

SDX Energy

Gas discovered at South Disouq

SDX has announced it has discovered gas in the Abu Madi structure of the South Disouq SD-1X well. The well came in on prognosis, validating the company's 3D seismic interpretation, and encountering 65ft of excellent quality net pay with average porosity of 25%. This unlocks 150–300bcf of the estimated 585bcf in the Abu Madi, with the remainder now de-risked in four other structures in the area. We expect this to be a material discovery that will contribute to a significant addition to the company reserves and resources (currently estimated to be 12.03mmboe on a 2P basis), increasing our RENAV from 57p to 76p/share.

Year end	Revenue (US\$m)	Reported PBT (US\$m)	Cash from operations (US\$m)	Net (debt) cash (US\$m)	Capex (US\$m)
12/15	11.4	11.1	(5.2)	8.2	(5.1)
12/16	12.9	(26.7)	(1.9)	4.7	(11.9)
12/17e	45.5	9.9	29.9	20.9	(22.9)
12/18e	80.9	35.9	56.4	35.1	(44.6)

Note: The financials above include the (unrisked) impact of South Disouq, which we estimate will require substantial capex in 2017 and 2018.

Remaining resources de-risked

The biggest risk pre drill was source/migration, as the nearest Abu Madi accumulation was 13km away. SD-1X has now proven the source. This de-risks the remainder of the 585bcf estimated to be contained in four similar structures in the area. Log data gathered across the reservoir indicate good mobility in the sands giving SDX confidence in the ability of the well to deliver on test. The deeper horizons (believed to be oil) are still being drilled. After these have been reached, we expect the gas discovery to be tested and completed as a producer. Given the proximity of the well to gas pipelines, first commercial production could start in late 2017, though this will depend on the characteristics of the gas and whether any treatment facilities will be needed.

Capital investment for development

As we model it, a gas development may require tens of millions of dollars, but SDX can control the timing of investment while cash flows should follow capital spend quickly. SDX's increased financial strength following the Circle Oil asset acquisition and its current 55% working interest means that it should be in a strong position to develop South Disouq without material equity dilution should it choose.

Valuation: NAV increased, awaiting deeper targets

We increase our risking on South Disouq to 75% on the 150-300bcf proven by the SD-1X well, with the remainder of the 585bcf risked at 40% to reflect the de-risking of the additional structures that will target this resource. We would expect to further review these riskings post testing of the SD-1X well and confirmation of the resources to be initially developed. This significantly increases our valuation to 76p/share. It is clear that this discovery is a material event and success at a scale of say half the 585bcf estimate could triple the SDX's net 2P resource base.

Drilling success

Oil & gas

19 April 2017

Price 56.0p

Market cap £105m

US\$/£0.8

Net cash (\$m) at 28 February 2017 18.3

Shares in issue 186.9m

Free float 59%

Code SDX

Primary exchange AIM

Secondary exchange TSX Venture

Share price performance



% 1m 3m 12m

Abs 21.4 60.6 N/A

Rel (local) 24.9 60.8 N/A

52-week high/low 56.0p 18.0p

Business description

SDX Energy is a North African onshore player listed in Toronto and London. It has plans to increase net production in Egypt (primarily through workovers and waterflood) while 2017 should see a carried exploration well. It has recently added high-value gas production in Morocco.

Next events

South Disouq results c May 2017

Meseda waterflood ramp-up Mid-2017

Analysts

Will Forbes +44 (0)20 3077 5749

Elaine Reynolds +44 (0)20 3077 5713

oilandgas@edisongroup.com

[Edison profile page](#)

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Valuation

For our valuation we assume that 225bcf is proven by SD-1X (being the mid-point of the current management estimate of 150–300bcf), and apply a CoS to this of 75%. We believe this risk to be reasonable given the confidence in gas mobility in the reservoir indicated by log data and that the well can be tied in immediately to existing infrastructure. In addition, SDX is fully funded for the development and we expect the Egyptian authorities to be supportive given the country gas shortages. The balance of the 585bcf is included as additional appraisal upside and risked at 40% in view of the de-risking of the remaining structures by SD-1X. At present, we assign no value to the deeper Abu Roash and AEB horizons, but will review this if oil is encountered in the case of success.

Exhibit 1: NAV summary

Asset	Number of shares: 187m			Recoverable Reserves			Net risked value			
	Country	Diluted WI	CoS	Gross	Net WI	Net	NPV	Absolute	GBp/share	C\$/share
		%	%	mmboe			\$/boe	\$m	12.5%	
Net (debt) cash - December 2016		100%	100%					5	2.0	0.03
Cash raised minus acqn minus costs		100%	100%					7	3.1	0.05
SG&A - NPV10 of 4yrs		100%	100%					(11)	(4.6)	(0.08)
Net financial income (expenses) NPV 2 years		100%	100%					0	0.0	0.00
2017 exploration		100%	100%					(4)	(1.7)	(0.03)
Receivable for gas and NGLs at Gemsa (as yet not invoiced)		100%	100%					2	0.6	0.01
Production										
Meseda Base case - Edison	Egypt	50%	100%	3.9	2.0	0.7	6.2	12	5.2	0.09
Meseda Base + Workovers - Edison	Egypt	50%	90%	4.5	2.3	0.9	6.0	12	5.3	0.09
Gemsa 1P	Egypt	50%	100%	4.1	2.1	2.1	9.4	19	8.3	0.14
Gemsa 2P	Egypt	50%	100%	1.9	1.0	1.0	9.9	10	4.1	0.07
Sebou 2P	Morocco	75%	100%	1.0	0.8	0.8	34.6	26	11.3	0.19
Acquired working capital (NPV of 4 year release)	Morocco	100%	100%					15	6.2	0.10
Core NAV				15.5	8.0	5.4	9.9	93	39.9	0.67
Development upside										
South Disouq SD-1X well	Egypt	55%	75%	38	21	20.6	2.5	39	16.9	0.28
Meseda Base + Workovers + Waterflood - Edison	Egypt	50%	40%	9.1	4.6	1.7	4.0	7	3.2	0.05
Gemsa - Edison modelling on full field	Egypt	50%	75%	1.2	0.6	0.6	5.7	3	1.1	0.02
Sebou - accelerated programme	Morocco	75%	40%	0.9	0.7	0.7	7.9	2	0.9	0.02
Exploration (known)										
South Disouq additional appraisal (gas only)	Egypt	55%	40%	59	32	0.0	2.5	33	14.1	0.24
Full NAV				122.9	66.7	29.0	2.7	177	76.0	1.27

