EDISON

Rockhopper Exploration

FY19 results

Parties committed to completing Sea Lion deal

Oil & gas

Rockhopper Exploration recently announced that its Greater Mediterranean assets generated $10.3m revenue in 2019 as it focused on progressing with Sea Lion Phase 1 development. In January, Rockhopper and Premier Oil announced that a Heads of Terms (HoT) had been signed with Navitas Petroleum to farm in for a 30% interest in the Sea Lion project. Despite the current macroeconomic situation, the company announced that progress has been made to convert the HoT into finalised agreements. Completion of the sale of its Egyptian assets, together with the HoT, leaves the company in a stable financial position. Our risked valuation now stands at 24.4p/share (-54%) for our mid-case based on revised long-term price assumptions, reflecting current market expectations.

Year-end	Revenue ($m)	PBT* ($m)	Cash from operations ($m)	Net cash** ($m)	Capex** ($m)
12/18	10.6	(7.1)	5.4	40.4	(15.8)
12/19	10.3	(20.6)	(0.2)	17.2	(23.9)
12/20e	2.2	(4.5)	(8.3)	10.2	(10.9)
12/21e	1.7	(4.1)	(5.2)	5.3	0.0

Note: *PBT normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments. **Assumes capex ahead of first oil funded by Premier and Navitas interest-free loan from 1 January 2020.

Balance sheet protected ahead of unheard-of times

Despite a positive share price reaction following the announcement of the Navitas farm-in deal, this has been reversed since early March due to the negative global macroeconomic outlook. Nevertheless, the company announced that it has made good progress in finalising the deal, with all parties committed to proceeding. Rockhopper has employed different initiatives since the beginning of the year to protect its balance sheet, leaving it in a stable financial position, with no debt and limited exposure to future development costs (excluding licence fees, taxes, costs incurred prior to 1 January 2020 and project wind-down costs) at Sea Lion.

Current market headwinds

2020 is proving to be a challenging year for the oil and gas industry. In January, geopolitical events around Iran resulted in market instability, followed later by the coronavirus outbreak and the Russia/Saudi Arabia oil price war. As a consequence, management initiated a cost reduction process to scale back headcount and activity at Sea Lion pending an improvement in the macro environment.

Valuation: RENAV at 24.4p/share

Our valuation suggests that the equity market is now applying a c 25% chance of success (CoS) for Sea Lion Phase 1. Our updated risked valuation accounts for FY19 results and the current market situation, with our long-term Brent assumptions also revised. Our analysis includes three scenarios with the 2020 Brent price inflated at 2.5%, at $40/bbl, $50/bbl (mid case) and $60/bbl. Our risked valuation now stands at 24.4p/share for our mid-case based on a Sea Lion Phase 1 CoS of 55%. We believe the project is more likely to proceed than not. However, recent global events will most likely affect the timing of a final investment decision.

23 April 2020

Price	**7.4p**
Market cap	**£34m**
	US$1.28/£
Net cash ($m) at 31 December 2019	17.2
Shares in issue	458.0m
Free float	99%
Code	RKH
Primary exchange	AIM
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	27.1	(64.1)	(75.3)
Rel (local)	13.6	(52.4)	(68.2)
52-week high/low		25.5p	4.0p

Business description

Rockhopper (RKH) is a London-listed E&P with fully funded development of Sea Lion, a 500mmbbl+ field in the Falklands with the potential for a similar size discovery to the south. RKH also holds production and exploration assets in the Mediterranean.

Next events

Ombrina Mare arbitration outcome	H120
SPA signing	Mid-2020
Farm-in completion	Q320

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Edison profile page

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Premier and Navitas committed to finalise farm-in

During 2019 Rockhopper achieved revenue of $10.3m from its Greater Mediterranean assets while progressing its Sea Lion project in the Falkland Islands. In January 2020, Rockhopper and Premier Oil announced that an HoT had been signed with Navitas Petroleum to farm in for a 30% interest in the Sea Lion project. The entry of an additional partner into the joint venture brings further industry validation and improves the likelihood of securing project financing for Phase 1 of the Sea Lion development. Rockhopper is now fully funded from the start of 2020 through to completion of Phase 1 of the project, which will develop 250mmbbls of gross resources. In addition, a contingent consideration of up to $48m is payable to Rockhopper by Premier Oil and Navitas for future phases of development in the North Falkland Basin. Finalisation of the sale and purchase agreement is expected during summer 2020.

