EUROPEAN GAS LIMITED

RESEARCH NOTE

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Cost Measures Take Effect

Investment Summary

- **Operational improvements result in production increase for the quarter.** Production was up 13% to 111,167MWh (0.42PJ) due to a number of operational improvements towards the end of the quarter including handover of Avion site management plus maintenance and expansion of gas injection facilities and adjustment of gas networks resulting in a greater injection capacity. The above improvements are likely to result in lower operating costs and greater production capacity going forward.

- **Cost management focus results in positive cash flow for the quarter.** Operational improvements and corporate cost initiatives initiated in the December Q, resulted in a marginally improved final cash position of €3.15m.

- **High gas prices to hit a low in June Q.** Gas prices held up for the March Q at an average of 23.4€/MWh (A$11.80/GJ) but are likely to fall to 15.50€/MWh (A$7.80/GJ) for the June Q. Further cost management will be prudent to maintaining profitability in a lower price environment.

- **70% expansion of CBM resources.** During the quarter the company completed a CBM contingent resource estimate for the recently granted Poissonniere Extension permit, resulting in a total 8150bcf across Gazonor on a 3C basis.

- **Expansion pre-feasibility studies ongoing.** EPG continued studies into an expansion of operations at Gazonor and potential conversion to power generation in order to reduce seasonality of earnings and increase revenue. These are expected to be completed this quarter.

- **Exploration and development expenditure on hold.** Exploration and development of EPG's assets is on hold pending discussions with several interested parties into potential joint venture arrangements. **We maintain our HOLD recommendation pending an outcome that would facilitate growth and realisation of EPG's large resource base.**

1 May 2009		
12mth Rating		**HOLD**
Price	A$	0.13
Target Price	A$	0.13
12m Total Return	%	4.0
RIC: **EPG.AX**		BBG: **EPG AU**
Shares o/s	m	199.2
Free Float	%	100.0
Market Cap.	A$m	24.9
Net Debt (Cash)	A$m	-81.9
Net Debt/Equity	%	na
3m Av. D. T'over	A$m	0.04
52wk High/Low	A$	0.80/0.00
2yr adj. beta		1.00
Valuation:		
Methodology		DCF
Value per share	A$	0.13

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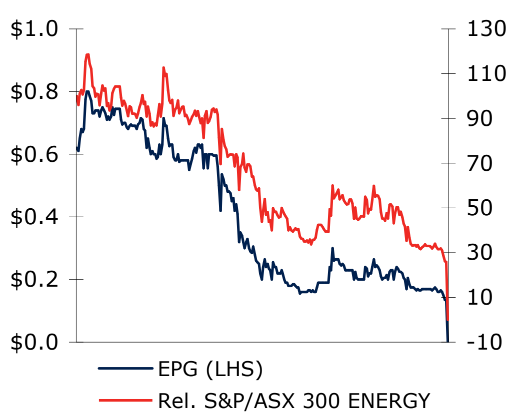
Year End June 30	2007A	2008A	2009F	2010F	2011F
A$					
Reported NPAT ($m)	(1.5)	(6.2)	(6.1)	(2.7)	0.4
Recurrent NPAT ($m)	(1.5)	(6.2)	(6.1)	(2.7)	0.4
Recurrent EPS (cents)	(0.8)	(3.1)	(3.1)	(1.3)	0.2
EPS Growth (%)	na	na	na	na	na
PER (x)	(16.1)	(4.0)	(4.1)	(9.4)	73.6
EBITDA ($m)	(1.5)	(1.6)	0.4	4.3	9.4
EV/EBITDA (x)	(16.4)	(50.0)	212.4	21.7	11.0
Capex ($m)	0.0	0.2	0.0	7.1	0.2
Free Cashflow	(7.8)	(7.9)	(11.3)	(5.8)	1.8
FCFPS (cents)	(3.9)	(4.0)	(5.7)	(2.9)	0.7
PFCF (x)	(3.2)	(3.1)	(2.2)	(4.3)	17.1
DPS (cents)	0.0	0.0	0.0	0.0	0.0
Yield (%)	0.0	0.0	0.0	0.0	0.0
Franking (%)	0.0	0.0	0.0	0.0	0.0

12 Month Share Price Performance



Performance %	1mth	3mth	12mth
Absolute	0.0	10.8	-73.7
Rel. S&P/ASX 300	4.6	16.7	-56.0

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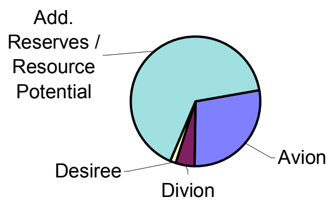
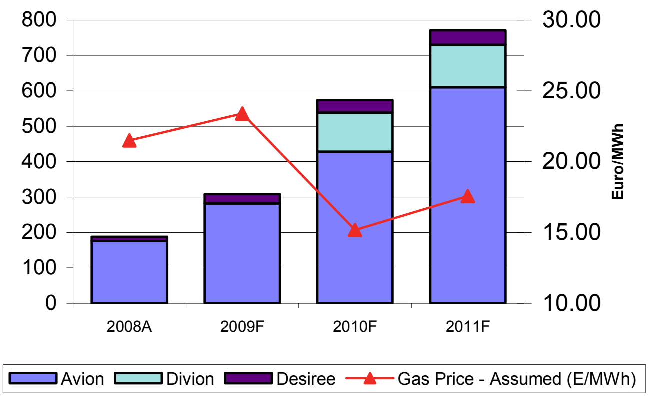
European Gas (EPG)		$0.13	
Valuation	**A$m**		**A$/sh**
Avion	54.28		0.27
Divion	8.96		0.04
Desiree	2.79		0.01
Add. Reserves / Resource Potential	127		0.64
Corporate	(20)		(0.10)
Cash	6		0.03
Debt	(76)		(0.38)
Total @ 10% Discount Rate	**104**		**0.52**
Price Target			**0.13**

