Zacks Equity Research

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Dejour Enterprises Ltd. (DEJ-AMEX)

DEJ: Zacks Co. Report – OUTPERFORM

Current Recommendation	**Outperform**
Prior Recommendation	Neutral
Date of Last Change	09/05/2010
Current Price (01/24/11)	$0.31
Six- Month Target Price	**$1.00**

OUTLOOK

Our rating on Dejour's stock remains Outperform based upon strong confidence in higher production levels due to successful drilling at the Halfway formation at Woodrush and the anticipation of the implementation of a waterflood project in February 2011. The company's production profile should improve after the removal of the British Columbia Oil and Gas Commission's allowable well production limits. In addition, the announcement of a JV to help fund of the development of deep oil at Woodrush should accelerate the improvement of the company's production profile and reserves. Our price target is $1.00 based on NAV analysis.

SUMMARY DATA

52-Week High	**$0.45**
52-Week Low	**$0.28**
One-Year Return (%)	**1.29**
Beta	**1.62**
Average Daily Volume (shrs.)	**1,023,175**
Shares Outstanding (millions)	**110**
Market Capitalization ($mil)	**$34**
Short Interest Ratio (days)	**0.59**
Institutional Ownership (%)	**0**
Insider Ownership (%)	**25**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**N/A**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/M**
P/E using 2011 Estimate	**N/M**
P/E using 2012 Estimate	**N/M**
Zacks Rank	**3**

Risk Level	**Above Average**
Type of Stock	**Small - Value**
Industry	**Oil – C$ E&P**
Zacks Rank in Industry	**7 of 14**

ZACKS ESTIMATES

Revenue
(in millions of $ CAD)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2009	2.72 A	1.68 A	1.06 A	1.33 A	6.79 A
2010	1.31 A	2.77 A	2.54 A	1.69 E	8.31 E
2011	2.33 E	3.39 E	4.72 A	4.82 E	15.26 E
2012					17.01 E

Earnings per Share
(EPS is operating earnings before non recurring items)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2009	-$0.03 A	-$0.01 A	-$0.03 A	-$0.03 A	-$0.11 A
2010	-$0.02 A	-$0.01 A	-$0.01 A	-$0.01 E	-$0.05 E
2011	-$0.01 E	-$0.01 E	-$0.00 E	-$0.00 E	-$0.02 E
2012					-$0.02 E

Zacks Projected EPS Growth Rate - Next 5 Years % **N/M**

2009 quarterly EPS do not equal annual EPS due to rounding.

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KEY POINTS

- The rating on Dejour's stock remains Outperform due to strong confidence in higher production levels due to a successful drilling program at Woodrush and the anticipation of the implementation of a waterflood project in February 2011. Our price target of $1.00 is derived assigning a 40% discount to the company's net asset value of $1.68 (see Valuation section).
- Significant fundamental events can considerably increase the company's valuation parameter in a step-fashion. One such event would be the Dejour's achievement of positive profitability, in which case the stock could experience rapid price appreciation.
- Management continues to take steps towards the development of its prime properties: Woodrush in British Columbia's Peace River Arch and Gibson Gulch in Colorado's Piceance Basin. During 2010, the company successful drilled three wells at Woodrush, bringing the company's total to nine producing wells. Recently, Dejour announced the formation of a joint venture for the exploration and production of deep oil on its Woodrush property. Importantly, the yet-to-be-named partner will fund most of the exploration costs, along with additional land purchases.
- Management has a strong track record of developing oil and gas properties. CEO Robert Hodgkinson has twice founded oil and gas companies that mounted successful, large-scale drilling programs. The companies were subsequently acquired by medium-capitalization exploration companies. President Harrison Blacker has a 30-year record of managing oil and gas operations around the globe.
- Consult our report dated August 12, 2010 for further background information.

