

26 October 2016

Energy & Petrochemicals | Exploration & Production

Reach Energy

Not Rated

Kazakhstan Acquisition Within Reach

Reach Energy is proposing to acquire a 60% stake in Paleontol BV, the owner and operator of the Emir Oil concession block in Kazakhstan. The block holds 70mbbls and 116.3Bscf of oil and gas 2P reserves with a concession period until 2036. We are positive on the acquisition as the producing oilfield will provide immediate cash flow with a potential lift in production in the near term. Our indicative valuation range is MYR1.07-MYR1.19.

Proposal for a Kazakhstan acquisition. Reach Energy is proposing to acquire 60% of Paleontol BV, which in turn controls 100% of Emir Oil LLP, the owner and operator of the Emir Oil concession block in Kazakhstan. The other 40% stake of Paleontol BV is held by MIE Holdings (1555 HK, NR), an independent upstream oil & gas based in Hong Kong. The total purchase consideration by Reach Energy is USD154.9m.

The asset. The Emir Oil concession block is an onshore field located in the Mangystau Oblast, in the South West region of Kazakhstan. The block has a total contract area of approximately 850.3 sq km. The asset comes with four producing fields; Aksaz (gas), Dolinnoe, Emir and Kariman (oil), with an exploration area of approximately 804.8 sq km comprising of two development fields and six future prospects. The oilfield is based on a concession fiscal regime with a period of production until 2036.

Reserves and location. Based on RPS Energy, an independent oilfield consultant, the block is estimated to hold 2P gross reserves of 70 thousand barrels (mbbls) of oil with a 2P associated gas gross reserves of 116.3bn of standard cubic feet (Bscf). 3P reserves are estimated at 116.1mbbls and 184.1Bscf of gross oil and gas reserves respectively.

Future upside. Apart from the on-going efforts to upgrade its 3P reserves to 2P reserves, the group is expected to start the operation of a new central processing facility, scheduled to be online by end-2016. There are also plans to construct a 25km oil and 35km gas pipeline to the state owned trunk lines which would reduce transportation costs.

Not rated. We are positive on the acquisition of the concession block, as the oilfield is already in production with a visible ramp up plan in sight. We understand that Reach Energy is expected to pay out c.30% of its free cash flow as dividends. Our indicative valuation range is MYR1.07-1.19, based on a DCF with a 10% WACC, typical of an oilfield WACC. Our oil price estimates are based on our house view, USD45.50/barrel (bbl) in 2016 and USD60/bbl from 2017 onwards. Key risks includes a drop in crude oil price and delays in the construction of the central processing facility.

Target Price:	NA
Price:	MYR0.72
Market Cap:	USD219m
Bloomberg Ticker:	REB MK

Share Data

Avg Daily Turnover (MYR/USD)	1.52m/0.37m
52-wk Price low/high (MYR)	0.62 - 0.72
Free Float (%)	45
Shares outstanding (m)	1,278
Estimated Return	-

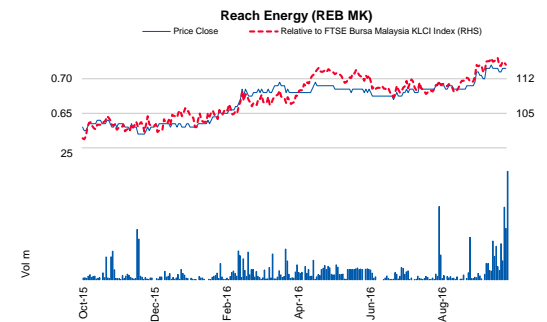
Shareholders (%)

Reach Energy	20.0
PAG	9.5
Lembaga Tabung Haji	8.0

Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	12.6	3.6	5.9	5.1	14.4
Relative	13.5	3.2	4.7	7.4	16.3

