

Sector: Oil & Gas

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INTEROIL CORPORATION (CDNX – IOL \$10.99)

Market Data

In Canadian Dollars

Last	\$10.99
12 Month High	\$14.22
12 Month Low	\$9.48
Fiscal Year End	31-Dec
Shares - O/S Basic (December 31, 2001)	20,183,870
Shares - O/S FD (December 31, 2001)	21,349,470
Market Capitalization - Basic	\$221,820,731
Total Net Debt	\$31,000,000
Enterprise Value	\$252,820,731
Possible Capital Appreciation	127%
Exchange Rate (US\$/CAD\$)	0.65

Recommendation:
STRONG BUY

Target Price:
\$25.00

Within the previous 36 months Jennings Capital Inc. has acted as underwriter or has performed paid services for the issuer of this security.

Year	<u>CAD\$</u> EPS (F.D.)	P/E	<u>CAD\$</u> CFPS (F.D.)	P/CF	<u>WTI</u> US\$/Barrel	<u>TAPIS</u> US\$/Barrel	<u>Kubutu Blend</u> US\$/Barrel	<u>Refinery</u> Capacity bpd
2004E	\$3.80	2.9X	\$4.18	2.6X	\$25.00	\$23.20	\$22.30	32,500
2005F	\$3.95	2.8X	\$4.34	2.5X	\$25.00	\$23.20	\$22.30	32,500
2006F	\$4.00	2.7X	\$4.35	2.5X	\$25.00	\$23.20	\$22.30	32,500

- InterOil Corporation is a Houston based Canadian company with its operational office in Cairns Australia. The Company's common shares were **recently posted for trading on The Toronto Venture Exchange** (formally the CDNX), with Jennings Capital Inc. acting as sponsoring broker.
- The author has followed the Company for the last four years and provides advisory services to the Company for fees.
- The Company is in the process of constructing the first refinery in Papua New Guinea (PNG), which is scheduled to commence operations late 2003. The refinery will process locally available light sweet crude oil to generate a product stream that is currently imported into the area at a substantial cost from a distance of 2,200 to 7,000 kms. **The refinery and distribution operations that InterOil is building will permit the Company to capture a substantial share of the petroleum product market in this Oceania region.** The niche market refinery is to be located about 4km by sea and 23 km by road from the PNG capital, Port Moresby, which has been visited by the author in the fall of 2000.
- **Once in operation the refinery is expected to generate sustainable earnings of around CAD\$3.80 per share**, based on petroleum product margins experienced in the region over the last 7 years. Current margins are 20% to 50% above these historical averages.
- Upstream, InterOil also is the second largest holder of exploratory petroleum acreage in PNG, and has recently reported the discovery of a new oil system that has substantial exploration potential. InterOil will commence an exploration-drilling program later this year that **offers targets with recoverable reserves of upwards to several hundred million barrels.**
- This research report describes the investment opportunities offered by InterOil Corporation. **Even if InterOil trades at the lower end of comparable multiples, the Company's common shares would trade at twice-current levels in the coming 12 to 18 months.**
- The Company has a focused and dedicated managements team, which has successfully raised **necessary funds to complete the refinery project, secured a debt financing backed by the US Government and won the support of two of the world's largest oil companies in this refinery venture.**