Price Target Sensitivity	-10%	0%	+10%
Gas Price Sensitivity (A$/sh)	0.46	0.52	0.58
Exchange Rate Sensitivity (A$/sh)	0.52	0.52	0.52

Valuation Summary of Operating Assets



Production Summary (GWh/year)



Reserves

Reserves - Net EPG	Oil/Cond (mmbbl)	Gas (PJ)	Total (mboe)
Gazonor			
1P	0.0	49.0	8.2
2P	0.0	140.0	23.3
3P	0.0	380.0	63.3

Directors

Name	Position
Anthony McClure	Managing Director
Alan Flavelle	Executive Director
Terence Willsteed	Non-Executive Director
Michael Atkinson	Non-Executive Director
Gauthier De Potter	Non-Executive Director
Mark E Pitts	Company Secretary

Substantial Shareholders	Shares (m)	%
Ward Ferry Management Ltd	12.1	6.1
Anglo Pacific Group	10.1	5.1
Henderson Global Investors	10.1	5.1

Year End June 30

Commodity Assumptions	2008A	2009F	2010F	2011F
A$:US$	0.90	0.71	0.67	0.70
A$:Euro	1.65	1.94	1.97	1.87
Crude Oil - WTI (USD/bbl)	96.97	65.44	57.50	77.50
Gas Price - Assumed (E/MWh)	21.50	23.41	15.19	17.56
Gas Price - Assumed (A$/MWh)	35.40	44.98	29.88	32.85

Production Summary	2008A	2009F	2010F	2011F
Avion (PJ)	0.6	0.9	1.5	2.3
Divion (PJ)	0.0	0.0	0.4	0.4
Desiree (PJ)	0.0	0.1	0.1	0.1
Total (PJ)	**0.6**	**1.0**	**2.1**	**2.9**
Avion (GWh)	176.3	282.1	428.4	609.9
Divion (GWh)	0.0	0.0	110.0	120.1
Desiree (GWh)	11.1	26.1	35.0	40.2
Total (GWh)	**187.4**	**308.2**	**573.5**	**770.2**

Profit & Loss (€$m)	2008A	2009F	2010F	2011F
Sales Revenue	**3.7**	**8.3**	**8.9**	**13.5**
Other Income	1.0	0.1	0.1	0.0
Operating Costs	2.1	5.0	4.7	6.4
Exploration Exp.	0.0	0.0	0.0	0.0
Corporate/Admin	3.6	3.2	2.0	2.1
Royalty	0.0	0.0	0.1	0.1
EBITDA	**(1.0)**	**0.2**	**2.2**	**5.0**
Depn & Amort	1.6	1.1	1.7	2.4
EBIT	**(2.6)**	**(0.9)**	**0.5**	**2.6**
Interest	1.4	2.2	1.9	2.3
Operating Profit	**(4.0)**	**(3.1)**	**(1.3)**	**0.3**
Tax expense	(0.2)	(0.0)	0.0	0.1
Minorites	0.0	0.0	0.0	0.0
Discontinued Operations	0.0	0.0	0.0	0.0
NPAT	**(3.8)**	**(3.1)**	**(1.3)**	**0.2**
Normalised NPAT	**(3.8)**	**(3.1)**	**(1.3)**	**0.2**

Cash Flow (€$m)	2008A	2009F	2010F	2011F
Adjusted Net Profit	(3.8)	(3.1)	(1.3)	0.2
+ Interest/Tax/Expl Exp	1.4	2.2	1.9	2.3
- Interest/Tax/Expl Inc	4.9	7.3	1.5	4.0
+ Depn/Amort	1.6	1.1	1.7	2.4
+/- Other	1.0	1.3	0.0	0.0
Operating Cashflow	**(4.7)**	**(5.8)**	**0.7**	**1.1**
- Capex (+asset sales)	0.1	0.0	3.6	0.1
- Working Capital Increase	0.0	0.0	0.0	0.0
Free Cashflow	**(4.8)**	**(5.8)**	**(2.9)**	**1.0**
- Dividends (ords & pref)	0.0	0.0	0.0	0.0
+ Equity raised	0.1	0.0	0.0	0.0
+ Debt drawdown (repaid)	36.2	0.0	0.0	0.0
+ Other	(25.7)	0.1	0.0	0.0
Net Change in Cash	**5.8**	**(5.7)**	**(2.9)**	**1.0**
Cash at End Period	8.8	3.1	0.2	1.1
Net Cash/(Debt)	(25.6)	(32.1)	(35.0)	(37.5)

Balance Sheet (€$m)	2008A	2009F	2010F	2011F
Cash	8.8	3.1	0.2	1.1
Total Assets	62.1	61.3	60.7	61.3
Total Debt	34.4	35.2	35.2	38.6
Total Liabilities	38.7	41.3	42.1	42.5
Shareholders Funds	23.4	20.0	18.6	18.8
Ratios				
Net Debt/Equity (%)	109.2	160.9	188.3	199.2
Interest Cover (x)	na	na	0.3	1.1
Return on Equity (%)	na	na	na	1.2

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