

01 November 2016

Reach Energy Bhd

Reaching SPAC graduation day?

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INVESTMENT MERIT

The proposed QA of the Emir-oil concession block in Kazakhstan appears to be attractive for shareholders to approve in the upcoming EGM this Friday given its: (i) relatively low acquisition price of USD2.9/mmboe, (ii) producing fields with immediate cash flows, and (iii) potential initiatives to further unlock value. We believe REACH will be a good trading proxy for the volatility in oil prices post QA while its cash value of RM0.75/share acts as a floor price should REACH fail to complete its QA by Aug 2017. Trading Buy call with FV of RM0.89/share.

Proposed to acquire Kazakhstan on-shore O&G asset. REACH has proposed to acquire 60% of the equity interest in Palaeontol B.V. in which holds the entire working interest in the Emir-Oil concession block and 60% of the shareholder loans from a Hong Kong listed company, MIEH for USD154.9m as a qualifying acquisition to graduate from SPAC. The proposed QA will use up c.84.4% of RM759.3m cash held in Islamic Trust Account. The voting EGM will be held on 4th November 2016. The transaction price is fairly low at USD2.9/mmboe (vs. recent similar transactions of USD3.07-7.58/mmboe) of 2P reserves considering that valuation is arrived at during low oil price market.

Early stage of production. The Emir-Oil concession block is located on-shore in the Mangstau Oblast, Kazakhstan with gross 2P reserves of 89.4 mmboe of oil and gas. The block consists of four high quality sweet and light crude producing fields, two fields under pilot production and six drillable prospects. According to the independent valuation report from RPS, the block is currently producing 3.3k bbl/day of oil and 5.7mmscf/day of gas with the potential to achieve peak production of >20k bbl/day by 2021. 37% of its 2P oil reserves are classified as both developed producing and non-producing reserves, suggesting that REACH will only require additional completion work to recover oil from existing wells instead of further development for these reserves.

Potential initiatives to enhance value. REACH has identified several measures to improve the overall project IRR, including the development of LPG value chain to improve LPG sales and extraction, construction of pipelines to reduce to transportation tariff and drilling cost reduction. Such initiatives, according to the circular, are able to improve its existing IRR from 18.7% to 22.9%. Inclusive of that, the required capex to develop the block for the next three years (net on REACH's 60%) are USD17-22m. Assuming oil prices stay at current oil prices, in our view, REACH might need to the fund capex via project/contractor financing.

Proposed placement to address potential cash shortfall. Meanwhile, REACH also has new shares placement to raise proceeds up to RM180m if the proposed QA is accepted with at least 75% shareholders' approval. The proposed placement is intended to solely repurchase the dissenting shares to replenish the funds in the Trust Account to complete the transaction. Depending on the percentage of dissenting shareholders, the proceeds will be mainly used to settle the remaining purchase consideration as well as committed capex in 2016.

Trading Buy, with fair value of RM0.89. According to the circular, which includes the independent valuation report from RPS, the NPV of 100% gross 2P reserves of the block at 10% discount rate is worth USD511m. Hence, the implied fair value for REACH is RM0.89/share based on: (i) 60% stake in Palaeontol B.V if the QA goes through, (ii) maximum placement shares at RM0.59/share, and (iii) RM4.00/USD assumption. Meanwhile, we believe the stock serves as a good trading proxy to the volatility in oil prices. Note that there are 958.4m outstanding warrants expiring in 2022 at exercise price of RM0.75. If the proposed QA is not approved in the EGM, REACH needs to propose another QA by 15th August 2017.

	Rating	Fair Value
Last Price	-	RM0.71
Kenanga	Trading Buy	RM0.89
Consensus	N.A.	N.A.

Stock Information

Shariah Compliant	Yes
Stock Name	REACH ENERGY BHD
CAT Code	5256
Industry	Oil & Gas
Industry Sub-sector	Oil Exploration & Production
YTD stock price chg	12%
Market Cap (RM m)	907.3
Issued shares (m)	1277.8
52-week range (Hi)	0.73
52-week range (Low)	0.61
3-mth avg daily vol:	2,552,806
Free Float	35%
Beta	0.4
Altman's Z-score	N.A.

