February 28, 2008

Contact Exploration (CEX-TSX.V)

Rating:	**BUY**
12-Month Target:	**$1.10**
Closing Price:	**$0.30**

Getting A Little More Defensive: Takes a Pass on Hungary

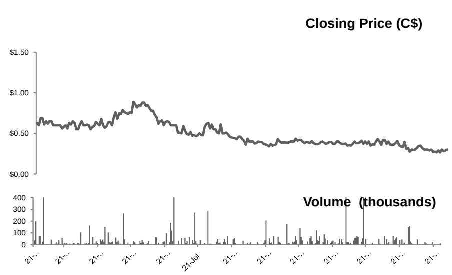
Estimates

	2006A	2007A	2008E	2009E
Annual Prod. (boe)	4,570	915	16,500	40,500
Rev. ($000s)	$195.8	$32.3	$1,620.5	$2,231.5
EPS	($0.05)	($0.30)	($0.01)	$0.00
CFPS	($0.01)	($0.01)	$0.00	$0.02
DACFPS	($0.01)	($0.01)	$0.00	$0.02
P/E	NMF	NMF	NMF	NMF
P/CF	NMF	NMF	NMF	15.0x
P/DACF	NMF	NMF	NMF	15.0x

Notes: [1] All share data is fully diluted
Consensus Estimates: 2007: CFPS; na; DACFPS: na
2008: CFPS: na, DACFPS: na

Shares O/S [2]:	**44.2 MM**	**52 Wk High**	**$0.89**
Float:	**43.2 MM**	**52 Wk Low:**	**$0.26**
Mkt. Cap.:	**$13.5MM**	**Wkly Vol (3m):**	**41,789**
Ent. Value:	**$13.5MM**		
Net Debt:	**$0 MM**	**Year-End:**	**March**

Historic Price and Trading Volume



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Highlights

Only six weeks after announcing a joint venture agreement in the Szolnok Hungarian exploration block with Toreador Resources Corporation (TRGL-Nasdaq) subsidiary Toreador Hungary Ltd., Contact Exploration has decided not to continue to participate in the exploration project. We believe that financing this venture at the Company's current stock price levels would have been too dilutive. Contact's unearned interest in the play is currently being transferred to a third-party and Contact does not have to pay any penalties.

Although the Horton Bluff volumetric test results from the two test wells in the Windsor Block are promising, this play could be very expensive to develop. The economic viability of the play will largely depend on production rates.

We continue to believe that Contact's shares afford exceptional value at current level: (1) The Company's G&A is covered from its current aggregate production of 85 bbl/day and it has no debt, (2) The Stoney Creek field continues to show potential for increased production, and may have more recoverable gas than originally thought, and (3) the Windsor shale play has promise, and Contact has the option to participate after reviewing the production test results. If Contact decides not to participate, it does not have to pay anything towards the exploration and development costs incurred thus far, and still retains a 5% royalty from production from this property.

We reiterate our BUY rating and a 12-month target price of $1.10. We are very confident that Contact will stay the course as a pure-play Atlantic Canadian oil and gas exploration company after the market's reaction to a suggestion to geographically diversify.

Company Description

Contact Exploration is a junior oil and natural gas company that engages in onshore exploration, development, and production of natural gas and oil in New Brunswick, Nova Scotia, and Newfoundland.
Company website: http://www.contactexp.com

Please refer to pages 6 and 7 for Analyst's Certification and Disclosure Statements

HUNGARY: SHORT LOVE AFFAIR

Only six weeks after announcing a joint venture agreement in the Szolnok Hungarian exploration block with Toreador Resources Corporation (TRGL-Nasdaq) subsidiary Toreador Hungary Ltd., Contact Exploration has decided not to continue to participate in the exploration project. Contact's unearned interest in the play is currently being transferred to a third-party, and Contact does not have to pay any penalties.

Why? Contact's share price has been under considerable pressure since it announced the Hungarian joint venture which we believe is the result of investors' preference for a pure-Atlantic Canadian E&P play. As a result, financing this venture would have been too dilutive.

Contact viewed the Hungarian joint venture as a way to increase its reserves and production from a non-operated position. While the economics of the play certainly had merit, we were sceptical of the move overseas because we felt that Contact should leverage its significant operating experience within Atlantic Canada, and focus its attention, as well as its capital, on increasing production from Stoney Creek field.