OVERVIEW

Based in Vancouver, British Columbia, Dejour Enterprises (DEJ) is a Canadian independent oil and natural gas company and holds interests in 122,000 net acres of oil and gas leases in North America. Proved and Probable Producing Reserves (as estimated by the independent petroleum engineering consultant firm GLJ Petroleum Consultants as of June 30, 2010) were 346 thousand barrels of oil (MBO)and 1,539 million of cubic feet (MMCF) of natural gas, totaling 604 thousand barrels of oil equivalent (MBOE). All Proved Producing Reserves (354 MBOE) are in the Canadian **Woodrush** area of the Peace River Arch, which has nine producing wells. Acreage holdings consist of 15,000 net acres in northeastern British Columbia and northwestern Alberta, and 107,000 net acres (all undeveloped) in Colorado and Utah in the Piceance, Uinta and Paradox Basins. Net Proved and Probable Undeveloped Reserves at **Gibson Gulch** (as estimated by the independent petroleum engineering consultant firm Gustavson Associates LLC as of December 31, 2009) were 1.37 million barrels of oil (MMBO) and 207 billions of cubic feet (BCF) of natural gas. The company is the operator of its developed acreage and approximately 88% of its undeveloped acreage. During 2009 Dejour sold its shares in Titan Uranium Inc., but still maintains a 10% carried interest and 1% Net Smelter Return on approximately 578,365 acres.

RECENT NEWS

In January 2011, Dejour presented at the Sidoti NYC Micro-Cap Conference on January 10th and announced a joint venture concerning the exploration and development of deep oil at Woodrush on January 20th. Both events added significant information about Dejour. First, Dejour's investment profile has become broader and deeper. At the end of 2010, the company's outlook was dependent mainly on the expected improving production profile of the three oil wells at Woodrush. Now, the company has two projects (Woodrush shallow oil and deep oil) on the front burners, and three other projects on the come (Gibson Gulch gas in the Williams Fork structure and deep gas in the Niobrara formation, along with an oil resource at South Rangely). Secondly, the announcement of the formation of a joint venture for the

exploration and production of deep oil on the Woodrush property not only opens a new avenue of exploration and development, along with its funding, but also outlines the probable structure of future JVs for funding exploration costs at Gibson Gulch.

On December 17, 2010 Dejour Enterprises announced that it received approval from the British Columbia Oil and Gas Commission (OGC) for the implementation of a waterflood program at its Woodrush oil and gas project in northeast British Columbia. The implementation of a waterflood program will increase oil production at Woodrush due to the eventual lifting of the well allowable restriction imposed by the OGC of British Columbia, which has artificially limited gross production to approximately 650 BOE/D.

PRODUCING PROPERTIES

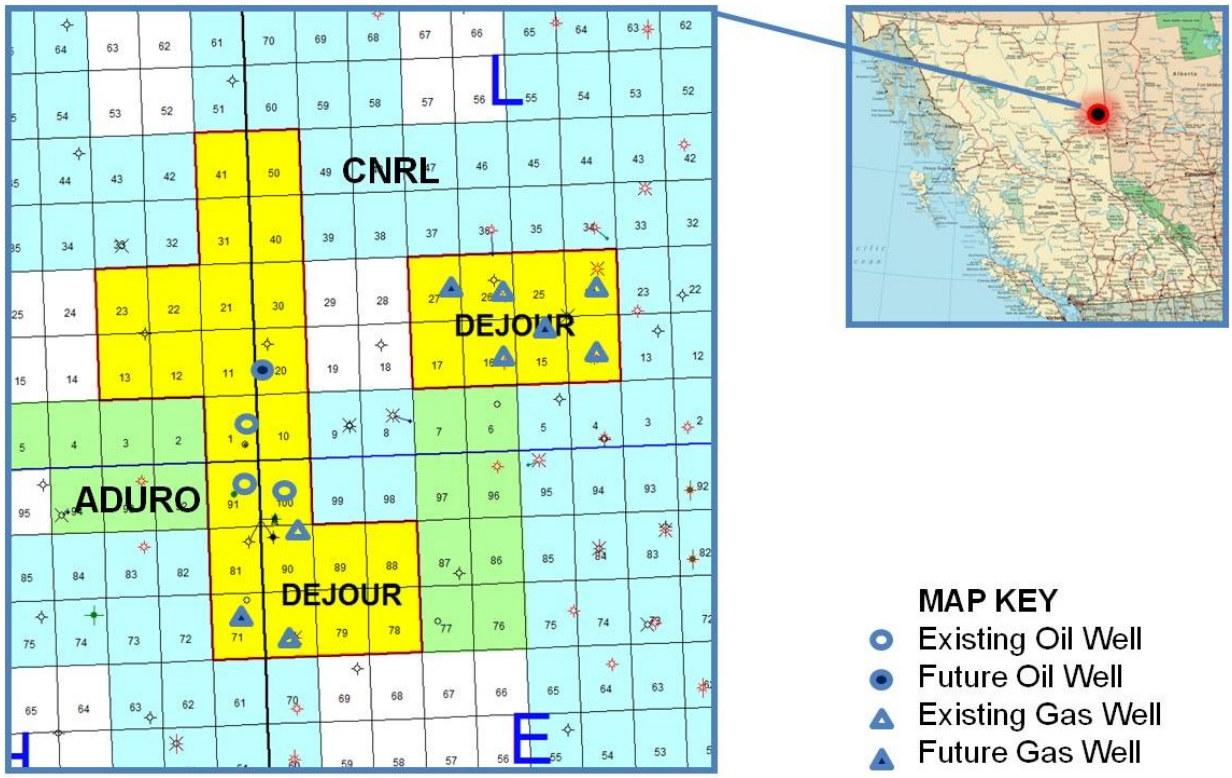
Peace River Arch in the Western Canadian Sedimentary Basin

