

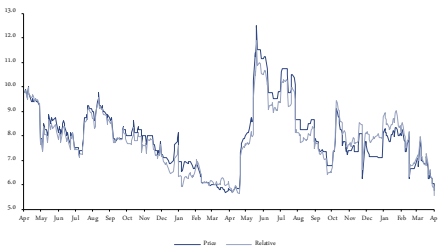
Egdon Resources (AIM: EDR LN)

BUY

Share Price (as at close: 05/04/2019)	5.8p
Target Price	20.0p
Upside to TP	248.6%
Market Cap (£'m)	14.9
Net Cash (£'m)	2.8
Enterprise Value (£'m)	12.2
Shares in Issue (m)	260.0
Free Float (%)	20.5%
Average Daily Volume (000, -3m)	260.0

12 month high/low	12.5p/5.7p		
(%)	1m	3m	12m
Absolute	-18.4	-19.4	-2.5
FTA relative	-20.8	-27.5	-8.2

Price & price relative (-2 year)



Source: Datastream

Next News

Springs Road-1 well

Business

Egdon is a UK-focused, oil & gas exploration and production company.

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Interim results and Resolution CPR

Egdon reported interim results to 31 January, with revenue up 88% to £1.2m and a narrower net loss of £0.7m. This was largely due to the restart of Ceres and a subsequent 67% increase in total output, which climbed to 164boepd. The refusal of the revised Wressle development plan was appealed, with a public inquiry expected later this year, but most of the excitement came post-close. The Biscathorpe-2 well disappointed (but could be revisited), while the Springs Road-1 well looked to be a play opener for UK shale. A new CPR on the Resolution field was also published, with 2C resources of 231bcf. We maintain our BUY recommendation and 20p target price.

Numbers improved thanks to Ceres

Egdon reported revenue of £1.2m (H1/18: £0.6m) on increased production of 164boepd (H1/18: 98boepd), a net loss of £0.7m (H1/18: -£0.8m), operating cashflow of -£0.3m (H1/18: -£0.6m) and capex of £0.7m (H1/18: £0.8m). Cash at period end was £1.8m (H1/18: £4.1m) with zero debt. The increase in production was largely thanks to the resumption of the Ceres field in October (following installation of a new flow meter). Total output averaged 240boepd during the first (calendar) quarter, and EDR is guiding 160-180boepd for FY19 (CFE: 171boepd).

Operations dominated by shale excitement

The Springs Road-1 well (EDR carried 14.5%) hit TD in late March after encountering all three targets (Bowland Shale, Millstone Grit and Arundian Shale), including a hydrocarbon-bearing sequence of over 250m in the Bowland and gas shows across the other horizons. Better than expected penetration rates also led to improved drilling performance and lower costs. Cores and logs are now being analysed, with results expected in Q2 providing further insight into potential resource volumes across EDR's 82,000 net acres. While it remains too early to speculate on figures, the excellent results bode well for the development of both Egdon's acres and the wider Gainsborough Trough.

Wider portfolio progressing, with Resolution a potential company-maker

A new CPR on the Resolution field (EDR 100%) attributes 2C resources of 231bcf, which includes only the Zechstein horizons encountered in the 1966 discovery well, ignoring the multi-tcf potential in underlying Carboniferous sandstones. Egdon expects an extension to be granted on the license, allowing the acquisition of 3D seismic across both Resolution and the neighbouring Endeavour discovery (EDR 100%) in September/October this year, with a partner being sought. The Biscathorpe-2 well (EDR 38.5%) proved disappointing, with the target sands poorly developed, although the play remains untested with a future sidetrack being considered. At Wressle, the revised development plan was refused in November, although consent for the site has been extended until January 2020, allowing an inquiry following the partners' subsequent appeal (timing to be confirmed).

Valuation unchanged, forecasts slightly tweaked

Our valuation remains unchanged, and we continue to construct our 20p target price using a combination of our Core NAV (producing assets, net cash and other corporate items), shale acreage transactional multiple (risked at a conservative 30%) and the near-term work programme. We tweak our forecasts, largely to capture the impact of deferred first production from Wressle. We maintain our BUY recommendation.

Valuation and recommendation

Our valuation remains unchanged following the interim results. We continue to construct our target price using a combination of our Core NAV (producing assets, net cash and other corporate items), shale valuation and the near-term work programme, as shown below. We maintain our BUY recommendation.