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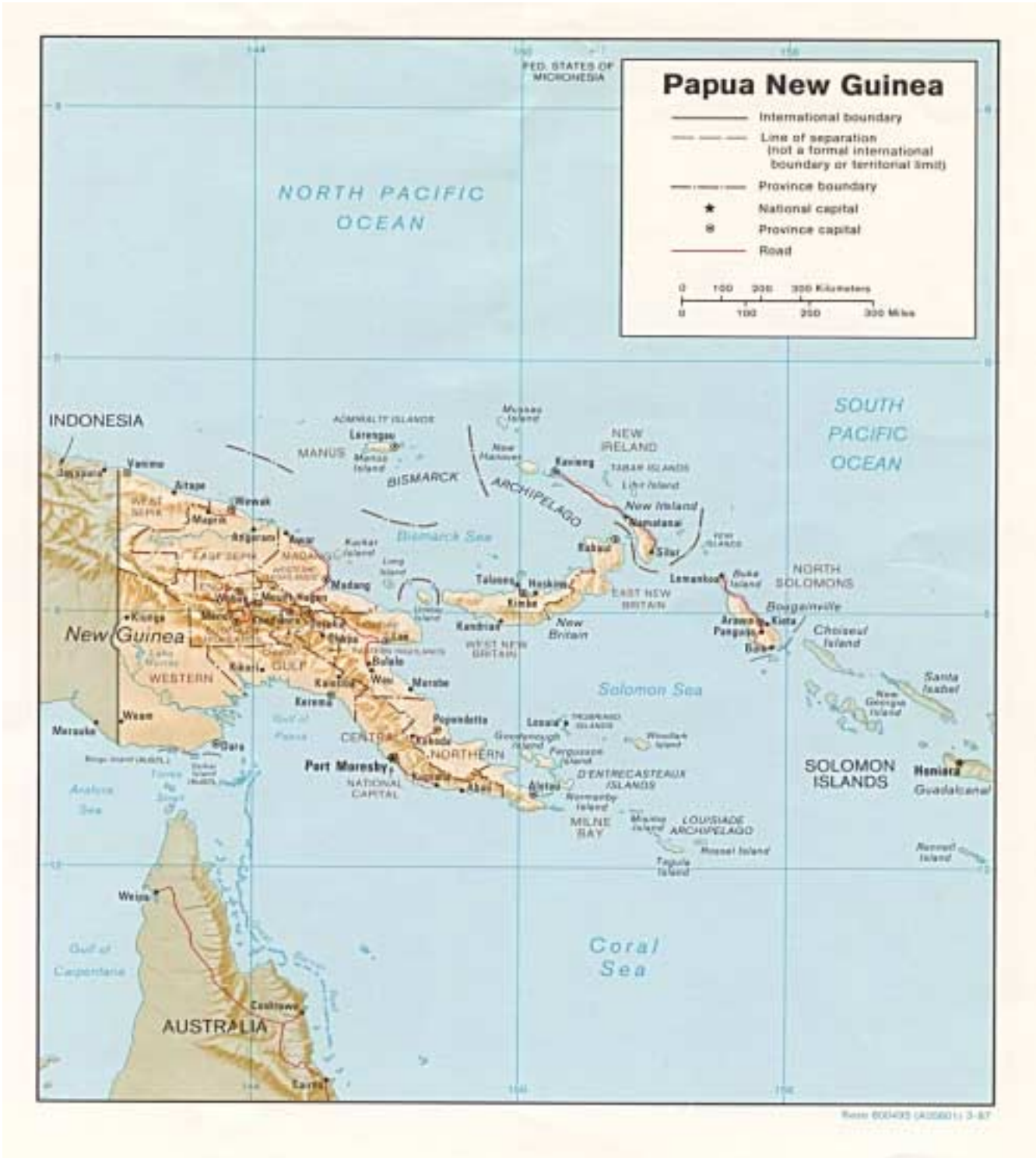
Member - CIPF

THE COMPANY

- InterOil was formed in 1996 with the sole purpose to finance and construct an intergraded energy business centered on a refinery in PNG and thereby exploit a highly profitable business opportunity.
- The Company was formed by way of a reverse take-over of a publicly listed Canadian company and the merging with a private company. The initial net assets of US\$46.4 million, consisted of the oil refinery at cost plus work done for a total of US\$39.7 million, and cash and cash equivalents of US\$6.7 million. As part of the amalgamation, InterOil issued an Offering Memorandum **and raised US\$52.7 million by the issue of special warrants at US\$14.25 each, in May 1997**. Each special warrant converted into one InterOil share.
- InterOil had 20,197,870 common shares with **management holding 35% of the issued and outstanding shares**. Stock options outstanding and exercisable at year-end December 31, 2001 totaled 1,165,600 with a weighted average exercise price of US\$4.00 per share.
- InterOil was admitted to the official list on the Australian Stock Exchange Limited (ASX) in mid-August 2000. Trading on the ASX is conducted using a derivative instrument called a CHES Depository Interest (a "CDI"), the Australian equivalent of the American Depository Receipt ("ADR"), an instrument used in the United States. **Ten CDIs will equal to one InterOil common share.**
- **InterOil was posted for trading on the Toronto Venture Exchange in April 2002.**
- Recently InterOil received an amount of US\$ 31 million from the **Overseas Private Investment Corporation** (OPIC) an agency of the US government. This is the first disbursement under the US\$85 million Loan Agreement negotiated for completion of InterOil's PNG refinery project. This is the largest loan OPIC has made, and the very first loan for a project in PNG.
- Lack of trading history in Canada has necessitated using the following chart to illustrates the Company's share price over the last twelve months on the "**Australia Stock Exchange**" (in the form of CDI i.e. **one tenth of a common share A\$/CDI**)



