.

Appendix 1: Leadership profile

Table 1 : Board of directors and management team

Name	Position	Background
Bruce McLeod	Executive Chairman	Mr. Bruce William McLeod, BSc (Maths), M. Comm.(Econ) has been the Executive Chairman and Chief Executive Officer of Empire Energy Group Ltd since 1997 (formerly Imperial Corporation Limited) and a Director since May 21, 1996. Mr. McLeod has had extensive experience in the Australian Corporate and Resource Capital markets. Over 20 years he has been involved in raising debt and equity capital for a number of property projects and companies, as well as the takeover and rationalisation of listed and unlisted companies. From 1983 to 1987, at a subsidiary of Bank of America Inc, where he ultimately served as an Executive Director of BA Australia Ltd., responsible for the financial and capital markets operations. Since 1980, he served in the securities broking industry in New Zealand before moving to Australia.
David Sutton	Non Executive Director	Mr. David Henry Sutton, B.Com, ASA, ACIS served as Chief Executive Officer of Sinovus Mining Limited from October 22, 2010 to July 22, 2011. Mr. Sutton was a Partner of several stock exchange member firms including Clarke & Co., and Macnab Clarke. He is an affiliate of the Australian Stock Exchange Limited, with many years experience in share broking and investment banking. He has many years experience in stock broking and investment banking. He serves as the Executive Chairman of WHI Securities Pty Limited.
Kevin Torpey	Non Executive Director	Mr Torpey has over the last 40 years been involved in the development of many diverse major projects involving oil, iron ore, aluminium, nickel, lead/zinc, uranium, magnesite, coal and gold, located in Australia, Ireland and Indonesia. Most of these projects have been associated with major companies such as Consolidated Goldfields, EZ Industries, Alcan, International Nickel, Tara Minerals Limited (Ireland), Noranda, Denison Mines (Canada), Toyota and Mitsubishi. He is currently a Director of Latrobe Magnesium Limited and Camberwell Coal Pty Limited.
David Hughes	Company Secretary	Mr Hughes has held similar positions with other listed companies for over 20 years. He is currently acting as Company Secretary or Joint Company Secretary for a number of other listed public companies.
Dr John Warburton	Director & CEO Imperial Oil & Gas Pty Ltd	Dr Warburton was appointed as an advisor to the Company in February 2010 and is a director and Chief Executive Officer to the Company's wholly owned subsidiary Imperial Oil and Gas Pty Ltd. John will be responsible for the development of the Company's extensive acreage in Australia new shale oil and gas targets once identified. A Geoscientist by profession, John has 28 years of technical and leadership experience in International Petroleum E&P including 11 years with BP and 4 years as General Manager Exploration & New Business for LASMO-ENI in Pakistan. John is a Director of Sydney based Petroleum Exploration Business Consultancy Insight Exploration and he maintains a strong global executive network.

Source: Company data

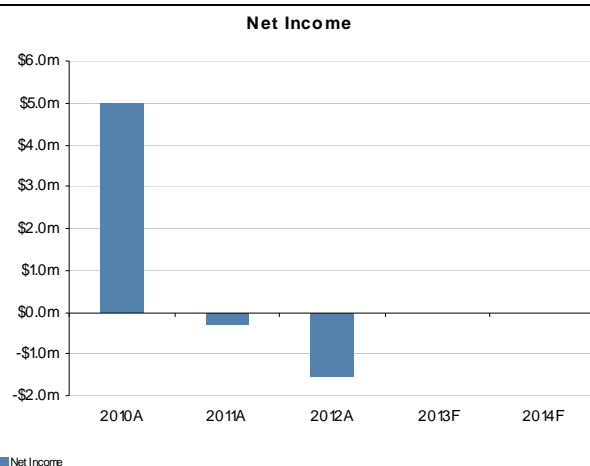
Top 3 Institutional Holders

Name	% Held
Macquarie Group, Ltd., Banking & Securities Investments	15.76%
Imperial Investment Group Pty Ltd.	4.99%

