ADX Energy

Corporate activity

Edison investment research

Near-term funding risk removed

Oil & gas

The recent announcements by ADX have de-risked areas of the company's portfolio. Through a deal with Gulfsands and a proposed deal with Rift Basin Resources on the onshore Tunisian Chorbane block, we consider that ADX has removed the funding risk from that particular work programme. In Romania, government ratification of its exploration licence has both unlocked the remaining €2.7m of farm-out cash (€3.25m in total) and kick-started the seismic programme, expected to complete in Q113. The Sicily Channel remains a longer-term value driver for the company, but requires a farm-out and/or a new funding facility to support a committed two well programme.

Year end	Revenue (A$m)	EBITDA (A$m)	PBT* (A$m)	Debt (A$m)	Net cash (A$m)	Capex (A$m)
06/11	0.0	(9.8)	(9.8)	0.0	0.8	(8.2)
06/12	0.0	(11.2)	(11.1)	0.0	0.5	(3.3)
06/13e	0.0	(1.2)	(1.2)	0.0	2.2	(4.8)
06/14e	0.0	(1.3)	(1.3)	0.0	0.8	(0.5)

Note: *PBT is normalised, excluding intangible amortisation and exceptional items.

Chorbane: Farm-outs remove funding risk

We consider the farm-out to Gulfsands and the proposed deal with Rift Basin Resources to have removed near-term funding risks from the onshore Tunisian work programme. Based on the Gulfsands deal of selling a 10% stake for A$0.7m, we consider the proposed disposal of an additional 15% interest to Rift should be sufficient to fund all near-term activities in Tunisia.

Romania: Near-term value driver, no funding risk expected

We believe that Romania offers near-term value with seismic and drilling expected to be completed in 2013. Through a farm-out to private partner RAG, ADX's share of the work programme is funded. Management considers the block to be relatively underexplored based on seismically identified potential.

Sicily Channel: Prize remains, funding still required

The Sicily Channel assets remain the most material driver of long-term value. With possibly over 1bnboe of resources, the assets could be transformational for ADX. However, given the cost of two committed offshore wells, there is a substantial funding gap, at its current interest. Until the company farms out its working interest position and/or secures additional funding facilities, the market is unlikely to begin to value its material portfolio. We understand the farm-out is ongoing.

Valuation: Sicily remains potentially transformational

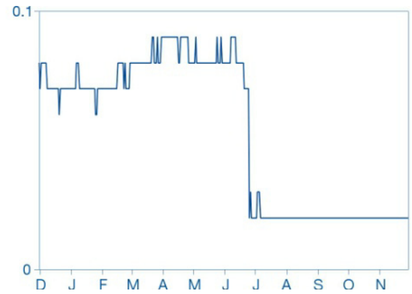
Based on recent deals agreed in Romania and Tunisia, and adjusted for net cash, G&A and its share of Riedel Resources, there is modest upside, to our RENAV of 1.9c per share, from the near-term onshore work programme. From deal metrics we would suggest a post farm-out undiluted valuation range of 3.5-5.9c. Adding this to our RENAV implies of an overall valuation range of 5.4c to 7.8c per share. In the longer term, the real value driver continues to be 1bn plus boe of gross unrisked prospective and contingent resources located in the company's Sicily Channel assets.

ADX Energy is a research client of Edison Investment Research Limited

30 November 2012

Price	**A$0.02**
Market cap	**A$8m**
	A$1.03/US$
Shares in issue	485.4m
Free float	85%
Code	ADX
Net cash (A$m)	0.6
Primary exchange	ASX

Share price performance



%	1m	3m	12m
Abs	(5.9)	(30.4)	(80.0)
Rel (local)	(4.8)	(31.5)	(81.7)
52-week high/low		A$0.094	A$0.015

Business description

ADX Energy is an oil and gas exploration and appraisal company with assets in Tunisia, Italy and Romania. It is listed on the Australian stock exchange. It also has a 26% share of an Australian-listed mining asset Riedel Resources.