RESEARCH REPORT



RESEARCH REPORT

DOWNSTREAM - THE REFINERY PROJECT

- PNG is one of the few oil-producing nations that relies entirely on imported refined products, sourced from Singapore and Australia at distances of 2,200 - 7,000 km. The construction of this refinery is **the first and most important step for InterOil becoming an integrated energy company** - spanning refining, production, and distribution.
- The unique geographical advantage of the refinery - provides a significant cost saving -as it is in close proximity to both the source of feedstock crude oil and markets for its refined product. **The avoided transport costs establish a natural niche market with base line profits.**
- PNG encompasses the eastern half of the island of New Guinea (the western half, Irian Jaya, forms a part of Indonesia) and its offshore islands, as well as the islands of the Bismarck Archipelago (New Britain, New Ireland, and the Admiralty Islands), Bougainville and Buka Island. Together these islands cover 462,840 square kilometres (178,704 square miles) of the southwestern Pacific, stretching from just south of the Equator to the Torres Strait. A mix of people, referred to as Melanesians, inhabit these islands. One of the principal challenges facing the government is the difficulty of welding together hundreds of diverse, once-isolated regional societies into a viable modern state nation.
- PNG is one of the few oil producing countries without a local refinery. Oil production in PNG started in 1992. Refined products totaling approximately 18,000 bpd were imported, primarily from Singapore. **Transportation shipping costs of approximately US\$4.00/barrel are incurred to move this product.**
- The State of PNG has supported the construction of the refinery, as this will capture and add value to the regions natural resources. InterOil began to implement a business plan to capture this opportunity by sourcing an existing refinery, and by working with the local government to further enhance project economics.
- Competition to supply the PNG market is limited by the strong natural barriers, resulting from both the markets relatively small size and the geographic shipping difficulties of importing. **PNG presents a highly profitable business opportunity for a small size niche refinery used to supply the area and nearby markets.**
- InterOil has entered into a 30 year Project Agreement with the PNG government for a commercial production period. In summary:
 - InterOil has the right to construct, manage and operate the refinery as well as the right to purchase domestic crude oil and sell refined products to the domestic market.
 - The State pledges to prevent domestic distributors and importers of refined products from predatory pricing or dumping, by implementing legislation if necessary.
 - The State will provide InterOil with damages to the extent it is harmed by being unable to purchase crude at the market price or sell its product at the Import Parity Price (IPP).
 - InterOil has rights and obligations with respect to infrastructure usage for project development such as power, water, land and shipping access.
 - InterOil will not charge a price greater than the IPP of equivalent product imported into PNG.
- InterOil sourced exactly what was required in the Nikiski refinery, owned and operated by Chevron U.S.A. in Kenai, Alaska. This unit, the "Nikiski", was designed by Chevron and brought online in 1963. **This refinery operated until 1991, processing light sweet crude oil from Alaska's Swanson River, Cook Inlet and the Alaskan North Slope Fields. The Cook Inlet crude oil is similar to PNG Kutubu blend crude.**

