Venture Research LLC

July 16, 2009
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Magnum Hunter Resources Corp NYSE Amex:MHR

Recommendation: Speculative Buy
Target Price: $1.10
Recent Price: $0.68
Initiating Coverage

Investment Summary

- Recent name change to Magnum Hunter Resources Corp from Petro Resources Corp.
- New, highly experienced management team is expected to grow the company through accretive acquisitions. Gary Evans, CEO and Ronald Ormand, CFO have been recruited and assumed these positions in May, 2009. Mr. Evans was the founder and CEO of Magnum Hunter Resources for twenty years before it was sold to Cimarex in 2005 for $2.2 billion. Over 100 acquisitions were made during this period. Mr. Ormand was most recently head of O&G Investment Banking for West LB, a German bank with $300 billion in assets.

- New strategy is to grow via accretive acquisitions. Current assets portfolio is good but only one field offers significant growth. Plan is to move from non-operated working interests to assume operating control. Disposition of some assets may be pursued. Management believes funding is available given distressed prices and their track record.

- Adequate liquidity. Capex has been cut over 50% from 2008 but the cash flow from operations should fund investments the rest of the '09 CY. The Company has $6.5 million of additional borrowing capacity should that be required. Management believes funding is available for their needs.

- Existing prospects justify $1.10 price target.

- Highly leveraged to production and commodity price increases, especially natural gas. A $10/barrel ($1.67/MCF) increase of net sales price increases the NAV $0.60/share, a nearly 100% increase over current levels. Acquisitions would likely retain this exposure.

Near Term Catalysts
- Accretive acquisition
- Production from Surprise Prospect
- Market awareness of disparity between price and value
- Higher natural gas prices

Snapshot			Estimates and Summary					
Shares Out, Basic and Diluted	36.8		FY end Dec 31	'07A	'08	'09E	'10E	'11E
Market Cap, $mil	$25		Production, boepd	342	572	861	1,404	1,691
Avg. Daily Volume (3 mo)	288,786		% Oil	79%	64%	43%	33%	26%
Net Debt, $ mil, mrq	$19.4		Net Sales Price,$/boe	$55.50	$69.43	$36.28	$38.87	$46.21
Book Value/sh	$0.88		EPS fd	(0.28)	(0.21)	(0.11)	0.04	0.23
P/B mrq	0.77		CFPS	0.04	0.09	0.05	0.16	0.32
P/S, ttm	1.7		P/CF	-	6.5x	13.6x	4.2x	2.1x

	Q1'09A	Q2'09E	Q3'09E	Q4'09E	FY'09E
WTI,$/B	43.18	58.90	67.00	66.00	58.70
Henry Hub,$/MCF	4.49	3.81	3.75	4.27	4.14
NSP,$/B	27.62	38.37	37.01	36.83	36.75
Revenue, $000	1,917	2,490	3,027	3,759	11,193
EPS	-0.04	-0.01	-0.03	-0.03	-0.11
CFPS	0.02	0.01	0.01	0.01	0.05

See last page for analyst certification and disclosure

Summary and Conclusion

MHR is a small, diversified O&G company with operations across the US most of which are low risk, development, non-operated interests. A very experienced management team has just recently (May 2009) been brought in to revamp operations. Their strategy is to grow via accretive acquisition and in so doing operate more of their assets than they do now. The recession and collapse of oil and gas prices presents opportunity to acquire assets at distressed prices. Management has significant experience in this area and grew Magnum Hunter Resources (prior company) through the several business cycles. The primary reason for ownership would be management's deal making experience, their ability to secure financing on attractive terms, and a recovery of commodity prices over the next 12-18 months.

This is a classic entrepreneurial oil and gas operation. They have some mature fields that are very low risk and generate cash, and participate in one exploratory field that, potentially, could be a real winner. The pricing assumptions in the forecast periods are very conservative: only an average of 20% increase over the next three years.

They have a 10% working interest in an exploratory field; the Surprise Prospect in East Texas that appears will be very successful. Goodrich (NYSE:GDP) is the operator and Devon (NYSE: DVN) is the 3rd partner in this field with multiple targets including the Haynesville and Bossier shales. The first four wells were successful. Although speculative, this field could have as much as 6 BCF gas to MHR's 10% interest and contribute to a near 3 fold production increase in the next three years.

Based on a fundamental valuation (price to book, price to sales, and price to earnings) MHR is currently 30% undervalued relative to its Peer Group. The target price is the NAV calculated based on production from existing fields, using very conservative commodity prices, discounted at 10%. An additional 20% risk adjustment was then applied to get a target price of $1.10/share.

Asset Base Discussion

"Cinco Terry Prospect" Permian Basin Crockett County, TX (Oil and Gas)

This is a 38,000 acre prospect operated by Approach Resources (NASDAQ: AREX) in which the Company acquired a 10% working interest (WI) in 2007. The primary objective is the Canyon Sand (7,500- 8100 ft) gas and the Ellenberger at 8,200- 8,800 ft (oil). These are low risk development wells (66 successful of 69 drilled to date). 38 wells were drilled in '08 and budget is 24 in '09. About 150 drill sites have been identified so several more years of drilling is expected. Average production has been 60 boepd gross and 6 boepd net and typical EUR is 100,000 – 350,000 per well.

"Secondary Recovery Project" -Williston Basin, North Dakota

In Q1 '07 the Company acquired a 43% WI in 15 fields operated by Eagle Operating Inc. They initiated a secondary recovery project in 2002 and now 7 of the 15 fields are showing positive response to the water flood re-pressurization program. The wells produce about 5 boepd gross or 351 boepd net to MHR in aggregate. Although very significant upside volumes exist as the water flood continues, capex has been curtailed in 2009 due to low oil prices and margins.

"Surprise Prospect" – Nacogdoches County, East Texas

Company acquired a 10% WI in this 3,000 acre prospect with options to acquire another 10% of an additional 3,000 acres. The operator is Goodrich Petroleum (NYSE: GDP) and Devon (NYSE:DVN) is the 3rd partner. The prospect targets a number of horizons including the James Lime, Travis Peak, Cotton Valley, Bossier and Haynesville shales. The first four wells drilled were all successfully completed and brought on to production early 2009. The fifth well was still being drilled as of 3/2/09.

