Armour Energy Limited

Update Report

Kincora steadily progressing

Energy exploration & production

Armour Energy Limited (AJQ.ASX) is a junior energy producer and explorer with assets across northern, southern and eastern Australia. The company has been listed on the ASX since April 2012. The opportunity set for Armour through FY21 has the capacity to materially reshape the company financially by delivering cash flow growth, reducing debt and progressing a range of exploration options. Although significant exploration drilling may not occur until the end of CY21 and into 2022, the company is likely to be in a stronger position to work its assets at its own pace and to its own plan. We will be looking for delivery of the Kincora production growth plan which aims to more than double production, to 20TJd and growing over the next 18-24 months.

Business model

Armour Energy is a junior oil and gas company holding a production base with expansion options; and an extensive exploration portfolio across three Australian states, dominantly focussed on exploring for gas. The portfolio consists of exploration plays, reflecting a mix of moderate risk and early exploration stage with transformational potential. The company is looking to leverage its production growth plan at Kincora to repair its balance sheet and service a more aggressive exploration strategy, without recourse to equity markets. Financing is always a concern at the small end and the company's high working interests provide options through partnering.

Surat well activity is progressing, rationalising exploration assets adds working capital (that's a good thing)

COVID issues continue to impact the industry, in this case the timing of the Surat Basin production enhancement activity. As recently reported the work programme is approaching completion, albeit activity has spilt over into the early part of 2021. Two wells have been connected and are beginning to be evidenced in daily gas output data, whilst installations on the Myall Creek wells should be in the commissioning phase. We expect to see continuing improvement in gas production although the target rate of up to 20TJd by may take longer to deliver due to these outside factors. The company has monetised its farm-out deal with Santos over a suite of South Nicholson Basin permits. Transferring its nominal (remaining) 30% interest in the portfolio for $12.25mn including the ATP 1087 area which contains the Egilabria gas discovery, whilst retaining adjacent ATP 1107 application area. Armour continues to hold a significant acreage position in Northern Australia through the Northern Territory.

Valuation – increased overall but reduced on a per share basis

Valuing early phase exploration and even production growth assets is a subjective exercise. We base our indicative valuation on risk-weighted development scenarios and typical unit NPV values across a range of prices and resource outcomes. Where appropriate we apply discretionary probability weightings to pricing, volume and success factors, which we believe are reasonable given the commercial operating environment and available data. On asset value and issued capital adjustments, we have made minor adjustments to our NAV and assign a risked valuation of $131m (10cps) to AJQ (previously $118mn/13cps). **The reference share price (5.5cps) would suggest the market is continuing to discount the production growth and transformational gas opportunities, likely on financing and corporate risks which should be somewhat alleviated by the Santos deal.** The company has a number of deliverable outcomes, particularly pertaining to Kincora production expansion that have the potential to re-rate market sentiment and crystallise asset values as ascribed.

19th January 2021

Share details

ASX Code	AJQ
Share price (18 Jan)	$0.055
Market Capitalisation	$75.33M
Shares on issue	1,276M
Cash (as at 30-Sep)	$5.6M
Free Float	~69%

Share performance (12 months)

Upside Case

- Above expectation results from Kincora gas growth programme…more gas, higher price, lower capex
- Northern Australia success and securing a farm-in partner for the NT assets. Referred success from regional exploration would crystallise value
- Success opens alternate financing options, improves the balance sheet and restricts dilution

Downside Case

- Gas growth is not delivered to expectation
- Current operating environment persists and all projects slow down
- Senior Secure Amortising Notes covenants require additional equity capital or asset divestment

Board of Directors

Brad Lingo	CEO
Nick Mather	Executive Chairman
Stephen Bizzell	Non-Executive Director
Roland Sleeman	Non-Executive Director
Eytan Uliel	Non-Executive Director

Company contacts

Brad Lingo (CEO) +61 7 3303 0620

blingo@armourenergy.com.au

RaaS Advisory contacts

Andrew Williams +61 417 880 680
andrew.williams@raasgroup.com

Finola Burke +61 414 354 712
finola.burke@raasgroup.com

Surat (Kincora) work programme slowed by weather and COVID

The initial stimulation and completion work programme on the Surat production enhancement campaign began in 4Q20 with three wells - Horseshoe-2, Horseshoe-4 and Warroon-1.

