

Stock Data

Share Price:	5.2p
Market Cap.:	£67.8m
Shares in issue:	1,304.8m*
52 week high/low:	7.80p/1.95p
*pre placing	

Company Profile

Sector:	Oil & Gas
Ticker:	ZPHR
Exchange:	AIM

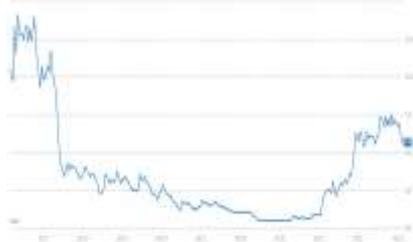
Activities

Zephyr Energy is an independent oil and gas E&P company with a strategic focus on carbon-neutral hydrocarbon development projects in the Rocky Mountain region of the US.

Company website:

www.zephyrplc.com

5-year share price performance



Source: LSE

Past performance is not an indication of future performance.

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Zephyr Energy PLC

Zephyr Energy is placing at least 240 million new shares at a price of 5.0p per share to raise gross proceeds of £12m. In tandem with this, the company has also confirmed a US\$28m senior debt facility. The combined proceeds will be used to complete the US\$36m acquisition of a large portfolio of non-operated working interests in 228 wells located in the Williston Basin, North Dakota and also to fund further activities in the Paradox Basin. We believe that this transaction will be transformational for the Company, contributing an additional 1,100 boepd net to the Company initially with output expected to increase steadily as more wells are brought on stream over the coming months.

Zephyr has already raised £3.325m through the issue of 66.5 million new shares under existing authorities. The balance of £8.675m, represented by the forthcoming issue of a further 173.5 million shares, is conditional upon shareholder approval at a General Meeting, scheduled to be held on 1 February 2022. Zephyr has also granted a Broker Option to TPI, under which TPI may raise an additional £1.2m from qualifying investors. Assuming the option is fully subscribed, this implies the issue of a further 24 million new shares at the placing price.

In tandem with the placing, Zephyr entered into a US\$28m senior debt facility consisting of a fully amortising \$18m, 48 months Term Loan and a US\$10m revolving credit facility (RCF). The Company will make monthly principal and interest payments on the Term Loan and monthly interest payments on the RCF. The facility has a fixed interest rate of 6.74%

The broad details of the acquisition remain unchanged since it was announced in November 2021. Zephyr will acquire a portfolio of 163 currently producing wells in addition to 5 proved not producing (PNP) and 13 drilled but uncompleted wells (DUC). The assets have longer term upside as the transaction also includes 47 further proved undeveloped (PUD) well locations for further low risk drilling activity.

The assets are spread across 22 separate drilling pads in Mountrail County, North Dakota and are operated by highly experienced player, Whiting Petroleum. Current production is over 1,100 boepd and independent consultant, Sproule has ascribed over 2.76 mmmboe of net reserves to the assets.

Zephyr has already paid a non-refundable deposit of US\$4.0m to the vendor out of the total consideration of \$36m. However, using Sproule's conservative commodity pricing, Zephyr has indicated a post-tax NPV (10%) of US\$46.3m for the assets. Opex per barrel is estimated to be less than US\$14.00/boe indicating high cash margins of over 75%. In this regard, Zephyr estimates that the acquisition's undiscounted free cash flow after capital expenditure will be up to US\$13.8m in 2022 and c.US\$73.6m over the life of the project.

In regard to Zephyr's activities in the Paradox Basin where the State 16-2 well was tested successfully in Q4 2021, the Company plans to use cash flow generated by the newly acquired assets to fund activities in the Paradox. This will include three additional wells targeting the Cane Creek reservoir in addition to overlying formations. Placing proceeds have also been earmarked for infrastructure investment at State 16-2 in order to monetise early gas production in 2022.

This landmark round of financing has provided Zephyr with the capacity to transform the business aggressively in both the Williston and Paradox Basins. With most indications of a sustained rally in oil prices continuing over 2022, we are confident that the economics of the Company's Williston Basin acquisition will prove to be conservative and that the assets could deliver considerable upside on the Company's current valuation.

