



Research & Investment Services

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Company Insight!

Industry: Oil & Gas Exploration & Production

Blugrass Energy Inc. US\$0.45

Blugrass Energy Inc. A Newly Formed Drillbit-Growth Company

Blugrass Energy Inc. (OTC BB: BLUG.OB) is a newly formed exploitation and production company seeking to acquire oil and natural gas producing properties domestically. Blugrass focuses strategically to acquire and exploit assets in the Permian Basin. BLUG owns a 60% working interest (WI) in 2,800 acres in the Grayburg Jackson Pool with thirty-two wells in production with excellent potential for increased production by implementing new extraction technologies and surface equipment optimization. There are more than one hundred possible new drilling opportunities on this property. Blugrass signed a joint operating agreement with an operator who holds the remaining 40% WI in the project and will perform repair job workovers and other oil-well enhancement activities on previously neglected and underperforming assets. Two weeks ago Blugrass signed a LOI to earn-in in significant leaseholds in West Texas, an area on trend with numerous giant gas fields. BLUG is required to raise \$5 million in order to complete the deal to participate in a five-year development program, with the potential of finding 500+ BCF. A few days ago Blugrass engaged a venture capital firm from China to obtain sufficient financing to participate in the first package of well drillings. BLUG has an impressive management team, key to success for a startup company, with extensive knowledge and strong relationships within the O&G industry. BLUG further intends to acquire more O&G properties to significantly increase revenue growth as the Company will bring more wells into production, creating shareholder value through responsible and sustainable growth. We are initiating coverage on Blugrass Energy Inc. with a SPECULATIVE BUY/4 rating and have set an 18 to 24-month target price of \$2.50.

Blugrass Energy, Inc

INVESTMENT HIGHLIGHTS:

Key Data

	FY2010	FY2011	FY2012	FY2013	FY2014
Production:					
Nat Gas (BCF)	1.726	7.489	11.521	14.556	16.066
Crude Oil	9335	21595	15484	12760	11096
Revenue (\$000)	8'608	35'923	53'930	67'627	74'415
Oper. CF (\$000)	(25'827)	(26'265)	(9'707)	22'044	76'361
CF per share	(\$0.34)	(\$0.006)	\$0.218	\$0.418	\$0.714
EBITDAX/Share	\$0.118	\$0.60	\$0.918	\$1.153	\$1.278

Source: Company reports, business plan, SEC filings

Financial Data

FY 2010	Ends June 30, 2010
Market Capitalization	US\$ 25.3 million
Shares outstanding (February 10, 2010)	51,050,000
Book Value/ Share (September 30, 2009)	-\$0.01
Price/Book Ratio	N/A
Est. 5 Year Earnings Growth	N/A

Stock Data

52-Week Range	\$1.14 – 0.22
Symbol / Exchange	OTC BB:BLUG
1-Year Return	-35.25 %

Stock Chart



In October 2009, Blugrass, acquired a 100% WI in the Cave Pool Unit

within the prolific Artesia Vacuum Trend located near Loco Hill in Eddy County in New Mexico. The Cave Pool Unit has approximately 2,800 contiguous producing acres, with Net Revenue Interests in the range of 68%-75%. This acquisition includes all equipment used to produce and sell crude oil and natural gas on the acreage including one water disposal well. Thirty-two wells are currently producing on the leasehold, with more than 100 possible new drilling and reworking targets, with potential gross reserves in excess of 3.0 million barrels-of-oil equivalent.

To expedite the reworking and redevelopment process in the Cave Pool Unit,

Blugrass and Doral Energy (OTC BB: DRLY) signed a joint operating agreement in late October 2009 whereby Doral acquired a 40% WI in the Cave Pool Unit from Blugrass. Doral is a registered oil and gas operator within the state of New Mexico and has extensive expertise as an operator in the area. Blugrass will benefit greatly from this cooperation. Already, ten shut-in wells on the properties have been identified and will be reworked and returned to production by Doral Energy, adding to the daily production from the properties. The redevelopment of the Cave Pool Unit could potentially add approximately 100 development drilling locations and potential gross reserves in excess of 3.0 million barrels-of-oil equivalent.

Just recently Blugrass completed its due diligence of the 16,554-acre Val Verde Basin natural gas project

that is privately owned and is located in West Texas. These leases are on trend with numerous giant gas fields including the Gomez Field, the Brown Bassett Field, and the JM Field. The Company has the opportunity to earn-in to the deep targets, specifically the Ellenburger/Strawn formations as well as shallow targets like the Canyon Sands. After the completion of the first package of well drilling, BLUG has the option of electing to continue participation in the project. The project could be a company-making asset.

We are initiating coverage on Blugrass Energy with a SPECULATIVE BUY/4 rating,

which is based on our favorable view of the O&G industry as well as the Company's business model and its participation with strong business partners who work solely in fields that have a long history of producing wells from the target formations and large production volumes. In addition, risk is minimized by acquiring and enhancing oil and gas properties in the Permian Basin and drilling with proven undeveloped-like targets adjacent to existing producing wells, with step-out drilling from there. BLUG inked a deal with a Venture Capital firm from China to raise the first \$5 million through equity financing. The current plan is to drill approx. 75 wells, within the next four to five years targeting Canon, Strawn and Ellenburger well locations. These wells are long lived (21 years+), with significant producers. We have set an 18 to 24-month target price of \$2.50 and believe our valuation is conservative.

