

NGE CAPITAL LIMITED SUMMARY

ASX ticker	NGE
Share price (31-Oct-19)	\$0.600
Shares outstanding	37,194,774
Market cap	\$22.3m
NTA per share before tax	\$0.785
NTA per share after tax	\$0.839
NTA before tax	\$29.2m
NTA after tax	\$31.2m

OVERVIEW

NGE Capital Limited is an internally managed Listed Investment Company which allows investors to gain exposure to a concentrated, high conviction, actively managed portfolio of financial assets. NGE primarily focuses on listed ASX and international equities, with the aim of generating strong risk-adjusted returns over the medium to long term.

INVESTMENT STRATEGY

NGE has a flexible investment mandate and invests according to a defined set of investment principles, summarised as follows:

- Only invest in a compelling opportunity, otherwise hold cash;
- Invest based on fundamental analysis;
- Target investments that can generate strong returns with an adequate margin of safety; and
- Aim to hold a concentrated portfolio of high conviction investments.

BOARD & MANAGEMENT

David Lamm	Executive Chairman & Chief Investment Officer
Adam Saunders	Executive Director & Portfolio Manager
Ilan Rimer	Non-Executive Director
Les Smith	Company Secretary & Chief Financial Officer

CONTACT DETAILS

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NET TANGIBLE ASSETS (NTA) PER SHARE

	31 Oct 2019	30 Sep 2019
NTA per share before tax	\$0.785	\$0.812
NTA per share after tax	\$0.839	\$0.867

NTA PER SHARE PERFORMANCE SUMMARY

1 month	Year-to-date	Last 12 months	Since inception ⁽¹⁾	
			(p.a.)	(cum.)
-3.4%	2.5%	-1.7%	15.9%	53.8%

Note: Returns are before tax and net of all expenses.

(1) From 30 November 2016, the date on which NGE became a LIC.

TOP HOLDINGS (% OF NTA)

Company	Ticker	%
Karoon Energy	ASX:KAR	49.0%
United Company RUSAL	HKE:0486	26.5%
Yellow Cake plc	LSE:YCA	14.2%
Horizon Oil	ASX:HZN	10.0%
Base Resources	ASX:BSE	6.1%

PORTFOLIO COMPOSITION

	31 Oct 2019
Listed equities	106%
Net cash and other	-6%
Total	100%

UNRECOGNISED TAX LOSSES

The Company has ~\$45 million of Australian unused and unrealised losses available as at 31 October 2019. In the aggregate these losses equate to a potential future tax benefit of ~\$12m or ~\$0.33 per share (of which only \$2.0m or \$0.054 per share is recognised in our after tax NTA). The Company has received tax advice that these losses are available to be offset against future tax liabilities so long as NGE continues to satisfy the continuity of ownership test as set out in Divisions 165 and 166 of the *Income Tax Assessment Act 1997* (Cth).

COMMENTARY

NGE's portfolio produced a return of -3.4% for the month of October.

During the month **Karoon Energy Ltd (ASX:KAR) (Karoon)** launched a much-anticipated equity raising to fund the acquisition of Bauna. The A\$284m fully underwritten rights issue is being done at an issue price of \$0.93 per share. ~A\$175m of the raise has already been settled via a placement and institutional entitlement offer. The retail portion of the offer is due to settle on 19 November.

The raise was larger than we hoped, mainly due to ~US\$50m cash required to be held in escrow for field abandonment and to maintain a minimum cash balance under the ING debt facility, and ~US\$30m of completion adjustments over and above the Bauna free cash flows and vendor interest charge. The raise was also done at below the pre-raise cash backing of ~A\$1.30 per share (including the US\$50m deposit already paid), making this a bargain deal for investors participating in the raise.

We subscribed for \$7.7m of shares in the institutional portion of the raise, having lightened up in previous months (at an average price of ~\$1.30) in anticipation of the raise, taking our holding to ~14.8m shares acquired at an average price of ~\$0.91. Accounting for all our purchases and sales of Karoon shares this year our effective entry price is ~\$0.83 and as at month end the total realised and unrealised profits from our investment was ~\$2.05m. The raise is fully underwritten which suggests strong interest from large institutional investors, and we expect the stock to trade better once the retail portion of the raise has been settled. There are still some conditions precedent to be

met prior to transaction close, however, so it may be several months until the share price better reflects the value proposition. Once Bauna is settled, Karoon will be a unique prospect on the ASX offering oil exposure as a small- to mid-cap producer via a large, high quality production asset with low costs of production. There is nothing else of this size and quality on the ASX.