Source: Capital IQ

EEG – financial summary

Year to 30 Jun (A\$m)	AIFRS	AIFRS	AIFRS	AIFRS	AIFRS
Income statement	2010A	2011A	2012A	2013F	2014F
Total Revenues	10	27.1	32.3	0.0	0.0
Cost Of Revenues	0.2	13.3	15.3	NA	NA
Gross Profit	0.9	13.9	17.0	NA	NA
Selling General & Admin Exp.	0.9	6.2	4.9	NA	NA
R & D Exp.	0.0	0.0	0.0	NA	NA
Other Operating Expenses	0.0	5.7	6.2	NA	NA
Operating Income	-0.1	2.0	6.0	0.0	0.0
Net Interest Exp.	0.1	-4.0	-5.9	0.0	0.0
EBT Excl Unusual Items	0.3	-2.0	-0.6	0.0	0.0
Total Unusual Items	4.7	-0.1	0.8	NA	NA
EBT Incl Unusual Items	5.0	-2.1	0.2	NA	NA
Income Tax Expense	0.0	-2.9	1.6	0.0	0.0
Earnings from Cont. Ops.	5.0	0.8	-1.4	0.0	0.0
Net Income	5.0	-0.3	-1.6	0.0	0.0
NI to Common Incl Extra Items	5.0	-0.3	-1.6	0.0	0.0
NI to Common Excl Extra Items	5.0	-0.3	-1.6	0.0	0.0
Basic EPS	0.0	0.0	0.0	0.00	0.00



Cash flow statement	2010A	2011A	2012A	2013F	2014F
Net Income	5.0	-0.3	-1.6	0.0	0.0
Depreciation & Amort., Total	0.2	5.7	6.0	0.0	0.0
Change in Working Capital	-0.3	-4.8	-2.5	NA	NA
Cash from Ops.	-0.6	2.7	4.5	0.0	0.0
Capital Expenditure	0.0	-12.6	-3.2	0.0	0.0
Cash from Investing	11.4	-63.3	-3.2	NA	NA
Total Debt Issued	0.0	84.4	0.3	NA	NA
Total Debt Repaid	-5.1	-27.2	-15.0	NA	NA
Issuance of Common Stock	1.1	0.0	16.5	NA	NA
Repurchase of Common	0.0	0.0	0.0	NA	NA
Issuance of Pref. Stock	0.0	0.0	0.0	NA	NA
Repurchase of Preferred	0.0	0.0	0.0	NA	NA
Total Dividends Paid	0.0	0.0	0.0	NA	NA
Cash from Financing	-4.1	57.2	0.7	NA	NA
Net Change in Cash	6.7	-2.7	1.8	NA	NA
Cash Interest Paid	0.5	2.4	3.6	NA	NA
Cash Taxes Paid	0.0	0.2	2.3	NA	NA

Balance sheet	2010A	2011A	2012A
Total Cash & ST Investments	6.8	2.7	4.4
Total Receivables	0.2	3.8	6.1
Inventory	0.0	0.6	0.6
Other Current Assets	0.0	2.2	4.7
Total Current Assets	7.0	9.3	15.8
Net Property, Plant & Equipment	2.2	103.2	100.3
Long-term Investments	3.7	0.9	0.9
Other Long-Term Assets	1.1	3.1	6.1
Total Assets	14.0	116.5	123.2
Accounts Payable	0.2	3.3	3.8
Current Portion of Long Term Debt	2.4	0.0	0.0
Curr. Port. of Cap. Leases	0.0	0.2	0.1
Other Current Liabilities	0.2	70.4	55.4
Total Current Liabilities	2.8	74.0	59.4
Long-Term Debt	0.0	0.0	0.0
Capital Leases	0.0	0.1	0.1
Other Non-Current Liabilities	0.0	10.5	13.7
Total Liabilities	2.8	84.6	73.1
Total Pref. Equity	0.0	0.0	0.0
Total Common Equity	11.2	29.6	48.3
Minority Interest	0.0	2.3	1.7
Total Liabilities And Equity	14.0	116.5	123.2

Multiples	2010A	2011A	2012A	2013F
TEV / Revenue	6.4x	5.9x	2.2x	#DIV/0!
TEV / EBITDA	NM	23.2x	7.1x	#DIV/0!
TEV / EBIT	NM	NM	14.7x	#DIV/0!
P / E	2.2x	1.8x	NM	NA
P / BV	0.8x	0.5x	0.7x	NA