Surprise Prospect- Initial Results			
	Initial Production		
Well	MCF/day	WI	Result
Hill No. 1	9,400	10%	Completed in Bossier Sand Shale
Tucker No. 1	600	5%	200 ft pay in Haynesville Shale, completed in Bossier Shale. Ultimately will be completed in Travis Peak
Lilly No. 1	3,000	10%	Completed in Travis Peak
Grigsby No. 1	2,900	10%	Completed in Travis Peak
Lewis No. 1	n/a	10%	Plan to test Haynesville and Bossier Shale as well as Travis Peak
Total	13,900	-	-

The 600 MCF/day production should be ignored as not being representative of the gas in the shale (needs horizontal wells and fraccing to optimize production). The statement that it will ultimately be completed in the Travis Peak indicates a triple play with success in three intervals from a single well. The conclusion is that this delineation drilling was very successful. Wells in this area typically are drilled on 640 acre spacing so there will eventually be 11 wells in the prospect assuming the option on the next 3,000 acres is taken up. MHR has an option to acquire 10% of this additional acreage at $1,000/acre (300 net acres x $1,000 = $300,000).

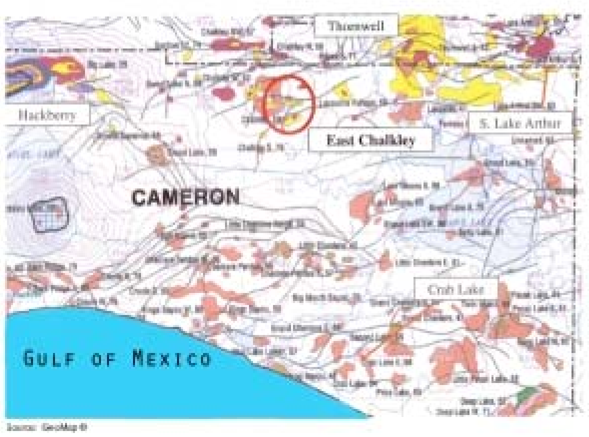
The geologic setting is similar to prolific fields nearby: see Table below. Seismic reports are positive. According to the US Geologic Service the Travis Peak-Hosston assessment unit contains 1.0 trillion cubic feet (TCF) of undiscovered conventional gas in the East Texas Basin. The Haynesville Shale is a massive unconventional gas play centered in north east Louisiana and apparently extends to East Texas. Petrohawk (NYSE:HK) has wells producing as much as 17 MMCF/day from 212 feet of pay in the Haynesville (Elm Grove Plantation #63) but this well was horizontal and had numerous hydraulic fracturing steps to get this level of production as is standard for shale fields.

Nearby Fields With Similar Geology (Per Company)		
Field	2007 Production, BCF*	Year Discovered
John Amoruso	59	2005
Savell	77	1997
Hilltop	Encana (NYSE:ECA) has nine active rigs and has identified 250 drilling locations	

* Source: Energy Information Administration, Top 100 Oil and Gas Fields, Encana

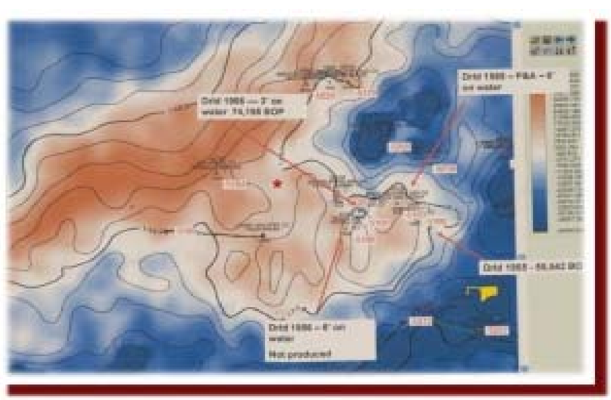
Estimating the reserve potential using only initial production (IP) data is speculative, but a rule of thumb is the estimated ultimate recovery (EUR) is 1,000 times the IP for deep gas wells in this region. In other words the well will produce quickly but only last three years. The average of the three conventional wells is 5 MMCF/day, times 1,000 equals 5 BCF/well EUR, times 11 wells x 10% WI is 6.0 BCF net to MHR equals 1 MMBOE. Even at today's low gas prices this will be very welcome source of revenue.

"East Chalkley Prospect"– Cameron Parish, Louisiana



This is a 714 acre prospect in which MHR has a 34% WI. The initial well was successful and brought onto production in late 2008. The '09 capex budget is \$900,000 and EUR is 2.5 MMB. Initial production was 100 bopd gross.

"Leblanc Prospect" – Allen Parish, La



This prospect is operated by MHR who have a 100% WI and plan to drill in Q2/Q3 '09. This is a shallow well with good seismic and has an EUR of 400,000 bbl.

Chama Basin, Northern New Mexico

This is a 90,000 acre prospect operated by Approach Resources and MHR has a 10% WI. The target is shallow oil with an unrisked potential of 30 million barrels and 1,200 prospective drill sites. Unfortunately pending regulations are holding up drilling and production.

"Boomerang Prospect" New Albany Shale/Illinois Basin – Kentucky

This is a 74,000 acre prospect in southwest KY that is prospective for natural gas. Targets are shallow wells of 1,500 to 3,500 ft depth. MHR has a 6.8% WI and the field is operated by Approach Resources.
Three test wells were drilled in 2007 but not completed or turned to sales.

Operating and Financial Results

Gas production has been growing at an average rate of 33% vs. the prior quarter while oil production has been much slower. This is due to the Cinco Terry Prospect growth vs. Williston Basin.

Production History and Trend						
	Q1'08	Q2'08	Q3'08	Q4'08	Q1'09	Avg. Growth vs. Prior Quarter
Oil, barrels	30,179	30,670	35,012	36,810	33,369	2.9%
Gas, MCF	42,275	75,637	105,239	117,901	121,874	33.4%
Natural gas liquids, barrels	4,035	5,522	4,801	4,786	12,100	44.1%
Production, BOE	41,260	48,798	57,353	61,246	65,781	12.5%
Production, % Oil	73%	63%	61%	60%	51%	-

Q1 '09 Results: Production was 65,781 BOE a 7.4% increase vs. prior quarter and 59% increase vs. year on year. Revenue was $1.8 million, a 20% decline vs. prior and 39% decline YoY. Lease operating expenses were $18.92/BOE, a 12% decline vs. prior quarter and 36% decline YoY.

Operating productivity (Lifting costs or lease operating costs per boe) has improved substantially and Q1'09 was the best quarter in the last year.

	2007FY	Q1'08	Q2'08	Q3'08	Q4'08	2008FY	Q1'09
LOE, $/BOE	28.15	29.63	27.60	26.02	21.52	25.78	18.92

Capital Expenses

Since MHR uses successful efforts accounting practices the cost of dry holes are expensed in the period incurred. As shown below dry holes represented 12.4% of capex in 2007 and 45% in 2008. Six wells in North Dakota (two deep and four shallow) were expensed and two prospects in New Mexico and Colorado were written off in FY 2008.

