

SDX Energy

Forecast update

NAV and forecast update - South Disouq delays

In this note, we update our short-term forecasts and NAV to reflect delays at South Disouq, with first gas postponed from mid-2019 to the end of 2019. Management is confident that first gas will be delivered in Q419, with the pipeline infrastructure largely installed. SDX retains the option to deliver first gas ahead of Q419 through a leased early production facility (EPF), but only a short window exists for this to be commercially viable ahead of the completion of the permanent central gas processing facility (CPF). Conservatively, we assume first gas at the end of 2019, a six-month delay to our previous forecasts. The impact of the South Disouq delay on NAV is small at -3%, as production is deferred, although there is a material impact on FY19 cash flow expectations (CFO -20%). However, the combined impact of the South Disouq delay and lower forecast Moroccan and NW Gemsa volumes reduce our RENAV by c 13% to 86.5p/share. We expect SDX Energy to end the year with \$11m in cash and no debt (\$10m undrawn). Delays are unlikely to have a knock-on effect on the company's committed eight- to nine-well H219 exploration programme.

Year-end	Revenue (\$m)	PBT* (\$m)	Operating cash flow (\$m)	Net cash (\$m)	Capex (\$m)	Production (kboed)
12/17	39.2	32.8	21.6	25.8	(24.9)**	3.2
12/18	53.7	7.1	36.2	17.3	(44.8)	3.6
12/19e	57.8	24.6	27.9	11.2	(36.0)	4.3
12/20e	79.3	36.3	53.9	36.4	(30.2)	9.7

Note: *PBT is normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments. **Excludes Circle acquisition (\$28.1m).

South Disouq pushed back

South Disouq is a key project for SDX and has the potential to be expanded from the current 50–60mmscfd of gas production to over 100mmscfd as incremental reserves are added. A six-month delay poses questions around the execution strategy and development concept, but ensuring alignment between the state, partners, local and international contractors can be a challenge, even for projects with local technical complexity.

SDX FY18 results in review

Production in FY18 at 3.6kboed was c 10% below our last published forecasts, driven by lower production at NW Gemsa where three wells remain shut in awaiting workover. Production continued to expand in Morocco reaching, more than 6mmscfd gross in March 2019 with the company guiding to a 9–11mmscfd exit rate for FY19. We now forecast average gross sales of 7.4mmscfd, down from 9.5mmscfd based on a slower than previously expected ramp-up in gas sales to new customers.

Valuation: NAV down 13% to 86.5p/share

Our NAV falls by 13%, driven by delays at South Disouq. However, the shares appear to be heavily discounting future growth potential in Egypt and Morocco. We believe successful delivery of South Disouq first gas by end 2019 and growth in Sebou gas sales to a 9–11mmscfd exit rate is required to drive a re-rating.

Oil & gas

16 April 2019

Price **32.0p**

Market cap **£66m**

US\$/£0.77

Net cash (\$m) at end December 2018 17.3

Shares in issue 204.7m

Free float 91%

Code SDX

Primary exchange AIM

Secondary exchange TSX Venture

Share price performance



% 1m 3m 12m

Abs (18.0) (22.9) (39.1)

Rel (local) (20.1) (28.4) (40.1)

52-week high/low 73.0p 32.0p

Business description

SDX Energy is a North African E&P listed in London. SDX produces oil and gas in Egypt and gas in Morocco.

Next event

AGM 17 May 2019

Analysts

Sanjeev Bahl +44 (0)20 3077 5700

Carlos Gomes +44 (0)20 3077 5700

Elaine Reynolds +44 (0)20 3077 5713

oilandgas@edisongroup.com

[Edison profile page](#)

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FY19 forecasts reflect South Disouq delay

During 2018, SDX achieved operational and commercial success by growing Sebou gas sales, maintaining Egypt production levels, but South Disouq project execution fell behind management guidance. In Morocco, the company completed its drilling campaign with seven discoveries from nine drilled wells. SDX also acquired and processed 240km² of 3D seismic leading to further drilling targets for its 12-well drilling campaign, expected to begin in Q319. Please see our [update note](#) published on 8 January for further details on upcoming drilling catalysts.