Source: Edison Investment Research

Financials

SDX is well capitalised, with \$18.3m cash in February and increased cash flows from the additional assets in Egypt and Morocco from the acquisition of the Circle Oil assets. Development of the gas horizons at South Disouq will likely take tens of millions of dollars, which we currently model as being spent in 2017 and 2018 but results in a steep production ramp-up.

We caution our modelled scenario is based on an assumed 585bcf (gross) development at South Disouq, a proportion of which will not be confirmed with the SD-1X well. However, success in the gas horizons (pending successful flow testing) is a material event for SDX and could lead to a step change in cash flows.

Exhibit 2: Financial summary – including South Disouq (unrisked)

Accounts: IFRS, Yr end: December, USD: Thousands	2014A	2015A	2016A	2017E	2018E
Total revenues	24,533	11,372	12,914	45,513	80,874
Cost of sales	(3,639)	(4,973)	(5,282)	(13,746)	(21,354)
Gross profit	20,894	6,399	7,632	31,766	59,520
SG&A (expenses)	(1,768)	(3,746)	(2,457)	(2,809)	(1,665)
R&D costs	0	0	0	0	0
Other income/(expense)	0	(3)	479	0	0
Exceptionals and adjustments	(3,831)	(7,676)	(29,089)	(1,000)	(1,000)
Depreciation and amortisation	(1,602)	(2,057)	(3,266)	(18,068)	(20,929)
Reported EBIT	13,693	(7,083)	(26,701)	9,890	35,925
Finance income/(expense)	(1,009)	(96)	4	0	0
Other income/(expense)	0	18,289	0	0	0
Exceptionals and adjustments	0	0	0	0	0
Reported PBT	12,684	11,110	(26,697)	9,890	35,925
Income tax expense (includes exceptionals)	(4,328)	(1,063)	(1,503)	(823)	(2,085)
Reported net income	8,356	10,047	(28,200)	9,066	33,840
Basic average number of shares, m	376	52	72	178	187
Basic EPS	0.1	0.2	(0.4)	0.1	0.2
Balance sheet					
Property, plant and equipment	9,392	18,401	12,605	31,339	50,590
Goodwill	0	0	0	0	0
Intangible assets	16,460	23,473	10,623	8,712	13,177
Other non-current assets	1,999	2,106	2,503	3,077	3,077
Total non-current assets	27,851	43,980	25,731	43,128	66,844
Cash and equivalents	17,935	8,170	4,725	20,895	35,137
Inventories	0	1,188	1,698	1,698	2,638
Trade and other receivables	3,306	6,678	9,463	38,463	30,770
Other current assets	0	0	0	0	0
Total current assets	21,241	16,036	15,886	61,056	68,546
Non-current loans and borrowings	0	0	0	0	0
Other non-current liabilities	608	286	290	290	290
Total non-current liabilities	608	286	290	290	290
Trade and other payables	1,686	3,556	3,674	18,174	14,539
Current loans and borrowings	2,207	0	0	0	0
Other current liabilities	5,142	928	389	389	389
Total current liabilities	9,035	4,484	4,063	18,563	14,928
Equity attributable to company	39,449	55,246	37,264	85,330	120,171
Non-controlling interest	0	0	0	0	0
Cash flow statement					
Profit before tax	12,684	11,110	(26,697)	9,890	35,925
Depreciation and amortisation	1,602	2,057	3,266	18,068	20,929
Share based payments	1,064	761	(47)	1,000	1,000
Other adjustments	1,670	(12,281)	25,742	(1,766)	(2,535)
Movements in working capital	12,941	(2,183)	(3,440)	3,500	3,118
Interest paid / received	0	0	0	0	0
Income taxes paid	(4,430)	(4,678)	(766)	(823)	(2,085)
Cash from operations (CFO)	25,531	(5,214)	(1,942)	29,868	56,353
Capex	(13,634)	(5,120)	(11,890)	(22,891)	(44,645)
Acquisitions & disposals net	0	0	0	(30,000)	0
Other investing activities	1,110	4,836	825	1,192	2,535
Cash used in investing activities (CFIA)	(12,524)	(284)	(11,065)	(51,699)	(42,111)
Net proceeds from issue of shares	0	0	10,127	38,000	0
Movements in debt	0	(3,702)	(96)	0	0
Other financing activities	0	0	0	0	0
Cash from financing activities (CFF)	0	(3,702)	10,031	38,000	0
Currency translation differences and other	0	0	0	0	0
Increase/(decrease) in cash and equivalents	13,007	(9,200)	(2,976)	16,170	14,243
Currency translation differences and other	(615)	(565)	(469)	0	0
Cash and equivalents at end of period	17,935	8,170	4,725	20,895	35,137
Net (debt)/cash	15,728	8,170	4,725	20,895	35,137

Source: Edison Investment Research, company accounts. Note: Forecasts currently reflect development of 585bcf of gas at South Disouq – forecasts will be updated post testing once volumes that can be developed from the SD-1X well have been confirmed.

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