Management projects a $7.3 million capital budget in 2009 and most of this is directed to the Cinco Terry and Surprise prospects in Texas. Expenditures in Q1 were $4.5 million therefore leaving $2.8 million for the next three quarters.

	2007FY	Q1'08	Q2'08	Q3'08	Q4'08	2008FY	Q1'09
Capital Expenditures	14,266,262	1,928,169	4,321,138	6,043,395	3,930,088	16,222,790	4,499,467
Exploration-Expensed	1,767,898	572,510	376,654	2,179,388	4,559,226	7,348,778	94,475
Dry Holes,% CapEx	12.4%	29.7%	8.7%	36.1%	116.0%	45.3%	2.1%

Production and Reserves		
	2007	2008
Extensions and discoveries, m boe	573	1,140
Revisions of previous estimates	(16)	(530)
Improved recovery	709	-
Net Increase	1,266	610
Production	125	209
Reserve Replacement Ratio	10.1	2.9
Proved Reserves, mboe	2,716	3,118
Proved Undeveloped Reserves (PUD)	984	1,298
PUD,% Proved	36%	42%
Reserve Life Ratio	0.2	13.0
Net wells	-	76.1
Average Reserves/well, mboe	-	35.7
Average daily production/net well, boepd/well	-	7.5
Net acreage, developed	-	7,784
Net acreage, undeveloped	-	43,281
Finding Costs (Capex), $mil	14.3	16.2
Net Reserve Increase, mboe	1,266	610
Finding Costs, $/boe	$11.29	$26.55

Liquidity. As of 3/31/09 MHR had working capital of $3,450,745 vs. $6,682,370 on 12/31/08; a decrease of 49%. On September 8, 2008 and March 19, 2009 MHR entered into a $50 million Credit Agreement and $15 million Second Lien Term Loan with CIT Capital USA and other lenders. The March amendments were necessary due to non-compliance with interest and debt covenants during Q4 '08. The defaults were waived but the borrowing base under the Credit Agreement reduced from $17 million to $12 million and other changes in the covenants and interest rates tightened. The Company has drawn down all $15 million of the Term facility and $6.5 million of the Credit line to replace the original credit facility established when they acquired the Williston Project in 2007. Assuming the interest and debt covenants do not restrict borrowings, MHR has $5.5 million in borrowing capacity. This should cover the capex which is budgeted at $7 million and $4.5 was spent in Q1. Management states the covenants are acceptable.

Derivatives. MHR has entered into several derivative financial transactions to hedge their oil and gas production. These instruments do not qualify for hedge accounting under SFAS 133 and are classified as Level Two under SFAS, Fair Value Measurements because they are transactions with private parties but based on public commodity indexes. Consequently the changes in fair value are reported in the financial statements.

The instruments are a swap agreement with a 3rd party requiring the 3rd party to pay MHR the fixed price and MHR to pay the floating price based on the NYMEX WTI month end price. In October 2008 they entered into an agreement for 207,500 barrels from October 2008 till December 2011 at $105/barrel. There was no cost to establish this contract but obligations are netted monthly to the party that is due funds. In June 2008, the height of the market, MHR bought put options on 100 b/d through 2009 with a strike price of $110/bbl at a cost of $363,175. In October 2008 they bought natural gas put options at a strike price of $7.75/MCF for 20,000 MCF/mo through CY 2009 at a cost of $200,400. This was extremely prescient since with the drop in commodity prices the oil and gas puts had a fair value of just over $2 million on 3/31/09 or 4 times their cost. In addition, the derivatives in aggregate generated about $1 million cash in Q1 '09 and this will continue at this rate throughout 2009 if commodity prices remain at current depressed levels. Higher prices, of course, will bring greater revenue more than offsetting potential derivative losses.

Derivative History

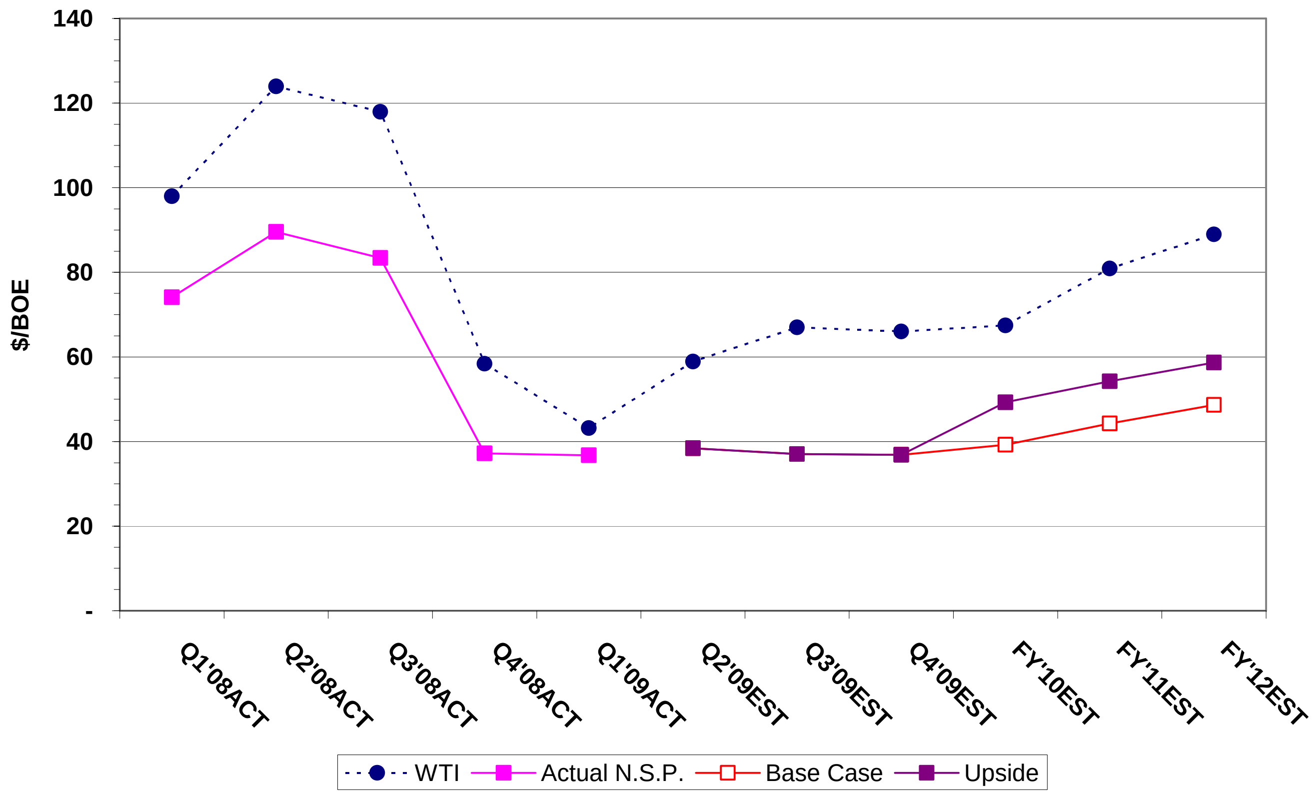
	Q1'08	Q2'08	Q3'08	Q4'08	2008FY	Q1'09
Oil Fixed Price, $/B-Receive	66.74	73.23	71.47	87.70	65.70	90.25
Oil Floating Price, $/B- Pay	97.95	123.96	117.98	58.37	58.37	42.96
Reported Derivatives Gain/(loss), $	(685,594)	(2,778,056)	2,477,405	8,297,500	7,311,255	556,315
Unrealized,$	(208,109)	(2,043,288)	1,399,820	9,967,722	9,116,145	(498,417)
Realized, $	(477,485)	(734,768)	1,077,585	(1,670,222)	(1,804,890)	1,054,732
Hedged Volume, boepd	169	159	141	226	-	317
Production, boepd	453	536	630	673	-	723
% Production Hedged	37%	30%	22%	34%	-	44%