SDX's FY18 net production increased 10% from FY17 to 3.6kboed, driving an 18% increase in EBITDA to \$25.0m while maintaining a healthy net cash position of \$17.3m as of 31 December 2018. Exhibit 1 below provides our updated forecasts for FY19 and FY20, and introduces forecasts for FY21, which reflect SDX's FY18 reported results, South Disouq delays and a small change to our underlying oil price assumptions (gas unchanged). FY18 production was approximately 10% lower than Edison forecasts, due to North West Gemsa well shut-ins and slower ramp-up in Sebou gas sales. For 2019, the delaying to first gas at South Disouq in addition to lower production forecasts for North West Gemsa and Sebou negatively impacts our FY19 production forecast by -49% due to the high-volume nature of the project. This consequently decreases our revenue and EBITDA forecast to \$57.8m and \$35.8m respectively.

Exhibit 1: Edison updated forecasts										
	Actuals	New			Old			Change		
	2018	2019e	2020e	2021e	2018e	2019e	2020e	2018e	2019e	2020e
Production (kboed)	3.6	4.3	9.7	9.4	4.0	8.3	10.0	(10%)	(49%)	(2%)
Revenue (\$m)	53.7	57.8	79.3	78.9	53.1	73.3	86.7	1%	(21%)	(9%)
EBITDA (\$m)	25.0	35.8	53.9	53.8	25.2	50.2	64.6	(1%)	(29%)	(17%)
FCF (\$m)	(8.0)	(6.1)	25.2	52.8	(9.9)	7.1	46.9	(19%)	(187%)	(46%)
Brent (\$/bbl)	71.19	65.15	62.00	65.92	71.40	61.00	64.58	N/A	7%	(4%)
SD gas price (\$/mcf)	2.85	2.85	2.85	2.85	2.85	2.85	2.85	N/A	N/A	N/A
Sebou gas price (\$/mcf)	10.50	10.47	10.55	10.44	10.50	10.47	10.55	N/A	N/A	N/A

Source: SDX Energy, Edison investment Research

South Disouq first gas

Achieving first gas at South Disouq is a key milestone for SDX to drive production volume and cash flow growth. Gross plateau production at 50–60mmscfd gross (55% SDX working interest) is expected to add c 5.5kboed to group production (group production was 3.6kboed for FY18), at a price of \$2.85/mcf. Gas will be sold to the Egyptian Natural Gas Holding Company (EGAS). However, early in April 2019, SDX announced a delay in the start-up for gas production at South Disouq awaiting completion of the main central gas processing facility (CPF), expected to be completed in Q419. Consequently, we update our valuation by delaying South Disouq gas production and revenue by six months to start at end 2019.

Valuation

We value SDX using a conventional NAV approach based on the NPV_{12.5} of the company's producing assets minus overheads and net financial liabilities. A full breakdown of our NAV is provided in Exhibit 2, using data available in the company's last published results, as well as public sources. Key changes from our previous valuation include:

1. a delay in South Disouq first gas to end 2019;
2. an increase in short-term oil price assumptions, which move to \$65.15/bbl and \$62.00/bbl for 2019 and 2020. Our long-term oil price assumption remains at US\$70.0/bbl Brent (2022);

3. lower production at NW Gemsa, due to well shut-ins and awaiting completion of workovers;
4. reduced production in Morocco from an average 9.5mmscfd gross to 7.4mmscfd gross based on a delay in signing up new offtake relative to previous forecasts; and
5. a minor change in go-forward FX from US\$/£0.78 to US\$/£0.77.

