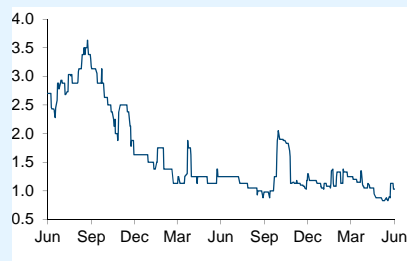


20 June 2016

Ticker	SAC	
Price	1.0p	
Target Price	2.7p	
Upside	162.0%	
Market Cap	£33.7m	
Index	FTSE AIM All Share	
Sector	Oil & Gas	
Net Cash	R107.3m	
Shares in Issue	3,269.8m	
Next Results	November - trading statement	
What's changed	From	To
Adj. EPS (FD)	0.0c	7.2c
Recommendation		
Target Price	2.8p	2.7p

Share Price Performance



Source: Thomson Reuters

%	1M	3M	12M
Actual	+17.0	-17.6	-8.8
Relative	+19.9	-16.2	+2.2

Company Description

An African independent upstream oil & gas company based in South Africa

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Re-initiation: Seeking growth opportunities

CORP

SacOil's new management team has delivered on its new strategy over the past two years: the company has successfully developed its first production project, which has the ability to generate substantial value as the project is expanded further; it has also built up an extensive exploration portfolio across three countries. Furthermore, SacOil is active in the downstream and is examining multiple project-led opportunities to expand its presence and ability to create value.

- Strategy is working.** SacOil's strategic goal of becoming a pan-African company with assets across the supply chain is falling into place. With a core production project, exploration acreage and potential opportunities in downstream projects, the company has built a good platform for potential future growth.
- Lagia has progressed.** Since acquisition in 2014, production has ramped up 20 to 1,000bbl/d at peak. With potential for lighter and other conventional crudes, there is considerable potential to create major value at this project and be the cash flow driver for the company.
- Potentially high impact exploration.** Although at an early stage, SacOil has secured acreage in the DRC, Botswana and Malawi. Based upon exploration success in similar geologies in neighbouring countries, this acreage could yield new resources in already proven play types.
- Downstream projects.** SacOil has gained a crude oil allocation from NNPC which it will jointly market with EER. It is also examining the potential for the development of a tank farm in Equatorial Guinea with a number of partners.
- Valuation and recommendation.** Our DCF for the Lagia field yields a value of 0.5p/share and our RENAV for Block II in the DRC yields 2.0p/share. Adding in last reported cash we re-initiate coverage with a target price of **2.7p/share**.

Year ending February (Rm)	2015A	2016A	2017E	2018E
Data				
Sales (Rm)	2.1	4.7	109.0	256.2
Adj EBITDA (Rm)	-511.2	-205.0	-11.0	131.2
Adj PBT (Rm)	-242.9	108.8	244.7	388.0
Tax rate (%)	nm	56	nm	nm
Adj EPS (FD) (c)	-8.5	3.1	7.2	11.6
DPS (c)	0.0	1.0	2.0	3.0
Ratios				
EV/Sales (x)	297.8	131.4	5.7	2.4
EV/EBITDA (x)	n/a	n/a	n/a	4.8
P/E (x)	n/a	7.2	3.1	1.9
Yield (%)	0.0	4.5	8.9	13.4
Cash flow yield (%)	-84.1	-42.7	6.2	25.8
EPS growth (%)	n/a	136.3	133.3	60.3

*Denotes corporate client of finncap . This research cannot be classified as objective under finncap research policy. Visit www.finncap.com

Key Financials

Income Statement				
Year ending February (Rm)	2015A	2016A	2017E	2018E
Sales	2.1	4.7	109.0	256.2
Gross profit	-1.1	-10.5	89.0	231.2
Operating expenses	-510.1	-194.4	-100.0	-100.0
Adjusted EBITDA	-511.2	-205.0	-11.0	131.2
Depreciation/Amortisation	0.0	0.0	0.0	0.0
Adjusted EBIT	-511.2	-205.0	-11.0	131.2
Associates/Other	261.4	305.0	246.7	246.7
Net interest	7.0	8.8	9.0	10.0
Adjusted PBT	-242.9	108.8	244.7	388.0
Adjustments	8.7	61.5	0.0	0.0
Reported PBT	-234.2	170.2	244.7	388.0
Taxation	-27.2	-60.4	0.0	0.0
Tax rate (%)	<i>nm</i>	56	<i>nm</i>	<i>nm</i>
Reported earnings	-261.4	109.8	244.7	388.0
Average no.shares (FD)	3,151.1	3,269.8	3,269.8	3,269.8
Adj. EPS (FD) (c)	-8.5	3.1	7.2	11.6
DPS (c)	0.0	1.0	2.0	3.0

