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Mar 17, 2014

Energy

AMEX

PED

Buy

Initiation

Current Price

$2.26

Target Price

$3.90

Market Capitalization
51.64M

Shares Outstanding
22.85M

Float
12.61M

Institutional Holdings
0.00%

12-month Low/High
$0.38/$5.64

Average 90-day Volume
131,328

Fiscal Year End
Dec 31

Revenues ($ MIL)

Period	2012	2013E	2014E
Q1	na	269A	na
Q2	na	156A	na
Q3	na	199A	na
Q4	na	552E	na
	503	1,176E	19,023E

EPS ($ MIL)

Period	2012	2013E	2014E
Q1	na	-0.16A	na
Q2	na	-0.13A	na
Q3	na	-0.45A	na
Q4	na	-0.01E	na
	-0.03	-0.76E	0.18E

PEDEVCO

Not Just Repeatable Drilling

- We initiate research coverage of PEDEVCO with a Buy rating and a price target of $3.90
- PEDEVCO should benefit significantly from two pending acquisitions of (1) Niobrara prospective properties in the Colorado portion of the D-J Basin, and of (2) control of Aral Petroleum, a Kazakhstan onshore oil producer
- Management is among the most entreprenurial in the E&P sector led by CEO Frank Ingriselli, and EVP and CFO Michael Peterson
- PEDEVCO benefits from a strategic partnership recently formed with RJ R MIE Group, a Chinese integrated oil company which can provide access to international opportunities
- Growth is likely to consist of relatively predictable results in the D-J Basin Niobrara and the Kansas Mississippi Lime, and favorable asset transactions internationally

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Evolving Company Description

PEDEVCO (formerly Pacific Energy Development) was formed in February 2011 by CEO Frank Ingriselli. Through a reverse merger with Blast Energy Services, Pacific Energy Development became a publicly traded company called PEDEVCO. PEDEVCO was joined at that time by Michael Peterson as Executive Vice President and CFO.

PEDEVCO is engaged in the acquisition and development of strategic, high growth energy projects, including shale oil and gas assets in the U. S. and Asia. It currently has operations in the D-J Basin, Niobrara, and the Kansas Mississippi Lime. The Niobrara operations have expanded significantly through a March 7 acquisition with new partner RJ Resources. PEDEVCO also holds a 20% interest in Niobrara-focused Coral Energy Technology, with MIE Group, a large Chinese oil company, holding the balance. MIE Group is a valuable strategic partner with PEDEVCO, and has been a source of money when timely.

Acquisition In Niobrara Core Area

The size of the company has increased several fold through the purchase of about 29,000 gross acres from Continental Resources in the Wattenburg and Wattenburg Extension areas of the Colorado Niobrara Shale. The properties are located almost entirely in Weld County where Anadarko Petroleum, Carrizo Oil & Gas and Noble Energy have been notably successful. The purchase price for the Continental acquisition was $28 million, a reasonable number in relation to 2013 cash flow of $13 million. According to the Energy Information Administration, total Niobrara oil production was a robust 290,000 bd in February, up from 284,000 bd in January.

The acquired properties had gross production in October of about 400 boed from 25 wells of which 11 are operated. The transaction also includes 15 after pay out interest wells. Potential company reserves (3P) are estimated to increase to 87.6 million barrels from the current base of 20.2 million barrels. The transaction closed last Friday March 7, effective back to December 1.

Legacy Interests In Niobrara

PEDEVCO also has ongoing interests in the Niobrara Shale through 20% ownership of Condor Energy Technology. MIE holds 80% of Condor, having established an original position in November 2011. Condor holds 10,224 acres in the Indian Peaks 3-D area. PEDEVCO also has direct interests in the Niobrara, giving PEDEVCO overall a 26.38% interests in the legacy holdings. Typical Niobrara wells have an average of 150,000 EURs and cost $3.8 million. These favorable economics have attracted considerable drilling by the industry.

PEDVECO's Niobrara gross production was recently about 400 boed. The company plans to drill two gross Niobrara wells in 2014. Looking further ahead, the acquired properties alone cover 28,727 gross acres. That area would arithmetically provide 180 net drilling locations on the 80 acre spacing that is typical in the

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Wattenburg Extension. Through the forced pooling that is permitted under Colorado regulations, the number of future drilling locations could increase significantly.