Q1 2009 Results. Production was 730 boepd in Q1'09 a 58% increase YoY and 7% increase in the sequential quarter. Net Selling Price (NSP) was $27.62/boe vs. $74.11 YoY and down 26% sequentially. Lease operating expenses were $18.92/boe vs. $29.32 Q1'08, a 36% decline. General and administrative costs were $11.35/boe vs. $31.33 YoY. The prior year included $594,365 of stock and option expenses but were only $192,775 in Q1'09. The operating loss was $1,476k vs. $455k YoY primarily due to much lower commodity prices.

Valuation

Method 1 NAV. Appendix Tables 1 and 2 show a summary DCF analysis of the projected cash flows. The production estimates are based on a field by field evaluation (see Appendix Table 3). The projected growth from the Surprise Prospect accounts for 50% of the total Company growth from '08 to '11 and the corresponding decline of oil as a % of production from 64% in '08 to 26% in '11 Production is forecast to grow 46% in '09 and then 60% in '10 due to continued growth at Cinco Terry and new wells in the Surprise Prospect and drilling in South Louisiana more than offsetting declines from Williston. No production is assumed from the Chama Field or Kentucky/New Albany Basin Field. Commodity prices are uncertain give the recession and timing of a recovery. A very conservative Base Case pricing scenario is that the MHR Net Selling Price (NSP) slowly increases to 70% of the '08 value of $69/boe. This takes into account the increasingly higher gas proportion of production and relatively lower gas prices vs. oil.

Figure 1
Price History and Forecasts



The Upside Case is for $10/bbl higher NSP in '10,'11 and '12.

MHR has experienced a substantial pricing discount relative to the WTI standard due to location and quality discounts as well as lower natural gas prices

Lease operating expenses are expected to continue to drop due to the recession and over supply and MHR focuses on cost controls. General and admin costs/boe should drop as production grows. The '09 capex budget is <50% of '08 or about $7 million. I am assuming even lower capex in the next few years but will result in increased production nevertheless.

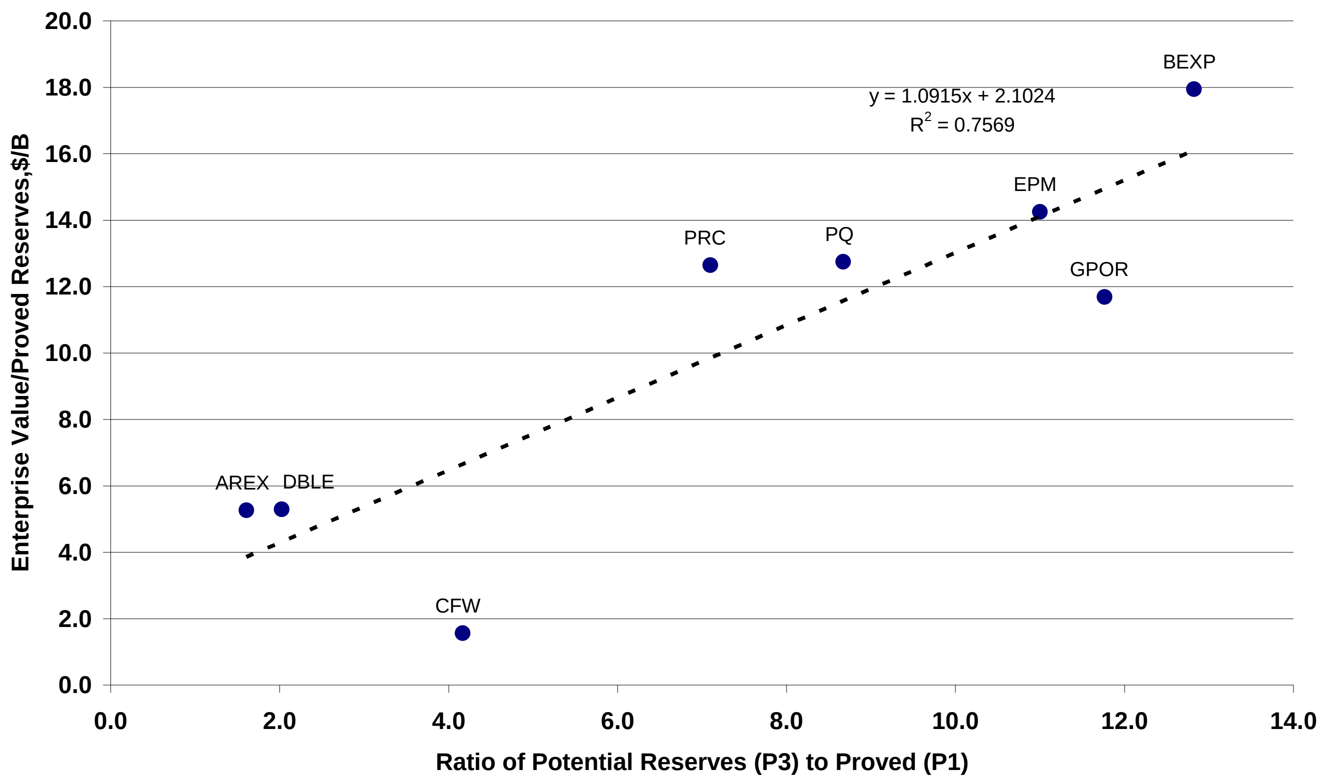
This analysis assumes the free cash flow and terminal value (5 times the 2012 operating cash flow) is discounted back at 10%. An additional 50% discount is applied to be conservative, address current financial risk, prospective nature of assumed cost reductions and aggressive finding costs of new reserves. See Appendix Tables 1 and 2 for detail.