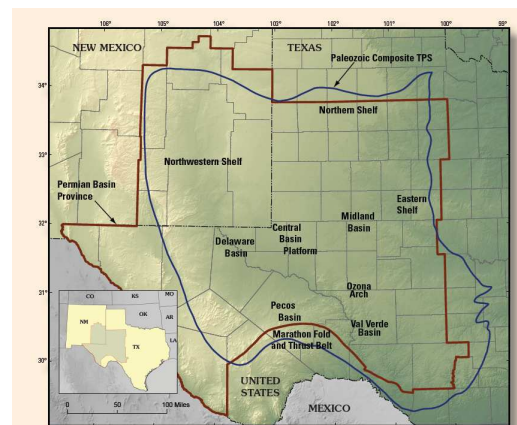
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COMPANY OVERVIEW

Blugrass Energy Inc. (OTC BB: BLUG.OB) is a newly formed Calgary based oil and gas company focused on exploration and production in known basins in North America. The Company's core area of focus is the Permian Basin of West Texas and New Mexico. This basin has been a top US oil and gas producing region for decades and still contains vast untapped oil reserves. Blugrass management is very well connected in the O&G industry, and its industry knowledge helps it to identify low to medium risk development targets with significant exploration upside. In its early stage of business development, Blugrass is seeking to acquire top oil and natural gas properties in the Permian Basin where implementation of new extraction technologies will increase existing production at nominal cost. BLUG is also seeking participation with industry partners in oil and gas exploration in targeted operating areas as well as other joint ventures. The next step of corporate development includes optimization of production of the acquired assets by leveraging the Company's established but under-exploited producing wells and growth through internally generated and developed prospects. Access to new and enhanced exploration techniques will allow the Company to significantly increase successful well completion ratios. Blugrass Energy Inc., intends to increase shareholder value by creating attractive returns on investment by improving under-exploited producing assets and by creating additional value through implementing infill development drilling programs. The Company's partners have identified more than 100 potential infill locations on its acquired properties in Eddy County, New Mexico as well as the potential to find more than 500 Bcf of natural gas on its earn-in opportunity in Val Verde and Crockett Counties in West Texas.

THE FOCUS OF INTEREST: THE PERMIAN BASIN

The Permian Basin is one of the largest structural basins in North America. It encompasses a surface area in excess of 86,000 square miles and includes all or parts of 52 counties located in West Texas and south-east New Mexico. The Permian Basin is one of the most prolific petroleum provinces of North America and is now in a mature stage of exploration and development. The US Geological Survey estimates a remaining mean of 41 trillion cubic feet of undiscovered natural gas and a mean of 1.3 billion barrels of undiscovered oil in the Permian Basin Province, using a geology-based assessment methodology. The Basin produces approx. 825,000 barrels of oil per day (approximately one quarter of the nation's domestically produced oil). The annual output is more than 350 million barrels of oil and 1,500 billion cubic feet of



ft. and mature. Reversing production decline is a major focus of current and future developments in this area. The redevelopment of the Cave Pool Unit as a waterflood project could potentially add 100 infill development drilling locations and potential gross reserves could be in excess of 3.0 million barrels of oil equivalent. In West Texas, in Val Verde and Crockett Counties, Blugrass' focus is on the Massie South Extension targeting numerous deep targets within the Ellenburger (14,000 ft.) and Strawn formations (12,000 ft.) as well as on the Childress-Soto Ranch Prospect near the multizone Miller Field (Ellenburger, Strawn, Devonian and Canyon formations).

RECENT DEVELOPMENTS

On October 13, 2009, Blugrass Energy Inc. successfully closed the acquisition of properties and corporate assets located in the Grayburg Jackson Pool within the Artesia Vacuum Trend in Eddy County, New Mexico. The block is adjacent to major players including Conoco, Exxon, EOG and Devon Energy. The new properties deliver minimal but immediate cash flow and new opportunities to this area. Blugrass has purchased a 100% working interest with net revenue interests in the range of 68%-75%, including all rights associated with the acreage acquisition of the Cave Pool Unit, which comprises approx. 2,800 acres, with plenty of drillable acreages. With this purchase, Blugrass also acquired all operating rights, with respect to the oil and gas leases acquired, including all equipment used to produce and sell crude oil and natural gas on the acquired acreages. The Cave Pool Project is very attractive because it's in shallow depths associated with lower drilling and completion costs and fewer operational risks when compared to deeper wells.

Cave Pool Unit Project, Eddy County, New Mexico

The Cave Pool Unit is located within the Grayburg Jackson Pool north of Loco Hills, one of thirteen reservoirs along the Artesia-Vacuum Trend with an aggregate annual production of more than 1 million barrels of oil. The Blugrass Cave Pool Unit produces approximately 12 BOPD and 30 MCFD of natural gas from 32 wells. Production can be optimized and increased by pump changes, upgrading wellheads, replacement of bad tubing, and new polish rods and stuffing boxes. There are approx. 10-12 wells that could be put on line with electric pump changes and tubing jobs, which should increase production significantly. Depths to the top of reservoirs range from 1,290 to 4,700 ft. The recent development of the lower permeability Grayburg sandstones in the Grayburg Jackson reservoir during the mid-1990s has been successful to the point of reversing production decline and is a major focus of current and future development in the area. The redevelopment of the Cave Pool Unit as a 20-acre 5-spot Grayburg waterflood project that could potentially add approximately 100 development drilling locations and potential gross reserves in excess of 3.0 million barrels-of-oil equivalent.