Major Shareholders

REACH ENERGY HOLDING	20.0%
MTD CAPITAL BHD	11.7%
PAG HOLDINGS LIMITED	9.5%

Financials

FYE Dec (RM'm)	2015A*	2016E	2017E
Revenue	41.1	0.0	367.6
PBT	-21.9	-24.4	53.8
Net Profit	-32.2	-32.5	22.1
EPS (sen)	-2.0	-2.1	1.4
BV/Share (RM)	0.02	0.46	0.48
PER (x)	-34.9	-34.6	50.7
Price/BV (x)	39.4	1.5	1.5
Net Gearing	N. cash	N. cash	N. cash
DPS	0.0	0.0	0.0
Dividend Yield (%)	0.0	0.0	0.0

Quarterly Financial Data (RM m)

	Feb-Jul 15 (6M)	Aug-Dec 15 (5M)	Jan-Jun 16 (6M)
PBT	-3.5	-16.0	-11.9
Net Profit	-6.1	-21.2	-16.1
EPS (sen)	-0.4	-1.3	-1.0

Peers Comparisons	Trailing PER (x)	Trailing Div. Yld (%)	Mkt Cap (RM m)
HIBISCS	-5.2	0.0	413.7

REACH	-34.9	0.0	907.3
FBMSC (Fwd)	10.7	2.5	-

*FY2015A consists a period of 17 months.



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Appendix:

	Gross (100%)			Attributable to Company post completion of the Proposed Acquisition (60%)		
	1P	2P	3P	1P	2P	3P
	Oil Reserves (MMstb)	24.6	70.0	116.1	14.8	42.0
Gas Reserves (Bscf)	17.7	116.3	184.1	10.6	69.8	110.4
Total Reserves (MMboe)	27.6	89.4	146.8	16.6	53.6	88.1

Source: Company

2P oil Reserves (MMstb)	Phase 1			Phase 2		Total
	Developed Producing Reserves	Developed Non-Producing Reserves	Undeveloped Reserves	Undeveloped Reserves		
Aksaz	0.744	-	-	2.627		3.371
Dolinnoe	2.147	2.162	0.815	4.852		9.977
Emir	0.709	-	0.711	2.106		3.527
Kariman North	10.989	7.321	3.154	18.258		39.723
Kariman	1.622	-	1.121	3.365		6.108
Yessen	-	3.637	-	3.672		7.309
Total	16.212	13.120	5.802	34.881		70.016

Source: Company

Field/Area	Type of field	Production commencement year	Type of contract	Duration (years)	Commencement date	Expiry date	Area (km sq)
Producing Fields:							
Kariman	Oil	2006	Production Contract	25	9 September 2011	9 September 2036	12.24
Dolinnoe	Oil	2004	Production Contract	25	9 September 2011	9 September 2036	18.24
Aksaz	Condensate-rich gas	2005	Production Contract	25	9 September 2011	9 September 2036	11.48
Emir	Oil	2004	Production Contract	17	1 March 2013	1 March 2030	3.53
Exploration Area	-		Exploration Contract	2	9 January 2015	9 January 2017	804.81
Total (approximately)							850.30