SotP target price

Target Price	£m	p
Core NAV	3.2	1.0
Wressle	2.4	0.7
North Kelsey	10.0	3.0
Shale acreage @ 30%	40.1	15.4
Total	55.7	20.0

Source: CFE Research estimates

While we might typically set this at parity to our Tangible NAV or full RENAV, in our view this is more representative of what investors might take into account over the coming year. This implies upside of c250%, despite our conservative risking of Egdon's shale acreage, and omission of significant additional assets including the Resolution field, which we view as indicative of the value inherent in the company's portfolio.

We continue to believe that Egdon provides significant exposure to the long-awaited UK shale gas revolution, with a valuation underpinned by existing production and near-term development, and near-term conventional exploration catalysts (including the North Kelsey prospect) which are exciting in their own right.

Valuation methodology

We value Egdon using a combination of a discounted cash flow (DCF) analysis of the company's producing assets and corporate items (including cash, the discounted effect of tax losses, G&A costs etc), which makes up our CNAV. The company's remaining development and appraisal assets are included within our TNAV on a risked basis and are valued via a combination of a DCF approach (for near and mid-term development) and indicative per barrel metrics. Our wider Risked Net Asset Valuation (RENAV) incorporates the upside associated with risked prospective resources (usually within a defined exploration programme).

We incorporate the following assumptions into our model:

Valuation assumptions

Metric	Assumption
Discount rate	10.00%
Long-term F/X rate (\$/£)	1.30
Shares in issue (m)	259.98
Brent pricing	2019: \$60/bbl, 2020+: \$62/bbl
NBP gas pricing	\$6/mcf
Inflation	2.00%

Source: CFE Research estimates

Our full RENAV table is shown below:

RENAV table

Country	Field	WI	CoS	Total		Risky NAV			Unrisky NAV	
		(%)	(%)	(mboe)	(\$m)	(\$/boe)	(p)	(\$m)	(\$/boe)	(p)
UK	Keddington	45.0%	100%	0.1	0.4	6.7	0.1	0.4	6.7	0.1
UK	Ceres	10.0%	100%	0.2	1.9	9.0	0.6	1.9	9.0	0.6
UK	Fiskerton Airfield	80.0%	100%	0.1	0.5	9.6	0.1	0.5	9.6	0.1
Developed Reserves				0.3	2.8	8.6	0.8	2.8	8.6	0.8
Net (debt)/cash			100%	3.6		1.1		3.6		1.1
Acquisition costs			100%	(0.5)		(0.2)		(0.5)		(0.2)
Post-tax E&A spend			100%	(3.3)		(1.0)		(3.3)		(1.0)
Tax losses (discounted)			100%	4.0		1.2		4.0		1.2
G&A (3 years)			100%	(3.4)		(1.0)		(3.4)		(1.0)
Corporate				0.4		0.1		0.4		0.1
Core NAV (CNAV)				0.3	3.2	9.8	1.0	3.2	9.8	1.0
UK	Wressle	30.0%	70%	0.2	2.4	13.4	0.7	3.5	19.2	1.0
UK	Wressle - Penistone Flags	30.0%	50%	0.4	6.5	14.7	1.9	13.0	29.5	3.8
UK	Resolution*	15.0%	35%	8.6	21.1	2.5	6.3	60.4	7.0	17.9
Undeveloped Resources				9.2	30.1	3.3	8.9	76.9	8.3	22.7
Tangible NAV (TNAV)				9.6	33.3	3.5	9.9	80.1	8.4	23.7
UK	Holmwood	18.4%	45%	1.1	4.1	3.6	1.2	9.1	8.0	2.7
UK	Holmwood KL	18.4%	35%	1.1	3.0	2.8	0.9	8.6	8.0	2.6
UK	North Kelsey	80.0%	24%	5.2	10.0	1.9	3.0	41.6	8.0	12.3
Defined Exploration				7.4	17.1	2.3	5.1	59.3	8.0	17.6
Risky Exploration NAV (RENAV)				17.0	50.4	3.0	14.9	139.4	8.2	41.3

Source: CFE Research estimates

* Assumes farm down from 100% WI

Risks

Risks include volatility in commodity prices, and those associated with oil & gas operations. Operational risks lie in reservoir uncertainty, plant and machinery issues, development delays and planning. Rising operational cost pressure may impact longer term profitability along with generic company risks including the unexpected departure of key management and senior personnel.