On October 29, 2009, Blugrass sold a 40% working interest in the Cave Pool Unit properties to its new joint operating partner, Doral Energy Corp. Doral currently owns and operates 186 wells on 66 leases and approximately 7,800 acres along the Artesia-Vacuum Trend. Doral West Corp., a subsidiary of Doral Energy Corp. will be the operator of the JV Cave Pool Unit Project. Initially, Blugrass will pay \$200,000 for start-up costs to rework and repair the joint operating assets.

Doral Energy Corp. is a publicly traded company trading on the Over the Counter Bulletin Board under the Symbol BLUG. The company is a rapidly growing oil and gas exploitation and production company focused on identifying, acquiring, operating and enhancing oil and gas properties in the Permian Basin of West Texas and New Mexico. The company performs repair job workovers and other oil-well enhancement activities on previously neglected and underperforming assets. Doral capitalizes on the opportunities identified for operational improvements to existing wells. Doral is the ideal partner for Blugrass; the Company utilizes and employs information, data, and experience gained in similar operations on other Doral-owned leases along the Artesia-Vacuum Trend, resulting in a significant savings to Blugrass. The Cave Pool Unit Project's acreage is located adjacent to 3 leases owned and operated by Doral, which contain 9 proven undeveloped drilling locations. The redevelopment of the Cave Pool Unit, currently envisioned by Doral as a 20-acre 5-spot waterflood project, could potentially add 100 infill development drilling locations, with potential gross reserves in excess of 3.0 million barrels of oil equivalent. The successful redevelopment of the Cave Pool Unit has the potential to be very lucrative for both Blugrass Energy and Doral Energy as well as for their shareholders by increasing probable reserves to the proven category and through increased production.

At time of this writing, no reserve report has been assigned to the Cave Pool Unit. According to the joint operating agreement, Doral will be responsible for preparing all geological and engineering data necessary in order to prepare a 3rd party engineering evaluation report. Doral is also responsible for 100% of the costs of the party engineering report, which we expect to be finalized during in the first quarter of 2010.

Doral is already undertaking an immediate assessment of the mechanical and operational integrity of existing wells, pumping units, and production facilities. The focus of initial well repairs will be the restoration of existing wells to production by repairing downhole pumps, rods, and tubing, along with surface pumping units and motors. After an initial geological review of the project, the operator plans to begin perforating and completing additional bypassed pay zones within the Grayburg Jackson Pool in the existing Cave Pool Unit Project wells. These operations will potentially add to oil production and increase proven developed reserves at a fraction of the cost required for the drilling and completion of new wells.

Financial Data and Projections: Cave Pool Project:

	2010E	2011E	2012E	2013E	2014E
Total Oil Production	9'335	21'595	15'484	12'760	11'096
Total Nat Gas Production	12'188	19'935	16'169	14'280	13'005
Net Oil & Gas Revenue	761'090	1'719'308	1'242'102	1'028'387	897'204
Total Cash Flow	496'823	1'306'555	990'609	783'618	653'069
Cumulative Cash Flow	496'823	809'732	1'800'341	3'367'578	4'020'647

EARN-IN OPPORTUNITY IN TEXAS, LOI SIGNED

Over the years, the management team of Blugrass has built a very close relationship to the privately owned Petro Grande LLC based in West Texas. Just two weeks ago, Blugrass signed a letter of intent to buy 75% of Petro Grande's working interest (WI) located in the Soto Lease and targeting Canyon formation and a 25% working interest in the Strawn and Ellenburger wells located in the South Massie Field prospect. In order to complete the deal, Blugrass needs an initial funding in the amount of \$5 million. On February 9, 2010, Blugrass announced a \$5 million equity raise and engaged a Venture Capital firm from China to act as its agent. Petro Grande LLC holds an 87.5% WI in 16,554 leased acres in Val Verde and Crockett Counties of West Texas. The leaseholds are on trend with numerous giant gas fields, including the Gomez Field (10.6 TCF), the Brown Bassett Field (1.6 TCF), and the JM Field that have produced in excess of 650 BCF to date. Petro Grande holds two blocks. The first is the Petro Grande South Massie Prospect, consisting of 11,747 acres, which is part of the existing Massie Field. 3D seismic studies have identified numerous deep targets in the historically productive Strawn formation (12,000 feet) and the Ellenburger formation (14,000 feet top). The second block consists of the Childress-Soto Ranch Prospect, comprising 4,807 acres near the multi zone Miller Field, which produces from the Ellenburger, Strawn, Devonian, and Canyon formations. This project merges into the Ozona Canyon gas field and there are currently productive wells on the lease. Numerous drilling targets have been identified in the shallower Canyon Sands (6,300 feet) formation. Petro Grande has a very experienced management, advisory, and technical team that has spent considerable time and resources to evaluate the project. To date, the Company has invested more than \$8.8 million in the Val Verde Project, gathering and analyzing data and preparing comprehensive development programs.