We note that SDX is relatively insensitive to oil price assumptions, with the bulk of the valuation consisting of gas sales at five-year fixed contracted prices in Morocco that average \$10.5/mcf. Our FX assumption has also changed slightly to US\$/£0.77, based on the average of the last six months ending in 31 March 2019. As a result, we have decreased our RENAV to 86.5p/share from 99.6p/share (-13%), with our core value decreasing from 83.6p/share to 70.1p/share (-16%).

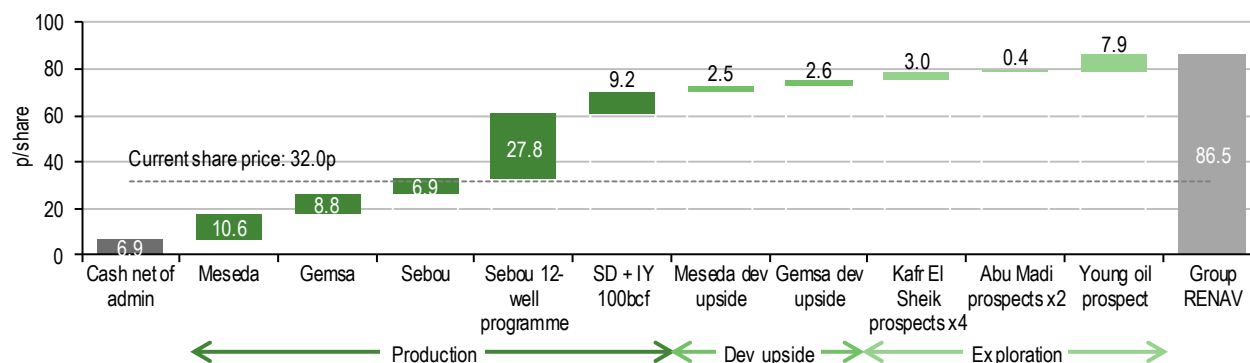
Exhibit 2: SDX Energy detailed valuation

Asset	Country	Diluted WI	CoS	Recoverable reserves			Net risked value @12.5%			
				Gross	Net WI	Net	NPV	Absolute	GBp/share	C\$/share
		%	%	mmboe	mmboe	mmboe	\$/boe	\$m		
Net cash at December 2018								17.3	6.6	0.1
SG&A - NPV _{12.5} of 3yrs								(18.1)	(6.9)	(0.1)
E&A expense for exploration prospects								(14.2)	(5.4)	(0.1)
NPV of net receivable recovery								16.8	6.3	0.1
Sebou Pipeline residual value (50% cost)								16.4	6.2	0.1
Production										
Meseda Base + Workovers + Rabul	Egypt	50%	90%	8.4	4.2	1.6	7.4	28.0	10.6	0.1
Gemsa 2P	Egypt	50%	100%	4.2	2.1	2.1	11.2	23.4	8.9	0.1
Sebou 2P volume + discoveries to be booked	Morocco	75%	100%	0.7	0.5	0.5	34.9	18.2	6.9	0.1
Sebou 12-well programme	Morocco	75%	75%	4.3	3.2	3.2	30.4	73.6	27.8	0.4
South Disouq/Ibn Yunus	Egypt	55%	100%	17.6	9.7	9.7	2.5	24.3	9.2	0.1
Core NAV				35.2	19.7	17.1	8.5	185.6	70.1	0.9
Development upside										
Meseda Waterflood Upside	Egypt	50%	50%	5.3	2.6	1.0	5.1	6.7	2.5	0.0
Gemsa - Edison modelling on full field	Egypt	50%	70%	1.8	0.9	0.9	9.9	6.8	2.6	0.0
Exploration (known)										
Kafir el Sheik prospect x4	Egypt	55%	27%	33.6	18.5	18.5	1.6	8.0	3.0	0.0
Abu Madi prospect x2	Egypt	55%	23%	5.7	3.1	3.1	1.6	1.1	0.4	0.0
Young oil prospect	Egypt	55%	19%	50.0	27.5	27.5	4.0	20.8	7.9	0.1
Group RENAV				131.6	72.4	68.2		229.0	86.5	1.1

Source: Edison Investment Research. Note: Number of shares = 204.7m, FX = US\$/£0.77.