Dejour Enterprises operates exploration and production projects in 20,000 acres (15,000 net acres) in the Peace River Arch located in northeastern British Columbia and northwestern Alberta. Dejour owns and has a 75% working interest in the **Woodrush** area of 6,000 gross acres (or 4,500 net acres), which is the source of the company's entire production and is the focus of drilling and exploration activity in 2011. Currently, the area has production from nine wells (three oil and six gas) with current average daily gross production of 650 barrels of oil equivalent per day (BOE/D). Four gas wells are producing from Notekwin formation (Dejour's parcel in the upper right near CNRL), and three oil wells and two gas wells producing from Halfway reservoir (Dejour's parcel in the lower left adjacent to ADURO). These three oil wells are in close proximity (500 meters) to each other. Gross production should increase to 1,300 BOE/D by the end of June 2011 as a waterflood project is implemented.

Due to the successful drilling of three shallow oil wells at Woodrush, a major U.S. oil company (yet-to-be named) has entered into a joint venture (JV) with Dejour to fund and drill two deep horizontal wells to explore and develop deep oil in the Montney oil resource at Woodrush. Up to $1 million will be paid to Dejour on Dejour's achievement of specific objectives in the first quarter of 2011, after which the JV will fund land purchases up to $5 million on a 65/35 basis (major U.S. oil company/Dejour). Afterwards two horizontal wells will be drilled on an 80/20 funding basis (major U.S. oil company/Dejour). Thereafter, the JV would continue to develop the project on an ongoing 50/50 basis beyond the earning period.

Woodrush (Peace River Arch) Project

In 2010, Dejour drilled three successful wells at Woodrush, bringing the company's total well count to nine. Of the three new wells, two (one oil well and one gas well) came on line in May, both of which were able to enjoy unlimited production for 90 days before being restricted with well allowables imposed by the British Columbia Oil and Gas Commission (OGC). For the first 90 days, production from the wells was unlimited, and then regulations required that production be lowered to an allowable level commensurate with maintaining the pressure level in the reservoir until a mechanism, such as the implementation of a water flood, is put into place to maintain the reservoir's pressure and conserve the oil resource. In the fall drilling season, Dejour successfully drilled another oil well at the southeast edge of the Halfway reservoir.



Courtesy of Dejour Enterprises

Currently, Dejour is restricting production from the Halfway reservoir to conform to British Columbia's allowable well production limits due to a naturally increasing gas component, which is a result of oil pressure in the downhole reservoir dropping below the bubble point. This temporary reduced production will lower sequential operating revenue and operating cash flow in the fourth quarter of 2010. Management expects average daily gross production from Woodrush to be approximately 650 BOE/D during the fourth quarter. For 2010, management expects total revenue of CAD $8 million, all from the Woodrush Field.