PACKAGE DEAL WITH PETRO GRANDE

An extensive 3D seismic data acquisition program over the entire acreage and surrounding areas has been completed by Petro Grande as well as advanced processing of this data in order to analyze the formations, faults, integrate the land culture, etc. This 3D seismic survey significantly lowers project risks and identifies potential targets with a much higher degree of accuracy than former surveys. This also helps to better define the Company's drilling plan and to specifically identify Strawn/Ellenburger reservoirs at depth within the fields. Structural maps and seismic attributes for the Strawn, Devonian, and Ellenburger

reservoirs have been generated for the Massie and Childress-Soto prospects and for the Canyon Sands at Childress-Soto. Based on data analysis, it is estimated that there is 500+BCF of natural gas in these leaseholds.

Blugrass management believes in a high success rate for the Val Verde Project and has negotiated favorable terms to participate in the exploration and development programs of these projects based on the following earn-in terms:

- For the deep Ellenburger/Strawn formation, Blugrass contributes 1/3 of drilling, operating and lease costs to earn a 25% working interest from Petro Grande's working interest.
- For the shallow Canyon Sands targets, Blugrass pays all drilling, operating and lease costs to earn a 75 % working interest on Petro Grande's WI.

THESE FACTS MAKE THIS PROJECT SO EXCITING FOR BLUGRASS:

- Blugrass earns-in to a desirable lease position in the acreage in the midst of large proven gas fields and active development by major industry players
- The Project is viewed as a resource-like play given known quantities of gas in targeted formations
- The acreage is in the midst of numerous surrounding fields that have a long history of producing wells from the target formations and large production volumes
- Drilling can begin with proven undeveloped-like targets immediately adjacent to existing producing wells, with step-out drilling from there
- Surrounding acreage has been leased by major companies that include HBP-EOG, ANADARKO, DEVON, CHEVRON, OXY and CHESAPEAKE, who own several hundred square miles in the area
- The opportunity exists to generate significant reserves of up to 500+ Bcf
- Drilling costs are down in the area and operators in the area utilize economical air hammer drilling

The plan is to drill approx. 75 wells - 60 Strawn and 15 Ellenburger within the next four to five years as well as some Canyon Sands. The Ellenburger wells are significant producers and Petro Grande estimated them to have average initial flow rates of 10 MMcfd in year one and an accumulative reserve over a 21-year well life of 16.6 Bcf. Ellenburger wells in the region have had reserves of up to 166 Bcf and initial flow rates of 10 to 50 MMcfd.

Blugrass and Petro Grande have agreed to initiate a package consisting of a four-well drilling program, with plans to drill one Ellenburger well, one Strawn well, and two Canyon Sands wells. Blugrass estimates expenditure costs for this four-well package to be \$4,554,066. After the completion of the four-hole drilling program, Blugrass will have the option of electing to continue participation in the project based on exactly the same terms. Blugrass management believes in a high success rate for the Val Verde Project and has negotiated favorable terms to participate in the exploration and development program of these projects based on the following earn-in terms:

- For the deep Ellenburger/Strawn formation, Blugrass contributes 1/3 of drilling, operating, and lease costs to earn a 25% working interest on Petro Grande's WI.
- For the shallow Canyon Sands targets, Blugrass pays all drilling, operating, and lease costs to earn a 75% working interest on Petro Grande's WI.

Well Expenditure Package

Management estimates the following expenditures per well:

	Ellenburger Well	Strawn Well	Canyon Sands Well
Seismic, land, lease payments:	748,000	412,000	24,000
Drilling & Completion:	3,200,000	2,600,000	727,000
Well Connection to Gathering Sys	250,000	250,000	100,000
Misc.	10,000	10,000	10,000
Subtotal	4,208,000	3,272,000	861,000
Contingency Fee	320,000	260,000	72,700
Total Cost of Expenditure	4,528,000	3,532,000	933,700
Blugrass Contribution	1,509,333	1,177,333	1,867,400
Total Package Costs			4,554,066

CAPEX = VALUE CREATION

Blugrass needs to raise \$5 million in order to complete the earn-in deal with Petro Grande. This would allow the Company to execute the initial drilling package in the Val Verde Project. To continue participation in the project, Blugrass needs to raise an additional \$15 million in FY2010, funded in equity, credit facilities, and early cash flow, to execute the drilling and development programs. Based on our cash flow analysis for FY2011, there would be enough cash flow generated to fund ongoing drilling and development programs in the project. If the Company is able to execute its plan successfully, we estimate it will grow significantly within the next 12 to 24 months and create value for its stockholders.

CAPITAL REQUIREMENTS

BLUGRASS Funding Requirements - Val Verde Basin Project

Initial Drilling Package (1 x Ellenburger, 1 x Strawn, 2 x Canyon):	\$4,544,066
Working Capital	\$455,934
Initial Funding Requirement:	\$5,000,000
Additional Funding for Continuation:	
Strawn/Ellenburger Program: Share of Year 1 Costs:	\$14,306,273
Less Initial Holes:	\$2,686,666
	\$11,619,607
Canyon Sands Program: Share of Costs to Nov. 2011:	\$16,444,806
Less Initial Holes:	\$1,867,400
Less Cash flow 2010:	\$6,666,200
	\$7,911,206
Total Project Funding Required:	\$24,530,813

Well Economics:

Ellenburger Well (TD 14,000 ft.)

The Ellenburger wells are estimated to have an initial average flow rate of 10 Mmcf/d and a cumulative reserve over a 21-year well life of 16.6 BCF. Ellenburger wells in the region have had reserves of up to 166 BCF and initial flow rates of 10 to 50 Mmcf/d.