Exhibit 3 breaks down our valuation by asset, showing where our base case core NAV sits relative to the current share price. SDX currently trades at a material discount to our core valuation, despite the South Disouq delay.

Exhibit 3: SDX Energy valuation waterfall

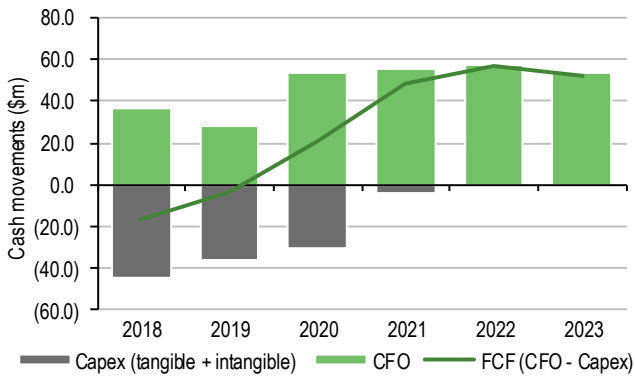


Source: Edison Investment Research

Financials

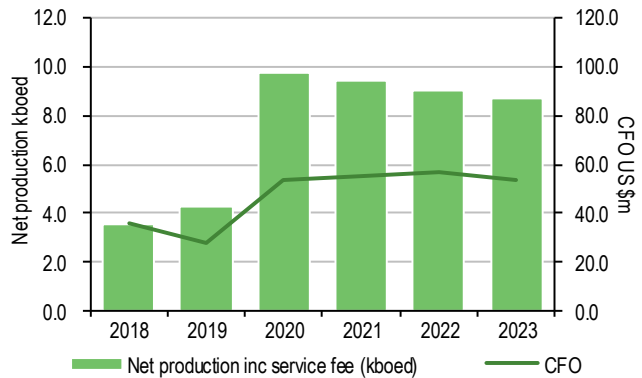
SDX retains a robust balance sheet, with cash and equivalents of \$17.3m at end FY18 and no drawn debt. The company has access to up to \$10m of its RBL borrowing base, which can be drawn down if required. Forecast cash or net debt will be driven by a combination of production start-up at South Disouq, production growth in Morocco and oil prices, as well as phasing of the company's planned drilling programme. On our base case, we expect SDX to end FY19 with \$11.2m of cash, but with a significant range of uncertainty without firm dates for the start-up of South Disouq, timing of Morocco gas sales FY19 exploration wells/costs.

Exhibit 4: Cash flow forecasts and committed capex



Source: Edison Investment Research

Exhibit 5: Group production expectations*



Source: Edison Investment Research. Note: *Assumes South Disouq first gas at end 2019.