Source: Company

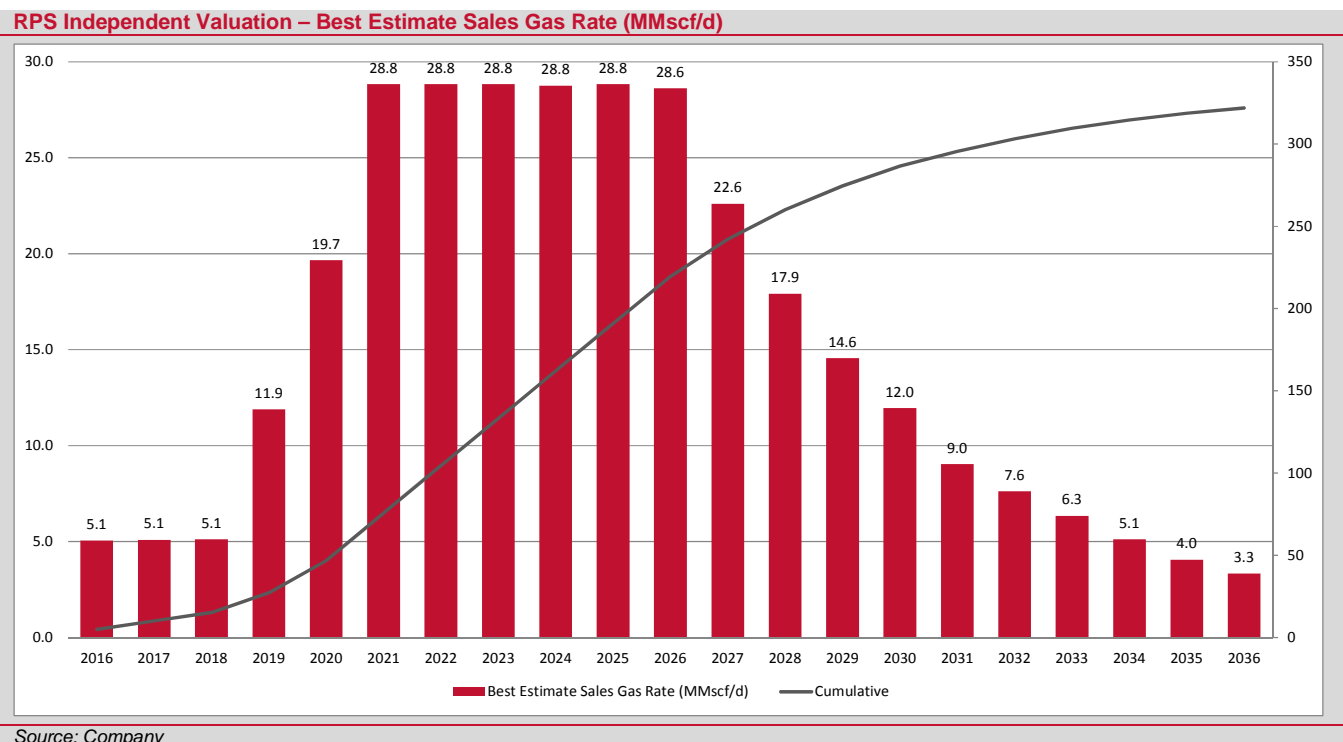
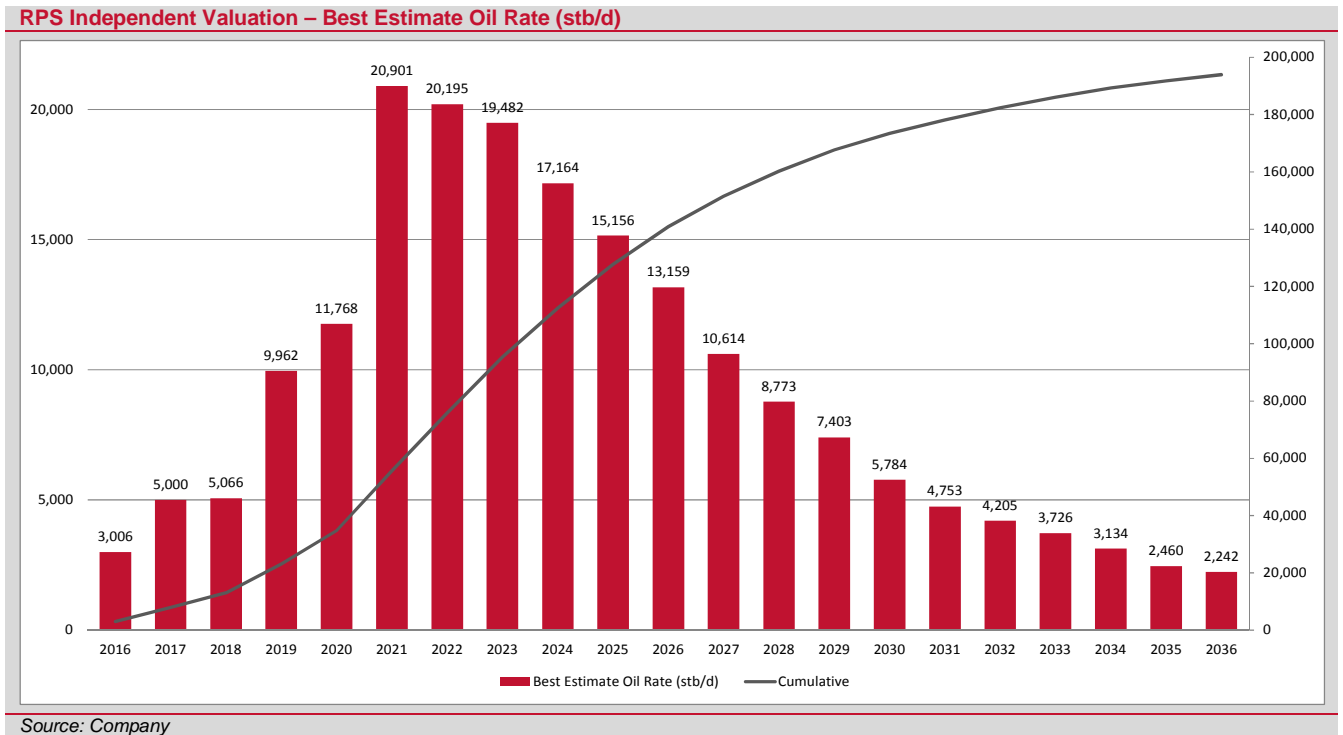
	USD '000
Enterprise value (before adjustment of Net Working Capital)	308,000
Net Working Capital	(49,852)
Equity value (100%)	258,148
Purchase consideration (60% of equity value)	154,889