Strawn Well (TD 12,000 ft.)

The Strawn wells are estimated to have an average initial flow rate of 2.5 MMcf/d and a cumulative reserve over a 21-year well life of 4.4 Bcf. Strawn wells in the region have had reserves of up to 10 BCF and initial flow rates of 3 to 10 MMcf/d.

Canyon Sands Well (TD 6,300 ft.)

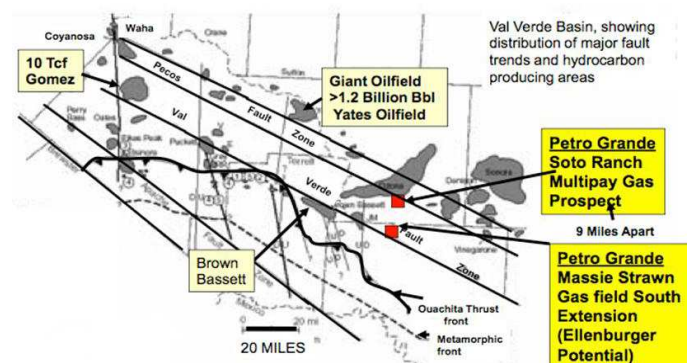
The Canyon Sands wells are estimated to have an average initial flow rate of 600 Mcfd and a cumulative reserve over a 21-year well life of 1.4 Bcf.

Financial Data/Projections Val Verde Project:

	2010E	2011E	2012E	2013E	2014E
Nat Gas Production (BCF)	1'726	7'489	11'521	14'556	16'066'
Net Gas Sales \$ (000)	7'908	34'303	52'769	66'670	73'583
Total Sales \$ (000)	8'225	36'229	55'573	70'002	76'654
Operating Cash Flow	24'973	20	18'062	33'904	56'295
Cumulative Cash Flow	24'973	24'994	6'931	26'972	83'267

VAL VERDE BASIN GEOLOGY AND EXPLORATION

The Val Verde basin is a northwest-southeast trending foreland basin contained within the southern portion of the Permian Basin. The Val Verde basin has several large fields such as the Gomez and Brown Bassett, which have a combined cumulative production of 12 TCF. Structurally, the major fields are complexly faulted features related to the differential uplift of basement blocks. Vertical and horizontal displacement resulted from a wrench system dominated by northwest and northerly trending faults. Reverse faults associated with the wrench

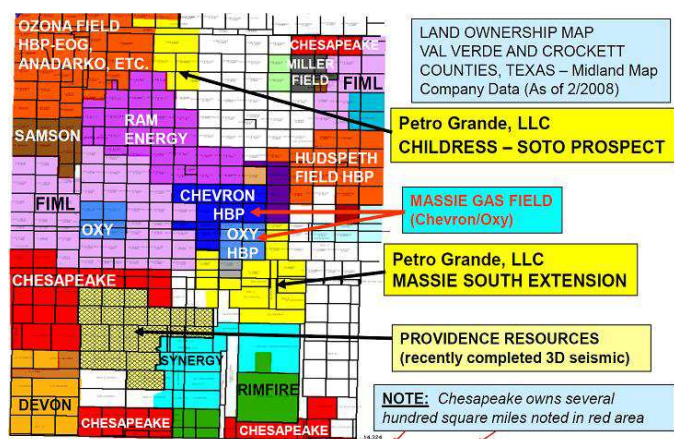


system appear to exhibit characteristics of both high-angle and low-angle faults, as is typical of foreland structures. Tectonism was initiated during the late Mississippian, consequent to Ouachita plate convergence, and continued into the Permian.

In the Massie Strawn Gas Field, there have been more than 60 wells drilled over the last 20 years, beginning in the mid-1980s, of which approximately 90% have been successfully completed and are producing, with an average recoverable gas in-place of approximately 2.7 BCF per well. An important aspect of the 3D surveys was the ability to obtain data from producing wells on adjacent properties, some of which have huge gas volumes as publicly reported. Petro Grande has been able to ascertain the precise subsurface features associated with these adjacent wells and has used this information in analyzing and projecting similar formation structures within the project area. In addition, the 3D technology allows superior interpretation of subsurface lithological and fluid properties, which provides a higher degree of accuracy in target identification and subsequent drilling decisions.

The results of this 3D analysis were used to generate structural maps and seismic attributes for the Strawn, Devonian, and Ellenburger reservoirs for the Massie South and Childress-Soto prospects. The data was also used to map the 6,300-foot Canyon Sands formation at Childress-Soto. Based on the careful interpretation of all 3D data, Petro Grande estimates that there is more than 500 BCF of natural gas in its acreage position.

GEOLOGY AND ACREAGES – VAL VERDE BASIN – NEARBY DEVELOPMENT ACTIVITY IS ROBUST



STRONG & EXPERIENCED MANAGEMENT TEAM

The Company has a strong management team of industry experts in both investment banking and the resource field and is led by **Ken J. Berscht, President & Director**, who has extensive investment banking and finance experience in resource field experience and has developed strong relationships with an extensive network of principals and senior management within the industry and by **Grace Sutherin, CFO & Director**, who has extensive experience in the O&G industry.