In December 2010, Dejour received approval from the British Columbia Oil and Gas Commission (OGC) for the implementation of a waterflood program at its Woodrush oil and gas project in northeast British Columbia. The project design has been completed and construction should begin in the first week of February. The scope of the waterflood project includes the drilling of a water supply well and converting one producing well to an injection well. Also, a second injector well will be drilled; the power generation capacity will be upgraded; pumps will be installed; and the necessary water treatment facilities constructed. The gross cost of the project is estimated to be C$3.2 million. Dejour has sufficient funding for the project, having completed a private placement of C$1,500,000 in common shares.

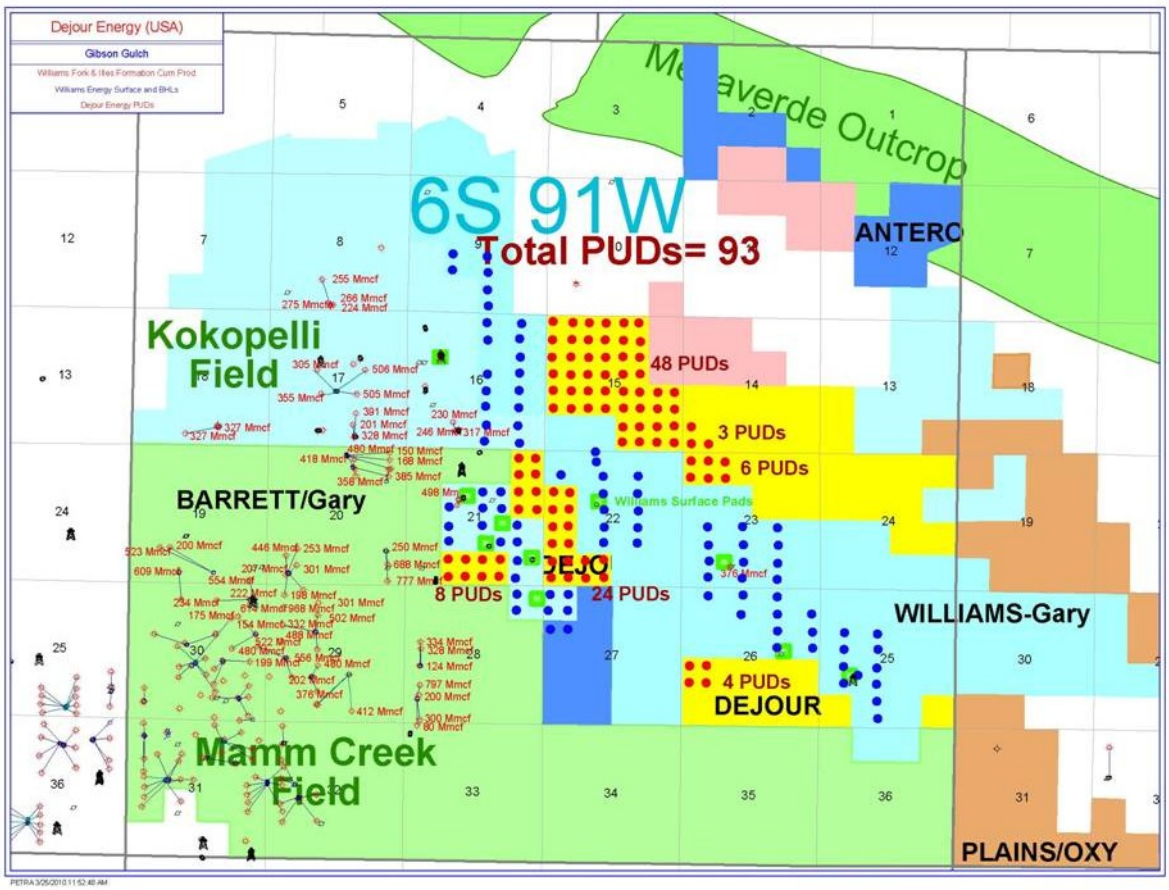
The implementation of a waterflood program will increase oil production at Woodrush. When the water injection begins in early February, there will be an immediate increase in production since the current well production allowable scheme mandated by British Columbia will be phased out as new pool rules take effect. Production from the Halfway pool at Woodrush should increase steadily with production peaking in the third quarter of 2011. The implementation of a waterflood will increase production to 1,300 BOE/D.