Next events

Romanian Seismic	Q113
Romanian Well	H213
Chorbane Seismic	2013

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Investment summary: Near-term funding risk removed

Chorbane: Farm-outs remove funding risk

On 26 November 2012, ADX announced that it had agreed to sell 10% of the onshore Tunisian Chorbane block to its existing partner, Gulfsands Petroleum, for US$100k in cash and US$600k carry on the 2013 seismic programme. Following this announcement, on 28 November 2012, ADX signed a letter of intent (LOI) with Rift Basin Resources Corp, a young TSX-listed company, for a further 15% disposal. If completed (expected by 15 December 2012), ADX would retain a 15% working interest, with Gulfsands at 70% and Rift at 15%. Based on the Gulfsands deal alone, it would imply ADX's resultant share could be worth US$1.05m.

We consider the recent farm-out to Gulfsands and the proposed deal with Rift Basin Resources to have removed funding risks from the company's onshore Tunisian work programme. We estimate the onshore work programme will consist of 2D seismic capture in 2013 (costing US$2m gross) followed in 2014 by an exploration well (costing US$3m gross). Post the farm-outs; this could cost c US$0.75m, net to ADX. We do not know how much consideration could be paid by Rift Basin Resources, but using the Gulfsands deal we derive a 100% valuation of the block at US$7m. Therefore, in theory, a farm-out of 25% could raise US$1.75m in funding, which should be sufficient to cover to the near-term commitments on the Chorbane block.

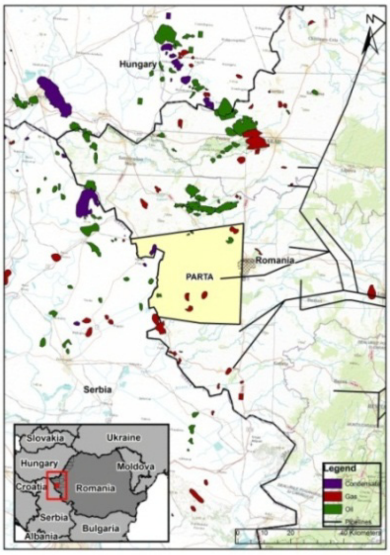
We believe this to be positive news and, yet again, this demonstrates the company's deal-making ability to fund work programmes through non-equity dilutive means. As a result of the recent deals, Gulfsands will now own a 70% working interest and will become operator. We consider this a further positive given Gulfsands' robust financial position and proven track record in exploring for hydrocarbons in the Middle East and North Africa.

Romania: Near-term value driver, no funding risk expected

The recent Romanian government approval of the company's exploration licence is a material achievement. Having experienced a number of delays, with this approval the remaining €2.7m (€3.25m total) farm-out consideration from its partner Rohoelaufsuchungsgesellschaft (RAG) will be received immediately enabling its seismic programme to begin. Dependent on the weather and ground conditions, we would expect the seismic acquisition to be completed by Q113. Assuming there are no delays in securing the necessary equipment and rig, we believe a well could be drilled as early as H213. Given the relatively shallow nature of onshore Romanian wells, we would forecast a 25- to 35-day drill time, with shallower gas and deeper oil prospects targeted.

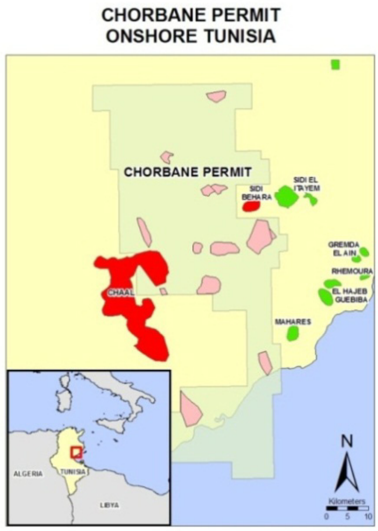
Using comparable capital expenditure costs we expect the seismic and drilling programme to cost €3.25m net to ADX, which should be covered by the farm-out consideration. We consider this could deliver near-term value versus the longer investment in Tunisia and the Sicily Channel, due to the ADX's control over operatorship in Romania and management's plan to complete its first well in 2013. Based on available seismic, the company believes the block is relatively unexplored. Romania is a proven oil and gas province and the company reports it has identified two independent fairways within the migration pathway of a large producing oil and gas field. The presence of a proven hydrocarbon pathway should de-risk the play, but given that new seismic will need to be shot before a well is drilled, we consider the geological risk to be relatively unknown at this point in time.