We were also concerned that Contact's participation in the Hungarian joint venture would challenge the Company's ability to raise capital for both Hungary and the Windsor shale play if each play's upside was not reflected in Contact's share price. We no longer have this concern with the Hungarian joint venture out of the picture.

In summary, while it was not a bad idea, and could have resulted in reserves and production in the near-term, we are happy to see it go.

STONEY CREEK FIELD PRODUCTION STILL MOVING FORWARD

Four wells, which we discussed in our note on January, 17, 2008, "Stoney Creek Production Increases: Contact Enters Hungary", are now producing oil at a combined rate of approximately 25 bbl/day. In total, Stoney Creek Field is producing oil at a rate of approximately 60 bbl/day.

Contact will evaluate an additional 15 to 20 existing wells as candidates for increasing oil production in 2008.

TRIANGLE PETROLEUM RELEASES HORTON BLUFF SHALE VOLUMETRIC TEST RESULTS

On January 20, 2008, Horton Bluff operator, Triangle Petroleum (TPLM-OTC.BB), released the volumetric test results from the two test wells in the Windsor Block. The Windsor property, which is 516,000 acres in size, is jointly owned by Contact Exploration (30%) and Triangle Petroleum (70%).

Results are Promising...

Log analysis from the Kennetcook #1 and Kennetcook #2 wells in the Windsor Basin of Nova Scotia yielded an estimated resource range of 89 to 109 bcf of OGIP per square mile. The estimated OGIP for the completed zones in the Kennetcook #1 and #2 are 42 bcf and 76 bcf per section, respectively.

Listed below is a summary of test results:

- **Original Gas in Place:** Log analysis on the two Kennetcook wells performed by Schlumberger yielded an estimated resource range of 89 to 109 bcf of OGIP for the Horton Bluff formation.
- **Total Organic Content:** Average total organic content (TOC) from all shale samples was 10%. Organic matter type was determined by organic facies analysis as Type II/III to Type III.
- **Vitrinite reflectance (Ro):** Maturity of the shales in the zones of interest as measured by the vitrinite reflectance (Ro) ranged from 1.53% to 2.07%, placing the shale's maturity within the peak window for natural gas generation.

As the table below illustrates, the TOC and Ro are consistent with the U.S. shale plays and the OGIP estimate of 89-to-109 bcf / square mile ranks second behind the Texas Barnett.

Table 1: Horton Bluff Shale Play versus U.S Shale Plays

	Barnett	Ohio & Equivalents	Antrim	New Albany	Lewis	Frederick Brook
Basin	Fort Worth	Appalachian	Michigan	Illinois	San Juan	Windsor
Age	Mississippian	Late Devonian	Late Devonian	Late Devonian	Late Cretaceous	Mississippian
Location	TX	OH, KY, NY, PA, WV, VA	MI, IN, OH	IL, IN, KY	CO, NM	NB, NS
Depth (metres)	1,980 to 2,590 m	610 to 1,520 m	180 to 610 m	150 to 610 m	910 to 1,830 m	1,370 to 1,830 m
Thickness (metres)	60 to 90 m	90 to 610 m	50 m	50 m	300 to 460 m	152 to 183 m
Net Thickness (metres)	15 to 30 m	10 to 30 m	20 to 40 m	5 to 40 m	60 to 90 m	na
Reservoir Pressure	3,000 to 4,000 psi	500 to 2,000 psi	400 psi	300 to 600 psi	1,000 to 1,500 psi	?
Total Porosity	1% to 6%	2% to 5%	2% to 10%	5% to 15%	0.5% to 5%	?
Gas Prod. Mcf/day/well	100 to 1,000 mcf	30 to 500 mcf	40 to 500 mcf	10 to 50 mcf	100 to 200 mcf	na
Recovery Factor	8% to 15%	10% to 20%	20% to 60%	10% to 20%	5% to 15%	?
Resources TCF	26.2 tcf	225 to 250 tcf	12 to 20 tcf	2 to 20 tcf	100 tcf	?
Total Organic Content	1 to 4.5%	0.5 to 23%	0.5 to 20%	1 to 20%	0.5 to 2.5%	1.53 to 2.07%
Maturity (Ro. %)	1.1 to 1.4%	1 to 1.3%	0.4 to 1.6%	0.6 to 1.3%	1.6 to 1.88 %	
Gasi-in-Place (BCF/sq mile)	142.5 bcf	5 to 10 bcf	6 to 15 bcf	7 to 10 bcf	8 to 50 bcf	89 to 109 bcf
Well Spacing Acres	80-160	40-160	40-160	80	80-320	na