- The Nikiski nameplate capacity of 22,500 bpd achieved throughputs up to 31,500 bpd. The plant was well maintained, with all government environmental certificates current at the time of closure.
- The contracted construction has guaranteed a processing capacity of 32,500 bpd. It is likely that the facility will be able to run 34,500 bpd, the expected limit of the light ends unit. **However, the economic model we have used is based upon a more conservative level 32,500 bpd.**
- The Nikiski distillation unit was acquired in 1994 by InterOil and moved offsite for shipment to a refurbishment yard. A steel deck ocean-going barge was purchased, refurbished and used to ship the distillation unit to Beaumont, Texas in 1997.
- Most of the products can be produced directly by distillation. To upgrade gasoline, a semi-regenerative catalytic reformer, with matching hydro desulphurizer was acquired from a refiner in Oklahoma. This unit was dismantled and also moved to Beaumont, Texas.
- Various specialists were hired prior to purchase, to inspect both the Nikiski refinery and Oklahoma reformer. A detailed program of refurbishment and modification has been developed and items not requiring modification have already undergone refurbishment, inspection and testing.
- Crude oil consists of hundreds if not thousands of different types hydrocarbons, plus a range of other chemicals. Every oil field is different, and crude selected as feedstock heavily influences refinery design. Crude oil is based on the value and quality of the products that can be made per barrel and the degree of processing necessary.
- In PNG, Kutubu was the original oil field producing into the Kumul Offshore Terminal. Other adjacent fields have since come onstream, specifically Gobe and Moran. These crude oils, called the Kutubu blend, have an assay very similar to the original Kutubu crude.
- The Kutubu blend is attractive, because it is low in sulphur (0.04%), therefore qualifying it as sweet. Also, the small quantity of H₂S in the fuel gas, falls well below the atmospheric emissions recommended by the World Bank. For these reasons diesel can be made by straightforward distillation, without the need to install sulphur removing hydrotreating facilities adding for exceptional economics.
- Kutubu blend is also classified as light, which means it contains a relatively small portion of hard to handle heavy fuel oil. Thus, from a refining perspective, the **Kutubu blend is well suited for a modest-cost refinery used to produce a range of locally demanded quality products.**
- Distillation, the heart of the refining process, is the heating of crude until it vaporizes and separates into discreet components by condensing the vapor at various controlled temperatures.
- Refineries limited to distillation, reforming, purification, and blending are known as *hydro-skimming refineries*. Those involving cracking or coking, where the molecular structure of the hydrocarbon molecules is manipulated, are known as *conversion refineries*. The InterOil refinery will be a very simple "*hydro-skimming refinery*", which is appropriate for the treatment of light sweet crude from the PNG fields.
- The range of products produced is influenced by the nature of the crude oil and the operation of the refinery. The refinery will have the capability to run with maximum kerosene (up to 20% of production) yielding diesel production of 26%, or with minimum kerosene (less than 7% of production) yielding diesel production of 40%. The existing demand in the PNG market indicates that the plant should operate to produce maximum diesel, but this may change.
- **Clough Niugini Limited** was awarded the contract to build the refinery. Under this contract InterOil is committed to pay US\$93 million, of which US\$83 is due to Clough Niugini Limited. The balance of US\$10 million is to fund related capital and financing costs for InterOil. Clough Niugini is the PNG operating arm of the leading Australian engineering and construction company Clough Engineering Limited. Clough has provided liquidated damages for 50% of the contract price to ensure construction is on time and refinery operates at 94% stream factor.

- Work on the project has begun and the refinery is due to be operational in late 2003. The contract calls for a completion guarantee by approximately 20 months, followed by a start-up period consisting of three months of commissioning and three months of testing. Experience at other refineries indicates that the allowance for commissioning and testing is conservative and some marketable product may be produced during the start-up period.
- The scope of the contract encompasses:
 - Site Civil Work
 - Storage Tank Farm
 - Crude Oil Distillation Unit
 - Catalytic Reforming Unit
 - Jetty with Ship Loading and Unloading Facilities
 - Utility Systems including Steam and Power Generation
 - Site Infrastructure and Support Facilities
- **The Overseas Private Investment Corporation (OPIC)**, an agency of the United States government, has signed the commitment documentation for US\$85 million debt facility used to construct the refinery. **These funds, together with InterOil's cash, provide US\$122 million of financing required for refinery completion.** The balance of the US\$180 million total project cost is covered by equipment and assets already owned and contributed by InterOil.
- **The site on Port Moresby harbor is well situated, adjacent to the new facility, with a deep-water harbor accessible to tankers.** This provides a good setting amongst low hills and proximity to Port Moresby, which is the second largest market for refined products in the country and allows access to labor and logistic support. The refinery layout was developed by engineer Kvaerner John Brown and optimized by Clough. The design has been consistent with modern industry standards to constrain operating capital and maintenance costs while maximizing safety and ease of compliance with environmental safeguards. The hill setting will also minimize the visual impact of the complex. Site construction, including road improvements, has commenced. The work in progress can be followed on the Company's website: www.interoil.com.
- The site is only 435 km from the Kutubu crude loading terminal at Kumul. The Port Moresby harbor and the site has deep-water access to crude tankers of up to 100,000 dwt.
- InterOil has signed a 99-year lease with the government of PNG which includes 76.8 hectares (180 acres) of industrial zoned land and more than 120 hectares (300 acres) of harbor rights for the refinery site.
- Refinery operations require reliable power supply. Two 3.5 MW gas turbine units will provide electric power. Both units are 'dual fuel', hence capable of operation using either liquid (Diesel or Naphtha) or gaseous fuel (high hydrogen content reformer off gas) provided from the refinery. Each unit can supply enough power for full plant operations. These units have already been purchased by InterOil and the installation cost is included in the lump sum construction contract.
- Access to fresh water required for steam generation, refinery cooling, firefighting, general plant services, and domestic and irrigation services will not be supplied from scarce local sources. A seawater distillation plant is incorporated into the plant design to provide balance.
- It is anticipated that ships of 20,000 to 80000 dwt will deliver crude to a jetty requiring minimum draft of 17 metres. The jetty is planned at an existing working seawater depth of between 17 and 21 metres, avoiding any dredging requirements. At this depth, tankers up to 100,000 dwt could be accommodated. The jetty construction will be combined with causeway/deck on pile structures and will include a spur to a smaller berth for finished product exports.
- InterOil has entered into an agreement with Shell Overseas Holdings Limited to purchase their retail and commercial assets in PNG for a total of US\$18 million in cash and convertible notes (2