Exhibit 1: PARTA block – Onshore Romania



Source: ADX Energy

Exhibit 2: Chorbane block – Onshore Tunisia



Source: ADX Energy

Sicily Channel: Prize remains, funding still required

Since our last update note in October 2012, Gulfsands has increased its working interest position in the Kerkouane/Pantelleria block to 40%, through the acquisition of Xstate Resources' 10% stake. This reduces the number of partners in the consortium from three to two, with ADX owning the other 60%.

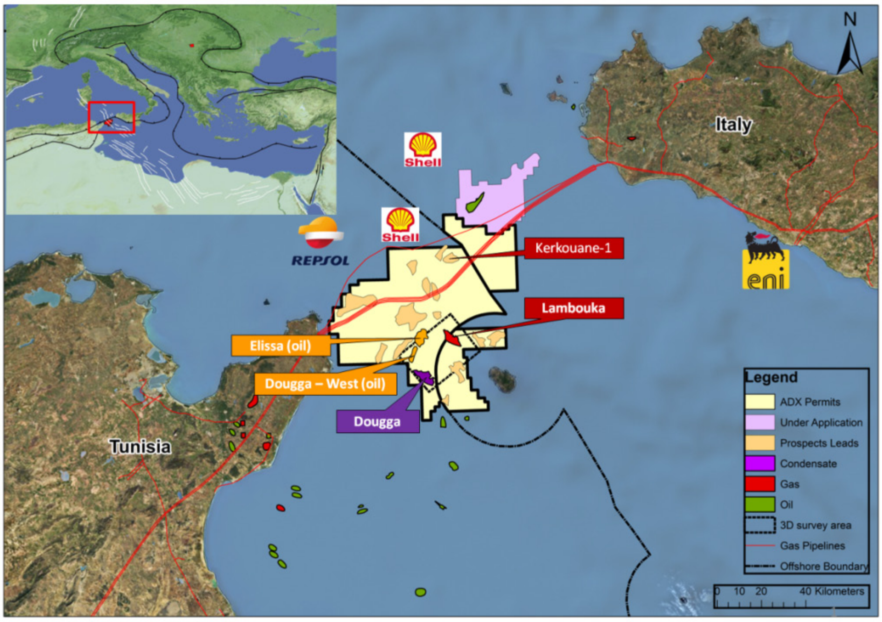
With one committed well and a re-entry to test the Lambouka well, we estimate that this programme could cost c US$33m net to ADX. As a result of the capex requirement, we await a farm-out deal and/or announcement of a new funding facility to demonstrate how the work programme will be funded. With the exploration licence set to expire in February 2014, there is a risk that the partners could lose the licence. However, we consider this risk to be small and believe that as long as the partners can demonstrate to the government that progress is under way, the licence will be extended. The potential prize remains transformational, with over 1bnboe in unrisked contingent and prospective resources contained on the block (Exhibit 3). However, until the company can demonstrate how it will fund its post farm-out share of the costs, we consider the Sicily Channel to be a longer-term value driver, which the market does not currently price.

Exhibit 3: Project summary

3D project name	Status	Pmean resource (mmboe)	Expected hydrocarbon
Dougga	Appraisal of contingent resources	173	Gas condensate
Lambouka	Appraisal	52	Gas only, condensate potential not quantified, estimated at 24mmbbl
Lambouka – Deep	Drill Deeper – Exploration	126	Gas condensate
Dougga West	Near Field – Exploration	226	Oil or gas condensate (resource given for oil case in Birsa)
Elissa	Exploration	616	Oil (Birsa) or condensate (Abiod)
Total covered by 3D seismic		1,193	

Source: ADX Energy

Exhibit 4: Sicily Channel block assets



Source: ADX

Valuation and financials

ADX currently has exploration assets and, as a result, we calculate its core NAV as a combination of forecast net cash or debt, the present value of G&A and its 26% share of ASX-listed Riedel Resources. This generates a core NAV of 0.8c per share. Our risked NAV includes valuations on the Romanian and onshore Tunisian assets based on the farm-out deals executed. This generates a RENAV of 1.9c per share.