The waterflood will provide for sustained oil production at Woodrush for at least five to six years, allowing Dejour to fund further development of oil production with operating cash flow. In addition, the incremental oil production increases Dejour's ability to accelerate repayment of existing credit lines and enhances the company's ability to access more attractive longer-term funding from conventional banking facilities.

Ultimately, management expects to have a total of more than 15 producing wells, plus injectors, operating at Woodrush. In addition, multiple oil pools have been detected by the 3-D seismic survey, and in due course, many will be developed. On the cost-side, considerable transportation cost improvement is possible when a seven-mile pipeline is constructed. Currently, oil is trucked over seven miles from the well heads to the nearest pipeline.

Peace River Arch in the Piceance Basin of western Colorado

Dejour has a 72% working interest of 2,200 gross acres (or 1,585 net acres) adjoining natural gas production from the Williams Fork sandstone (the upper portion of the Mesaverde Group). This **Gibson Gulch** acreage is one of the company's leading prospects due to its proximity to the producing properties (some within one mile) in the Kokopelli Field, which has estimated unproven reserves of 1.5 billion cubic feet per well. In August 2009, Williams Companies (WMB - NYSE) acquired the Kokopelli Field and is currently drilling over 100 wells adjacent to Dejour's Gibson Gulch acreage. In addition, Williams is extending its pipeline from its Grand Valley gathering system to link it with its proposed Kokopelli Field gathering system.



There are two structures within Gibson Gulch from which to extract gas: the 7,000 feet deep **Williams Fork** structure and the 13,000 feet deep **Niobrara** formation. The Williams Fork structure in the Piceance Basin is amongst the lowest quartile of supply cost natural gas basins in North America[1] leading to upper quartile after-tax typical well returns[2]. To access the resources in the Williams Fork structure, the company has delineated 93 PUDs (Proven Undeveloped Reserves) on 600 of the 2,200 gross acres. Each PUD is based on 10 acre spacing among the wells. Initially, management plans on drilling 16 wells

[1] Based on a study conducted by FirstEnergy Capital Corp. and MGM Energy Corp. in April 2010.

[2] Based on information delivered by Williams Companies at the Jefferies Global Energy Conference in December 2010.

between the first quarter of 2012 and the end of 2015, after receiving the necessary approvals and permits, along with securing the necessary financing. Ultimately, Dejour plans to drill 220 wells (158 wells net to Dejour) at Gibson Gulch.

Dejour also has exposure to a deep high-pressure gas opportunity in the Niobrara formation at Gibson Gulch. Management estimates the Niobrara gas reserves to be 215 billion cubic feet (BCF). Though the development of this unconventional resource opportunity is several years in the future, another company has drilled five wells into the formation, and land prices are rising in the area.

In March 2010, the company announced the results of the area's initial reserve evaluation of Gibson Gulch effective December 31, 2009. Proved and Probable Undeveloped reserves are 1.4 MMBO, 207 BCF for a total of 35.9 MMBOE. This year-end reserve report also assessed a statistically derived Prospective Resource Best Estimate of Dejour's entire leasehold position in Colorado and Utah. In addition to Gibson Gulch assessment, Proved and Probable Undeveloped reserves are 124 MMBO, 1.4 TCF for a total of 350 MMBOE net to Dejour.

South Rangely in the Piceance Basin – Dejour has 7,000 gross acres on the south side of Rangely field and management plans to drill two wells, when the company can secure financing or enlist a development partner. Management estimates that the contingent oil resources[3] are 8 million barrels oil (MMBO).