Summary Ratios	2010A	2011A	2012A
Profitability			
Return on Assets	-0.4%	0.0%	3.1%
Return on Capital	-0.4%	0.0%	3.7%
Return on Equity	46.7%	0.0%	-3.5%
Margin Analysis			
Gross Margin	83.8%	51.0%	52.7%
EBITDA Margin	10.8%	28.2%	36.9%
Net Income Margin	480.5%	-1.2%	-4.8%
Short-Term Liquidity			
Current Ratio	251.5%	12.6%	26.7%
Quick Ratio	250.5%	8.8%	17.8%
Avg. Days Sales Outstanding	5628.3%	0.0%	5123.5%
Avg. Days Inventory Outstand	0.0%	0.0%	1472.9%
Long-Term Solvency			
Total Debt / Equity	22.3%	212.9%	108.1%
Total Debt / Capital	18.3%	68.0%	51.9%
EBITDA / Interest Expense	23.1%	190.7%	201.2%
(EBITDA-CAPEX) / Interest E	215% NM		146.7%
Total Debt / EBITDA	2235.9%	886.6%	452.9%

Source: Company data, RBS Morgans forecasts

QUEENSLAND

BRISBANE	(07) 3334 4888
BUNDABERG	(07) 4153 1050
CAIRNS	(07) 4222 0555
CALOUNDRA	(07) 5491 5422
CAPALABA	(07) 3245 5466
CHERMSIDE	(07) 3350 9000
EDWARD STREET	(07) 3121 5677
EMERALD	(07) 4988 2777
GLADSTONE	(07) 4972 8000
GOLD COAST	(07) 5581 5777
IPSWICH	(07) 3202 3995
MACKAY	(07) 4957 3033
MILTON	(07) 3114 8600
NOOSA	(07) 5449 9511
REDCLIFFE	(07) 3897 3999
ROCKHAMPTON	(07) 4922 5855
SPRING HILL	(07) 3833 9333
SUNSHINE COAST	(07) 5479 2757
TOOWOOMBA	(07) 4639 1277
TOWNSVILLE	(07) 4725 5787
YEPPON	(07) 4939 3021

NEW SOUTH WALES

SYDNEY	(02) 8215 5055
ARMIDALE	(02) 6770 3300
BALLINA	(02) 6686 4144
BALMAIN	(02) 8755 3333
CHATSWOOD	(02) 8116 1700
COFFS HARBOUR	(02) 6651 5700
GOSFORD	(02) 4325 0884
HURSTVILLE	(02) 9570 5755
MERIMBULA	(02) 6495 2869
NEUTRAL BAY	(02) 8969 7500
NEWCASTLE	(02) 4926 4044
NEWPORT	(02) 9998 4200
ORANGE	(02) 5310 2111

PARRAMATTA	(02) 9615 4500
PORT MACQUARIE	(02) 6583 1735
SCONE	(02) 6544 3144
SYDNEY – LEVEL 9	(02) 8215 5000
SYDNEY – LEVEL 33	(02) 8216 5111
SYDNEY – MACQUARIE STREET	(02) 9125 1788
SYDNEY – REYNOLDS EQUITIES	(02) 9373 4452
WOLLONGONG	(02) 4227 3022

ACT

CANBERRA	(02) 6232 4999
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VICTORIA

MELBOURNE	(03) 9947 4111
BERWICK	(03) 8762 1400
BRIGHTON	(03) 9519 3555
CAMBERWELL	(03) 9813 2945
CARLTON	(03) 9066 3200
FARRER HOUSE	(03) 8644 5488
GEE LONG	(03) 5222 5128
RICHMOND	(03) 9916 4000
SOUTH YARRA	(03) 9098 8511
TRARALGON	(03) 5176 6055
WARRNAMBOOL	(03) 5559 1500

WESTERN AUSTRALIA

PERTH	(08) 6462 1999
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SOUTH AUSTRALIA

ADELAIDE	(08) 8464 5000
NORWOOD	(08) 8461 2800

NORTHERN TERRITORY

DARWIN	(08) 8981 9555
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TASMANIA

HOBART	(03) 6236 9000
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