Cash Flow				
Year ending February (Rm)	2015A	2016A	2017E	2018E
EBITDA	-511.2	-205.0	-11.0	131.2
Net change in working capital	0.0	0.0	0.0	0.0
Other items	-6.6	2.0	50.0	50.0
Operating cash flow	-517.8	-203.0	39.0	181.2
Cash interest	7.0	8.8	9.0	10.0
Tax paid	-27.2	-60.4	0.0	0.0
Capex	-76.8	-57.8	-2.5	-2.5
Free cash flow	-614.8	-312.4	45.5	188.7
Disposals	0.0	-0.1	0.0	0.0
Acquisitions	-44.5	0.0	0.0	0.0
Dividends	0.0	0.0	0.0	0.0
Other	7.9	6.4	0.0	0.0
Issue of share capital/(Buyback)	0.0	0.0	0.0	0.0
Net Change in cash flow	-651.4	-306.1	45.5	188.7
Opening net (debt)/cash	381.6	229.4	107.3	143.1
Closing net (debt)/cash	229.4	107.3	143.1	95.7

Balance Sheet				
Year ending February (Rm)	2015A	2016A	2017E	2018E
Tangible assets	331.6	383.1	400.0	400.0
Goodwill	0.0	0.0	0.0	0.0
Other intangible	0.0	0.0	0.0	0.0
Other	606.0	529.7	701.8	1,127.8
Non current assets	937.7	912.9	1,101.8	1,527.8
Inventories	6.6	9.3	10.0	10.0
Trade receivables	7.2	3.4	3.5	3.5
Cash	229.4	107.3	143.1	95.7
Other	21.8	0.0	0.0	0.0
Current assets	265.1	120.1	156.6	109.2
Trade payables	25.6	22.4	25.0	25.0
Other current liabilities	292.1	12.9	0.0	0.0
Short term debt	0.0	0.0	0.0	0.0
Net current assets	582.8	155.3	181.6	134.2
Long term debt	0.0	0.0	0.0	0.0
Pension	0.0	0.0	0.0	0.0
Other/Minorities	97.1	78.5	78.5	78.5
Net assets	1,617.6	1,146.7	1,361.9	1,740.5
Net working capital	39.3	35.1	38.5	38.5
NAV per share (c)	51.3	35.1	41.6	53.2
NTA per share (c)	51.3	35.1	41.6	53.2

Ratio Analysis				
Year ending February	2015A	2016A	2017E	2018E
Growth				
Revenue growth (%)	n/a	126.5	2,196.7	135.1
EBITDA growth (%)	n/a	59.9	94.6	1,292.8
EPS growth (%)	n/a	136.3	133.3	60.3
DPS growth (%)	n/a	n/a	100.0	50.0
Returns				
Gross margin (%)	n/a	n/a	81.7	90.2
EBITDA margin (%)	n/a	n/a	n/a	51.2
EBIT margin (%)	n/a	n/a	n/a	51.2
RoE (%)	n/a	9.6	18.0	22.3
RoCE (%)	n/a	n/a	n/a	7.9
Liquidity				
Net debt/equity (%)	n/a	n/a	n/a	n/a
Net debt/EBITDA (x)	0.4	0.5	13.0	n/a
Interest cover (x)	<i>nm</i>	<i>nm</i>	<i>nm</i>	<i>nm</i>
Net working capital to sales (%)	1,878.2	739.5	35.3	15.0
Cash conversion (%)	120.3	152.4	-413.6	143.8
Dividend cover (x)	n/a	3.1	3.6	3.9

