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SacOil Holdings - African oil play with the promise of early production - Reiterate recommendation of Speculative Buy at 4.125p with a 27p target price

Key Data	
EPIC	SAC
Share Price	4.125p
Spread	4p – 4.25p
12 Month Range	3.125p – 20p
Market Cap	£28.21 million
Total no. of shares	683.93 million
Market	AIM
Website	www.sacoilholdings.com
Sector	Oil & Gas
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Dual-listed SacOil is an independent African upstream oil and gas business. The company offers investors the promise of early production and cash flow as well as the chance to add substantial value by moving opportunities up the value chain. The recently announced interim results served to remind the market of the African oil play's impressive portfolio. The focus of attention over the past six months has been on the blue sky opportunity in Block III in the highly prospective Albertine Basin the Democratic Republic of Congo (DRC) which has been neatly de-risked following a farm-in by Total. At the same time the team has also has been fast tracking progressing the OPL 233 and OPL 281 concession blocks in Nigeria towards early production and revenues. In October, the company announced a $25 million Standby Equity Distribution Agreement with Yorkville which followed a R75 million (£5.9 million) funding at R0.67 (5.28p) by Timtex Investments which should help provide the funds to accelerate these projects.

Interim results for the six months to 31st August 2011 showed that revenues from the Greenhills manganese operation increased by 17% to R19.3 million. Pre-tax profit came out at R19.15 million compared to a loss of R6.95 million at the halfway stage last year due to principally to receipts and fair value adjustments. In this period, SacOil through its 50%-owned DRC vehicle Semliki Energy SPRL (other 50% holder is DIG Oil Proprietary Limited) successfully concluded the farm-out and transfer of 60% stake in Block III to Total. In this move, SacOil gained cash of $7.5 million, a future contingent cash bonus of $54.0 million payable in two tranches, full carry on exploration costs of at least $35 million until the final investment decision and also the settlement of a $1.4 million loan provided to DIG. Importantly, SacOil has maintained representation on the management committee of Block III in which it now has a 12.5% effective stake that is fully funded.

Block III in the DRC occupies a large acreage in the Albertine Graben which forms part of the Eastern African Rift System where modern era exploration began only in 1999. Since then around 800MMbbls of recoverable oil resources have been discovered, which includes Tullow's Kingfisher (200MMbbl) and the Giraffe-Buffalo (300MMbbl) discoveries, just the other side of the border in Uganda. On trend with Tullow's discoveries lies Block III which represents a high risk exploration project where SacOil will be fully funded by Total until after a commercial reserve has been proved. Total's first plans have been for a gravity magnetic survey to outline the basin edges and to understand the workings of the petroleum system in that part of the prolific Albertine Graben. Next year will see the acquisition of seismic data to be followed by the drilling of two exploration wells, one either at the end of 2012 or beginning of 2013, followed by a second well in 2013. Under the term of the farm-in deal Total is required not only meet the work obligations on Block III but to reach a final investment decision by 31 March 2014.

In Nigeria, the company has been buying into projects at what would appear to be a 70% discount to open market prices. Indigenisation policies of the Nigerian Government coupled with minimum work commitments are bringing licences back onto the market that have not been looked at for the last 3-5 years. By partnering up with a local company, SacOil has been able to gain a sensible stake in the OPL 233 and OPL 281 licences. These are two blocks which both have already seen oil discoveries where there is obvious scope to add value by turning a contingent resource into reserves. The plan here is to book reserves and start production. The priority is OPL 233 where investors will not have long to wait as a seismic survey is due to be shot in Q1 2012 with an appraisal well planned for Q4 2012. There does seem scope for a substantial increase in reserves at OPL 233 with consultants TRACS identifying more than 100 feet of net oil and given that this block lies adjacent to the 600 million barrels (MMbbls) plus Apoi field. Good seismic here together with this well data could allow a significant resource to be proved up by the end of 2012. Two wells already exist on OPL 281 as well as good seismic data which points to one large field that may potentially contain close on 100 million barrels. All that could be confirmed by future appraisal drilling which looks set to begin by Q2 2013.

The prediction is that by 2020 Africa will account for 20% of world oil production. In recent years there has been a scramble for African oil and gas licences following some sensational discoveries. SacOil is led by a Board that has an enviable network in the continent and that are used to doing business in Africa coupled with a real depth of experience in the oil and gas industry. Two recent appointments have been John Bentley and Bill Guest who became Non-Executive Directors in May 2011. John was behind JSE-listed Energy Africa Limited which he turned into one of the leading independent upstream companies with operations in a dozen African countries and several big hydrocarbon resource discoveries in the late 1990’s before it was acquired by Petronas. John was also the Executive Chairman of FirstOil Africa until taken over by Bowleven in 2007. Bill Guest has been a Director of a number of UK-quoted exploration and production companies which includes being President of Gulf Keystone Petroleum and a Non-Executive Director of Matra Petroleum.

The business model of this AIM and JSE-listed oil play is to provide the finance and enter joint ventures with local partners in a number of African countries with a clear focus on projects where value can rapidly be added by supplying the necessary financing. Given these sort of fundamentals it is little surprise that investors have got very excited about the potential of SacOil which caused the share price to climb above 20p in Johannesburg ahead of the AIM flotation. The dust has now settled and today the shares sit at a quarter of that price and that begs the attention of serious investors. We initiate our coverage on the stock with a **Speculative Buy** recommendation and with a target price of 27p.

Forecasts Table

Year to 28th February	Sales (ZAR’000)	Pre-tax Profit (ZAR’000)	Earnings per share (cents)	Price Earnings Ratio (x)	Dividend (cents)	Yield (per cent)
2009A	20,802	(27,115)	(8.65)	NA	0	0.0
2010A	31,723	(34)	0.72	NA	0	0.0
2011A	35,143	(29,751)	(6.67)	NA	0	0.0
2012E	38,000	(20,000)	(9.00)	NA	0	0.0

Source: Growth Equities & Company Research

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