External factors that might delay final investment decision

Progress on the preliminary information memorandum (PIM), submitted by the Sea Lion joint venture in August 2019 and a key milestone for final investment decision (FID) for Sea Lion, was held up as a result of the UK general election, and is now expected to move forward. Progress is contingent on Premier completing its corporate actions (North Sea M&A/equity raise) and a recovery in the oil prices.

In January 2020, Premier also announced a series of significant North Sea M&A deals, which would materially strengthen its balance sheet and further support Sea Lion project financing discussions. Had oil prices stayed at 2019 levels, the additional cash flow would have accelerated the company's debt reduction, increasing the likelihood that project finance could be secured for Sea Lion Phase 1. However, the coronavirus outbreak and the Russia/Saudi Arabia oil price war led to an unprecedented decrease in oil prices and a decrease of c 70% in Premier's market cap.

Notwithstanding the current external headwinds Rockhopper is facing, it announced that good progress was made during Q120 to convert the HoT into fully documented agreements, and that despite the current oil price environment, all parties remain committed to finalising the Navitas farm-in agreement, with completion subject to agreed consents and approvals. Sale of the Egyptian assets, together with the HoT signed with Premier and Navitas, leave the company in a relatively stable financial position with unaudited cash resources of $21.9m as at 1 April 2020, no debt and limited exposure to future development costs (excluding licence fees, taxes, costs incurred prior to 1 January 2020 and project wind-down costs) at Sea Lion.

Ombrina Mare arbitration

In March 2017, Rockhopper started international arbitration proceedings against the Republic of Italy in relation to the Ombrina Mare field it acquired from Mediterranean Oil & Gas. Rockhopper believes it has strong prospects of recovering 'significant monetary damages' based on lost profits as a result of the Republic of Italy's breaches of the Energy Charter Treaty. We estimate that these will be recoverable at c $20m on a risked basis in our valuation using a simplified approach, which assumes a 50% chance of recovering the associated acquisition costs. We have not carried out a loss of profits calculation, but press reports suggest it could be materially higher, with the claim running up to €275m plus interest. Clearly, there is material upside to our valuation in the event of a damages award to Rockhopper. Indicatively, a $50m award to Rockhopper net of costs would be worth up to 8.5p/share to equity holders. On 26 June 2019, the tribunal rejected Italy's request for suspension of the arbitration and its intra-EU jurisdictional objections. Rockhopper expects a final outcome and potential damages award in the coming months.

Valuation

We value Rockhopper's asset base using a conventional risked net asset value (NAV) approach, based on a risked valuation for proven reserves, and contingent and prospective resources. Key assumptions in our valuation include estimates of production profiles, asset development costs and operational costs, in addition to realised commodity prices and costs of capital. We use publicly available sources for key assumptions, including company guidance.

We have updated our forecasts and NAV to reflect Rockhopper's FY19 results, together with the impact of the coronavirus and Russia/Saudi Arabia oil price war, in our pricing assumptions. Our risked valuation has decreased to 24.4p/share. The main change in our modelling includes our long-term Brent assumption. We have revised down our long-term oil price expectation of $70/bbl Brent from 2022 to reflect current oil price volatility. We present three scenarios with Brent in 2020 at $40/bbl in our low case scenario, $50/bbl in our mid-case scenario and $60/bbl in our high case scenario, inflated at 2.5% per year, resulting in 2022 prices of $42.0/bbl, $52.5/bbl and $63.0/bbl respectively. Given the current oil price volatility, we will continue to monitor market conditions closely and may revisit these assumptions in due course. The NAV table below, in Exhibit 1, provides a breakdown of our valuation by asset.

Exhibit 1: Edison breakdown of Rockhopper NAV

				Recoverable reserves				Low case ($40/bbl)	Mid case ($50/bbl)	High case ($60/bbl)
Asset	**Country**	**WI**	**CoS**	**Gross**	**Net**	**NPV/boe**	**Net risked value**	Net risked value per share		
		%	%	mmboe	mmboe	$/boe	$m	p/share	p/share	p/share
Net cash at 31 December 2019							17	2.9	2.9	2.9
SG&A ($NPV_{12.5}$ of 5 years)							(20)	(3.4)	(3.4)	(3.4)
Proceeds from Abu Sennan disposal							12	2.0	2.0	2.0
Production										
Civita	Italy	100%	100%	0.0	0.0	(36.4)	(1)	0.0	0.0	0.0
Guendalina	Italy	20%	100%	0.4	0.1	18.5	2	0.3	0.3	0.3
Development										
Sea Lion Phase 1	Falkland Islands	30%	55%	249	75	1.8	76	6.4	12.9	23.7
Sea Lion Phase 2 in PL32	Falkland Islands	30%	20%	87	26	2.1	11	0.4	1.8	3.3
Sea Lion Phase 2 in PL04	Falkland Islands	30%	20%	214	64	2.1	26	0.9	4.5	8.1
Ombrina Mare - under arbitration*	Italy						20	3.4	3.4	3.4
Core NAV				**551**	**165**		**143**	**12.9**	**24.4**	**40.2**