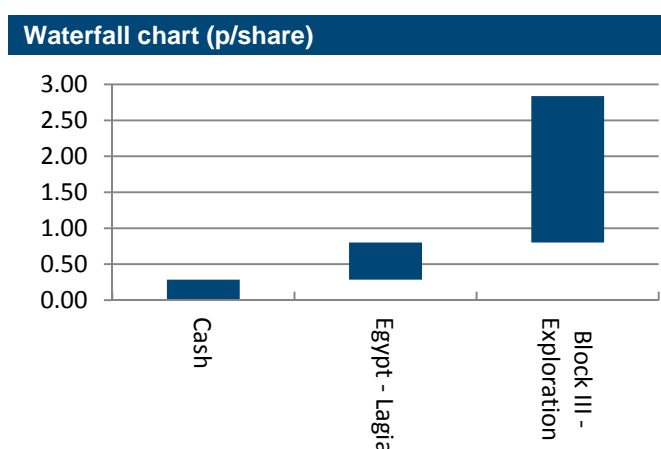
Valuation

We have valued SacOil on a DCF basis using the assumptions which are summarised in the Lagia section later in this note.

We have also included a RENAV for its DRC Block III acreage. Given the early stage of exploration activities and lack of CPR we have not yet included a valuation for Botswana and Malawi.

Again given their early stage nature, we have not yet included a valuation for the Nigerian oil trading business or the proposed Equatorial Guinea oil terminal project. However, we do highlight that there we do see these projects maturing and adding value in future.

Sum-of-the-parts		
	£m	p/share
Block III - Exploration	66.6	2.0
Egypt - Lagia	15.8	0.5
Cash	4.7	0.1
Value	87.1	2.7



Source: Company reports, finnCap estimates

Source: Company reports, finnCap estimates

Potential share price drivers

We highlight a number of future share price triggers which we feel could have a significant impact on valuation:

- Substantial increases in global oil price benchmarks will result in increased revenues and cash flow from the Lagia field
- Addition of new upstream assets and downstream projects to the portfolio
- Recovery of the US\$12.5m from Transcorp

Target price

Our DCF for the Lagia field yields a value of 0.5p/share and our RENAV for Block II in the DRC yields 2.0p/share. Adding in last reported cash we re-initiate coverage with a target price of **2.7p/share**.

Strategy review

SacOil is building an Africa-focused portfolio of assets across the supply chain. The company intends to have a balanced portfolio with assets at various stages of maturity across the supply chain.

Upstream – asset led

Over the past two years the company has developed the Lagia project in Egypt, where it has substantially increased production since acquiring it in 2014. The company is also conducting preliminary exploration work in Botswana, Malawi and the DRC, where it feels it has identified highly prospective acreage based on exploration success in similar geologies.

Downstream – project led

SacOil is examining the potential for making investments across a number of downstream projects. So far it is studying the possibility of investing in infrastructure projects such as oil terminal expansion in Equatorial Guinea, and has also established oil trading capability in Nigeria.

Potential acquisitions

Finally, there is scope for portfolio expansion via acquisition, either at the asset level or at the company level. Given the high level of both distressed assets due to low oil prices and companies which have debt problems, this approach could quickly expand the portfolio.

Our view on SacOil's strategy

Having a balanced portfolio always makes strategic sense in what we have seen to be a volatile market in the past two years. The progress in developing its first production project at Lagia shows that it is able to act as operator and to develop a project quickly, both of which are very encouraging.

Exploration always takes time, and again it is encouraging that SacOil has identified potentially highly prospective acreage with limited capital commitments.

Finally, SacOil has shown that it has the ability to identify interesting projects at an early stage. Possibly more importantly, it has shown that if such a project does not meet its strategic goals it has the bravery to walk away before capital commitments become too high, thereby protecting its balance sheet.

Upstream asset overview

SacOil has developed its first production project with great success in a short period of time. It has also built up an early-stage exploration portfolio which could be highly prospective.

Egypt (SAC: 100%)

In September 2014, SacOil acquired a 100% operating interest in the Lagia heavy oil field, located onshore Sinai Peninsula, from MENA Hydrocarbons. The consideration was US\$10m in value of SacOil shares; c183.7m shares will be issued. SacOil also paid MENA's cash liabilities of US\$4.1m.