Source: Company

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Production volume of the Emir-Oil Concession Block					
Average daily net production	FYE 31 December				
	2012	2013	2014	2015	FPE 30 June 2016
Crude oil (bbl/d)	2,787	4,320	5,201	3,412	3,296
Gas (MMscfd)	4.50	5.00	5.88	5.89	5.71

Source: Company



Daily Charting – Reach Energy Berhad



Comment: The underlying outlook of REACH is still positively intact, as the stock is still trading along its 1-year upward trend channel. At this point of time, it is currently retracing from its two-year high level of RM0.73 (R1) while consolidating to find some support footing closer towards its trend channel support trend line of RM0.695 (S1). Short-term consolidation is likely to persist as depicted by its tapering momentum indicators such as MACD histogram, RSI and Stochastic. Nonetheless, the near oversold Stochastic is suggesting that downside could be limited from here. Hence, interested investors could look to accumulate on weakness closer towards the RM0.695 (S1). Any technical breakout above the RM0.725 (R1) level will see the stock gear higher up towards RM0.745 (R2)/RM0.775 (R3). On the flip side, a breakdown below its trend channel support of RM0.695 (S1) will see the stock decline towards RM0.67 (S2)/ RM0.645 (S3).

Source: Kenanga Research

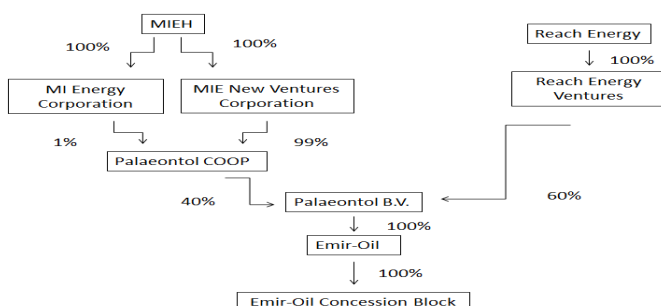
About the stock:

Name : Reach Energy Berhad
Bursa Code : REACH
CAT Code : 5256

Key Support & Resistance level

Resistance : RM0.725 (R1) RM0.745 (R2) RM0.775 (R3)
Support : RM0.695 (S1) RM0.67 (S2) RM0.645 (S3)
Outlook : Bullish

Corporate Structure After Proposed Acquisition



COMPANY DESCRIPTION

Reach Energy Berhad is a Special Purpose Acquisition Company (SPAC), with the Proposed Acquisition (PA) being 60% of the equity interest in Palaeontol B.V. in which holds the entire working interest in the Emir-Oil concession block and 60% of the shareholder loans from Hong Kong listed company, MIEH for USD154.9m. An Extra Ordinary Meeting (EGM) will be held on the 4th November 2016 to decide on the PA – requiring 75% of shareholders’ approval (excluding shares held by management). REACH has until 15th August 2017 for a successful acquisition, failure to do so will result in the company being liquidated, with the cash value of RM0.75/share to be distributed to shareholders.

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