million convertible notes at US\$7 conversion price, plus US\$4 million cash payable 12 months after refinery start up). InterOil will in turn lease back the outlets to Shell, at a base return of about 9%.

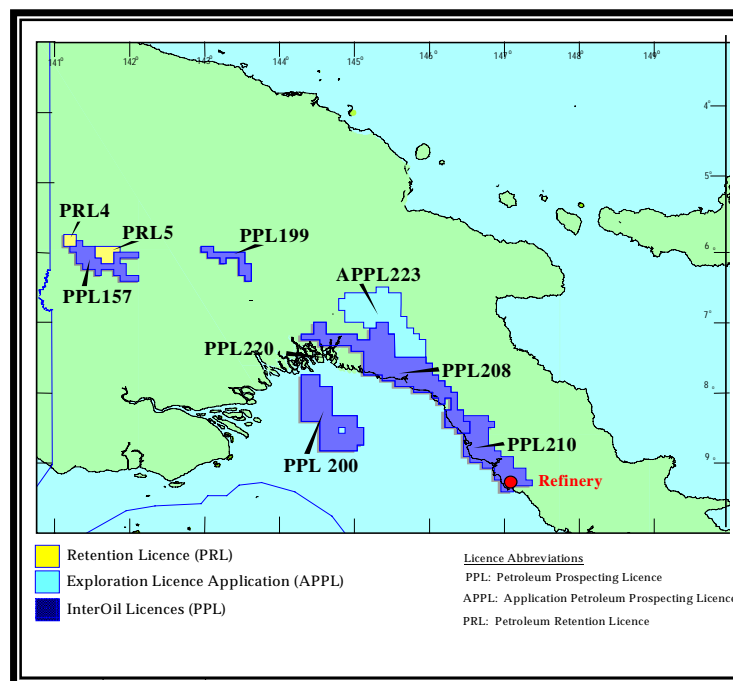
- The InterOil agreement with Shell has removed for the Company an offtake risk on the refinery product stream, for the first 3 years, Shell will purchase all of the refineries output at prevailing prices. Subsequently, Shell will purchase their entire PNG refined product from the refinery, which accounts for about 70% of the refineries total output. The refinery will earn standard operating margins on all sales and InterOil will share equally in the profits of the distribution company. The strategic alliance contracts with Shell become effective as soon as the Refinery begins commercial operations which is expected in late 2003.
- The following Table summarizes our economic model in ***US Funds*** for the InterOil refining and marketing operation. Our assumptions are based on the last seven-year average spreads, **which are considerably lower than currently enjoyed in the region.**