Lagia location map



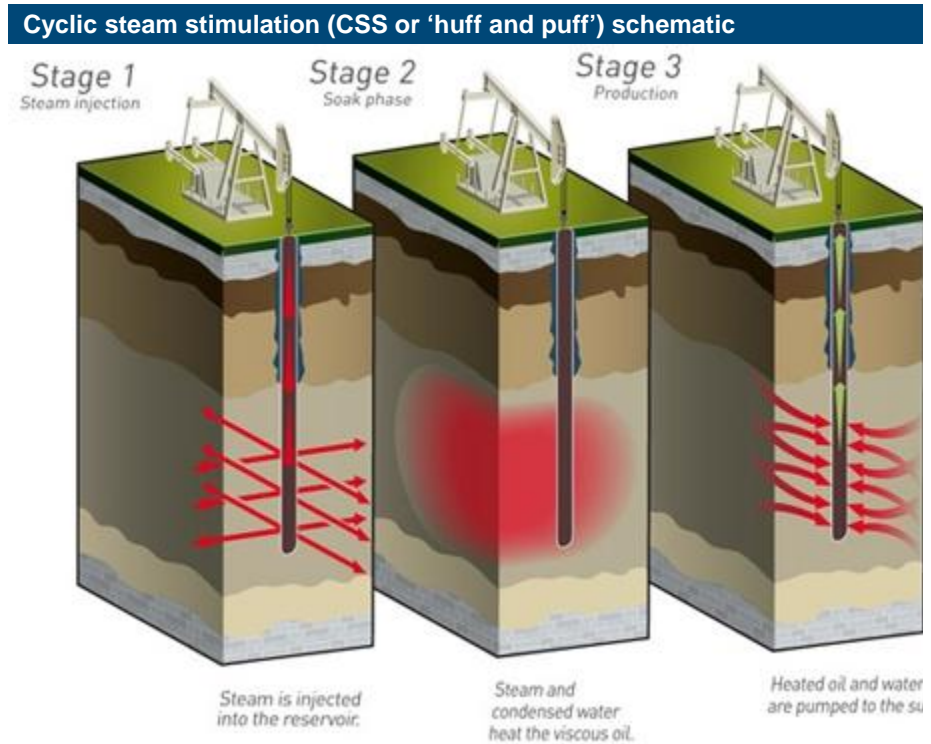
Source: SacOil

The Lagia field contains heavy oil and therefore needs to use unconventional methods to enhance oil production.

Cyclic steam stimulation (CSS)

CSS comprises three stages: injection, soaking and production. CSS recovery rates are typically c20% of the oil in place volume.

1. Steam is injected into the reservoir.
2. The steam is left in the reservoir typically for a few days to increase its mobility.
3. Oil is then produced via the same well, usually under natural flow initially and then under artificial lift. As the oil cools, production decreases to a point where it is uneconomic. The three-stage cycle is then repeated.



Source: Total

Work prior to acquisition

The Lagia field has produced from the Nukhul formation, which holds heavy oil. The previous operator had installed production facilities and 3,000bbl of oil storage, which resulted in peak production under cold flow of 750bbl/d in 2012. Upon acquisition there were two wells and production was 20bbl/d.

Work since acquisition

Under two phases of development, SacOil drilled and fraced ten new wells and also installed new steam facilities. Under hot flow conditions, production from these ten wells peaked at 1,000bbl/d, but due to lower oil prices this production has now been scaled back.

One of the new wells was drilled deeper, targeting the Thebes formation. Analysis of the oil shows it is lighter, with an API of 24°.

Future work programme

Given the success of the development so far, SacOil is reviewing the data in order to optimise the steam and production cycles with the aim of reducing interference between the wells. This optimisation should result consistent production in a cost-effective way and therefore enhance the economics of the field.

The field currently only has 2D seismic and as a result the CPR does not give full credit for Lagia's prospectivity. SacOil is investigating the potential for 3D seismic for two key reasons:

- Fully delineate the field and determine its prospectivity across all of the identified formations.
- To probe deeper prospectivity in the Nubia formation in the cretaceous. This formation has been proven to be prolific and oil in this formation is much lighter and could be produced using conventional methods if shown to be in the licence.

The potential for lighter oil and conventional oil could be highly beneficial to the Lagia project. Production costs for these crudes would be lower as no steaming or fracking would be required. Also, by blending these crudes a smaller discount relative to benchmark would be realised increasing revenue.