Exhibit 5: Valuation summary

Assets	EMV (A$m)	Value/share (c)
FY 13 Cash/(Net Debt)	2.3	0.5
G&A	-0.7	-0.1
Share of Riedel Resources (as of 29/11/2012)	2.6	0.5
Core NAV	Total	0.8
Appraisal/Exploration	5.4	1.1
RENAV	Total	1.9

Source: Edison Investment Research

Due to the necessity of a farm-out, we continue to exclude the Sicily Channel from our RENAV. However, as discussed in our last note, utilising the Xstate/Gulfsands deal and an assumed US$5/bbl per barrel calculation, we are able to derive a valuation range of 3.5c to 5.9c. This would imply an overall valuation range of 5.4c to 7.8c per share.

Financials

As of Q113 cash on hand was A$611k. Given the farm-outs in Romania and Tunisia, we would expect ADX's 2013/14 work programme to be fully funded. The key influence on cash outflow over 2013/14 will be non-operating G&A related costs. We consider it a key priority to continue to minimise G&A spend given that in 2012 the run rate was A$1.6m; we have forecast A$1.2m for 2013. With no capex assumed for the Sicily Channel as yet, we forecast net cash to be A$2.2m at the end of 2013.

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Exhibit 6: Financial summary

A$'000s	2011	2012	2013e	2014e
Year end June	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS				
Revenue	0	0	0	0
Cost of Sales	0	0	0	0
Gross Profit	0	0	0	0
EBITDA	(9,793)	(11,152)	(1,200)	(1,320)
Operating Profit (before amort. and except.)	(9,831)	(11,152)	(1,200)	(1,320)
Intangible Amortisation	0	0	0	0
Exceptionals	3,941	(2,000)	6,077	0
Other	0	0	0	0
Operating Profit	(5,890)	(13,152)	4,877	(1,320)
Net Interest	53	27	10	44
Profit Before Tax (norm)	(9,778)	(11,125)	(1,190)	(1,276)
Profit Before Tax (FRS 3)	(5,837)	(13,125)	4,887	(1,276)
Tax	0	(17)	0	0
Profit After Tax (norm)	(9,778)	(11,142)	(1,190)	(1,276)
Profit After Tax (FRS 3)	(5,837)	(13,142)	4,887	(1,276)
Average Number of Shares Outstanding (m)	370.8	424.5	485.6	485.6
EPS - normalised (c)	(2.6)	(2.6)	(0.2)	(0.3)
EPS - normalised and fully diluted (c)	(2.6)	(2.6)	(0.2)	(0.3)
EPS - (IFRS) (c)	(1.6)	(3.1)	1.0	(0.3)
Dividend per share (c)	0.0	0.0	0.0	0.0
Gross Margin (%)	N/A	N/A	N/A	N/A
EBITDA Margin (%)	N/A	N/A	N/A	N/A
Operating Margin (before GW and except.) (%)	N/A	N/A	N/A	N/A
BALANCE SHEET				
Fixed Assets	14,475	8,458	13,268	13,716
Intangible Assets	9,578	6,201	10,518	10,968
Tangible Assets	119	247	209	209
Investments	4,778	2,010	2,541	2,539
Current Assets	3,608	1,898	3,335	1,711
Stocks	0	110	0	0
Debtors	2,818	1,280	1,000	800
Cash	783	500	2,217	793
Other	7	8	118	118
Current Liabilities	(1,525)	(2,514)	(2,621)	(2,721)
Creditors	(1,525)	(2,493)	(2,621)	(2,721)
Provisions	0	(21)	0	0
Long Term Liabilities	0	(666)	(666)	(666)
Long term borrowings	0	0	0	0
Other long term liabilities	0	(666)	(666)	(666)
Net Assets	16,558	7,176	13,316	12,041
CASH FLOW				
Operating Cash Flow	(1,621)	(879)	(294)	(974)
Net Interest	0	0	0	0
Tax	0	0	0	0
Capex	(8,213)	(3,316)	(4,818)	(450)
Acquisitions/disposals	0	0	0	0
Financing	8,366	3,796	6,829	0
Dividends	0	0	0	0
Net Cash Flow	(1,468)	(399)	1,717	(1,424)
Opening net debt/(cash)	(2,271)	(783)	(500)	(2,217)
FX Movements	(20)	116	0	0
Other	0	0	0	0
Closing net debt/(cash)	(783)	(500)	(2,217)	(793)

Source: Edison Investment Research, ADX accounts

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