VALUATION

NAV Formulation

The valuation process for small and mid-cap E&P oil & gas companies is based upon Net Asset Value (NAV), which involves evaluating a company's assets and reserves, and then determining an appropriate discount at which the stock should trade. The NAV calculation entails applying several subjective inputs, such as land valuation (cost or market), a predicted oil price, oil versus gas mix, predicted gas price, drilling costs deep offshore wells versus, drilling success rate, mix of development and exploratory wells, etc. The discount attempts to quantify many factors, including but not limited to the average length of time that will be required to put the reserve additions on the company's books, R/P (reserves to annual production ratio), the company's PUD (Proved Undeveloped reserve) to 2P reserve ratio, and the stock's liquidity.

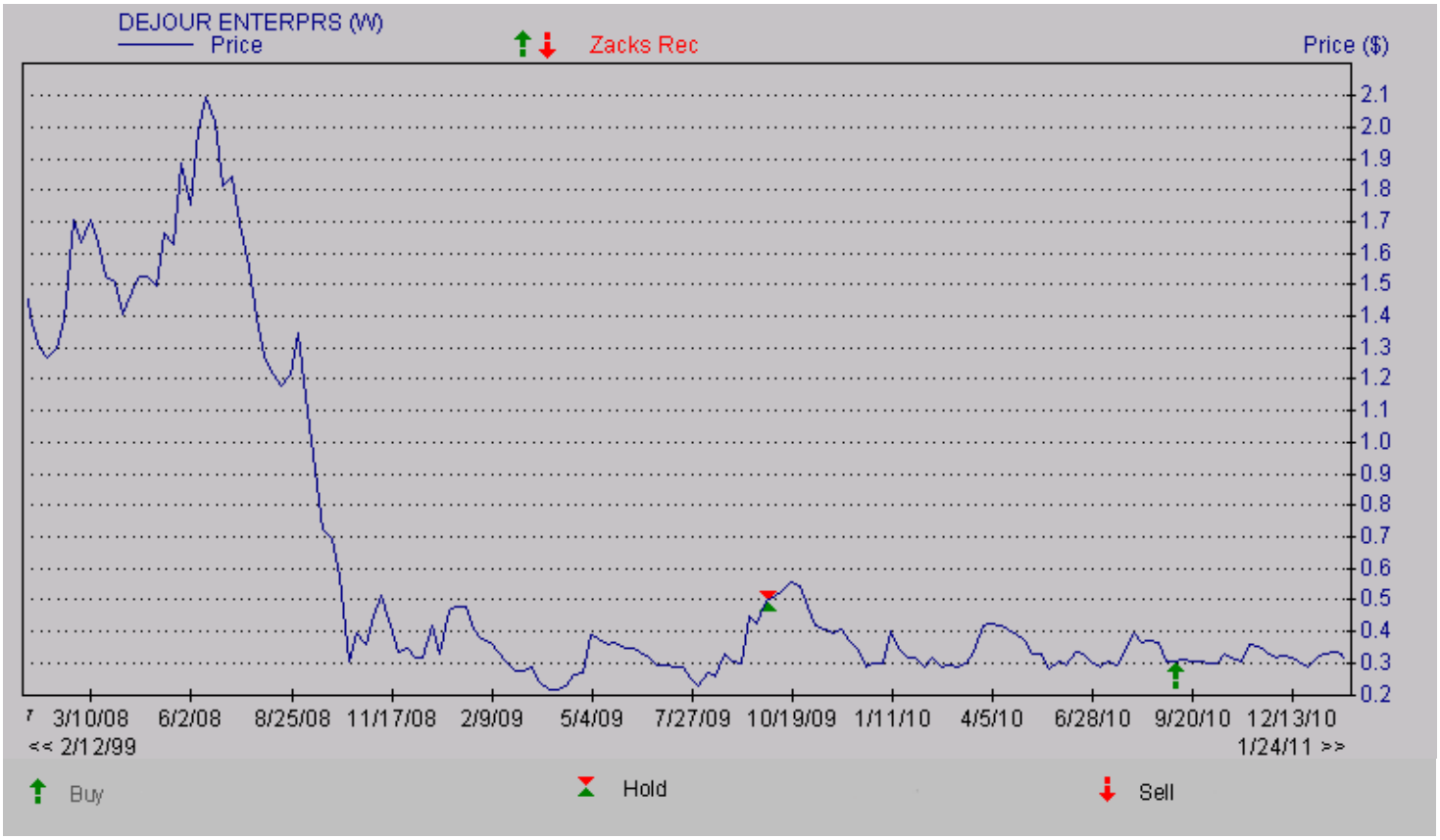
Dejour's NAV is estimated to be $185 million (or $1.68 per share) as of December 31, 2010. The $185 million is attained by adding the company's assets of $20 million of land (at cost) and $170 million of PV-10 Proved Reserves ($21 million at Woodrush and $149 million at Gibson Gulch) and deducting $5 million in debt (listed as a current liability on the company's balance sheet). The NAV is then discounted by 40% to attain our target price of $1.00 per share. Though a 40% discount may appear high, it is well within the range of 13% to 59% discounts at which mid-cap E&P companies are currently trading. In addition, with Dejour's stock trading only $125,000 worth of stock on an average day, the stock's illiquidity also factors into the estimated 40% discount.