As a result of COVID travel restrictions the campaign, which was scheduled to be completed around end-2020, will spill over into early 2021 with the Horseshoe-2 well expected to commence post-stimulation evaluation in January.

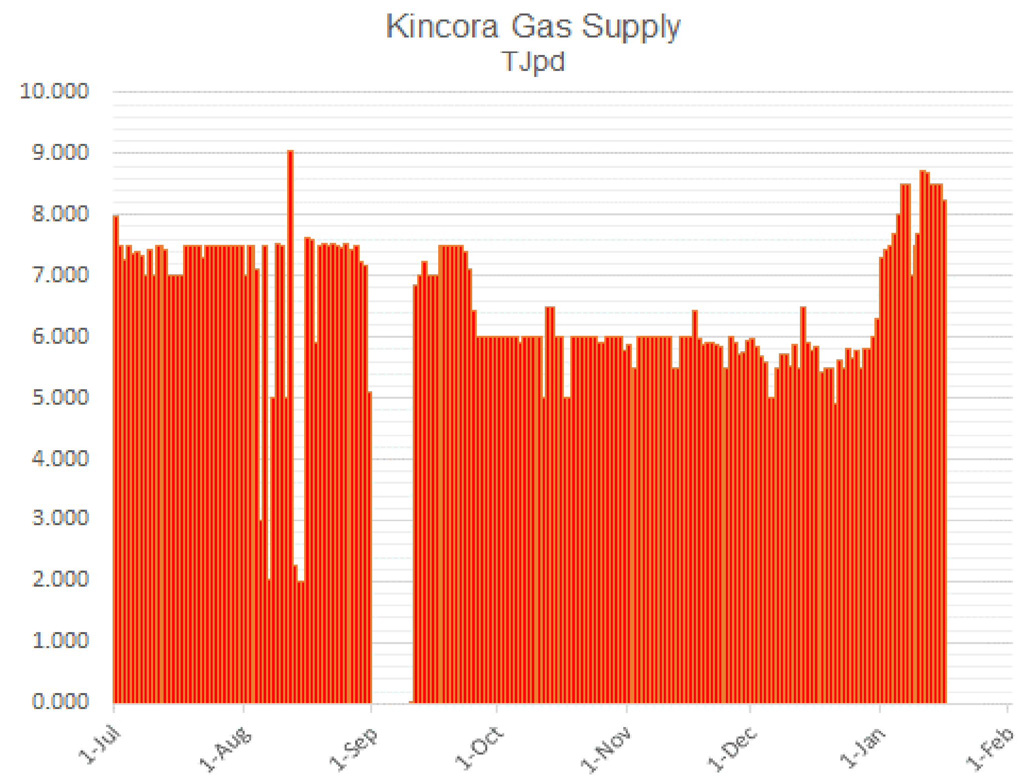
Results to date have been significantly positive with the definition and proving up of a **new, liquids rich pay zone** in the field in the Rewan Formation.

New zones provide growth opportunities at relatively low cost and can deliver significant upside through higher production rates, increased reserves and extended field life. The liquids rich nature of the gas can drive higher operating margins, particularly as in general, gas liquids are brought to surface as a by-product of gas production at marginal operating cost.

However, we do note that the high liquids yields at Kincora will likely require artificial lift (down-hole pumps). With production currently constrained by well deliverability, the company is conducting a series of artificial lift projects.

As of late December, the Warroon-1 and Horseshoe-4 wells had been connected into the field network and were still in a clean-up/evaluation phase.