More work needs to be done to prove up the resource potential, but if proven to be the case, this project should substantially increase in value.

Lagia heavy oil assumptions

Egypt utilises production sharing agreements (PSCs) in the oil and gas sector. In the case of Lagia the terms are:

- No royalty or tax;
- 35% cost oil limit, with excess cost oil added to profit oil; and
- Profit oil is shared with EGPC on a sliding scale based on production. In this case, SacOil retains 26% up to production of 5,000bbl/d.

We have assumed the following costs for the project:

- Drilling, fracking, pump and tie in: US\$460,000 per well;
- Steam generator: US\$750,000. We assume two more will be required;
- Well life: four years;
- Fixed opex of US\$0.76m in 2016 increasing to US\$2.4m in 2021;
- Variable opex: US\$7.00/bbl;
- Oil price is set at 75% of Egypt Gharib Blend which historically has been discounted to Brent by 8%; and
- Brent assumption: 2017: US\$60/bbl, 2018: US\$70/bbl, 2018+: US\$80/bbl.

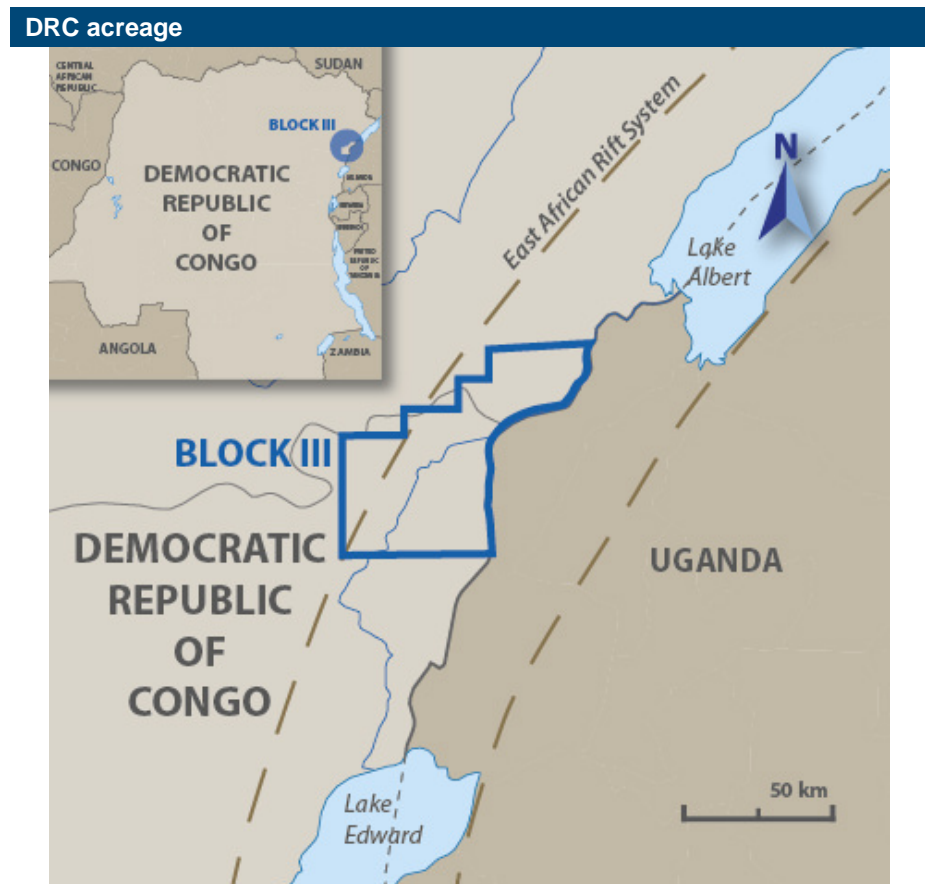
E&A portfolio

SacOil has acquired exploration acreage in the DRC, Botswana and Malawi which it feels is highly prospective given exploration success in similar geologies in nearby countries.

DRC (SAC: 12.5%)

SacOil has a 12.5% effective interest in Block III, which covers an area of 3,177km² of the Albertine Graben Basin. This basin has been prolific on the Ugandan side, with 1.2bn bbl of discoveries having been made by Heritage Oil and Tullow Oil in recent years.