Ken J. Berscht - President & Director

Mr. Berscht has had an extensive career in investment banking and finance in the resource field. He has worked worldwide with investors in Europe and Asia as well as North America. In the past five years, he has worked as Vice President of International Enerplus, one of Canada's leading income trusts, managing its offshore branch in Europe. He was previously the President of Odyssey Management in the Cayman Islands. Mr. Berscht graduated with an Honours degree in Business Administration from the University of Western Ontario. In his years in the investment business he has been qualified with the IDA in Canada as an investment advisor and in the United States as a General Principal with the NYSE. He is a member of the SME and qualified in Europe as an IFA.

Grace Sutherin - Chief Financial Officer & Director

Ms. Sutherin has vast experience in both domestic and international business as an administrator, accountant, and finance manager. Her work experience includes serving as the Director of Finance at the American Chamber of Commerce in Moscow, External Auditor and Collateral Examiner for Wells Fargo Business Credit, Inc., and Manager for Euro-Asian Projects for Firecreek Global. Her oil and gas experience includes project oversight and development for oilfield acquisition as well as due diligence coordination for oil field properties in Kazakhstan and the Ukraine. Ms. Sutherin holds a BA in Russian Studies from Skidmore College in Saratoga Springs, New York, a degree in International Management from Thunderbird American Graduate School of International Management in Glendale, Arizona, and she graduated from The Russian School of Norwich University, Norwich, Vermont.

Edward W. Karasek - Director

Mr. Karasek has worked, since 2000, with Peak Consulting Group, Inc. of New Albany, Indiana, a consulting firm specializing in management and organizational development and training. He is a founder and has served as the President of Peak Consulting Group since 1984. Mr. Karasek holds a BS in Business, with an emphasis in Personal and Industrial Relations. He received an Associate Degree in Computer Science from Purdue University, Fort Wayne Extension. Mr. Karasek holds a Master of Science degree from Indiana University, majoring in Counseling Psychology. His prior work includes work at EDS, Marriott Corporation, and Morgan Stanley as well as having consulted with numerous other Fortune 100 companies in the areas of employee and management development needs.

ADVISORY BOARD

Mr. Don Hathaway

Mr. Hathaway is a professional corporate director specializing in corporate governance and reorganization to build shareholder value. Mr. Hathaway's career has spanned manufacturing, business and academia with more than twenty years at the executive level. Mr. Hathaway has accumulated expertise in strategy, marketing, finance, general management, and corporate governance, plus executive contacts across North America, Europe, India, and Hong Kong. Mr. Hathaway was a senior partner and practice leader with the international management consulting firm Ernst and Whinney. He is the Chairman of Manna Asset Management and sits on the board of four other companies. He has a BEng (Electrical) and a BSc (Mathematics) from Sir George Williams University, and an MBA from York University. He is a former Dean of Business at Waterloo University, a former Dean of York University, and a former Chair of the MBA Society of Canada.

Mr. Brian Gusko

Mr. Gusko brings with him significant resource, technology, and international business experience. Most recently, Mr. Gusko was the CFO of UC Resources Ltd., an emerging producer of silver and gold in Mexico. He is currently actively involved with several projects in Latin America and is a director of Grenville Gold Corporation. Mr. Gusko received a Bachelor of Arts in Biology from Carleton University, and an MBA from the University of Calgary. He is also a recipient of the Duke of Edinburgh Gold Award.

BLUGRASS SHARE TRANSACTIONS & SHAREHOLDER INFORMATION

Share Transactions September 2009 - January 2010

Date	Description	Shares
10.09.2009	Balance	50,050,000
12.31.2009	Cancelled Elizabeth Sawyer ex CFO	-500,000
12.31.2009	Cancelled L. Schaefer, Former CEO	-3,500,000
01.31.2010	Shares for Management	5,000,000
02.28.2010	Fundraising \$5M at \$0.50/Share	10,000,000
02.28.2010	Total shares outstanding	61,050,000

MAJOR SHAREHOLDERS

Beneficial Owner	Amount of Shares	Percent
Share issued and outstanding	61,050,000	100.00%
Management	5,000,000	8.19%
Bluefin Financial Group,	10,000,000	16.38%
HLB Productions, Inc.	10,000,000	16.38%
New Investors (Fundraising)	10,000,000	16.38%
Sub-Total	35,000,000	57.33%
Retail/Institutional Shareholders	26,050,000	42.67%

SALES OPERATING CASH FLOW FORECAST

Assuming that Blugrass Energy will be able to successfully finance its business developments by equity and debt financing, and obtain sufficient financing to fund its workover and development programs, we expect significant revenue growth as the Company acquires and brings more wells into production in the Permian Basin. There exist significant oil and gas development opportunities for the companies in the region. We believe Blugrass will be able to capitalize on this opportunity and create a steady revenue stream for the years to come. The Company's acquisitions are characterized as low-risk with high reward and short payback in historically successful and well-known productive regions. Estimated CAPEX is \$15 million for the period 2010/2011 financed through equity and debt finance instruments.