NAV Analysis		
	Base Case	Upside
Avg. '10-'12 NSP, $/boe	$44	$54
NAV, $/sh	$1.08	$1.69

The NSP in Q1'09 was $27.62 so the Base Case is moderate price increases for the next three years but coupled with the dramatic production increases and cost controls produce very profitable operations. The Upside Case shows the sensitivity of the NAV to prices: a $10/bbl increase increases NAV $0.61 or nearly 60% higher.

Method 2- Reserve Multiple. Examining a Peer Group to determine a valuation multiple shows a wide range. In Figure 1 below I show an Enterprise Value (EV) to Proved Reserves (P1) ratio between 1.8 and 18 for an apparently similar group of companies. The explanatory factor is that the companies have widely ranging variances of growth prospects as measured by the potential reserves (proved plus probable plus possible or P3) to P1 Ratio. This ratio explains 75% of the variance of the EV/P1 values. This is a reasonable result as one would expect some of the potential reserves to eventually become proved given good management, money and perhaps some luck.

Figure 2
Peer Group Valuation Multiple ($/B) vs Reserve Growth Potential



MHR has unrisked potential net reserves of about 23MMbbl (P3) which is 7.7 times the P1 value of 3.0MMbbl as of 12/31/08. The Company is trading at about 13 times the P3/P1 ratio which is above the trend line but not unreasonable. Going through a field by field analysis (Appendix Table 3) I risked the P3 reserves 48% to 10 MMbbl which is a very rough estimate of P1 reserves in 1-2 years given these assets. Applying the mean EV/P1 multiple of 10.0 times 10MMbbl you have an EV of $104 million. Adding the net cash ($7 mil) and dividing by the outstanding shares gives you a target price of $2.47 (111/45).

Method 2- Reserve Multiple		
'09 Potential Reserves (3P Basis), MMBOE	23	Unrisked
'09 Potential- Risked	10.4	Risked Reserves
12/31/08 Proved reserves	3.0	
Ratio 3P/1P Reserves	7.6	
Development Cost, $mil	20	Estimate
Apparent Finding Cost, $/bbl	0.86	low due to mature low risk fields
Assumed Enterprise Value/P1 Ratio	10	per Fig 1
Imputed Enterprise Value, $mil	104	EV/P1 Ratio x risked Reserve Potential
Less Net Debt, $mil	(12)	
Market Cap	92	
Shares Outstanding, mil	37	
New Shares Issued @ $0.37/sh	8	
Future Shares Outstanding,mil	45	
Target Value, $/share	$ 2.03	

The projected cumulative operating cash flow from '09-'12 is >$30 million which is about 150% of the estimated capex providing a reasonable cushion and suggesting additional debt may not be necessary. The dilution noted is from the vesting of options and restricted shares recently awarded the management team.

Method 3 – Peer Group Fundamentals. The selected Peer Group of eight companies can be used to value MHR today. After eliminating the outliers the mean price to book, price to sales and price to earnings can be calculated. MHR is valued at a discount to the Peer Group mean P/B but higher than P/S ratio. The P/E below is for MHR FY'11 EPS. Applying the mean ratio's to MHR book value, sales and '11 EPS and taking the average of the three methods gives a valuation of $1.02/share which is 50% higher than the current $0.68 value.

Peer Group Fundamentals				
	P/B	P/S	P/E	Avg. of 3
Peer Group Avg.	0.90	1.14	7.9	
MHR	0.77	1.71	3.0	
MHR Price @ Peer Group Multiple,$/sh	0.80	0.45	1.82	1.02

This analysis excludes the growth prospects reviewed in Methods 1 and 2. See Table 3 for detail.

A target price of $1.10 over the next 12 months is accepted as the approximate value of the NAV (Method 1). If commodity prices, especially natural gas, begin to increase, then the upside target of $1.50 would be considered. The Reserve Multiple Method #2 value is substantially higher and not considered but does support a valuation above $1.00/share. This value gives additional support to an M&A strategy.

Valuation Summary				
Method	Peer Fundamentals	NAV Base Case	NAV Upside	Reserve Multiple
Current Value	$1.02	-	-	-
Target Price 12-18 Months	-	$1.08	$1.69	$2.03

Management

Gary C. Evans serves as Chairman of the Board. Mr. Evans founded and served as the Chairman and Chief Executive Officer of Magnum Hunter Resources, a NYSE listed company, for twenty years before selling Magnum Hunter Resources to Cimarex Energy for approximately $2.2 billion in June 2005. In 2005, Mr. Evans formed Wind Energy, LLC, a renewable energy company which was subsequently acquired in December 2006 by GreenHunter Energy, Inc.; a NYSE Amex listed renewable energy company focusing on biodiesel, wind and biomass power. Mr. Evans has served as Chairman and Chief Executive Officer of GreenHunter Energy, Inc. since December 2006. Mr. Evans serves as an Individual Trustee of TEL Offshore Trust, a NASDAQ listed oil and gas trust, and is the Lead Director of Novavax Inc., a NASDAQ listed clinical-stage vaccine biotechnology company. Mr. Evans was recognized by Ernst and Young as the Southwest Area 2004 Entrepreneur of the Year for the Energy Sector and was subsequently inducted into the World Hall of Fame for Ernst & Young Entrepreneurs.

Don Kirkendall serves as President. Mr. Kirkendall brings more than 25 years of diversified energy experience to Magnum Hunter Resources. His background includes six years of interstate pipeline business along with 19 years of natural gas marketing and exploration experience. Mr. Kirkendall received his BBA from Southwest Texas State University.

Jim Denny serves as Executive Vice President and Chief Operating Officer. Mr. Denny brings more than 35 years of industry related experience to the company. Prior to joining Magnum Hunter Resources, Mr. Denny served as President and Chief Executive Officer of Gulf Energy Management Company, a wholly owned subsidiary of Harken Energy Corporation. He is a registered Professional Engineer (Louisiana) and is a Certified Earth Scientist. He is also a member of various industry associations, including the American Petroleum Institute, National Society of Professional Engineers, Society of Petroleum Engineers, and the Society of Petroleum Evaluation Engineers. He is a graduate of the University of Louisiana-Lafayette with a B. S. in Petroleum Engineering.