Early Stage Of Activity In The Kansas Mississippian Lime

PEDEVCO has formed a subsidiary called Red Hawk Petroleum to enter the oil rich Mississippian Lime. The transaction involves the purchase from Berexco LLC of a 49.2% working interest in 6,763 net acres in southern Kansas.The Mississippian typically has EURs of 320 mboe at an average cost of $3.3 million. The acreage is located in parts of Barber, Comanche, Harper, and Viola Counties. Under the agreement with Berexco, PED is committed to drill three gross horizontal wells in 2014. Berexco retains a 25% overriding royalty.

Activity on Miss Lime acreage in Kansas has seen mixed results, having less continuity than the Oklahoma portion. Nevertheless, Harper County has been very active. Total oil production in Harper was 3,827 bd through October 2013, up 45% from the full year 2012 average, and more than triple 2010. Gas production has risen to 29 million mcfd, leaving an oil ratio of about 45%. However, neighboring Barber County was 5,474 boed through October, down 11% from the 2012 full year.

PEDEVCO has initially identified more than 40 drilling locations on its Miss Lime acreage, assuming 160 acre spacing. The typical well cost is approximately $3.4 million for an average EUR of 320,000 boe. Initially, the company will focus on the Tyler Ranch area where three successful wells have already been drilled by others.

Enters Kazakhstan

Part of PEDEVCO's business plan is to participate opportunistically in projects outside the U.S., sourced by Mr. Ingresselli's strong international relationships. So far, the company has entered an agreement to acquire a 34% indirect but controlling interest in Aral Petroleum, which is now shared 50-50 with RJ Resources. Aral holds a 380,000 acre license exploration and production license called the North Block onshore Kazakhstan. The North Block contains the Zhagabulak Area in the southeastern corner. MI Ocean Group, which has its second largest producing field in Kazakhstan, was likely to have been involved in identifying this opportunity.

The Kazakhstan government has estimated that the greater Zhagabulak Area contains 642 million barrels of oil in place, of which 259 million is recoverable. The North Block also contains the Baktygaryn Area in the northwestern portion. The government estimates that this field contains 863 million barrels, of which 259 million barrels are recoverable. There are additional areas on the Block which are bruited by the government to contain major prospects.

Aral is owned 66.5% by Asia Sixth and 33.5% by Caspian Energy. Assuming government approval, PEDEVCO/KR Resources will own 51% of Asia Sixth, giving them an effective 33.9% control of Aral. Asia Sixth has been financing the efforts of Aral to continue the North Block drilling program, which most recently has provided two strong well re-completions.

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The North Block contains the East and West Zhagabulak fields where both production, re-completions, and development are ongoing. Wells are targeting the KT-I formation at about 11.500 feet, and the KT-II at 14,500 feet. Production was recently averaging about 1,500 bd of oil from two of five wells.

The deal is expected to close in the September quarter, pending Ministry of Oil and Gas approval. PEDEVCO/JK Resources will initially pay $10 million to Asia Sixth. Upon closing there is an increment of $20 million if production equals or exceeds 1,500 bd, and a lesser $15 million if production is between 1,000 and 1,500 bd. The higher target appears likely since production is currently around 1,500 bd.

Net Production Should Be Growing Rapidly Over The Next Several Years

The most recently reported production levels were for the September quarter of 2013. Equivalent net production was 271 boed, of which 87% was oil. PEDEVCO itself directly was 13 boed, Condor was 36 boed, and White Hawk (since sold) was 22 boed. The 20% interest was treated as a cost item. It was in the balance sheet but not the consolidated results.

The Niobrara acquisition provided 400 gross boed as of September, implying a one third contribution during the fourth quarter. Kazakhstan should add gross production of at least 1,500 boed to the base by September 2014, or 510 boed net. However, like Coral Energy, Kazakhstan will be accounted for in the balance sheet only.

All in, we estimate that production in 2014 should average at least 670 boed, including 170 boed of indirect equity in Aral Petroleum. Embedded in these estimates is a 2014 average of at least 500 boed from the Niobrara acquisition and the Miss Lime. These operations will be consolidated. The Mississippian Lime is difficult to estimate because drilling has not yet begun. Nevertheless, an initial contribution is likely in 2014, and a couple of hundred boed in 2015.

Growing Production Should Support EBITDA Of $15E Million in 2014

The recent Niobrara acquisition should mark the transition to EBITDA and net income.Our preliminary expectation is that growth will continue in 2015, as the Niobrara acquisition contributes for the full year. Our preliminary estimate is that production will double in 2015.