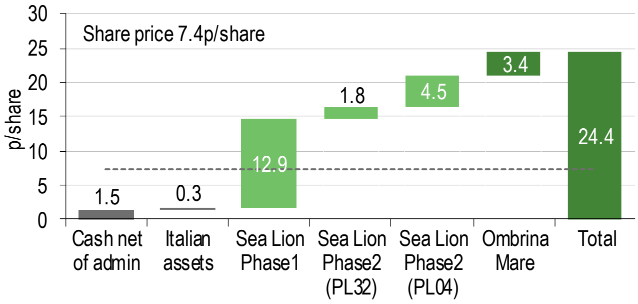
Source: Edison Investment Research. Note: Number of shares: 458m; FX = US$1.28/£. *Based on 50% chance of recovering acquisition costs rather than risked recovery of loss of profit.

Rockhopper currently trades at 7.4p/share relative to our risked valuation of 24.4p/share. Although an increase in the share price was observed following the deal announcement, it has been completely erased by the impact of the coronavirus on energy markets in combination with the Russia/ Saudi Arabia price war in early March 2020. The current share price suggests an implied chance of success of between 20% and 30% for Phase 1 at $50/bbl or c 50% at $40/bbl. We believe the project is more likely to proceed than not, now reinforced by the Navitas deal, hence our 55% commercial chance of success for Phase 1. However, recent global events will most likely affect timings, especially around closing funding and financing agreements for the Sea Lion joint venture, and consequently a final investment decision.

Exhibit 2: Core assets and Sea Lion Phase 1 sensitivity			
Phase 1 CoS/ Edison scenarios	Low case ($40/bbl)	Mid case ($50/bbl)	High case ($60/bbl)
10%	3.0	4.1	6.1
20%	4.1	6.5	10.4
30%	5.3	8.8	14.7
40%	6.5	11.1	19.0
50%	7.6	13.5	23.3
55%	8.2	**14.7**	25.5

Source: Edison Investment Research

Exhibit 3: Rockhopper NAV waterfall



Source: Edison Investment Research

If the current oil price environment persists, we also expect to see significant cost deflation which will improve the project economics and valuation of Sea Lion Phase 1 development. In the table below we provide a sensitivity to the impact of capex on Sea Lion Phase 1.

Exhibit 4: Core assets and Sea Lion Phase 1 sensitivity to lower capex

Discount to capex/ Edison scenario	Low case ($40/bbl)	Mid case ($50/bbl)	High case ($60/bbl)
0%	8.1	**14.6**	25.5
10%	8.2	14.7	27.6
20%	8.3	15.2	29.7
30%	8.4	17.1	32.1

Source: Edison Investment Research

Financials

Rockhopper ended FY19 with c $17m of cash on the balance sheet and no debt, in line with our estimates, and announced unaudited cash resources of $21.9m as at 1 April 2020. With the disposal of Abu Sennan, our forecast Italian asset capex and SG&A are covered for the coming years at $5m in 2020 and $4m in 2021. This represents a c 30% cost reduction versus 2019, in line with company guidance as a response to the coronavirus pandemic and market developments. As a consequence of the Navitas farm-in, Rockhopper is fully funded through to Sea Lion Phase 1 project completion given the newly agreed interest-free loan from Navitas and Premier (excluding licence fees, taxes, costs incurred prior to 1 January 2020 and project wind down costs at Sea Lion). We are accounting for this partnership loan in the company's balance sheet. However, we do not believe Rockhopper will need to access any additional funding for Sea Lion Phase 1 development. Project funding for the joint venture is expected to be split into vendor financing, export credit/bank finance and upstream partner equity.