[3] Contingent resources are those quantities of oil and gas estimated to be potentially recoverable but are not currently economic.

FINANCIAL STATEMENT (EARNINGS MODEL)

Dejour Enterprises Ltd. Earnings Model												
FISCAL YRS ENDING 12/31	Q1	Q2	Q3	Q4 E	2010 E	Q1 E	Q2 E	Q3 E	Q4 E	2011 E	2012 E	2013 E
PROVED RESERVES (net)												
Natural gas (MMCF)					**87,911**					**92,000**	**105,000**	**115,000**
Crude oil (MBO)					**775**					**835**	**1,000**	**1,250**
Natural gas liquids (MBO)												
Total (MMCFE)					**87,911**					**92,000**	**105,000**	**115,000**
Total (MBOE)					**14,652**					**15,333**	**17,500**	**19,167**
PRODUCTION VOLUMES (net)												
Natural gas (MMCF)	96.6	136.5	167.3	186.3	**586.7**	186.3	184.3	184.3	186.3	**741.2**	**750.0**	**750.0**
Crude oil (MBO)	11.8	31.8	28.2	13.8	**85.6**	20.7	34.1	50.5	51.1	**156.4**	**200.0**	**200.0**
Natural gas liquids (BBLS)	0.6											
Total (MMCFE)	100.3	136.5	167.3	186.3	**1,100.3**	186.3	184.3	184.3	186.3	**1,679.5**	**1,950.0**	**1,950.0**
Total (MBOE)	28.5	54.5	56.1	44.9	**183.4**	51.8	64.8	81.2	82.1	**279.9**	**325.0**	**325.0**
OIL PRICE REALIZATIONS / GAS HUB PRICES												
Natural gas (CAD/MCF)	5.04	4.29	3.81	3.80	**16.94**	3.95	3.95	3.95	3.95	**3.95**	**4.00**	**4.15**
Oil (CAD/BBL)	71.60	65.79	66.77	75.00	**279.16**	77.00	78.00	79.00	80.00	**78.50**	**85.00**	**92.00**
Natural gas liquids (CAD/BBL)	23.58											
INCOME STATEMENT (CAD 000 except EPS)												
Natural gas revenues	487	586	638	708	**2,419**	736	728	728	736	**2,928**	**3,000**	**3,113**
Crude oil revenues	846	2,089	1,885	1,035	**5,855**	1,594	2,662	3,990	4,085	**12,330**	**17,000**	**18,400**
Natural gas liquids revenues	15				**15**							
Total oil and gas revenues	1,347	2,676	2,523	1,743	**8,288**	2,330	3,390	4,718	4,821	**15,258**	**20,000**	**21,513**
Other operating revenues	(42)	93	21	0	**72**	0	0	0	0	**0**	**0**	**0**
TOTAL REVENUES	1,305	2,769	2,544	1,743	**8,361**	2,330	3,390	4,718	4,821	**15,258**	**20,000**	**21,513**
Operating expenses												
Royalties	221	551	362	366	**1,500**	489	712	991	1,012	**3,204**	**4,200**	**4,518**
Operating and transportation	843	660	543	581	**2,626**	575	575	575	575	**2,300**	**2,461**	**2,633**
Amortization, depletion & acc.	746	1,351	1,393	934	**4,424**	1,249	1,817	2,529	2,584	**8,178**	**11,000**	**11,832**
General and administrative	987	769	670	665	**3,091**	665	665	675	675	**2,680**	**3,500**	**4,200**
Stock based compensation	164	150	150	150	**615**	150	150	175	175	**650**	**750**	**800**
Total operating expenses	2,961	3,481	3,118	2,696	**12,256**	3,128	3,919	4,944	5,021	**17,012**	**21,911**	**23,983**
OPERATING INCOME	(1,656)	(713)	(574)	(953)	**(3,896)**	(798)	(529)	(227)	(201)	**(1,754)**	**(1,911)**	**(2,470)**
Interest expense	(252)	(275)	(309)	(300)	**(1,137)**	(275)	(250)	(200)	(150)	**(875)**	**(500)**	**(250)**
Interest income	9	8	9	5	**31**	5	5	2	2	**14**	**12**	**10**
Gain (loss) on investments					**0**							
Equity income (loss)					**0**							
Impairments			(10)		**(10)**							
Foreign exchange gain (loss)	(16)	13	(9)	0	**(12)**	0	0	0	0	**0**	**0**	**0**
Pretax income	(1,915)	(968)	(893)	(1,248)	**(5,024)**	(1,068)	(774)	(425)	(349)	**(2,615)**	**(2,399)**	**(2,710)**
Inc. tax recovery (expense)	0	0	0	0	**0**	0	0	0	0	**0**	**0**	**0**
Net Income before non-reoccurin	(1,915)	(968)	(893)	(1,248)	**(5,024)**	(1,068)	(774)	(425)	(349)	**(2,615)**	**(2,399)**	**(2,710)**
Less: non-recurring items	0	0	0	0	**0**	0	0	0	0	**0**	**0**	**0**
REPORTED NET INCOME	(1,915)	(968)	(893)	(1,248)	**(5,024)**	(1,068)	(774)	(425)	(349)	**(2,615)**	**(2,399)**	**(2,710)**
Weighted Avg. Shares Out.	97,727	98,698	99,198	102,000	**99,406**	110,000	113,000	115,000	125,000	**115,750**	**130,000**	**140,000**
EPS before NRI	(0.02)	(0.01)	(0.01)	(0.01)	**(0.05)**	(0.01)	(0.01)	(0.00)	(0.00)	**(0.02)**	**(0.02)**	**(0.02)**
REPORTED NET INCOME	(0.02)	(0.01)	(0.01)	(0.01)	**(0.05)**	(0.01)	(0.01)	(0.00)	(0.00)	**(0.02)**	**(0.02)**	**(0.02)**