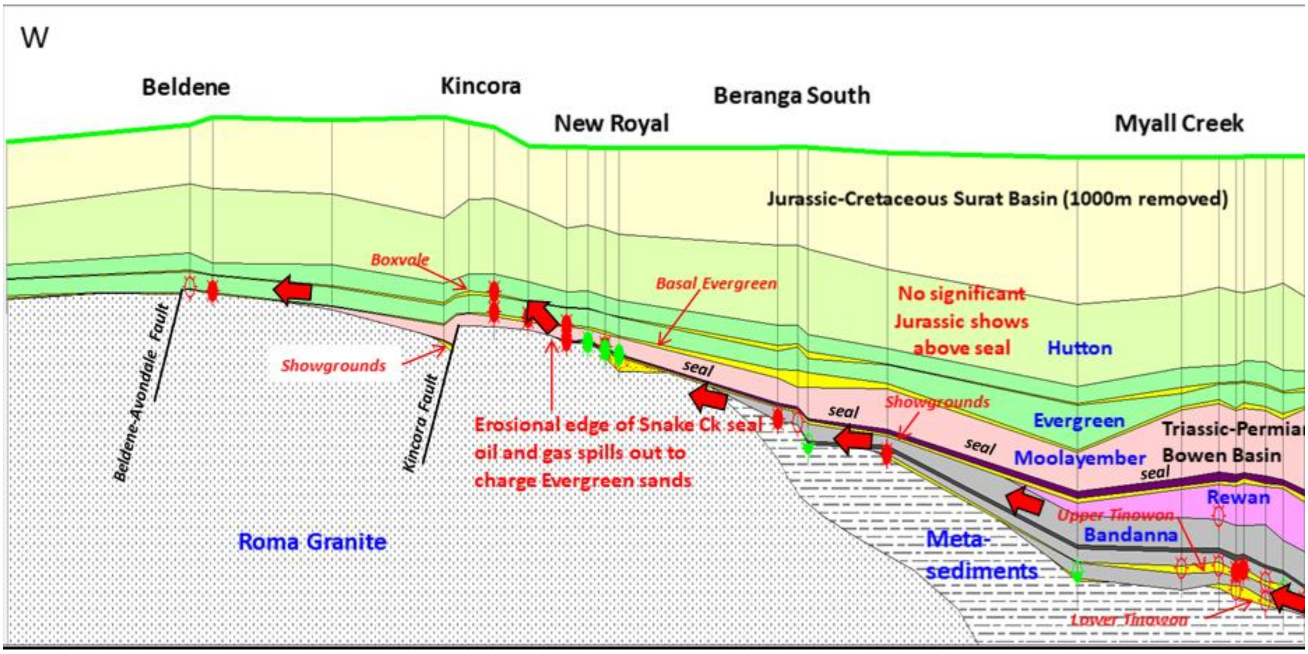
Exhibit 1: Field deliverability beginning to pick up…we expect rates to continue to climb



Source: AEMO data

The field has been operating at lower rates since around start-Oct with wells now being reconnected after work-overs and pump installations. January daily rates are edging gas production up, establishing a new base…and we expect gas output to continue to climb through the clean-up and commissioning phase.

Exhibit 2: There are multiple plays to chase to bring more gas to production…2021 will be an interesting year



Source: Company data

It's worthwhile reminding that the Surat deeps opportunities can be transformational

As highlighted in our Scoping Report (Sep-2020), AJQ is also chasing next phase gas in under-explored plays in and around Kincora.

The basin-centred gas plays (BCG) are typically regionally pervasive accumulations of gas saturated reservoirs, abnormally pressured (can be over or under-pressured), commonly lack a downdip water contact and have low-permeability. Despite the technical challenges, tight gas plays can be considered to be 'multi-Tcf' opportunities.