Source: Bloomberg



Source: Bloomberg

Forecasts and Valuations	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Total turnover (MYRm)	0	0	0	402	407
Reported net profit (MYRm)	(5)	69	(32)	114	114
Recurring net profit (MYRm)	(5)	69	(32)	114	114
Recurring net profit growth (%)	0.0	0.0	(146.7)	0.0	0.3
Recurring EPS (MYR)	(0.00)	0.05	(0.03)	0.09	0.09
DPS (MYR)	na	na	na	0.01	0.01
Recurring P/E (x)	na	13.3	na	8.0	8.0
P/B (x)	41.1	32.0	32.0	7.1	4.0
P/CF (x)	na	11.4	na	4.8	9.9
Dividend Yield (%)	na	na	na	1.6	1.6
EV/EBITDA (x)	na	na	na	3.85	3.84
Return on average equity (%)	0.0	271.2	(112.6)	145.7	64.6
Net debt to equity	net cash	net cash	net cash	net cash	net cash
Our vs consensus EPS (adjusted)					

Source: Company data, RHB

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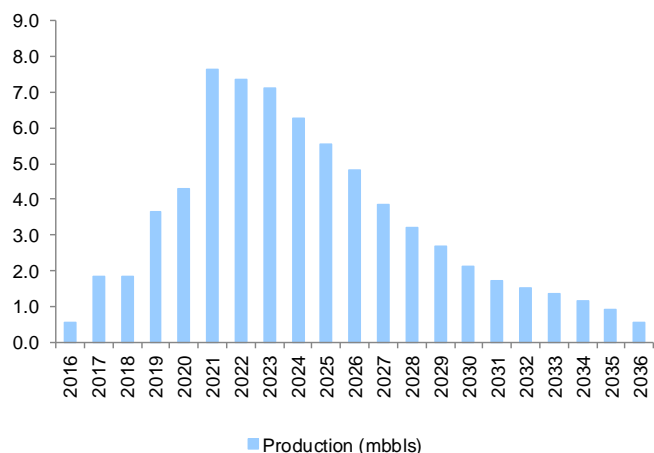
Financial Exhibits

Financial model updated on: 2016-10-25.

Asia	Financial summary	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Malaysia	Recurring EPS (MYR)	(0.00)	0.05	(0.03)	0.09	0.09
Energy & Petrochemicals	EPS (MYR)	(0.00)	0.05	(0.03)	0.09	0.09
Reach Energy	DPS (MYR)	0.00	0.00	0.00	0.01	0.01
Bloomberg REB MK	BVPS (MYR)	0.02	0.02	0.02	0.10	0.18
Not Rated	Weighted avg adjusted shares (m)	1,278	1,278	1,278	1,278	1,278
Valuation basis	Valuation metrics	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
DCF at 10% WACC	Recurring P/E (x)	na	13.3	na	8.0	8.0
Indicative range of MYR1.19-1.33	P/E (x)	na	13.3	na	8.0	8.0
Key drivers	P/B (x)	41.1	32.0	32.0	7.1	4.0
i. Higher crude oil price;	FCF Yield (%)	(0.5)	8.7	(7.3)	20.8	10.1
ii. Higher production figures.	Dividend Yield (%)	0.0	0.0	0.0	1.6	1.6
Key risks	EV/EBITDA (x)	na	na	na	3.85	3.84
i. Lower than expected production profile;	EV/EBIT (x)	na	na	na	3.85	3.84
ii. Lower than estimated crude oil price.	Income statement (MYRm)	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
Company Profile	Total turnover	0.00	0.00	0.00	401.77	407.03
Reach Energy is a special purpose acquisition company (SPAC) proposing to buy a stake into an oilfield in Kazakhstan.	Gross profit	0.00	0.00	0.00	189.89	190.55
	EBITDA	(5.16)	(13.35)	(17.58)	189.89	190.55
	Operating profit	(5.16)	(13.35)	(17.58)	189.89	190.55
	Net interest	0.33	82.21	(40.96)	0.00	0.00
	Income from associates & JVs	0.00	0.00	34.70	0.00	0.00
	Pre-tax profit	(4.83)	68.86	(23.85)	189.89	190.55
	Taxation	0.00	0.00	(8.29)	0.00	0.00
	Minority interests	0.00	0.00	0.00	(75.95)	(76.22)
	Recurring net profit	(4.83)	68.86	(32.15)	113.93	114.33
	Cash flow (MYRm)	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
	Change in working capital	0.00	0.82	0.00	0.00	(98.39)
	Cash flow from operations	(4.83)	79.87	(66.84)	189.89	92.16
	Proceeds from issue of shares		(62.57)	0.00	0.00	0.00
	Cash flow from financing activities	0.00	(62.57)	0.00	0.00	0.00
	Cash at beginning of period		23.18	778.36	778.36	182.04
	Net change in cash	(4.83)	17.30	(66.84)	189.89	92.16
	Ending balance cash	(4.83)	40.48	711.52	968.24	274.19
	Balance sheet (MYRm)	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
	Total cash and equivalents	23.2	778.4	778.4	182.0	182.0
	Tangible fixed assets	0.1	0.3	0.3	596.3	596.3
	Total assets	46.9	778.9	778.9	778.5	876.9
	Other liabilities	0.0	738.1	738.1	0.0	0.0
	Total liabilities	24.7	750.3	750.3	650.7	650.7
	Shareholders' equity	22.2	28.5	28.5	127.8	226.2
	Total equity	22.2	28.5	28.5	127.8	226.2
	Net debt	(23.2)	(778.4)	(778.4)	(182.0)	(182.0)
	Total liabilities & equity	46.9	778.9	778.9	778.5	876.9
	Key metrics	Dec-14	Dec-15	Dec-16F	Dec-17F	Dec-18F
	Revenue growth (%)	0.0	0.0	0.0	0.0	1.3
	Recurrent EPS growth (%)	0.0	0.0	(146.7)	0.0	0.3
	Gross margin (%)	0.0	0.0	0.0	47.3	46.8
	Operating EBITDA margin (%)	0.0	0.0	0.0	47.3	46.8
	Net profit margin (%)	0.0	0.0	0.0	28.4	28.1
	Interest cover (x)		0.32471309	-0.42926424		