HISTORICAL ZACKS RECOMMENDATIONS



GLOSSARY AND KEY TO ABBREVIATIONS

1P - Proved reserves
2P - Proved reserves plus Probable reserves
3P - Proved reserves plus Probable reserves plus Possible reserves
API - American Petroleum Institute
BCF - Billion cubic feet
BCFE - Billions of cubic feet equivalent
BLM - U.S. Dept of the Interior, Bureau of Land Management
BOE - Barrel of oil equivalent (6 MCF of natural gas = 1 BOE)
BOE/D - Barrel of oil equivalent per day
BOPD - Barrels of oil per day
E&P – Exploration and Production
MBO - Thousand barrels oil
MBOE - Thousand barrels of oil equivalent
MCF - Thousand cubic feet natural gas
MCFD - Thousand cubic feet per day
MMBO - Million barrels oil
MMBOE - Million barrels of oil equivalent
MMCF - Million cubic feet
MMCFD - Million cubic feet per day
NAV - Net Asset Value
OGC – the British Columbia Oil and Gas Commission

Operating Netback - non-GAAP measure of oil and gas sales net of royalties, production and transportation expenses
P50 - Probable reserves with a 50% confidence level of recovery aka 2P
PD - Proved Developed reserves
PUD - Proved undeveloped reserves
PV-10 - Present value calculated at a 10% discount rate.

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