		<u>2004E</u>	<u>2005E</u>	<u>2006E</u>	<u>2007E</u>
Crude Usage per Day - (bpd)		32,500	32,500	32,500	32,500
Crude Usage per Year - MMBbls		11.9	11.9	11.9	11.9
Oil Prices					
	WTI \$US per Barrel	\$25.00	\$25.00	\$25.00	\$25.00
	TAPIS \$US per Barrel	\$23.20	\$23.20	\$23.20	\$23.20
	KUTUBU BLEND \$US per Barrel	\$22.30	\$22.30	\$22.30	\$22.30
Product Sales					
On-stream Factor		97%	97%	97%	97%
	Product Sales	31,500	31,500	31,500	31,500
	% of Capacity	100.00%	100.00%	100.00%	100.00%
Product Sales per Year - MMBbls		11.5	11.5	11.5	11.5
	Refinery Yield-%				
Diesel	36.4%	11,466	11,466	11,466	11,466
Naphtha	26.5%	8,348	8,348	8,348	8,348
Marine Diesel Oil	18.9%	5,954	5,954	5,954	5,954
Kerosene/Jet Fuel	8.5%	2,678	2,678	2,678	2,678
Motor Gasoline	7.5%	2,363	2,363	2,363	2,363
LPG	2.2%	693	693	693	693
Total	100.0%	31,500	31,500	31,500	31,500
PNG Sales					
Diesel	95.7%	10,973	10,973	10,973	10,973
Naphtha	0.0%	0	0	0	0
Marine Diesel Oil	71.9%	4,281	4,281	4,281	4,281
Kerosene/Jet Fuel	93.1%	2,493	2,493	2,493	2,493
Motor Gasoline	87.7%	2,072	2,072	2,072	2,072
LPG	24.3%	168	168	168	168
	63.4%	19,987	19,987	19,987	19,987
Export Sales					
Diesel	4.3%	493	493	493	493
Naphtha	100.0%	8,348	8,348	8,348	8,348
Marine Diesel Oil	28.1%	1,673	1,673	1,673	1,673
Kerosene/Jet Fuel	6.9%	185	185	185	185
Motor Gasoline	12.3%	291	291	291	291
LPG	75.7%	525	525	525	525
	36.6%	11,513	11,513	11,513	11,513

	<u>2004E</u>	<u>2005E</u>	<u>2006E</u>	<u>2007E</u>
<u>Domestic Spread - 7 Year Average</u>				
Diesel	\$10.40	\$10.40	\$10.40	\$10.40
Naphtha	\$0.00	\$0.00	\$0.00	\$0.00
Marine Diesel Oil	\$6.87	\$6.87	\$6.87	\$6.87
Kerosene/Jet Fuel	\$9.75	\$9.75	\$9.75	\$9.75
Motor Gasoline	\$9.01	\$9.01	\$9.01	\$9.01
LPG	\$14.26	\$14.26	\$14.26	\$14.26
Weighted Average	\$9.45	\$9.45	\$9.45	\$9.45
<u>Export Spread - 7 Year Average</u>				
Diesel	\$8.40	\$8.40	\$8.40	\$8.40
Naphtha	\$3.90	\$3.90	\$3.90	\$3.90
Marine Diesel Oil	\$4.87	\$4.87	\$4.87	\$4.87
Kerosene/Jet Fuel	\$7.75	\$7.75	\$7.75	\$7.75
Motor Gasoline	\$7.01	\$7.01	\$7.01	\$7.01
LPG	\$12.26	\$12.26	\$12.26	\$12.26
Weighted Average	\$4.75	\$4.75	\$4.75	\$4.75
Average Spread	\$7.73	\$7.73	\$7.73	\$7.73
Revenues				
Investment Income	\$1.0	\$1.0	\$1.0	\$1.0
PNG Sales Revenues	\$231.6	\$232.3	\$231.6	\$231.6
Marketing Revenue 50/50 Split	\$3.6	\$3.6	\$3.6	\$3.6
Export Sales Revenues	\$113.7	\$114.0	\$113.7	\$113.7
Total Revenues	\$350.0	\$350.9	\$350.0	\$350.0
Expenses				
Crude Purchase	\$264.5	\$264.5	\$264.5	\$264.5
Crude Shipping	\$4.5	\$4.5	\$4.5	\$4.5
Operating & Maintenance	\$7.5	\$7.5	\$7.5	\$7.5
Sales and General Administration	\$4.0	\$4.0	\$4.0	\$4.0
Interest Expenses	\$6.8	\$5.5	\$4.3	\$2.9
Depreciation & Depletion	\$5.8	\$5.6	\$5.4	\$5.2
Total	\$293.1	\$291.7	\$290.2	\$288.7
Income Tax	\$0.0	\$0.0	\$0.0	\$0.0
EBITD	\$69.4	\$70.3	\$69.4	\$69.4
Net Income	\$56.9	\$59.2	\$59.8	\$61.3
Cash Flow	\$62.6	\$64.8	\$65.2	\$66.5
E.P.S. (US\$)	\$2.47	\$2.57	\$2.60	\$2.66
C.F.P.S. (US\$)	\$2.72	\$2.82	\$2.83	\$2.89
Long-term Debt	\$85.0	\$85.0	\$69.3	\$53.1
Debt / Cash Flow	1.4X	1.1X	0.8X	0.6X