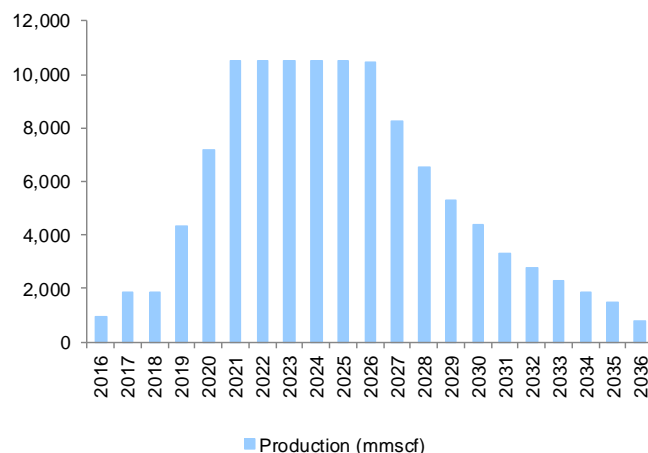
Source: Company data, RHB

Figure 1: Base case oil production profile (mmbbls)



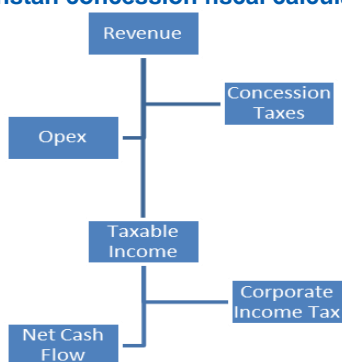
Source: Company data

Figure 2: Base case gas production profile (mmscf)