Source: American Association of Petroleum Geologists, Company reports, and Acadian Securities Research

...But Post Frac Production Rates are Key

We know the gas is there, but the big question still remains - is the gas economically recoverable. Before we have an indication of this we will have to wait for production rates. We are still waiting for flow-back to be completed and then production testing:

- **Complete Flow-back (Est. Mid-March):** This is expected to take approximately 30 days. Triangle has installed down-hole pumps on both the Kennetcook #1 and #2 wells to enhance fluid recovery rates.
- **Production Testing (Est. Mid-April):** Once flow back is completed, production testing will begin. We expect that initial production testing will take another 30 days.

This play could be very expensive to develop. We estimate that the two vertical wells drilled in 2007 (Kennetcook #1 and #2) each cost approximately $2 million to drill and complete, and we believe that horizontal wells, which are typical for shale gas production, could cost approximately $4 million. Then there are the fraccing costs, which can be substantial because the equipment and crews are outsourced from western Canada. So knowing there is gas in the ground is one thing: being able to produce it economically may very well be another.

OTHER UPDATES

South Stoney Creek – Conventional

Contact announced that it has increased its working interest in this prospect from 60% to 72%, which was driven by the financial constraints of its farm-in partner, Shoal Point Energy (Private Company). Shoal Point's 28% interest of the prospect reflects the Company's proportion of funding for this prospect to date. Contact will now have to finance the full cost of the planned Pound Hill exploration well.

Contact now plans to spud the exploration well in the Weldon prospect (Pound Hill C-67-2328) located to the south east of the Stoney Creek Field in spring 2008, after the spring load restriction (the well was originally expected to be spuded in February, 2008.

South Stoney Creek – Deep Rights

Triangle Petroleum has fulfilled the first part of the farm-out agreement with Contact, for a 70% interest in South Stoney Creek's deep rights. Triangle will acquire seismic data or drill a well on this property during 2008.

Newfoundland - Portland Creek and Parson's Pond

Contact has entered into two farm-out agreements with a private company which could lead to two wells being drilled over the next two year. The primary target is the Trenton - Black River formation. Contact will have carried interests in these wells from 15-20% with the option to participate for additional working interests if desired.

In exchange for a smaller working interest in these blocks, Contact received a non-operator interest in a third block. At the end of the day, Contact is non-operator in a larger piece of property than it originally had, and is not required to pay licensing renewal fees on these properties.

OUTLOOK AND FINANCIAL FORECAST

Our fiscal 2008 and 2009 estimates remain unchanged. The incremental 25 bbl/day production from the four Stoney Creek Field wells recently put online have already been reflected in our estimates. Our EPS estimates are -$0.01 and $0.00, respectively, and we are expecting CFPS of $0.00 for fiscal 2008 and $0.02 for 2009. The following table summarizes our fiscal 2008 and 2009 estimates.

Table 2: Acadian Securities Estimates

(Year-end: March)	F2008E	F2009E
Production (bbl)	16,499	40,515
Average Production (bbl/day)	45	111
Revenues (Net of Royalties)	$1,258,588	$2,231,497
Net Income	-$275,530	$115,418
EPS	-$0.01	$0.00
CFPS	$0.00	$0.02
DACFPS	$0.00	$0.02

Source: Acadian Securities Research

Production Forecast

2008: We are anticipating an exit fiscal 2008 production rate of 85 bbl/day versus our previous forecast of 30 bbl/day. Our 2008 aggregate production estimate is 16,500 bbls.

2009: We are expecting 111 bbl/day, which yields an aggregate fiscal 2009 production rate of 40,500 bbls. We believe that Contact will continue to focus its efforts on increasing oil production as opposed to gas production over the next 12-to-24 months since its lack of infrastructure for transportation of natural gas.

VALUATION AND RECOMMENDATION

We reiterate our BUY rating and a 12-month target price of $1.10. We are very confident that Contact will stay the course as a pure-play Atlantic Canadian oil and gas exploration company after the market's reaction to a suggestion to geographically diversify.

The table below summarizes our 12-month target price. Despite the encouraging results from the Windsor play, we are still hesitant to assign it a value (except for its estimated land value) until production test results are performed and released. We did not assign any value to the Hungarian joint venture.