Ron Ormand serves as Chief Financial Officer and Executive Vice President. Mr. Ormand is a member of the Board of Directors of Tremisis Energy Acquisition Corporation II, a NYSE Amex listed special purpose acquisition corporation, and served as President and Chief Financial Officer of Tremisis from November 2007 to March 2009. Mr. Ormand has over twenty-five years of investment and commercial banking experience in the energy industry. From April 2005 to October 2007, he served as a Managing Director with West LB, a German-based international bank with over $300 billion in assets, where he covered the energy industry and served as Head of the Oil and Gas Investment Banking Group for the Americas. Mr. Ormand received a B.A. and an M.B.A. from the University of California at Los Angeles and attended Cambridge University in Cambridge, England where he studied Economics.

Harry Stout serves as our Executive Vice President and General Counsel. From August 1991 until the merger of KCS Energy into Petrohawk Energy Corporation during August 2006, he served as President of KCS Energy Services, Inc. where he was responsible for closing more than $400 million in producer finance acquisitions. Mr. Stout received a B.S. degree from Stephen F. Austin State College and a J. D. from St. Mary's School of Law.

Allen R. McGee serves as Senior Vice President and Chief Accounting Officer. Mr. McGee began his career with Arthur Andersen in 1971 in the auditing department. He then served three years at Gulf Oil

Corporation with his last position being Director of Financial Accounting for Gulf Oil Refining and Marketing. Mr. McGee received his BBA from Baylor University and is a Certified Public Accountant.

Risks

Upside Risks: The commodity prices assumed are very conservative. If the developed world economies recover more quickly their demand will increase especially when coupled with ongoing demand from the emerging markets such as China, India, Brazil and Russia. Natural gas prices are a more local market and have fallen drastically. Drilling activity has fallen off dramatically and if demand recovers more quickly, supplies may not be adequate resulting in higher prices which will benefit MHR due to their increasing exposure to gas from the Surprise prospect. The valuation does not assume accretive acquisitions are made so these would represent upside values.

Downside Risks: Significant production increases are forecast for the Surprise Prospect in East Texas which may not be realized, or not in the time frame forecast. The assumed capital expenditures required may not be sufficient. MHR may not have the cash to meet capital calls in a timely manner. Working capital has fallen significantly in the last quarter both sequentially and over the last year. Continued low commodity prices could worsen this situation. MHR mostly has small non-operated positions in each field and is not able to influence the operator as to any key decisions. For example an operator may choose to develop other fields than the one in which MHR has an interest. The stock is very thinly traded and is likely to remain very volatile for the foreseeable future.

Date	Recommendation	Price Target
July 16, 2009	Buy	$1.10

DISCLOSURES

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About

Venture Research LLC is an independent research and consulting firm offering equity research services on micro capital stocks for institutional investors, broker/dealers, registered advisors and investors. The Company is not a broker/dealer and does not expect investment banking compensation.

Mr. Mahaffey began his career with Exxon in engineering and later moved into board room level international business development for a major petrochemical company. He conducted merger and acquisition services for The Sterling Group in Houston, TX and led an LBO program for a Boston based investment firm. He worked with an SEC Registered Investment Advisor and has held Series 7 and 65 licensees. He has covered chemical, oil and gas, refining and energy stocks as an independent equity analyst with Redchip and other research providers. He is a private investor in oil and gas prospects. He received a "Five Star" rating from Yahoo Finance for performance results from coverage of oil refiners. He has been quoted in numerous local and international publications including Bloomberg News. Mr. Mahaffey holds a BS in Chemical Engineering from Louisiana State University and an MBA from The Wharton School, University of Pennsylvania. He holds the Chartered Financial Analyst (CFA) charter and is a member of the New York Society of Securities Analysts.

Table 1
NAV- Base Case- Slow Commodity Price Recovery

	2008Act	2009Est	2010Est	2011Est	2012Est	Terminal Value
Production, boe	208,657	314,094	512,576	617,077	678,785	
Sales realization, $/b	69.43	36.28	38.87	46.21	51	
Lease Operating Costs, $/boe	25.78	19.5	20.0	20.0	18.0	
G&A,$/boe	19.0	9.0	5.5	4.6	4.2	
Interest Expense,$/boe	5.0	-	-	-	-	
Other Costs	8.7	(1.0)	-	-	-	
Operating Cash Flow, $/boe	11.0	8.8	13.4	21.6	28.7	
Operating Cash Flow, $	2,303,533	2,754,788	6,843,716	13,348,179	19,460,076	
Capex,$	(16,222,790)	(7,499,000)	(6,000,000)	(5,000,000)	(5,000,000)	
Free Cash Flow, $	(13,919,257)	(4,744,212)	843,716	8,348,179	14,460,076	97,300,379
Present Value of Cash Flows, $		$12,532,902				
Present Value of Terminal Value		$60,415,880				
Total Present Value		$72,948,783				
Less Net Debt		($12,392,211)				
Risk Factor		20%				
Net Present Value, Risked		$48,445,257				
Shares Outstanding		45,000,000				
Present Value, $/sh		$ 1.08				

Table 2
NAV- Upside Price Recovery Case: + $10/B vs Base Case in '10-'12

	2008Act	2009Est	2010Est	2011Est	2012Est	Terminal Value
Production, boe	208,657	314,094	512,576	617,077	678,785	
Sales realization, $/b	69.43	36.28	48.87	56.21	60.83	
Lifting Costs, $/boe	25.78	19.5	20.0	20.0	18.0	
G&A,$/boe	19.0	9.0	5.5	4.6	4.2	
Interest Expense, $/boe	5.0	0.0	0.0	0.0	0.0	
Other Costs	8.7	(1.0)	-	-	-	
Cash Flow, $/boe	11.0	8.8	23.4	31.6	38.7	
Operating Cash Flow, $	2,303,533	2,754,788	11,969,475	19,518,953	26,247,927	
Capex,$	(16,222,790)	(7,499,000)	(6,000,000)	(5,000,000)	(5,000,000)	
Free Cash Flow, $	(13,919,257)	(4,744,212)	5,969,475	14,518,953	21,247,927	131,239,635
Present Value of Cash Flows, $		$26,041,454				
Present Value of Terminal Value		$81,489,488				
Present Value		$107,530,942				
Less Net Debt		($12,392,211)				
Risk Factor		20%				
Net Present Value, Risked		$76,110,985				
Shares Outstanding		45,000,000				
Present Value, $/sh		$ 1.69				
Assumptions						
Discount Rate, %			10%			
G&A Costs, $/boe			decline inversely with production			
Terminal Value, multiple '12 cash flow			5			
12FYvs FY'11 Production/NSP increase			10%			