Equity fund raising

Zephyr is placing 240 million new shares at 5.0p per share to raise gross proceeds of £12.0m before expenses. Of these funds, £9.0m is conditional upon the approval of the Company's shareholders which will be sought at a General Meeting (GM) scheduled to be held on 10 February 2022.

The Company is also launching a Broker Option to enable existing and new shareholders to participate in the placing. This Broker Option, which will remain open for a period of 24 hours following today's announcement, will enable Zephyr to raise up to an additional £1.2m.

Details of the placing

A total of £3.325m, which represents the issue of 66.5 million placing shares at the placing price of 5.0p, has been raised within Zephyr's existing share allotment authority which was granted at the Company's AGM on 30 June 2021. It is expected that these shares will commence trading on AIM on or around 1 February 2022.

The balance of the placing, represented by the issue of 173.5 million shares at 5.0p per share, is conditional on shareholder approval at the upcoming GM. Assuming that the resolutions outlined at the GM are passed, the Company expects that this second tranche of equity will commence trading on or around 11 February 2022.

Warrants

Zephyr plans to issue one warrant for every four placing shares indicating that 66 million warrants will be issued as part of the aggregate equity raising. These 'Investor Warrants' will be exercisable at a price of 7.5p per share for a period of three years after issue.

Zephyr will also issue its broker TPI up to 17.6 million 'Broker Warrants' to subscribe for the same number of ordinary shares at a price of 7.5p per share for a period of three years after issue. TPI will also receive commission of one additional Broker Warrant for every 10 Investor Warrant and additional warrants exercised. Up to 4.4 million Additional Broker Warrants to subscribe for the same number of shares will be granted to TPI. These will be exercisable at a price of 11.25p per share for a period of three years from the date of grant.

As with the larger tranche of the placing equity, the issue of the aforementioned warrants is conditional on the passing of resolutions that will be put to shareholders at the upcoming GM.

Broker Option

TPI may elect to accept or not accept bids under the terms of the Broker Option in the event of additional demand from investors. However, any shares issued under the terms of the broker warrant will be issued on the same terms and conditions as the placing shares.

There is no obligation for TPI to issue any shares under the Broker Option agreement. However, the maximum number of shares that may be issued under these terms is 24 million. As such, the maximum aggregate number of shares that may be issued under the terms of the equity placing is 264 million.

Total number of shares in issue

As at the date of this report, Zephyr had 1,304.75 million shares in issue. Following the issue of first tranche of the equity amounting to 66.5 million new shares, we anticipate that there will be 1,371.25 million shares in issue on 1 February 2022 and following the second tranche of 173.5 million new shares, the number of shares in issue will amount to 1,544.75 million on 11 February 2022 assuming a successful GM.

As outlined above, the issue of the maximum number of shares (24 million) under the Broker Option implies 1,568.75 million shares in issue upon completion of the equity raise.

Senior debt facility

Zephyr has also entered into a US\$28.0m senior debt facility consisting of a fully amortising US\$18.0m, 48 months term loan (Term Loan) and a US\$10.0m revolving credit facility (RCF). The Company will make monthly principal and interest payments on the Term Loan and monthly interest payments on the RCF. The facility has a fixed interest rate of 6.74% and the loan is secured on the Company's current and future assets and has an unlimited full recourse corporate guarantee from Zephyr.

Transformational acquisition in the Williston Basin

On 22 November 2021, Zephyr entered into a binding agreement with Kaiser Acquisition and Development – Sanish Non-op LLC, a private US E&P Company, to acquire a portfolio of non-operated interests in wells located on the Sanish field located in the Williston Basin, North Dakota. This equates to 1,960 net acres for an acquisition price of US\$36.0m of which US\$4.0m has already been paid in non-refundable deposits. We note that closing adjustments will include US\$3.8m payable in respect of the balance of capex due and will be further adjusted for the net income generated since 1 December 2021, the Effective Date of the acquisition.

The assets are operated by Whiting Petroleum Corporation, a large and highly experienced operator in the Williston Basin and a Company that already operates a number of Zephyr's existing assets where the Company holds several non-operated well interests.