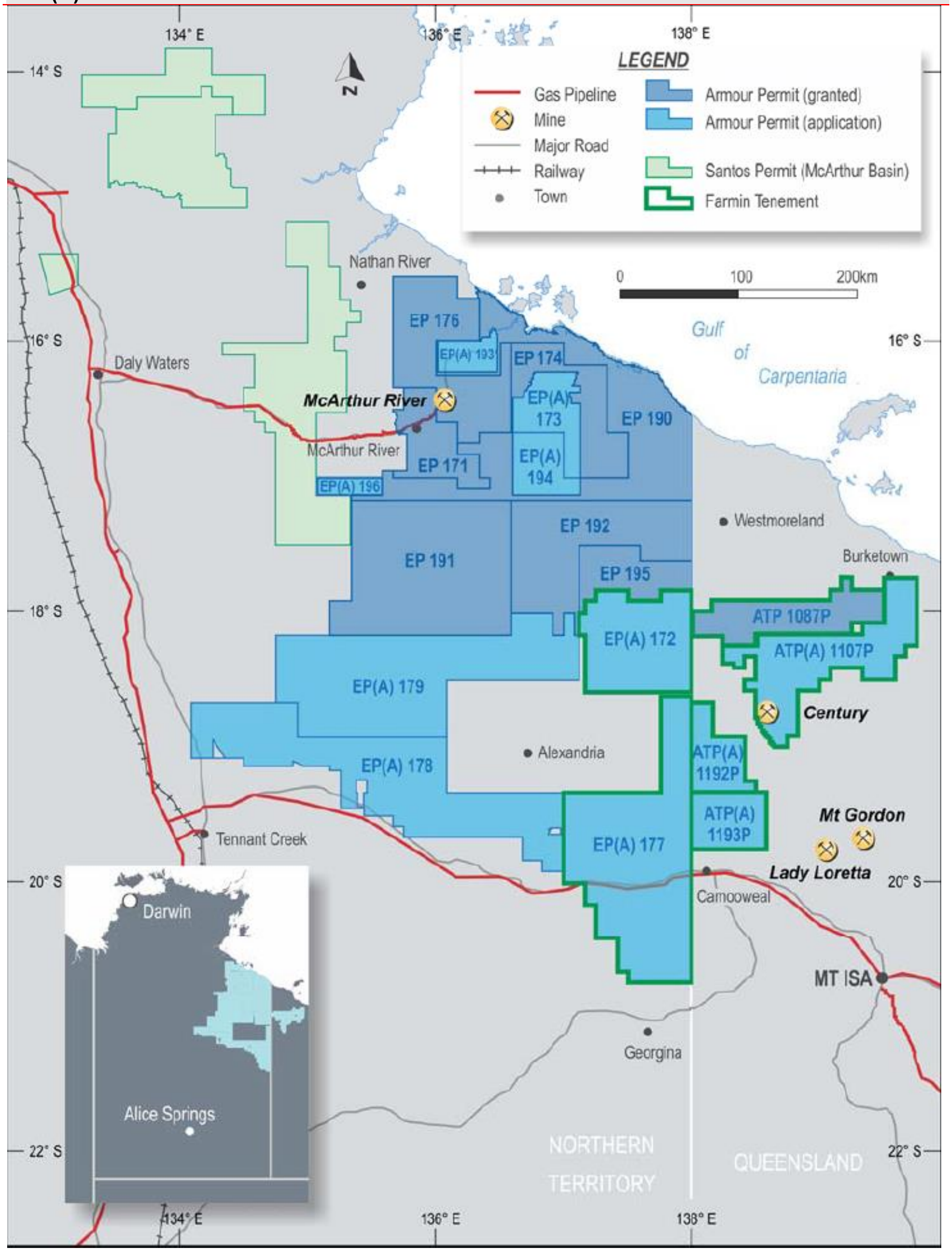
Armour is investigating the wet gas potential of the eastern part of its Surat Basin portfolio, recognizing a basin centred gas play. Initial investigated by Santos and Shell (QGC) have not delivered commercial results but results have been positive and the play has been identified across the company's holdings, which will be the subject of FY21 3D seismic surveys.

Rationalising exploration assets provides additional working capital.

Armour announced on 22-Dec that it had entered into a binding agreement for the sale of a portfolio of South Nicholson Basin permits to Santos for a cash consideration of A$12.25mn.

The permits in question encompass the areas covered by the (now superseded) farm-out agreement to Santos, that would have carried AJQ through some $65mn of exploration and administrative costs.