Table 3: Contact's Net Asset Value per Share

Contact Exploration
NAV
Reserves Estimated as at March 31, 2006

	Quantity	Btax Value ($000's)	per / Share	% of Total
Reserves Values - Stoney Creek Field				
Proved - Producing				
Light Oil	78.0 mbbl	$1,834	$0.04	*3.5%*
NGLs	0.0 mbbl	$0	$0.00	*0.0%*
Natural Gas	0.8 bcf	$0	$0.00	*0.0%*
Total:	**78.1 mboe**	**$1,834**	**$0.04**	***3.5%***
Proved - Non-Producing				
Light Oil	48.0 mbbl	$1,180	$0.03	*2.3%*
NGLs	0.0 mbbl	$0	$0.00	*0.0%*
Natural Gas	0.8 bcf	$622	$0.01	*1.2%*
Total:	**48.1 mboe**	**$1,802**	**$0.04**	***3.4%***
Probable				
Light Oil	1256.0 mbbl	$12,001	$0.27	*22.9%*
NGLs	0.0 mbbl	$0	$0.00	*0.0%*
Natural Gas	7.1 bcf	$12,072	$0.27	*23.0%*
Total:	**1,257.2 mboe**	**$24,073**	**$0.55**	***45.9%***
Total Proven + Probable				
Light Oil	1382.0 mbbl	$15,015	$0.34	*28.6%*
NGLs	0.0 mbbl	$0	$0.00	*0.0%*
Natural Gas	8.6 bcf	$12,694	$0.29	*24.2%*
Total:	**1,383.4 mboe**	**$27,709**	**$0.63**	***52.8%***

	Value ($000's)	per / Share	% of Total
Saskatchewan Production	**$1,125.0**	**$0.03**	*2.1%*
Land Value			
Undeveloped Land	**435,612 acres**		
Valued @ $50/acre	**$21,781**	**$0.50**	*41.5%*
Adjustments			
Working Capital Surplus (Deficiency)	-$3,264	-$0.07	*-6.2%*
Long-Term Debt	$0	$0.00	*0.0%*
Proceeds From Options	$8,364	$0.19	*16.0%*
Present Value Of Tax Liability	-$3,277	-$0.07	*-6.2%*
	$1,823	**$0.04**	***3.5%***
Grand Total:	**$52,438**	**$1.19**	
Valuation			
Target Price-to-NAV (Reserves)	*-15%*		
Target Price	**$1.10**		
Current Share Price	**$0.30**		
Premium / Discount to NAV	**-73%**		
Basic Shares O/S (MM))	*38.0*		
Fully Diluted Shares O/S (MM)	*44.0*		

Source: Martin & Brusset Associates reserve report for the Stoney Creek Field (March 31, 2007) and Acadian Securities Research estimates

We continue to believe that Contact's shares afford exceptional value at current level.

- The Company's G&A is covered from its current aggregate production of 85 bbl/day and has no debt. Going forward incremental production can help fund exploration/development activities.
- The Stoney Creek field continues to show potential for increased production, and may have more recoverable gas than originally thought.
- The Windsor shale play has promise, and Contact has the option to participate after reviewing the production test results. If Contact decides not to participate, it does not have to pay anything towards the exploration and development costs incurred thus far, and still retains a 5% royalty from production from this property.

We believe that the price-to- NAV discount gap, which is currently a discount of 44%, should contract as the Stoney Creek field progresses.

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Company Risk Disclosure

In addition to the general risks involved in investing, the following risks pertain to Contact Exploration: (1) No assurance that commercial quantities of hydrocarbons will be recovered by Contact in the future, (2) Contact presently does not have sufficient financial resources to undertake all of its planned exploration and development programs, (3) The oil and natural gas industry is subject to extensive controls and regulations imposed by various levels of government, (4) All phases of the oil and natural gas business present environmental risks and hazards and are subject to environmental regulation pursuant to a variety of federal, provincial and local laws and regulations, (5) The marketability and price of oil and natural gas will be affected by numerous factors, and (6) There are numerous uncertainties inherent in estimating quantities of oil, natural gas and natural gas liquids reserves.

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BUY: Investment in this stock has the potential for a total return in excess of 15% over the next 12 months

HOLD: Investment in this stock has the potential for a total return between 0 to 15% over the next 12 months

SELL: Investment in this stock has the potential for a negative total return over the next 12 months

Other
The analyst has viewed operations of an issuer in detail. Acadian Securities incurred the costs of the analyst's travel expenses for such visits.

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