The acquisitions of the Niobrara properties and the Aral interest are requiring financing of up to $48 million. In addition, the company plans a total of five net wells which may add another $18 million. In the past three months, the company has raised about $14 million through two public stock offerings and $34.5 million of three year notes, of which half will be for the account of JR Resources. The budget could require additional debt and equity financing later in the year.

Management Has Excellent Leadership Abilities

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The CEO of PEDEVCO is Frank Ingriselli who has previously held top management positions with Texaco, including President of Texaco International. He previously served as Founder, President, and CEO of CAMAC Energy (originally named). Mr. Ingriselli owns 5% of PEDEVCO.

The Executive Vice President and CFO is Michael Peterson. Mr. Peterson joined PEDEVCO in 2011 at the time the company was founded. He had previously been CEO of Blast Energy Services which merged with PEDEVCO in 2012. His background is in finance and management of small cap companies, with over 10 years at Goldman Sachs. Prior to joining Blast, he had held directorships and management positions in Aemetis Energy (Founder, Lead Investor, and Board Member), Solargen Energy (Founder, Chairman and CEO), and Pascal Management (Founder and Managing Partner).

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Valuation Summary

PEDEVCO is selling at an EV multiple of 7.9x 2014E EBITDA of $15 million. The average for our micro cap universe is 7.8x. We believe that U.S. operations separately could be valued at slightly above the micro-cap average, or 7.8x, considering the early stage of strong growth. At that multiple, the value for U.S. operations alone would be would be $2.90.

The Aral investment is more difficult to estimate. We know that PEDEVCO may pay up $10 million for its pending net investment in Aral. In the immediate future, Aral plans to redeploy cash flow to additional drilling.

More of PEDEVCO's expectations for Aral should be available by September when the transaction is completed. We believe that Aral will add value to the properties, but it is not certain how much or how soon.

Strategically, Aral is likely to be the first examples of the possible international game plan i.e. (1) BUY, (2) REJUVENATE, (3) (SELL). Sale of the Aral investment could fetch $40 million net for a net gain of $30 million.

These things considered, we give the Aral investment alone a minimum value of $1.00 per share, for a total price target of $3.90.

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PEDEVCO	Year 2012	1Q2013	2Q2013	3Q2013	4Q2013E	Year 2013E	Year 2014E	Year 2015
Oil Production							210,000	420,000
Average Price							$85.00	$90.00
Oil Revenues							$17,850,000	$37,800,000
Gas Production							293,460	586,920
Average Gas Price							$4.00	$4.00
Gas Revenues							$1,173,840	$1,173,840
Revenues	**$503,153**	**$269,067**	**$156,146**	**$198,768**	**$552,000**	**$1,175,981**	**$19,023,840**	**$38,973,840**
Equivalent Barrels	0	0	0	0	0	0	244,550	489,100
Lease Operating Expense	-$381	-$119,676	-$269	-$123,859	-$344,400	-$588,204	-$3,914,000	-$9,782,000
Operating Expense Per BOE	0.00	$0.00	$0.00	$0.00	$0.00	$0.00	-$16.00	-$20.00
SG&A	-$3,730	-$1,260,089	-$1,288,253	-$1,121,053	-$125,000	-$3,794,395	-$16	$0
Impairment of Goodwill	-$6,820	$0	$0	-$6,820,203	$0	-$6,820,203	$0	$0
Impairment Of Properties	-$180	-$34,641	-$15,862	$0	$0	-$50,503	$0	$0
DD&A	-$131	-$138,451	-$116,570	-$59,407	-$166,340	-$480,768	-$6,113,750	-$12,227,500
DD&A Per Equivalent Barrel	0	0	0	0	0	0	-$25.00	-$25.00
Settlement of Payables	$140	$0	$0	-$139,874	$0	-$139,874	$0	$0
Loss On Deposit	$0	$0	-$200,000	$0	$0	-$200,000	$0	$0
Profit On Equity Affiliates	$0	-$85,301	-$282,303	$0	$0	-$367,604	$0	$0
Gains On Investments	-$293	$0	$0	$0	$0	$0	$0	$0
Net Interest Expense	-$950	-$114,777	-$390,492	-$298,501	-$300,000	-$1,103,770	-$3,500,000	-$3,000,000
Debt Retirement	$9	$0	$0	-$159,913	$0	-$159,913	$0	$0
Gain On Derivatives	$0	$2,545	$11,460	$0	$0	$14,005	$0	$0
Operating Income	-$12,013	-$1,481,323	-$2,432,931	-$8,469,119	-$383,740	-$12,767,113	$5,496,090	$13,964,340
Shares Outstanding	186,507	8,879,985	13,913,815	17,283,641	26,100,000	12,223,450	30,000,000	30,000,000
Diluted EPS	-$0.65	-$0.17	-$0.17	-$0.49	-$0.01	-$0.84	$0.18	$0.47
Adjustments	$0.62	$0.01	$0.04	$0.04	$0.00	$0.09	$0.00	$0.00
Adjusted EPS	-$0.03	-$0.16	-$0.13	-$0.45	-$0.01	-$0.76	$0.18	$0.47