Exhibit 3: Santos acquisition outlined in green – previously subject to farm-in. AJQ retains ATP(A) 1107P



Source: Company data

Importantly AJQ retains 100% of the application area ATP(A) 1107P, immediately adjacent to the Egilabria gas discovery.

The consideration of $12.25mn will be paid in two tranches - $3mn upon execution of the term sheet and the remainder upon the usual finalisation of requisite approvals and transfers. Completion of the sale is expected by 31-Jan.

What AJQ has done, is monetise a long-dated exploration carry and although the magnitude of the carry was significant (Santos was to carry 100% of Armour's costs for the work programmes within the Farm-in Tenements up to a combined total expenditure of $A65mn for a 70% working interest), the carry would cover only **two significant wells**, with no specific timing on their drilling.

We should read this as being indicative of the scale of the background work still to be undertaken and reflection of the early-stage nature of the exploration process.

Importantly Armour will retain 100% ownership of its other tenements in Northern Australia covering approximately 774mn acres, including the McArthur Basin in the Northern Territory.

The $12.25mn cash injection will assist the company in servicing debt obligations and provide working capital to progress in field works at Kincora, which can deliver significant and tangible upside rapidly in an operating environment where commodity prices look increasingly supportive.

The long-dated nature of the exploration process underscores the importance of pursuing the production growth opportunities inherent at Kincora and within the Newstead gas Storage option.

Adjusting the valuation

We value AJQ using estimated unit values on reserves and; contingent and prospective resources adjusted for discretionary probability weightings (1-risk %), to derive a gross portfolio worth. Probability weightings are subject to change as the company delivers the next phase of exploration results and operating conditions.

Where possible we model development outcomes based on broad guidance and historical outcomes but note these are adjusted and overlain by the RaaS risk outlook reflecting our views of the technical and commercial uncertainties associated with delivering the projects as modelled.

The current work programmes associated with Kincora have the capacity to materially alter our project assumptions and weightings over the next 9 months or so.

We note that beyond Kincora, most of the remaining portfolio is early stage exploration and ascribed values are subject to potentially significant change related to drilling results – both direct and indirect.

We have made adjustments to our NAV based on:

- The slower progress on Kincora field works defers some of the production increase as previously modelled and lowers the NPV on softer FY21 assumptions;
- The swap of 'acreage' for cash and adjustments to the risk weighting of the remaining NT portfolio on recent look-through successes increases the net value of the asset;
- On a larger capital raise we lift the issued capital to 1,275mn shares (as at 23-Dec).

In absolute terms our A$mn value of the portfolio increases to $131mn (previously $118mn) but is offset by higher share dilution than previously modelled, such that our NAV is marginally lower at $0.10/share (previously $0.13/share).

RaaS
Research as a Service

Exhibit 4: AJQ NAV – the share price continues to reflect an overly risked outlook

			Pr	A$mn	A$/share	
Queensland						
Kincora	Various	100%	50%	$71	$0.06	RaaS development scenario on 2P volumes
Newstead storage		100%	50%	$13	$0.01	With 'risked' expansion
Exploration	Various	100%		$10	$0.01	Includes conventional and unconventional opportunities…nominal only
Northern Australia						
MacArthur Basin	Various	100%	2.5%	$67	$0.05	Using risk weighted 2C and Low Case Prospective Resources
Cooper Basin						
Exploration	Various	100%		$10	$0.01	Nominal only
Victoria						
Wombat-Trifon	PRL 2	15%	25%	$10	$0.01	Based on a risk weighted development model and ascribed 2C volumes
Otway-1	PEP 169	51%	6%	$3	<$0.01	Drill-ready opportunity with low economic threshold…likely to be small (but potentially profitable)
Other				$3	<$0.01	Includes a 6.12% LKO shareholding
				$187	**$0.15**	
Net debt (as at 30-Jun)				($51)	($0.04)	
Corporate				($5)	($0.00)	
TOTAL				**$131**	**$0.10**	
Shares issued (mn)*		1,275				

Source: RaaS analysis; Risked values based on look through Probabilities of Success (POS) for drilling and weighted by a RaaS risk overlay. Weightings at RaaS discretion.