Financial forecasts

We have updated our financial forecasts to reflect the interims and pushed back the startup of the Wressle field given the uncertainty of the timing of the appeals process. The impact on this is to reduce near-term revenue and cashflow, and as a result we now forecast a c£1.0m shortfall by YE20 (previously c£0.1m). We would therefore expect the company to seek additional funding in order to continue to develop its portfolio prior to this point.

Income Statement

Year end Jul (£m)	2017A	2018A	2019E	2020E	2021E
Revenue	1.0	1.0	1.9	2.5	3.5
Cost of sales	(1.4)	(1.4)	(2.2)	(2.3)	(2.7)
Gross profit	(0.3)	(0.4)	(0.3)	0.2	0.9
Exploration write-off	(0.0)	(1.0)	(0.5)	-	-
Impairments	(0.2)	0.6	-	-	-
Other	0.1	(0.1)	-	-	-
G&A	(1.2)	(1.1)	(1.1)	(1.2)	(1.2)
Operating profit	(1.7)	(1.9)	(1.9)	(1.0)	(0.4)
Other	-	-	-	-	-
Exceptionals	-	-	-	-	-
Net interest	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)
Profit before tax	(1.7)	(2.0)	(1.9)	(1.0)	(0.4)
Tax	-	-	-	-	-
FX	-	-	-	-	-
Minority interests	-	-	-	-	-
Net income	(1.7)	(2.0)	(1.9)	(1.0)	(0.4)
EPS (f.dil, p)	(0.7)	(0.8)	(0.7)	(0.4)	(0.2)

Source: Company data, CFE Research estimates

Cashflow Statement

Year end Jul (£m)	2017A	2018A	2019E	2020E	2021E
Profit before tax	(1.7)	(2.0)	(1.9)	(1.0)	(0.4)
Impairments	-	-	-	-	-
DD&A	0.5	(0.3)	1.0	1.1	1.3
Exploration write-off	0.2	1.0	0.5	-	-
Other non-cash	0.1	0.2	-	-	-
Working capital	0.6	(0.6)	-	-	-
Tax	-	-	-	-	-
Cashflow from operations	(0.4)	(1.6)	(0.5)	0.0	0.9
Capex	(1.1)	(1.8)	(1.6)	(1.4)	(0.1)
Acquisitions/divestments	-	0.1	-	(0.4)	-
Other	0.0	0.0	-	-	-
Cashflow from investments	(1.0)	(1.7)	(1.6)	(1.8)	(0.1)
Issue/(repurchase) of equity	5.1	-	-	-	-
Issue/(reduction) of debt	(0.2)	-	-	-	-
Dividends paid	-	-	-	-	-
Other	-	-	-	-	-
Cashflow from financing	4.9	-	-	-	-
FX	(0.0)	0.0	-	-	-
Increase/(decrease) in cash	3.4	(3.3)	(2.1)	(1.7)	0.8

Source: Company data, CFE Research estimates

Balance Sheet

Year end Jul (£m)	2017A	2018A	2019E	2020E	2021E
Intangibles	19.2	19.6	20.2	21.1	21.1
PP&E	9.3	10.5	10.0	9.9	8.7
Other	-	-	-	-	-
Non-current assets	28.5	30.1	30.2	30.9	29.8
Inventories	-	0.0	0.0	0.0	0.0
Receivables	1.6	1.2	1.2	1.2	1.2
Tax receivable	-	-	-	-	-
Cash and equivalents	6.1	2.8	0.7	(1.0)	(0.3)
Other	-	-	-	-	-
Total assets	36.1	34.1	32.2	31.2	30.8
ST debt	-	-	-	-	-
Payables	1.2	1.2	1.2	1.2	1.2
Tax payable	-	-	-	-	-
Other	-	-	(3.0)	(2.0)	(1.0)
Current liabilities	1.2	1.2	(1.8)	(0.8)	0.2
LT debt	-	-	-	-	-
Deferred tax	-	-	-	-	-
Provisions	2.2	2.2	2.4	2.5	2.6
Other	-	-	-	-	-
Total liabilities	3.4	3.4	0.5	1.6	2.8
Net assets	32.7	30.7	31.7	29.5	28.0
Net debt/(cash)	(6.1)	(2.8)	(0.7)	1.0	0.3

Source: Company data, CFE Research estimates

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Key

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