Table 3
Peer Group Fundamentals

Symbol	Name	Last Trade	52-wk Range	Market Cap,$mil	P/B	P/S	P/E, F'wrd	EBITDA, $mil	Ent. Value, $mil
DBLE	Double Eagle Petroleum Co	3.92	3.00 - 18.99	36	0.67	0.73	5.5	30.7	78.3
AREX	Approach Resources	6.68	3.2-26.46	138	0.61	1.95	24.7	47.1	185
CXPO.OB	CRIMSON EXPLORATION	3.4	0.80 - 14.65	21.89	0.17	0.13	-	66.0	328.5
GPOR	Gulfport	5.81	1.50-15.73	248	1.98	1.82	9.0	83.6	298
PQ	Petroquest	2.83	0.61-28.62	144	0.74	0.47	9.3	213.6	393
BEXP	Brigham Exploration	2.71	1.04-17.62	126.7	43	1.13	-	92.0	410
CFW	Cano	0.68	.22-7.09	30	0.19	0.75	-	(2.2)	75
EPM	Evolution	2.41		68	1.97	8.43	-	0.2	57
Average					0.90	1.14	7.93		
MHR	Magnum Hunter Resources	0.68	0.19 - 3.36	25.0	0.77	1.71	3.0	-2.44	39.2
								Avg. of 3	
MHR Price at Peer Group Mean					0.80	0.45	$1.82	1.02	

Table 4 Field Summary and Assumptions

Basin	State	Comment	Gross Acres	Working Interest, %	Gross Reserve Potential ,MMBOE	Basis	MHR Net Reserve Potential, MMBOE	Risked Factor	MHR Risked Reserves, MMBOE	Est. Capex '09-'11 Total
Cinco Terry Prospect	Texas-Permian Basin	Approach Resources is operator, multi-year drilling plan, 24 wells in 2009, 90% success in 2008	38,000	10%	30	150 wells @ 200,000B/wel	3.0	1	3.0	9
Williston Basin	North Dakota	Secondary Recovery program underway in six fields	15,000	43.50%	25	stated	8.9	0.5	4.5	2
Surprise Prospect	TX- Nacogdoches Cty	Goodrich Petroleum operates, 100% success in initial drilling- 5 wells producing	7,000	10%	10	11 wells at 5.5 BCF/well	1.0	0.8	0.8	5
East Chalkley	LA- Cameron Parish	1st well drilled and producing	714	34%			0.9	0.8	0.7	0.9
Leblanc Prospect	LA-Allen Parish	MHR operates, will drill in 2009	240	50%			0.4	0.5	0.2	0.8
Chama Basin	New Mexico	Drilling deferred pending regulatory issues	90,000	10%			2.4	0	-	0
Boomerang Prospect, New Albany Shale	KY- Illinois Basin	Approach Resources operates, long lived/low production gas field, shallow wells. Test wells not successful.	72,000	6.70%			6.3	0.2	1.3	0
Misc/New		TBN								2
Total							22.9	0.45	10.4	20

Table 5- Income Statement, $000

	Q1'08ACT	Q2'08ACT	Q3'08ACT	Q4'08ACT	FY'08ACT	Q1'09ACT	Q2'09EST	Q3'09EST	Q4'09EST	FY'09EST	FY'10EST	FY'11EST
Production, boe	41,260	48,798	57,353	61,246	208,657	65,781	66,871	85,899	99,293	314,094	512,576	617,077
Production, % oil	73%	63%	61%	60%	64%	51%	48%	34%	39%	43%	33%	26%
Commodity Price, Oil, WTI,$/b	98	124	118	58	100	43	59	67	66	59	67	81
Gas, Henry Hub, $/MMBTU	$ 8.72	$ 11.47	$ 9.00	$ 6.38	$ 8.89	$ 4.49	$ 3.81	$ 3.75	$ 4.27	$ 4.14	$ 5.49	$ 6.59
PRC, Net Sales Realization, $/boe	$ 74.12	$ 89.52	$ 83.39	$ 37.18	$ 69.43	$ 27.62	$ 37.24	$ 35.23	$ 37.86	$ 36.28	$ 38.87	$ 46.21
Total Revenue	3,158	4,368	5,965	2,392	15,883	1,917	2,490	3,027	3,759	11,193	19,922	28,517
Lease Operations	1,222	1,347	1,492	1,318	5,379	1,245	1,204	1,546	1,787	5,782	9,226	11,107
Exploration	573	38	2,179	4,559	7,349	94	67	86	99	347	1,025	1,234
Operating Expenses	1,795	1,384	3,672	5,877	12,728	1,339	1,271	1,632	1,887	6,128	10,252	12,342
Gross Profit	1,363	2,984	2,293	(3,485)	3,155	578	1,220	1,394	1,872	5,065	9,671	16,175
Sales, General and Admin.	1,293	894	818	959	3,964	747	693	693	693	2,827	2,827	2,827
Impairment Expense	-	-	-	1,973	1,973	-	-	-	-	-	-	-
Dep, Depletion & Amortization	525	612	719	5,827	7,683	1,308	1,168	1,538	1,822	5,836	3,623	2,234
Operating Income	(456)	1,478	757	(12,244)	(10,465)	(1,476)	(641)	(836)	(642)	(3,595)	3,221	11,114
Interest Income	76	63	41	9	189	1	5	4	2	12	4	8
Gain/(loss) Derivatives	(686)	(2,778)	2,477	8,298	7,311	556	658	-	-	1,214	-	-
Earnings Before Interest and Tax	(1,066)	(1,237)	3,275	(3,937)	(2,965)	(919)	22	(832)	(640)	(2,369)	3,225	11,122
Interest Expense	515	591	1,066	600	2,772	571	557	557	557	2,242	2,228	2,228
Earnings Before Tax	(1,581)	(1,828)	2,209	(4,537)	(5,737)	(1,490)	(535)	(1,389)	(1,197)	(4,610)	998	8,894
Less: Net Loss of Minority Interest	127	223	322	968	1,640	119	176	184	163	642	709	786
Net Income	(1,453)	(1,605)	(260)	(3,568)	(6,886)	(1,371)	(359)	(1,205)	(1,034)	(3,969)	1,707	9,680
Dividends on Pref. Stock	(181)	181	(734)	-	(734)	-	-	-	-	-	-	-
Net Income Applicable to Common	(1,634)	(1,424)	(994)	(3,568)	(7,620)	(1,371)	(359)	(1,205)	(1,034)	(3,969)	1,707	9,680
Avg Shares Out, FD	36,652,831	36,718,186	36,708,199	36,714,489	36,714,489	36,778,172	36,800,000	36,900,000	37,000,000	36,869,543	39,536,210	42,202,876
EPS, FD	$(0.04)	$(0.04)	$(0.03)	$(0.10)	$(0.21)	$(0.04)	$(0.01)	$(0.03)	$(0.03)	$(0.11)	$ 0.04	$ 0.23