Exhibit 5: Financial Summary

ARMOUR ENERGY LTD		AJQ
YEAR END		June
NAV	A$cps	$0.10
SHARE PRICE	Acps	$0.055
MARKET CAP	A$mn	70.1
ORDINARY SHARES	M	1,275
OPTIONS	M	

nm = not meaningful
na = not applicable

As per ASX data 18 Jan

COMMODITY ASSUMPTIONS		FY19A	FY20E	FY21E	FY22E
Realised liquids price	US$/b	96.03	66.26	64.16	65.82
Realised gas price	US$/mcf	6.06	5.76	5.57	5.72
Realised LPG Price	A$/t	581	484	468	481
Exchange Rate	A$:US$	0.7157	0.6989	0.7468	0.7710

RATIO ANALYSIS		FY19A	FY20E	FY21E	FY22E
Shares Outstanding	M	509	779	1,275	1,275
EPS (pre sig items)	Acps	(2.4)	(1.5)	0.0	1.8
EPS (post sig items)	Acps				
PER (pre sig items)	x	na	na	971.3x	3.1x
OCFPS	Acps	(1.9)	(10.3)	(5.0)	27.1
CFR	x	na	na	-1.1x	0.2x
DPS	Acps				
Dividend Yield	%				
BVPS	Acps	87.9	59.2	40.2	58.0
Price/Book	x	nm	nm	nm	nm
ROE	%	(29%)	(21%)	0%	30%
ROA	%	(11%)	(8%)	0%	16%
(Trailing) Debt/Cash	x		18.1x	45.8x	17.7x
Interest Cover	x		nm	1.0x	11.5x
Gross Profit/share	Acps		8.1	6.7	33.4
EBITDAX	A$M	10.0	10.4	15.4	44.7
EBITDAX Ratio	%				

EARNINGS	A$000s	FY19A	FY20E	FY21E	FY22E
Revenue		27,819	23,208	30,677	73,220
Cost of sales		(19,018)	(16,931)	(22,092)	(30,577)
Gross Profit		**8,801**	**6,277**	**8,585**	**42,642**
Other revenue		78	2,879	5,000	0
Other income		193	123	69	44
Exploration written off		0	(520)	0	0
Finance costs		(13,656)	(5,276)	(3,357)	(3,042)
Impairment		(71)	0	0	0
Other expenses		(19,990)	(15,810)	(8,577)	(10,732)
EBIT		2,467	(4,257)	3,365	34,952
Profit before tax		**(10,996)**	**(9,410)**	**77**	**31,954**
Taxes		(688)	(403)	(7)	(9,586)
NPAT Reported		**(11,684)**	**(9,812)**	**70**	**22,368**
Underlying Adjustments					
NPAT Underlying					

CASHFLOW	A$000s	FY19A	FY20E	FY21E	FY22E
Operational Cash Flow		**1,436**	**11,223**	**17,027**	**62,060**
Net Interest		204	(5,153)	(3,896)	(3,150)
Taxes Paid		0	0	0	0
Other		(2,219)	(24,375)	(27,248)	(30,694)
Net Operating Cashflow		**(987)**	**(7,999)**	**(6,324)**	**34,517**
Exploration		(169)	(529)	0	0
PP&E		(22)	0	0	0
Petroleum Assets		(16,714)	(16,686)	(10,200)	(22,500)
Net Asset Sales/other		3,217	17,842	19,750	5,000
Net Investing Cashflow		**(13,688)**	**628**	**9,550**	**(17,500)**
Dividends Paid					
Net Debt Drawdown		11,612	(6,066)	(11,350)	(15,559)
Equity Issues/(Buyback)		7,184	7,457	6,234	0
Other					
Net Financing Cashflow		**18,796**	**1,391**	**(5,116)**	**(15,559)**
Net Change in Cash		**4,121**	**(5,980)**	**(1,891)**	**1,457**