UPSTREAM – AN EXCITING EXPLORATION STORY

- In order to meet its longer-term objective to become a significant producer of hydrocarbons, InterOil has acquired varying interests (15-100%) in 25,604 square kilometres (6.2 million acres) of exploration concessions in PNG, where major oil and gas fields have been discovered and are in production.
- The country is a proven and relatively unexplored petroliferous region, with one well every 1,900 sq. km (469,000 acres) in the “Foreland “ and 1 well per 580 sq. km. (143,000 acres) in the “Fold Belt “.
- **The under-explored nature of PNG offers opportunities for large hydrocarbon discoveries.** The first commercial crude oil production commenced in 1992, following many years of erratic exploration efforts. Since the discovery of oil in the Toro Sandstone at Kutubu, exploration activity has concentrated on the Toro Sandstone fairway in the Foldbelt and Forelands in west PNG. This region is remote with very difficult topographical terrain, making exploration for hydrocarbons very expensive.
- **InterOil considered that the under-explored Eastern Papuan Basin had petroleum potential due to oil and gas seeps and 1610 bopd flowed from the Puri well. The area has the logistical advantages of moderate terrain and barge access to infrastructure including the InterOil refinery under construction.**
- Petroleum activities in PNG are conducted under a traditional licensing regime, where exclusive rights are granted to companies to conduct operations. Exploration activities are conducted under a six year *Petroleum Prospecting Licence (PPL)*.
- InterOil has assembled an extensive portfolio of seven exploration concessions, totaling 6.2 million acres. These concessions give InterOil the second largest holding of oil and gas exploratory licences in the country.



RESEARCH REPORT

- The potential to transport oil to the refinery by truck or barge could avoid building or connecting to export facilities. This would reduce development costs and increasing the profitability of some fields, making marginal fields economic to develop. Larger discoveries can be exported via InterOil's jetty in Port Moresby. **InterOil's licence selection has favored locations that capture these benefits.**
- The costs to drill in PPLs 230, 210, and 220 will be substantially less than drilling in the highlands, since transport by road or barge to Port Moresby refinery is practical. PPL210 (a licence 100% held by InterOil), is in immediate proximity to the refinery location, which dramatically enhances the prospects economics.
- **In January this year, InterOil announced the discovery of a "New Oil System" in PNG.** Two stratigraphic wells drilled by InterOil have cored over 1,600 feet (492 m) with 1230 feet (375m) of good reservoir quality "Pale Sandstone". There are hydrocarbons throughout the Pale Sandstone. These hydrocarbons are bitumen residue of Jurassic-sourced oil. Analysis by independent experts indicates that the key elements of a petroleum system (i.e. reservoir, regional seal, hydrocarbon generation and charge) are present, and the reservoir quality of the Pale sandstone is regarded as good. The petroleum system is oil prone rather than gas.
- In 2002, InterOil is now planning to conduct field surveys, four shallow wells and seismic acquisition, processing and interpretation. Based on InterOil's experience the shallow wells could each be drilled for US\$ 750,000 up to 6,000 feet.
- Our review of InterOil's geological analysis is very encouraging. Abundant oil seeps with impressive exploration drilling success rates indicate that much of the country's petroleum potential remains untapped. **Less than 140 exploratory wells have been drilled in the country with approximately 30% encountering substantial hydrocarbons.** The exploratory concessions have a high prospect potential.
- Exploration efforts in PNG, as in any emerging petroleum region, have focused on finding oil rather than gas. However, the exploration effort has left little doubt that some areas in PNG have much more gas than oil. **Proven gas reserves are currently estimated at about 14 trillion cubic feet (tcf). In energy equivalent terms, that is about seven times the size of the remaining oil reserves.**
- Ultimate total recoverable gas reserves could be up to 40 tcf. However, commercializing the gas will be a difficult challenge. The pre-eminent scheme for development is the "PNG gas to Queensland" project. It will involve investment of around US\$2.1 billion in PNG and US\$1.55 billion in Australia. The 2,400 kilometre pipeline will be the largest industrial development in PNG. The project is not yet approved, but a commercial decision is expected within the coming year(s).
- This pipeline will have a material positive impact on the petroleum activity in PNG. InterOil's refinery facility and deepwater terminal is expected to bestow logistical advantages, especially in the marketing of associated condensate and natural gas liquids. However, it is currently impossible to quantify the net benefits that can be derived from this logistical advantage.
- InterOil has an enviable exposure to provide exceptional value creation to shareholders through the unexplored opportunities in the eastern portion of PNG and the development of this huge untapped natural gas potential. We are convinced that the Company will be able to attract serious industry partners in their upstream program.
- At this early stage it is difficult to assign a Net Asset Value for InterOil's upstream holdings. **The exploration exposure offered in the Company's 6.2 million acres has the potential for 11 world class oilfields each containing 60 to 500 million barrels.**