PEDEVCO PED | CURRENT PRICE $2.26 | Buy | 03/17/2014
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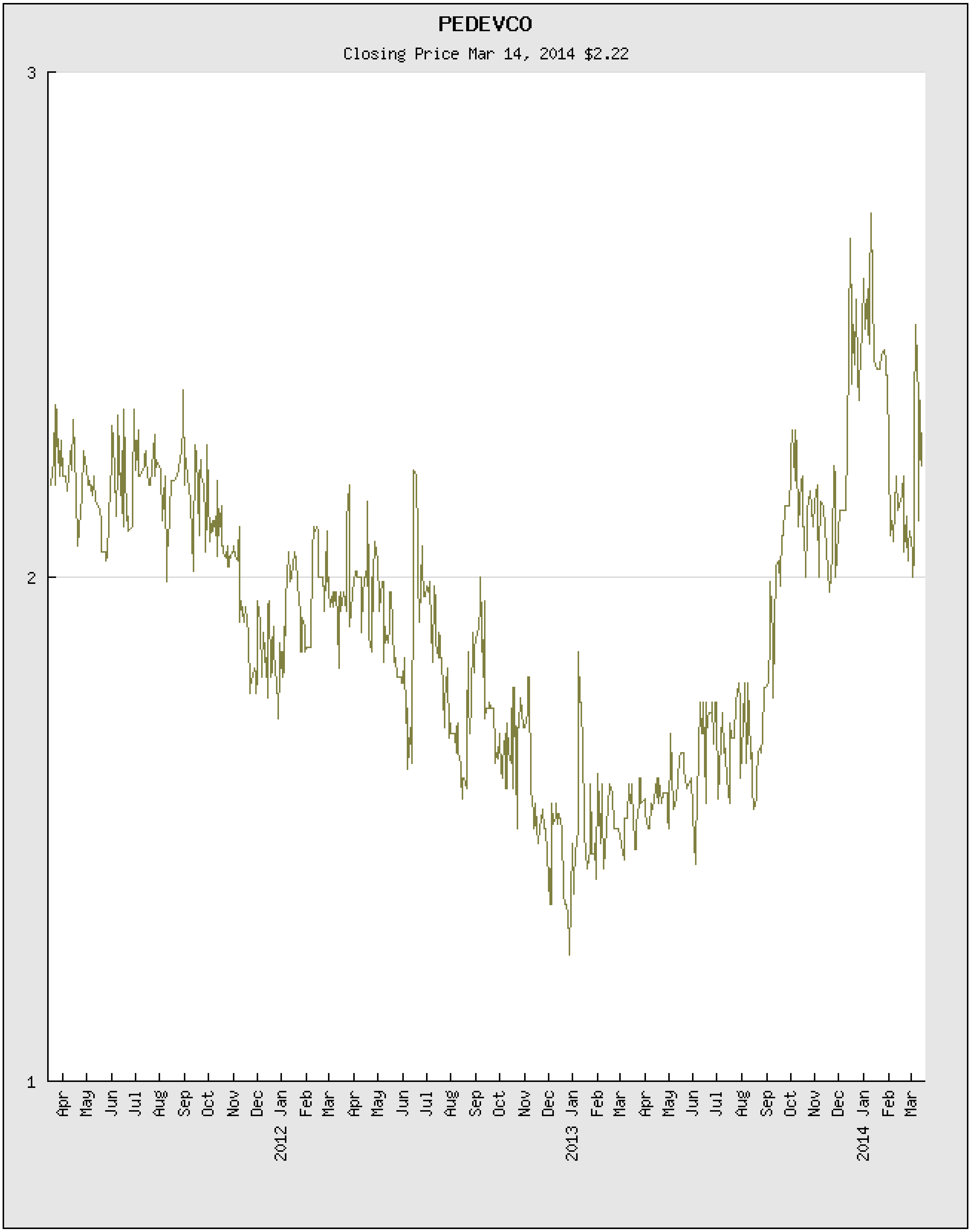

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Report ID: 7153