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Exhibit 5: Financial summary

Accounts: IFRS, year-end: 31 December, US$000s	2017	2018	2019	2020e	2021e
PROFIT & LOSS					
Total revenues	10,401	10,580	10,328	2,167	1,666
Cost of sales	(9,573)	(8,531)	(10,385)	(1,051)	(764)
Gross profit	828	2,049	(57)	1,116	901
SG&A (expenses)	(5,282)	(5,386)	(5,942)	(5,000)	(4,000)
Other income/(expense)	(3,422)	(5,014)	(1,974)	0	0
Exceptionals and adjustments	(1,830)	673	(12,991)	(1,307)	(1,307)
Reported EBIT	(9,706)	(7,678)	(20,964)	(5,191)	(4,406)
Finance income/(expense)	783	825	624	710	323
Other income/(expense)	(39)	(253)	(291)	0	0
Exceptionals and adjustments	0	0	0	0	0
Reported PBT	(8,962)	(7,106)	(20,631)	(4,481)	(4,083)
Income tax expense (includes exceptionals)	2,823	(25)	0	0	0
Reported net income	(6,139)	(7,131)	(20,631)	(4,481)	(4,083)
Basic average number of shares, m	457	457	455	458	458
Basic EPS	(1.3)	(1.6)	(4.5)	(9.8)	(8.9)
Adjusted EBITDA	(2,403)	(4,383)	(2,235)	(3,277)	(2,644)
Adjusted EBIT	(13,349)	(12,319)	(13,711)	(4,491)	(3,554)
Adjusted PBT	(12,605)	(11,747)	(13,378)	(3,781)	(3,231)
Adjusted EPS (c)	(5)	(1)	(44)	(7)	(6)
Adjusted diluted EPS (c)	(5)	(1)	(44)	(7)	(6)
BALANCE SHEET					
Property, plant and equipment	11,585	11,836	1,814	911	456
Goodwill	0	0	0	0	0
Intangible assets	432,147	447,035	465,820	465,517	465,517
Other non-current assets	10,789	10,308	1,883	1,883	1,883
Total non-current assets	454,521	469,179	469,517	468,310	467,856
Cash and equivalents	50,729	40,426	17,223	10,224	5,346
Inventories	1,621	1,779	1,463	1,463	1,463
Trade and other receivables	16,840	9,510	3,501	3,501	3,501
Other current assets	4,354	568	18,538	18,538	18,538
Total current assets	73,544	52,283	40,725	33,726	28,848
Non-current loans and borrowings	0	0	0	0	0
Other non-current liabilities	85,245	90,971	93,759	93,759	93,759
Total non-current liabilities	85,245	90,971	93,759	93,759	93,759
Trade and other payables	12,772	15,148	17,943	12,911	10,354
Current loans and borrowings	0	0	0	0	0
Other current liabilities	9,450	0	2,426	2,426	2,426
Total current liabilities	22,222	15,148	20,369	15,337	12,780
Equity attributable to company	420,598	415,343	396,114	392,940	390,164
Non-controlling interest	0	0	0	0	0
CASH FLOW STATEMENT					
Profit for the year	(8,962)	(7,106)	(20,631)	(4,481)	(4,083)
Taxation expenses	0	0	0	0	0
Net finance expenses	(743)	(572)	(333)	(710)	(323)
Depreciation and amortisation	5,687	4,111	4,544	607	455
Share based payments	864	1,478	1,307	1,307	1,307
Other adjustments (impairments)	5,652	1,628	13,228	0	0
Movements in working capital	(868)	5,891	1,661	(5,032)	(2,557)
Interest paid / received	0	0	0	0	0
Income taxes paid	0	0	0	0	0
Cash from operations (CFO)	1,630	5,430	(224)	(8,309)	(5,201)
Capex *	(26,817)	(15,784)	(23,895)	(10,900)	0
Acquisitions & disposals net	(6,266)	(658)	0	11,500	0
Other investing activities	521	722	31,121	710	323
Cash used in investing activities (CFIA)	(32,562)	(15,720)	7,226	1,310	323
Net proceeds from issue of shares	0	0	0	0	0
Movements in debt	0	0	0	0	0
Other financing activities (includes rig settlement)	(13)	18	(247)	0	0
Cash from financing activities (CFF)	(13)	18	(247)	0	0
Increase/(decrease) in cash	(30,945)	(10,272)	6,755	(6,999)	(4,878)
Currency translation differences and other	655	(31)	42	0	0
Cash at end of period	20,729	10,426	17,223	10,224	5,346
Net (debt) cash including term deposits	50,729	40,426	17,223	10,224	5,346

Source: Rockhopper Exploration, Edison Investment Research. Note: *Assumes capex ahead of Sea Lion Phase 1 first oil funded by Premier and Navitas interest-free loan from 1 January 2020.

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