Table 6 Cash Flow, $000

	Q1'08ACT	Q2'08ACT	Q3'08ACT	Q4'08ACT	FY'08ACT	Q1'09ACT	Q2'09EST	Q3'09EST	Q4'09EST	FY'09EST	FY'10EST	FY'11EST
Net Income	(1.453)	(1.605)	(260)	(3.568)	(6.886)	(1.371)	(359)	(1.205)	(1.034)	(3.969)	1.707	9.680
Cash Flows-Operating Activities												
Depreciation	891	1.041	1.486	6.001	9.419	1.410	1.168	1.538	1.822	5.836	3.623	2.234
Unrealized Derivatives, other	1.141	2.117	648	(2.383)	1.523	603	320	978	978	2.879	2.379	2.130
Changes in Operating Activities												
Accounts Receivable	(433)	(238)	(18)	574	(115)	(153)	(176)	(295)	(402)	(1.026)	(702)	(1.194)
Other Operating Activities	26	(160)	20	64	(50)	62	-	-	-	-	-	-
Liabilities	(404)	(151)	960	(860)	(455)	2	(169)	(157)	(259)	(584)	19	470
Net Operating C.F.	(232)	1.005	2.836	(172)	3.437	553	438	407	444	1.842	6.343	13.322
CF/sh	(0.01)	0.03	0.08	(0.00)	0.09	0.02	0.01	0.01	0.01	0.05	0.16	0.32
Cash Flows-Investing Activities												
Capital Expenditures	(1.928)	(4.684)	(6.043)	(3.567)	(16.222)	(4.499)	(1.000)	(1.000)	(1.000)	(7.499)	(6.000)	(5.000)
Other Investing Activities	-	(533)	6.362	15	5.844	-	-	-	-	-	-	-
Net Cash Flows-Investing	(1.928)	(5.218)	319	(3.552)	(10.379)	(4.499)	(1.000)	(1.000)	(1.000)	(7.499)	(6.000)	(5.000)
Cash Flows-Financing Activities												
Sale and Purchase of Stock	-	-	(7.967)	-	(7.967)	-	-	-	-	-	-	-
Net Borrowings	1.490	(46)	(644)	4.828	5.628	(20)	-	-	-	-	-	(6.000)
Net Cash Flows-Financing	1.490	(46)	(8.610)	4.828	(2.338)	(20)	-	-	-	-	-	(6.000)
Net Cash Flow	(670)	(4.259)	(5.455)	1.105	(9.279)	(3.966)	(562)	(593)	(556)	(5.657)	343	2.322

Table 7 Balance Sheet, $000

	Q1'08ACT	Q2'08ACT	Q3'08ACT	Q4'08ACT	Q1'09ACT	Q2'09EST	Q3'09EST	Q4'09EST	FY'10EST	FY'11EST
Cash	14,730	10,471	5,016	6,120	2,154	1,592	999	443	786	3,108
Derivative Assets	-	-	-	2,945	2,964	3,840	3,701	3,561	3,374	-
Net Receivables	1,357	1,595	,613	1,039	1,192	1,368	1,663	2,065	2,767	3,961
Other Current Assets	-	160	139	75	14	14	14	14	14	14
Total Current Assets	16,087	12,226	,769	10,180	6,324	6,814	6,377	6,084	6,942	7,082
Long Term Assets										
Long Term Inv. & Derivative Assets	3,893	4,686	823	4,339	3,821	3,314	2,722	2,130	-	-
Fixed Assets	45,628	50,638	3,836	45,938	48,551	47,863	47,346	46,775	49,065	53,040
Other Assets	10	10	10	10	10	10	10	10	10	10
Deferred Asset Charges	1,946	1,514	1,289	1,198	1,095	1,095	1,095	1,095	1,095	1,095
Total Assets	67,564	69,074	62,727	61,665	59,801	59,096	57,549	56,094	57,112	61,227
Current Liabilities										
Accounts Payable	1,735	2,242	3,974	3,497	2,873	2,704	2,546	2,287	2,307	2,777
Total Current Liabilities	1,735	2,358	3,974	3,497	2,873	2,704	2,546	2,287	2,307	2,777
Derivative Liabilities	2,040	3,980	1,441							
Long Term Debt	13,321	13,748	16,500	21,500	21,500	21,500	21,500	21,500	21,500	15,500
Asset Retirement Obligation	1,471	1,523	1,568	1,589	1,646	1,646	1,646	1,646	1,646	1,646
Minority Interest	2,899	2,675	2,353	1,385	1,266	1,090	906	743	35	-
Total Liabilities	21,466	24,284	25,835	27,972	27,286	26,940	26,598	26,177	25,487	19,923
Redeemable Stocks	7,413	7,691	-	-	-	-	-	-	-	-
Stock Holders Equity										
Common Stocks	367	367	367	368	368	368	368	368	368	368
Capital Surplus	50,317	50,614	50,943	51,312	51,504	51,504	51,504	51,504	51,504	51,504
Retained Earnings	(11,999)	(13,882)	(14,418)	(17,986)	(19,357)	(19,716)	(20,921)	(21,955)	(20,248)	(10,568)
Total Equity	38,685	37,099	36,892	33,693	32,515	32,156	30,951	29,917	31,624	41,304
Liabilities and Equity	67,564	69,074	62,727	61,665	59,801	59,096	57,550	56,094	57,111	61,227

Financial Ratios	Q1'08ACT	Q2'08ACT	Q3'08ACT	Q4'08ACT	Q1'09ACT	Q2'09EST	Q3'09EST	Q4'09EST	FY'10EST	FY'11EST
Working Capital	14,352	9,868	2,795	6,683	3,451	4,110	3,830	3,796	4,635	4,306
Working Capital/Total Assets	0.21	0.14	0.04	0.11	0.06	0.07	0.07	0.07	0.08	0.07
EBITDA	69	2,090	1,476	(4,444)	(168)	527	702	1,180	6,844	13,348
Capex	1,928	4,684	6,043	3,567	4,499	1,000	1,000	1,000	6,000	5,000
EBITDAX	1,997	6,774	7,519	(877)	4,331	1,527	1,702	2,180	12,844	18,348
interest paid	515	591	1,066	600	571	557	557	557	2,228	2,228
EBITDAX/interest	3.9	11.5	7.1	(1.5)	7.6	2.7	3.1	3.9	5.8	8.2
Book Value	1.06	1.01	1.01	0.92	0.88	0.87	0.84	0.81	0.80	0.98