Based upon the airborne gravity and magnetic survey acquired in the north of the block, the various play types which have been so successful in Uganda are also present in Block III. The company is now in the process of acquiring up to 300km of 2D seismic over potential prospects in the block, ahead of drilling a potential exploration well. On completion of the acquisition of the seismic, all work obligations will have been met.



Source: Company data

In March 2011, Total acquired an interest in the block that has now increased to 67%. Previously, Total was part of the consortium which farmed into the Heritage/Tullow Oil acreage in Uganda, so it has a high degree of knowledge and understanding of the geology in the region.

Under the farm-in terms, SacOil is carried to FID and will also receive US\$58m at this point and then an additional US\$50m on first oil. Under the terms of the PSA, the operator must acquire a minimum of 200km of 2D and 200km² of 3D seismic as well as drill two exploration wells during the initial five-year period. Following two extensions, the licence will now expire in 2018.

Block III resource estimates		
Scenario	Unrisked gross STOIP (mmSTB)	Unrisked gross GIIP (mmcf*)
Low	853.87	256.16
Best	1,940.71	582.21
High	3,731.29	1,119.39

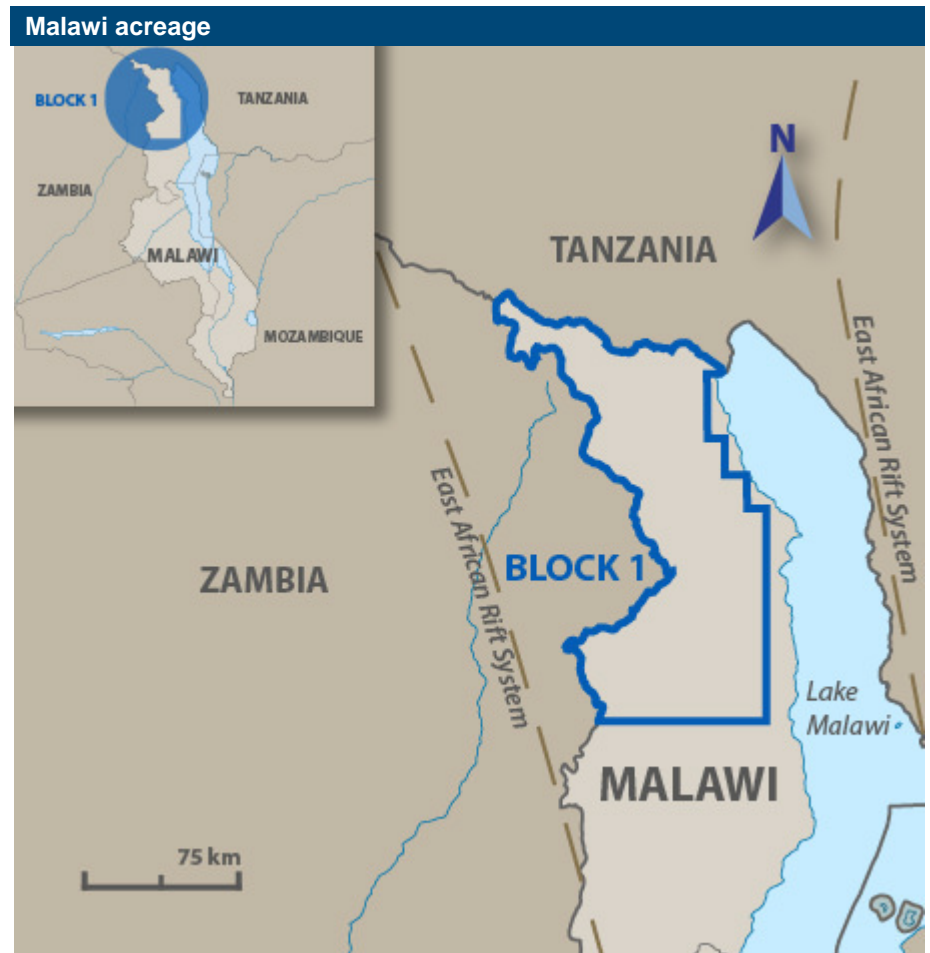
Source: Bayphase CPR May 2012. *Associated gas

