



22<sup>nd</sup> August 2011

Dear Shareholder

I am writing to inform you about some important developments recently announced by your company.

### **Proposal by Santos to acquire your Eastern Star Gas shares**

On 18<sup>th</sup> July 2011 Eastern Star Gas Limited ("ESG") announced it had entered into an agreement with Santos Limited ("Santos") under which Santos would acquire all the issued ordinary shares of ESG not already held by Santos and TRUenergy Investments Pty Limited ("TRUenergy") through a Scheme of Arrangement (the "Proposal" or "Scheme").

Santos is ESG's largest shareholder, holding approximately 20.9% of the issued ordinary shares, and is one of Australia's largest diversified oil and gas exploration and production companies, which has been providing Australia with natural gas for more than 40 years. Santos has interests in four LNG projects including their Gladstone Coal Seam Gas to LNG Project. Santos has over 2,400 employees working across its operations in Australia and Asia.

### **What is the Proposal?**

Under the Proposal, ESG shareholders will receive 0.6881 Santos shares for every 10 ESG shares held<sup>1</sup>. Based on Santos's closing share price on the day prior to announcement of the transaction<sup>2</sup>, the Proposal is equivalent to A\$0.90 per ESG share, valuing the company at approximately A\$924 million.

### **The Proposal represents a significant premium to the ESG share price**

Based on the Santos share price one day prior to the Proposal announcement, the implied offer price of A\$0.90 per ESG share represents an attractive premium for ESG shareholders:

- a 51% premium to ESG's closing share price of A\$0.595 on Friday 15<sup>th</sup> July 2011, the last trading day prior to the announcement; and
- a 48% premium to the 30 day Volume Weighted Average Price of Eastern Star Gas shares prior to the announcement.

<sup>1</sup> Since the Proposal was announced, Santos has declared an interim dividend of A\$0.15 per share resulting in an upward adjustment to the ratio of Santos shares for every 10 ESG shares held from the initially announced figure of 0.6803 to 0.6881. This revised ratio applies to the Santos share price from the 24th August 2011, after it trades ex-dividend.

<sup>2</sup> Adjusted for the Santos interim dividend of A\$0.15 per share.



## **Proposal presents significant benefits to ESG shareholders**

The Proposal provides ESG shareholders with the following key benefits:

- the opportunity to crystallise the future value of their ESG shares now, thus reducing commercialisation, development and financing risks associated with a standalone development of the Narrabri Gas Project;
- the project development experience and capability, balance sheet strength and benefits associated with being part of a larger and more diversified oil and gas company;
- continued exposure to the Narrabri Gas Project and the Eastern Australian gas market through a shareholding in Santos; and
- Capital Gains Tax rollover relief for eligible shareholders.

## **Unanimous board recommendation of an acquisition by Scheme**

***After considering the Proposal in detail, the ESG Directors formed the view that the Proposal is in the best interests of ESG shareholders. Accordingly, the Directors unanimously recommend that ESG shareholders vote in favour of the Proposal, in the absence of a superior proposal and subject to an Independent Expert's opinion that the Scheme is in the best interests of ESG shareholders. Each ESG Director intends to vote all ESG shares controlled by him in favour of the relevant resolution.***

The Eastern Star Gas Board has commissioned Grant Samuel & Associates Pty Limited as the Independent Expert, supported by MHA Petroleum Consultants LLC as technical specialist, to provide an Independent Expert's Report in relation to the Proposal.

Full details of the conditions and other terms of the Scheme are set out in the Scheme Implementation Deed, which was released to the ASX on 18<sup>th</sup> July 2011 and is available on the ASX website at [www.asx.com.au](http://www.asx.com.au) and the ESG website at [www.easternstar.com.au](http://www.easternstar.com.au).

## **PEL 238 Licence renewal**

On 4<sup>th</sup> August 2011, ESG announced that it was in the routine process of renewing the PEL 238 joint venture licence. The licence expired on 2<sup>nd</sup> August 2011, and the New South Wales legislation states that continuation of title occurs pending renewal. ESG anticipates that the terms of renewal will be finalised in due course.

## **Reserves assessment**

On 10<sup>th</sup> August 2011, ESG provided an update on its Tintsville pilot and the next reserves assessment which had been anticipated for mid-August. Due to the level of initial production from the Tintsville pilot since it commenced operations at the start of April, coupled with an inability to drill coreholes and pilot wells due to delays in receiving requisite government approvals, ESG's independent Reserves Certifier (Netherland, Sewell and Associates, Inc.) has confirmed that there is not yet sufficient data available to warrant an updated reserves report.



## Santos interim results

On 19<sup>th</sup> August 2011, Santos released its results for the half year ended 30<sup>th</sup> June 2011. Highlights of these results included:

- Continued good operational and financial performance with net profit of A\$504 million for the half, 155% higher than the previous first half;
- Maintenance of a strong balance sheet with A\$6.7 billion of funding capacity;
- Confirmation that Santos' new LNG projects remain on track for first production from PNG LNG in 2014 and GLNG in 2015; and
- Declaration of an interim dividend of A\$0.15 per Santos share, fully franked.

## Next steps

A Scheme booklet containing all the information relating to the Proposal and the reasons for the ESG's Directors' unanimous recommendation of the Proposal will be dispatched to shareholders next month. The report of the Independent Expert will be included in the Scheme booklet.

The ESG Directors encourage you to read the Scheme booklet when you receive it and exercise your right to vote at the Scheme Meetings. If the Scheme is approved and implemented, it is expected that you will receive the Scheme consideration in late October to early November. A detailed finalised timetable of the key dates will be included within the Scheme booklet.

## What should you do now?

There is no action required by you at this stage. We will be writing again as the Proposal progresses and will provide you with the Scheme booklet, Notice of Meeting and Voting Form (for proxy voting and direct voting) with ample time for you to consider them.

I recommend that you also keep yourself informed of the progress of the Proposal by speaking to your adviser or checking the ESG website [www.easternstar.com.au](http://www.easternstar.com.au).

I would like to take this opportunity to thank you for your support of ESG, and I look forward to your participation at the Scheme Meetings. I encourage you to call the ESG information line on 1800 704 395 in Australia or +61 2 8256 3393 outside Australia if you have any queries.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'John Anderson', with a horizontal line drawn underneath it.

The Hon. John Anderson  
Chairman