	2010E	2011E	2012E	2013E	2014E
Commodity Prices:					
Natgas	6.00	6.00	6.00	6.00	6.00
Crude Oil	75.00	75.00	75.00	75.00	75.00
Nat Gas Production BCF	1'726	7'489	11'521	14'556	16'066
Crude Oil Production	9'335	21'595	15'484	12'760	11'096
Oil & Gas Revenue (000)	8'608	35'923	53'930	67'627	74'415
Growth in %		317.3%	50.1%	25.4%	10.3%
Operating CF (000)	25'827	438	16'559	31'758	54'316
Outstanding Shares	66,050	66,050	66,050	66,050	66,050
Cash Flow per share	\$0.391	\$0.007	\$0.251	\$0.481	\$0.822

VALUATION METHODOLOGY

Our valuation methodology bases all target prices on a blend of 50% of estimated net asset value and FY2011 estimates of EV/EBITDAX ratio. We used a conservative long-term commodity price forecast of \$75/barrel for crude oil and \$6.00 for natural gas and incorporated into our target price a 5.0x 2011E EV/EBITDAX multiple, which is on the low-end, the traditional E&P valuation ranges from 5.0x to 7.0x. Although we believe the potential upside from exploratory successes would more than justify a higher multiple, we also feel we must take the early stage of exploration and development activities of the Company into account. For our NAV valuation we used 130% of NAV, which is in line with the peer group average.

EBITDAX OUR PRIMARY PRICING METRIC

EBITDAX - Earnings Before Interest, Taxes, Depreciation, Depletion, Amortization and Exploration Costs is a primary pricing metric for E&P companies. EBITDAX represents EBITDA before exploration costs for successful efforts companies. EBITDAX is a measure commonly reported and widely used by investors as an indicator of a company's operating performance and ability to incur and service debt. EBITDAX assists investors in comparing a company's performance on a consistent basis without regard to depreciation, depletion and amortization, impairment of natural gas and oil properties and exploration expenses, which can vary significantly depending upon accounting methods.

	2010E	2011E	2012E	2013E	2014E
Net Income (000)	-28'798	-13'137	-2'664	7'468	27'478
Add back:					
Income Tax	1'108	6'217	9'551	11'978	13'285
DD&A	2'970	12'699	19'223	24'282	26'837
Exploration	32'493	33'860	34'502	32'458	16'806
EBITDAX (000)	7'774	39'639	60'613	76'188	84'408
Outstanding Shares (000)	66'050	66'050	66'050	66'050	66'050
EBITDAX/Share	\$0.118	\$0.600	\$0.918	\$1.153	\$1.278
5.0x Valuation	\$0.59	\$3.00	\$4.59	\$5.77	\$6.39

PV@10% VALUATION

We obtained the estimated valuation matrix 2010 to 2014 from the Company's business plan, based on the aggressive drilling program planned by Petro Grande. Successful Strawn/Ellenburger drilling will have a major impact on P2 value creation of Blugrass Energy Inc.

Classification	2010	2011	2012	2013	2014
PV10 - PDP	27,409	60,683	87,274	102,395	87,285
PV10 - PUD	14,786	39,976	65,075	85,854	88,839
Total PV10 - 2P	42,196	100,659	152,349	188,249	176,125
Premium 30%	12,658	30,197	45,704	56,474	52,837
PV10 & Premium	54,854	130,856	198,053	244,723	228,962
Shares issued	66,050	66,050	66,050	66,050	66,050
Price Target	\$0.83	\$1.98	\$3.00	\$3.70	\$3.47

Using the above metrics, we obtained a valuation by the end of 2011 of \$2.50/share. We anticipate that the Company will finance its business development by selling company shares for funds and debt financing. We increased outstanding shares from the current 51,050,000 to 66,050,000 to reflect the financing and arrived at an 18- to 24-month target price of \$2.50.

INVESTMENT RECOMMENDATION

We are initiating coverage on Blugrass Energy Inc. with a SPECULATIVE BUY/4 rating, which is based on our favorable view of the O&G industry as well as the Company's business model and its participation with strong business partners in fields that have a long history of producing wells from the target formations as well as large production volumes. The Company basically started from scratch in mid-2009, with no oil and gas assets, and is already partnering with much larger and more experienced E&P companies in well known producing areas. Blugrass' risk is minimized by acquiring and enhancing oil and gas properties in core areas like the Permian Basin of West Texas and New Mexico as well as drilling with proven undeveloped-like targets adjacent to existing producing wells, with step-out drilling from there. The current plan is to drill approx. 75 wells - 60 Strawn and 15 Ellenburger within the next four to five years, which could meaningfully increase reserves and production growth over the next several years. These wells are long-lived (21 years+) and significant producers, and the Project could be a company-maker for Blugrass. For a small cap like Blugrass, a good position in any repeatable gas-resource play is a winning ticket. We have set an 18- to 24-month target price of \$2.50, which is based on our valuation methodology of a blend of 50% of estimated net asset value two years from now and a FY2011 5.0 times EV/EBITDAX ratio.

INVESTMENT RISK

Blugrass Energy Inc. is a newly formed junior exploration and production company and it is subject to several risks associated with the specific business it carries out and the market within which it operates. In particular, the natural gas market is much more volatile in price movements than the oil market. The biggest investment risk we see at this moment clearly revolves around the Company's ability to successfully obtain sufficient financing to fund all of its development programs in the Permian Basin.

ANALYST DISCLOSURE

Analyst: Ernest C. Schlotter

Ernest C. Schlotter has been an analyst in the energy field since 1998. He is a securities analyst covering energy with SISM Research & Investment Services, Zurich, Switzerland. His areas of focus have included all energy industry sub-sectors, with a focus on independent companies in exploration/production. According to the tracking firm StarMine based in San Francisco, Ernest C. Schlotter is a four out of five star analyst for EPS estimate accuracy and stock target price projection.