BALANCE SHEET	A$000s	FY19A	FY20E	FY21E	FY22E
Cash & Equivalents		9,225	3,245	1,354	2,812
PP&E & Development		42,382	61,107	69,531	75,986
Exploration		49,277	33,824	40,074	40,074
Total Assets		**116,552**	**124,446**	**123,877**	**135,694**
Debt		58,618	61,975	49,753	33,381
Total Liabilities		**71,793**	**78,308**	**72,664**	**61,676**
Total Net Assets/Equity		**44,759**	**46,138**	**51,213**	**74,018**
Net Cash/(Debt)		(49,393)	(58,730)	(48,398)	(30,570)
Gearing dn/(dn+e)		52%	56%	49%	29%

PRODUCTION		FY19A	FY20E	FY21E	FY22E
Condensate/Crude Oil	kboe	56.2	55.2	118.1	156.9
Nat Gas	PJ	3.3	2.7	3.8	10.1
LPG	kt	4.5	4.2	8.8	20.7
TOTAL	**kboe**	**627**	**527**	**814**	**1,973**
Product Revenue	A$mn	27.8	23.2	30.7	73.2
Cash Costs	A$mn	17.9	15.7	20.3	28.5
Ave Price Realised	A$/boe	44.34	44.02	37.69	37.11
Cash Costs	A$/boe	28.53	29.73	24.95	14.46
Cash Margin		**36%**	**32%**	**34%**	**61%**

		Reserves			Contingent	
Net To AJQ		1P	2P	3P	1C	2C
Kincora Reserves						
Sales Gas	PJ	67.4	150.3	321.1		
LPG	kt	139	310	663		
Condensate	kb	670	1,493	3,191		
Oil	kb	246	1,221	2,640		
MacArthur Basin plays						
Conventional	PJ				2.5	6.2
Wombat-Triton						
Sales Gas	PJ				437	818
Otway-1						
Sales Gas	PJ					35

Prospective Resources		1U	2U	3U
MacArthur Basin plays				
Conventional	PJ	1,351	4,990	31,081
Unconventional	PJ	3,950	31,185	345,634
TOTAL	PJ	5,301	36,175	376,715

EQUITY VALUATION	Interest	Pr	A$mn	A$/share
Queensland				
Kincora	Various	50%	$71	$0.06
Exploration	Various		$10	$0.01
Newstead Gas Storage		50%	$13	$0.01
Northern Australia				
McArthur Basin	Various	3%	$67	$0.05
Cooper Basin				
Exploration	Various		$10	$0.01
Victoria				
Wombat - Trifon	PRL 2	25%	$10	$0.01
Otway-1	PEP 169	6%	$3	$0.00
Other			$3	$0.00
			$187	$0.15
Net cash/(debt)			($51)	($0.05)
Corporate costs			($5)	($0.00)
TOTAL			**$131**	**$0.10**
Shares on issue (mn)			**1,275**	

Source: RaaS Advisory, Company data

FINANCIAL SERVICES GUIDE

RaaS Advisory Pty Ltd

ABN 99 614 783 363

Corporate Authorised Representative, number 1248415

of

BR SECURITIES AUSTRALIA PTY LTD

ABN 92 168 734 530

AFSL 456663

Effective Date: 26th November 2018

About Us

BR Securities Australia Pty Ltd (BR) is the holder of Australian Financial Services License ("AFSL") number 456663. RaaS Advisory Pty Ltd (RaaS) is an Authorised Representative (number 1248415) of BR.

This Financial Service Guide (FSG) is designed to assist you in deciding whether to use RaaS's services and includes such things as

- who we are
- our services
- how we transact with you
- how we are paid, and
- complaint processes

Contact Details, BR and RaaS

BR Head Office: Level 14, 344 Queen Street, Brisbane, QLD, 4000

RaaS. 20 Halls Road Arcadia, NSW 2159

P: +61 414 354712

E: finola.burke@raasgroup.com

RaaS is the entity providing the authorised AFSL services to you as a retail or wholesale client.

What Financial Services are we authorised to provide? RaaS is authorised to

- provide general advice to retail and wholesale clients in relation to
  - Securities
- deal on behalf of retail and wholesale clients in relation to
  - Securities

The distribution of this FSG by RaaS is authorized by BR.