Block III						
Gross unrisked STOIP (mmboe)	Recovery factor (%)	Gross unrisked prospective resources (mmboe)	Risk factor (%)	Gross unrisked prospective resources (mmboe)	Interest (%)	Net risked resources (mmboe)
1,940.71	33	642.91	21	134.67	12.5	16.83

Source: Bayphase CPR May 2012 2012

Malawi (SAC: 100%)

SacOil was awarded operatorship and a 100% interest in Block 1 in December 2012. The block is located in the Great Rift Valley, which has already yielded oil discoveries for Tullow Oil and Africa Oil on the Kenyan side. Tullow estimates that the valley could yield up to 10bn bbl of resources, with an estimated 1bn boe already discovered.

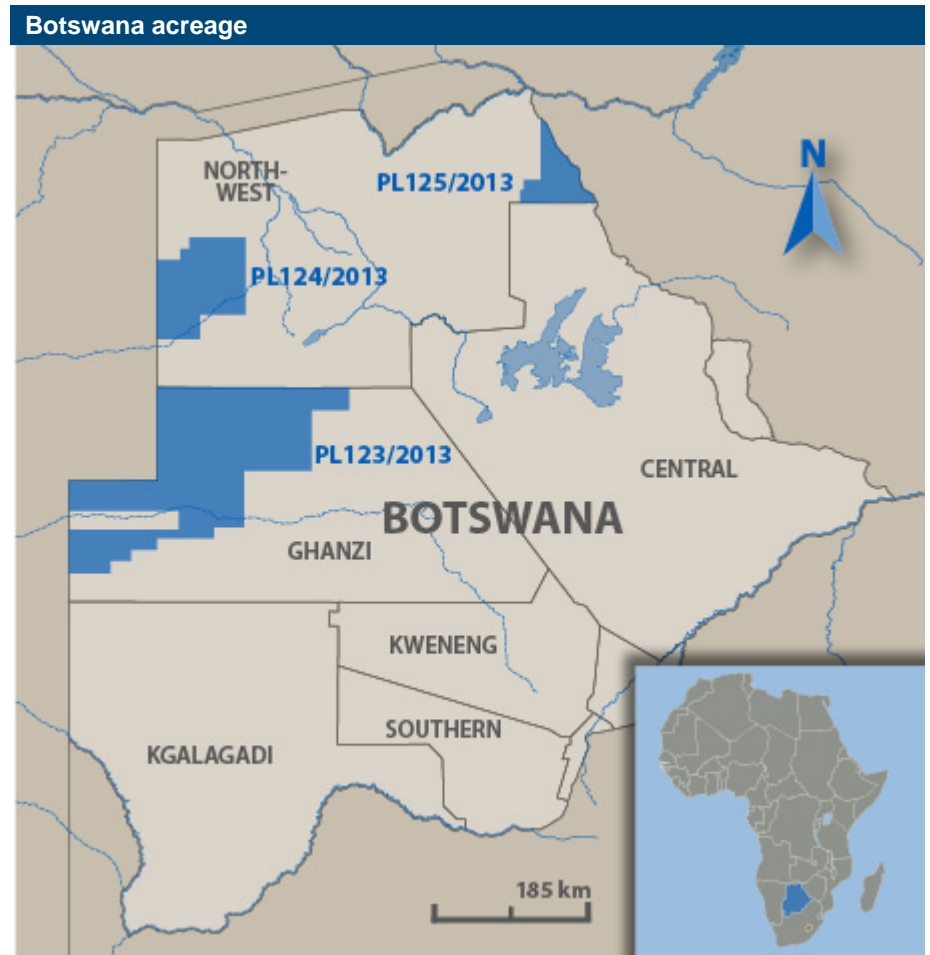


Source: Company data

The geology is made up of several half-grabens of opposing asymmetry along its length. Operations have started in the block and the company is in the process of completing the environmental Social Impact assessment. SacOil hopes to have the work programme (which includes a gravity magnetic survey) completed by the end of 2016.

Botswana (SAC: 100%)

In July 2013, licences 123, 124 and 125 were awarded to Transfer Holdings, which is 70% owned by SacOil. These licences have a three-year term and cover 49,463km².



Source: Company data

The EIS has been completed and approved and the company has committed US\$1m for a new aeromagnetic survey as well as processing gravity magnetic data.