Analyst Certification:

I, Ernest Schlotter, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the recommendations or views expressed in this research report.

	Q1FY0E	Q2FY10E	Q3FY10E	Q4FY10E	YE2010E	Q1FY11E	Q2FY11E	Q3FY11E	Q4FY11E	YE2011E	YE2012E	YE2013E	YE2014E
	03.31.2010	06.31.2010	09.30.2010	12.31.2010	12.31.2010	03.31.2011	06.31.2011	09.30.2011	12.31.2011	12.31.2011	12.31.2011	12.31.2011	12.31.2011
Operating Revenues													
Nat gas Production Ellenburger Strawn	9'338	28'013	177'413	448'200	662'963	713'385	935'618	1'088'753	1'169'055	3'906'810	5'410'708	6'026'209	5'042'020
Nat gas Production Canyon Sands	11'812	153'551	354'348	531'522	1'051'232	649'638	811'063	968'551	1'133'914	3'563'166	6'094'786	8'530'600	11'024'160
Nat gas Production Cave Pool	1'450	2'321	3'712	4'704	12'188	5'400	5'222	4'803	4'510	19'935	16'160	14'280	13'005
Total Gas Production (MCF)	22'599	183'885	535'473	984'426	1'726'383	1'368'423	1'751'903	2'062'107	2'307'478	7'489'911	11'521'653	14'556'809	16'066'180
Nat Gas Price Henry Hub	6.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00
Gross Gas Revenue	135'595	1'103'309	3'212'838	5'906'556	10'358'297	8'210'535	10'511'419	12'372'643	13'844'871	44'939'468	69'129'917	87'340'853	96'397'081
Expenses													
Waha Discount (\$0.47 + \$0.25 backhaul)	16'271	132'397	385'541	708'787	1'242'996	985'264	1'261'370	1'484'717	1'661'384	5'392'736	8'295'590	10'480'902	11'567'650
Gathering Fee at \$0.25 on gas volume	5'650	45'971	133'868	246'106	431'596	342'106	437'976	515'527	576'870	1'872'478	2'880'413	3'639'202	4'016'545
Subtotal	115'417	924'940	2'693'429	4'951'663	8'685'449	6'883'166	8'812'073	10'372'399	11'606'617	37'674'254	57'953'914	73'220'748	80'812'887
7.5% Servance Tax	10'170	82'748	240'963	442'992	776'872	615'790	788'356	927'948	1'038'365	3'370'460	5'184'744	6'550'564	7'229'781
Net Revenue Natgas	105'247	842'192	2'452'466	4'508'671	7'908'577	6'267'375	8'023'716	9'444'451	10'568'251	34'303'794	52'769'170	66'670'184	73'583'106
Crude Oil Production Cave Pool	269	1'191	3'096	4'780	9'335	6'081	5'807	5'096	4'611	21'595	15'484	12'760	11'096
Oil Price	75.00	75.00	75.00	75.00	75.00	75.00	75.00	75.00	75.00	75.00	75.00	75.00	75.00
Net Oil Revenue	20'167	89'304	232'205	358'474	700'150	456'087	435'529	382'212	345'804	1'619'632	1'161'305	956'987	832'177
Total Revenue	125'414	931'496	2'684'672	4'867'145	8'608'727	6'723'462	8'459'245	9'826'663	10'914'055	35'923'426	53'930'475	67'627'171	74'415'283
General Overhead	99'999	99'999	99'999	99'999	399'996	99'999	99'999	99'999	99'999	399'996	399'996	400'000	400'000
Lease Operating	138'450	343'506	643'968	244'430	1'370'354	344'898	345'378	345'852	346'350	1'382'478	1'390'236	1'664'489	1'404'007
Valorem Tax (2% Gross Revenue)	2'508	18'630	53'693	97'343	172'175	134'469	169'185	196'533	218'281	718'469	1'078'610	1'352'543	1'488'306
Cash Flow before Drilling Expenses	-115'543	469'361	1'887'011	4'425'373	6'666'202	6'144'096	7'844'684	9'184'278	10'249'425	33'422'483	51'061'634	64'210'139	71'122'970
Drilling & Completion Cost	2'593'080	10'045'560	11'561'177	8'293'852	32'493'669	6'971'706	9'092'552	10'026'252	7'770'406	33'860'916	34'502'815	32'458'254	16'806'600
Operating Cash Flow	-2'708'623	-9'576'199	-9'674'166	-3'868'479	-25'827'467	-827'610	-1'247'868	-841'974	2'479'019	-438'433	16'558'819	31'751'885	54'316'370
Cumulative Cash Flow	-2'708'623	-12'284'822	-21'958'988	-25'827'467	-25'827'467	-26'655'077	-27'902'946	-28'744'919	-26'265'900	-26'265'900	-9'707'081	22'044'804	76'361'174
EBITDAX	-68'774	514'655	2'176'090	5'246'433	7'774'865	7'284'870	9'304'716	10'893'220	12'156'681	39'639'487	60'613'213	76'188'300	84'408'527
Average number of common shares out-standing	61,050,000	66,050,000	66,050,000	66,050,000	66,050,000	66,050,000	66,050,000	66,050,000	66,050,000	66,050,000	66,050,000	66,050,000	66,050,000
Basic PROFIT and LOSS per share	-0.001	0.008	0.033	0.079	0.118	0.110	0.141	0.165	0.184	0.600	0.918	1.153	1.278