Source: Company data

Figure 3: Kazakhstan concession fiscal calculation



Source: Company

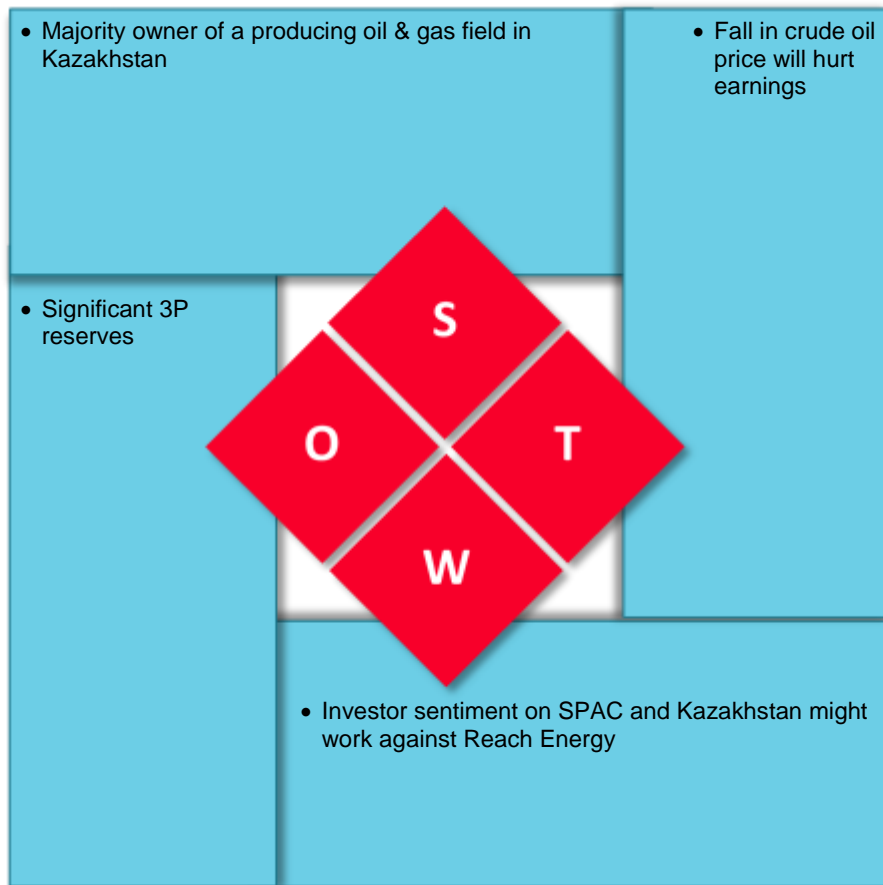
Figure 4: Concession taxes

Mineral extraction taxes	Increases with higher annual production, ring fenced to each production contract Current oil export is taxed at 5%, domestic oil & gas at 2.5% and 0.5% respectively
Export duty	Based on annual production and price of crude oil
Export rent tax	Indexed to oil price
Excess profit tax	Applicable once the ratio of annual aggregate income to annual tax deductions exceed 1.25x Deductibles include all expenses, capex and loss carry forward
Property tax	1.5% on average net book value of oil & gas properties

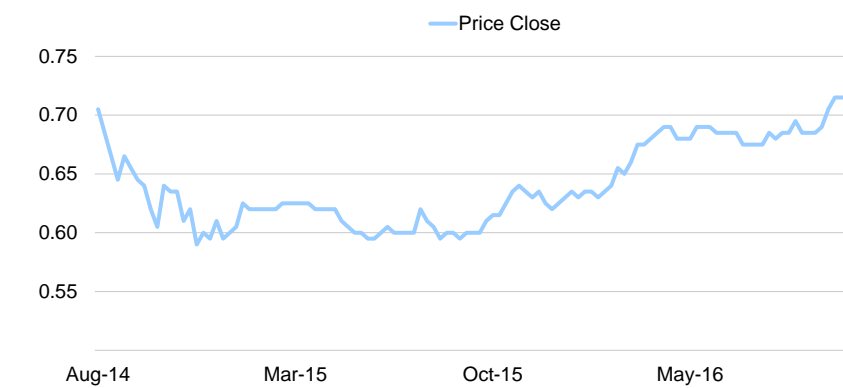
Source: Company

Private placement. Reach Energy still has another one year to go to get a qualifying acquisition. However, we believe this potential asset would be a value accretive asset to the company. In the event that there is no dissenting shareholder, Reach Energy would have sufficient funds in its trust account to pay for the entire acquisition, USD154.9m. The acquisition is expected to only go through if less than 25% shareholders, excluding the management's stake, agree to the acquisition. Reach Energy intends to buy out the dissenting shareholders. The shortfall in funds after paying for the dissenting shareholders will be plugged by a private placement. It is expected to be done after the proposal for the acquisition is passed through. We estimate the cash back to be MYR0.76.

SWOT Analysis



Recommendation Chart



Source: RHB, Bloomberg

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