Other projects

SacOil is also active in two other projects in Nigeria and Equatorial Guinea.

Nigerian crude trading

In April 2016, SacOil and EER were awarded a 12-month contract to purchase Nigerian crude by NNPC. SacOil and EER will set up a 50/50 joint venture which will be the contracting party which will execute the sale and purchase of the oil. SacOil is focusing on generating cash flow throughout the oil and gas supply chain and we feel that this MoU is a positive step in reaching this strategic goal.

Bioko oil terminal

In November 2015, the company signed an MoU with the Ministry of Mines in Equatorial Guinea to conduct a detailed evaluation for the development of a tank farm. The government's goal is that Equatorial Guinea will become the premier storage location in West and Central Africa as well as becoming a major transit point for global oil and gas deliveries.

Income Statement				
Year ending February (Rm)	2015A	2016A	2017E	2018E
Sales	2.1	4.7	109.0	256.2
Sales growth (%)	n/a	126.5	2,196.7	135.1
Cost of sales	-3.2	-15.3	-20.0	-25.0
Gross profit	-1.1	-10.5	89.0	231.2
Gross margin (%)	-53.9	-222.1	81.7	90.2
Operating expenses	-510.1	-194.4	-100.0	-100.0
Adjusted EBITDA	-511.2	-205.0	-11.0	131.2
Depreciation/Amortisation	0.0	0.0	0.0	0.0
Adjusted EBIT	-511.2	-205.0	-11.0	131.2
Adjusted EBIT margin (%)	-24,402.7	-4,318.8	-10.1	51.2
Associates/Other	261.4	305.0	246.7	246.7
Net interest	7.0	8.8	9.0	10.0
Adjusted PBT	-242.9	108.8	244.7	388.0
Adjustments	8.7	61.5	0.0	0.0
Reported PBT	-234.2	170.2	244.7	388.0
Taxation	-27.2	-60.4	0.0	0.0
Tax rate (%)	nm	56	nm	nm
Post tax profit	-261.4	109.8	244.7	388.0
Minorities	0.0	0.0	0.0	0.0
Reported earnings	-261.4	109.8	244.7	388.0
Weighted average no.shares	3,151.1	3,269.8	3,269.8	3,269.8
Average no.shares (FD)	3,151.1	3,269.8	3,269.8	3,269.8
Stated EPS (c)	-8.5	3.1	7.2	11.6
Adj. EPS (FD) (c)	-8.5	3.1	7.2	11.6
DPS (c)	0.0	1.0	2.0	3.0

Source: Company reports, finnCap estimates

Cash Flow				
Year ending February (Rm)	2015A	2016A	2017E	2018E
EBITDA	-511.2	-205.0	-11.0	131.2
Net change in working capital	0.0	0.0	0.0	0.0
Share based payments	0.0	0.0	0.0	0.0
Profit/loss on disposal	0.0	0.0	0.0	0.0
Net pensions charge	0.0	0.0	0.0	0.0
Change in provision	0.0	0.0	0.0	0.0
Other items	-6.6	2.0	50.0	50.0
Operating cash flow	-517.8	-203.0	39.0	181.2
Cash interest	7.0	8.8	9.0	10.0
Tax paid	-27.2	-60.4	0.0	0.0
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Acquisitions	-44.5	0.0	0.0	0.0
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Other	7.9	6.4	0.0	0.0
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Trade payables	25.6	22.4	25.0	25.0
Other current liabilities	292.1	12.9	0.0	0.0
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Net current assets	582.8	155.3	181.6	134.2
Long term debt	0.0	0.0	0.0	0.0
Pension	0.0	0.0	0.0	0.0
Other/Minorities	97.1	78.5	78.5	78.5
Net assets	1,617.6	1,146.7	1,361.9	1,740.5
<i>Net working capital</i>	<i>39.3</i>	<i>35.1</i>	<i>38.5</i>	<i>38.5</i>
<i>NAV per share (c)</i>	<i>51.3</i>	<i>35.1</i>	<i>41.6</i>	<i>53.2</i>
<i>NTA per share (c)</i>	<i>51.3</i>	<i>35.1</i>	<i>41.6</i>	<i>53.2</i>

Source: Company reports, finnCap estimates

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