SUMMARY AND CONCLUSION

- Although Clough will guarantee a throughput capacity of 32,500 bpd of crude oil, in our economic analysis we have assumed a more conservative 30,000 bpd throughput in the first year, ramping up to 32,500 bpd by the beginning of the third year. After allowing for refinery crude usages, refined product output will be 31,250 bpd. We have assumed that the refinery is up and running in the late 2003, although some product will be sold during the commissioning and testing stage.
- Refined products including diesel, kerosene/jet fuel, marine diesel, motor gasoline and LPG's will be produced for domestic consumption and export markets. In addition, high-quality naphtha will be produced for exporting to an already contracted major oil trader. The quality of the naphtha is suited to the large South East Asia petrochemical industry.
- Revenue assumptions are based on the 1993-99 average **Singapore refinery price - Kutubu spread** for various products. The crack spread is one of key elements impacting all refineries. With the refinery selling product at the Import Parity Price ("IPP") and buying crude at market price, the gross margin will be determine by the margin between IPP and Kutubu crude. **In our model the weighted average margin for all products is forecast to be around US\$10.25 per barrel** and from this, we deducted the operating costs of the refinery.
- Even though it is of modest size, the refinery will have low operating costs because of its simplicity. The economics of the refinery are compelling - **forecast earnings of US\$60 million per annum, or US\$2.50 per fully diluted share (\$3.85 in Canadian funds). With the current share price trading at approximately \$10 per share InterOil is trading at less than 3X forecasted operating earnings.**
- The following Table provides the trading comparables for Canadian listed integrated oil and gas companies. All of these companies are substantially larger than InterOil, and with the exception of Hurricane Hydrocarbons, have all, or the majority, of their assets in Canada. Nevertheless, we would argue that InterOil is trading at a bargain basement valuation. As the refinery project moves towards completion we expect that InterOil's share price will see significant appreciation.
- **We would also suggest that the exploration opportunities, offered by InterOil's upstream holdings, add significant speculative appeal. We expect that, in time, InterOil will attract a P/E ratio closer to some of the Canadian comparables. If we conservatively consider only Hurricane's multiple of 6.5X we can see a share price in the mid \$20's.**

		Previous Close	ACTUAL 2001				ESTIMATED 2002			
			FD EPS	P/E	FD CFPS	P/CF	FD EPS	P/E	FD CFPS	P/CF
Hurricane Hydrocarbons Ltd.	HHLA	21.85	\$3.37	6.5X	\$3.87	5.6X	\$3.48	6.3X	\$4.38	5.0X
Husky Energy Inc.	HSE	16.55	\$1.64	10.1X	\$4.68	3.5X	\$1.00	16.6X	\$3.87	4.3X
Imperial Oil Ltd.	IMO	48.30	\$3.16	15.3X	\$5.06	9.5X	\$2.13	22.7X	\$4.01	12.0X
Petro-Canada Ltd.	PCA	43.12	\$3.38	12.8X	\$6.32	6.8X	\$2.14	20.1X	\$5.36	8.0X
Shell Canada Ltd.	SHC	55.10	\$3.65	15.1X	\$5.41	10.2X	\$1.98	27.8X	\$3.62	15.2X
Suncor Energy Ltd.	SU	54.66	\$1.61	34.0X	\$2.93	18.7X	\$2.04	26.8X	\$4.87	11.2X
Average				15.6X		9.1X		20.0X		9.3X