The portfolio of wells are spread across 22 separate drilling pads in Mountrail County, North Dakota and independent consultant, Sproule Incorporated estimates that the assets contain 2.764 mmbob of proven reserves net to Zephyr's prospective interest. Of this amount, 68% is oil with 17% gas and 15% NGLs (natural gas liquids), the details of which are in the table below. The average working interest across the acreage is approximately 4.1% per well net to Zephyr.

Zephyr will acquire working interests in 163* (see note below table) proved developed producing (PDP) wells which are currently producing 1,105 boepd (December 2021 numbers). In addition, the acquisition includes interests in 5 further proved not producing (PNP) wells and 13 drilled but uncompleted (DUC) wells, all of which are expected to come on stream over the next few months. The deal also includes 47 further proved but undeveloped (PUD) locations for future drilling which illustrate the longer term potential of the assets.

Proven reserves summary

Reserves category	Well count	Oil reserves	Gas reserves	NGL reserves	DCF (10%)
		Net (mmbbl)	Net (mmcf)	Net (mmbbl)	
PDP*	179	1,097	1,823	281	30.5
PNP	5	48	71	11	1.2
DUC/PUD	13	325	372	57	7.5
PUD	47	415	473	73	7.2
Total	244	1,885	2,739	422	46.3

Source: Sproule (via RNS)

*Note that the PDP well count includes the 163 wells which constitute the assets being acquired in addition to 16 After Payout (APO) wells which are classified as PDP but do not convert to a paying interest. Only the abandonment costs have been included for these additional wells.

Financial metrics

Zephyr estimates that the acquisition cost of US\$36m equates to 2.1x forecasted EBITDA for the assets in 2022 (est. c.US\$17.1m). With anticipated low opex of US\$13.91 per boe across the portfolio, the Company also forecasts high cash margins in excess of 75% over the next three years as oil prices continue to strengthen. In combination with the Company's existing Williston Basin assets, Zephyr has forecasted a pro-forma EBITDA of US\$24m in 2022. This is based on Company net production of approximately 2,250 boepd in Q1 2022, reducing to 1,250 boepd by Q4 2022 based on Sproule's estimates. Production is expected to increase in 2023 as DUC wells are brought on stream.

The board currently estimates a post-tax NPV (10%) of US\$46.3m using Sproule's oil price forecasts of US\$71/bbl in 2022 falling to US\$68/bbl in 2023 and US\$66/bbl in 2024. Gas prices are assumed to be US\$5.00/mmbtu in 2021 falling to US\$3.25/mmbtu over the same time period and NGL prices are estimated at US\$30/bbl in 2021 declining to US\$26.40/bbl in 2024. Prices are escalated at 2% per annum thereafter.

The economics of the acquisition are enhanced by Zephyr's historical tax losses position which currently totals more than US\$16m.

Paradox project update

Zephyr plans to reinvest cash flow generated from its new acquisition into its wider Paradox Basin project. In particular, the Company is planning a three well drilling programme in H2 2022 to further delineate the scale of the project. This will include:

- 1 delineation/development well targeting the Cane Creek reservoir in Zephyr's existing 25,000 acre White Sands Unit (WSU)
- 1 exploration well targeting the WSU's shallow Paradox formation
- 1 delineation/development well targeting the Cane Creek reservoir in new acreage to the south of the WSU

The Company has identified over 150 additional drilling targets across nine reservoirs within the Paradox Basin project and is actively considering strategic partners for a wider scale development project.

In tandem with cash flow from significantly increased production, the Company will have an estimated US\$6.0m available from the placing proceeds to fund capex plans. This capital will accelerate drilling and infrastructure construction across Zephyr's wider portfolio.

Following the successful production testing at the State 16-2 well, the Company is planning to equip the well for gas production which will be sold locally to a proposed 2MW co-located cryptocurrency mining facility initially in Q2 2022. Following the build-out of further infrastructure at State 16-2, further gas sales through a nearby pipeline is expected, with work related to a tie-in anticipated to commence in H2 2022 for planned sales in 2023.

In this regard, Zephyr has commissioned Sproule to complete a Competent Persons Report (CPR) to assess the Company's reserves within the Cane Creek reservoir and also the eight overlying reservoirs. This document is expected to be published in Q1 2022.

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