Our general advice service

Please note that any advice given by RaaS is general advice, as the information or advice given will not take into account your particular objectives, financial situation or needs. You should, before acting on the advice, consider the appropriateness of the advice, having regard to your objectives, financial situation and needs. If our advice relates to the acquisition, or possible acquisition, of a particular financial product you should read any relevant Prospectus, Product Disclosure Statement or like instrument. As we only provide general advice we will not be providing a Statement of Advice. We will provide you with recommendations on securities

Our dealing service

RaaS can arrange for you to invest in securities issued under a prospectus by firstly sending you the offer document and then assisting you fill out the application form if needed.

How are we paid?

RaaS earns fees for producing research reports. Sometimes these fees are from companies for producing research reports and/or a financial model. When the fee is derived from a company, this is clearly highlighted on the front page of the report and in the disclaimers and disclosures section of the report.

We may also receive a fee for our dealing service, from the company issuing the securities.

Associations and Relationships

BR, RaaS, its directors and related parties have no associations or relationships with any product issuers other than when advising retail clients to invest in managed funds when the managers of these funds may also be clients of BR. RaaS's representatives may from time to time deal in or otherwise have a financial interest in financial products recommended to you but any material ownership will be disclosed to you when relevant advice is provided.

Complaints

If you have a complaint about our service you should contact your representative and tell them about your complaint. The representative will follow BR's internal dispute resolution policy, which includes sending you a copy of the policy when required to. If you aren't satisfied with an outcome, you may contact AFCA, see below. BR is a member of the Australian Financial Complaints Authority (AFCA). AFCA provide fair and independent financial services complaint resolution that is free to consumers.

Website: www.afca.org.au; Email: info@afca.org.au; Telephone: 1800931678 (free call)

In writing to: Australian Financial Complaints Authority, GPO Box 3, Melbourne, VIC, 3001.

Professional Indemnity Insurance

BR has in place Professional Indemnity Insurance which satisfies the requirements for compensation under s912B of the Corporations Act and that covers our authorized representatives.

DISCLAIMERS and DISCLOSURES

This report has been commissioned by Armour Energy Ltd prepared and issued by RaaS Advisory Pty Ltd. RaaS Advisory has been paid a fee to prepare this report. RaaS Advisory's principals, employees and associates may hold shares in companies that are covered and, if so, this will be clearly stated on the front page of each report. This research is issued in Australia by RaaS Advisory and any access to it should be read in conjunction with the Financial Services Guide on the preceding two pages. All information used in the publication of this report has been compiled from publicly available sources that are believed to be reliable. Opinions contained in this report represent those of the principals of RaaS Advisory at the time of publication. RaaS Advisory provides this financial advice as an honest and reasonable opinion held at a point in time about an investment's risk profile and merit and the information is provided by the RaaS Advisory in good faith. The views of the adviser(s) do not necessarily reflect the views of the AFS Licensee. RaaS Advisory has no obligation to update the opinion unless RaaS Advisory is currently contracted to provide such an updated opinion. RaaS Advisory does not warrant the accuracy of any information it sources from others. All statements as to future matters are not guaranteed to be accurate and any statements as to past performance do not represent future performance.

Assessment of risk can be subjective. Portfolios of equity investments need to be well diversified and the risk appropriate for the investor. Equity investments in listed or unlisted companies yet to achieve a profit or with an equity value less than $50 million should collectively be a small component of a balanced portfolio, with smaller individual investment sizes than otherwise. Investors are responsible for their own investment decisions, unless a contract stipulates otherwise. RaaS Advisory does not stand behind the capital value or performance of any investment. Subject to any terms implied by law and which cannot be excluded, RaaS Advisory shall not be liable for any errors, omissions, defects or misrepresentations in the information (including by reasons of negligence, negligent misstatement or otherwise) or for any loss or damage (whether direct or indirect) suffered by persons who use or rely on the information. If any law prohibits the exclusion of such liability, RaaS Advisory limits its liability to the re-supply of the Information, provided that such limitation is permitted by law and is fair and reasonable.