Exhibit 6: Financial summary

IFRS, Year-end: December, US\$000s	2017	2018	2019e	2020e	2021e
INCOME STATEMENT					
Total revenues	39,166	53,679	57,786	79,327	78,950
Cost of sales (direct expense)	(10,254)	(11,934)	(15,059)	(17,780)	(16,700)
Gross profit	28,912	41,745	42,727	61,547	62,250
SG&A (expenses)	(8,793)	(7,270)	(7,634)	(8,015)	(8,416)
Other income/(expense)	1,820	1,025	1,914	1,526	1,194
Exceptionals and adjustments	(725)	(10,458)	(1,194)	(1,194)	(1,194)
Depreciation and amortisation	(17,824)	(17,268)	(11,007)	(17,436)	(15,787)
Reported EBIT	3,390	7,774	24,806	36,428	38,047
Finance income/(expense)	(129)	(542)	0	0	0
Other income/(expense)	29,558	(174)	(174)	(174)	(174)
Exceptionals and adjustments	0	0	0	0	0
Reported PBT	32,819	7,058	24,632	36,254	37,873
Income tax expense (includes exceptionals)	(4,541)	(7,021)	(2,564)	(2,186)	(1,865)
Reported net income	28,278	37	22,068	34,068	36,007
Shares at end of period - basic	204	205	205	205	205
BALANCE SHEET					
Property, plant and equipment	54,445	48,680	68,176	76,379	63,719
Goodwill	0	0	0	0	0
Intangible assets	15,231	39,128	44,591	49,184	49,744
Other non-current assets	2,724	3,394	3,394	3,394	3,394
Total non-current assets	72,400	91,202	116,161	128,956	116,857
Cash and equivalents	25,844	17,345	11,199	36,367	89,127
Inventories	5,157	5,236	6,607	7,801	7,327
Trade and other receivables	37,656	24,324	25,959	20,767	16,614
Other current assets	0	0	0	0	0
Total current assets	68,657	46,905	43,766	64,935	113,068
Non-current loans and borrowings	0	0	0	0	0
Other non-current liabilities	4,506	4,572	4,572	4,572	4,572
Total non-current liabilities	4,506	4,572	4,572	4,572	4,572
Trade and other payables	19,459	14,418	12,976	11,679	10,511
Current loans and borrowings	0	0	0	0	0
Other current liabilities	2,473	3,078	3,078	3,078	3,078
Total current liabilities	21,932	17,496	16,054	14,757	13,589
Equity attributable to company	114,619	116,039	139,301	174,563	211,764
Non-controlling interest	0	0	0	0	0
CASH FLOW STATEMENT					
Profit before tax	32,819	7,058	24,632	36,254	37,873
Net finance expenses	0	0	0	0	0
Depreciation and amortisation	17,824	17,268	11,007	17,436	15,787
Share based payments	538	1,194	1,194	1,194	1,194
Other adjustments	(34,613)	3,224	(1,914)	(1,526)	(1,194)
Movements in working capital	5,412	8,584	(4,448)	2,700	3,460
Interest paid / received	0	0	0	0	0
Income taxes paid	(364)	(1,091)	(2,564)	(2,186)	(1,865)
Cash from operations (CFO)	21,616	36,237	27,907	53,872	55,254
Capex	(24,917)	(44,810)	(35,967)	(30,231)	(3,688)
Acquisitions & disposals net	(24,948)	0	0	0	0
Other investing activities	760	525	1,914	1,526	1,194
Cash used in investing activities (CFIA)	(49,105)	(44,285)	(34,053)	(28,704)	(2,494)
Net proceeds from issue of shares	48,510	114	0	0	0
Movements in debt	(43)	(197)	0	0	0
Other financing activities	0	0	0	0	0
Cash from financing activities (CFF)	48,467	(83)	0	0	0
Increase/(decrease) in cash and equivalents	20,978	(8,131)	(6,146)	25,167	52,761
Currency translation differences and other	141	(368)	0	0	0
Cash and equivalents at end of period	25,844	17,345	11,199	36,367	89,127
Net (debt) cash start of period	25,844	17,345	11,199	36,367	89,127
Movement in net (debt) cash over period	21,119	(8,499)	(6,146)	25,167	52,761

Source: Company accounts, Edison Investment Research

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Frankfurt +49 (0)69 78 8076 960
Schumannstrasse 34b
60325 Frankfurt
Germany

London +44 (0)20 3077 5700
280 High Holborn
London, WC1V 7EE
United Kingdom

New York +1 646 653 7026
1,185 Avenue of the Americas
3rd Floor, New York, NY 10036
United States of America

Sydney +61 (0)2 8249 8342
Level 4, Office 1205
95 Pitt Street, Sydney
NSW 2000, Australia