Bauna is an offshore oil and gas field located in shallow water (225-295m) in the Santos Basin. The field has been in production since February 2013. The field currently produces ~19,350bopd via 6 production wells, 3 water injection wells and 1 gas injection well tied into the FPSO Cidade de Itajai, a chartered production vessel with production capacity of 80,000bopd. The FPSO is owned 50/50 by Teekay Offshore Partners L.P. (NYS:TOO) and Ocyan S.A.; Ocyan operates the unit. All gas is reinjected back into the reservoirs.

We estimate Bauna will have 2P reserves of ~44mmbbls at transaction close (assuming 31 March 2020 settlement), and once Patola is tied-in these fields should produce ~58mmbbls over 10 years.

We estimate Bauna will produce ~5.6mmbbls in the first 12 months of ownership, barring any unforeseen operational issues and a smooth monthly production decline rate. We estimate opex to be relatively fixed at ~US\$124m p.a. (~US\$340k/day) – made up of FPSO charter rate, O&M rate, and associated lifting costs. Opex should remain relatively steady over time, and may even reduce when the initial FPSO contract term expires in February 2022, as has been the case for other Teekay-owned vessels. There is a 10% revenue royalty, and a special participation levy which appears only to apply above a production rate of ~20kbopd. We also factor in an abandonment cost provision of US\$2.25/bbl. At US\$60/bbl Brent oil and an assumed zero premium/discount to benchmark, Karoon should generate free cash flow of ~US\$165m (~A\$240m) from Bauna in the first 12 months.

In 2021 Karoon intends to undertake some well workovers and replace several electric submersible pumps at Bauna, as well as tie-in the Patola discovery. We estimate the cost of this work could be ~US\$230m, and is expected to result in production peaking at close to 40kbopd, and average ~33kbopd for 2022, or ~11.8mmbbls for the year. At that level of production, we forecast free cash flow in 2022 to be ~US\$380m (~A\$560m) at US\$60/bbl oil.

We have refined and rerun our valuation from [July](#), updated for new information disclosures and the equity raise. We have also lowered our base case oil price to US\$60/bbl:

	Book value	Valuation	
	A\$m	A\$m	A\$/sh
Bauna/Patola tie-in (DCF valuation)		\$1,173	\$2.12
Cash post transaction		\$188	\$0.34
Debt post transaction		-\$365	-\$0.66
Corporate costs		-\$100	-\$0.18
Neon development	\$113	\$0-\$650	\$0-\$1.18
Peru exploration	\$67	?	?
Australian exploration	\$29	?	?
Other net assets and liabilities	\$6	?	?
PV Poseidon contingent payments	\$0	\$0-\$175	\$0-\$0.32
Total SOTP valuation		\$896-\$1,721+	\$1.62-\$3.11+

Note: Book value as at 30 June 2019. USD converted to AUD at AUDUSD FX rate of 0.6850.

Karoon will be highly leveraged to the oil price post transaction – an 8% increase in the oil price leads to a 15% increase in value of Bauna:

Brent oil price (US\$/bbl)				
Base case				
\$50	\$55	\$60	\$65	\$70
\$1.45	\$1.79	\$2.12	\$2.45	\$2.77

We understand that the risk of the transaction not completing is low. In any case, the downside to our investment is relatively low as the stock is trading in line with the post-raise cash backing of ~A\$0.93 per share (or ~A\$1.06 if the US\$50m deposit is recoverable in certain instances).

Karoon offers potential upside through a development of Neon, which is ~50-60km from Bauna. This is close enough to tie-in Neon, if feasible. Further upside could be achieved in the near-term with success of the Marina-1 exploration well in Peru, to be drilled in 1Q20. Additionally, the recent acquisition by Santos of ConocoPhillips' northern Australian assets, including the Poseidon field, is probably a positive development for Karoon. Santos noted in its investor presentation that Poseidon represents a "[p]ost 2025 dated development opportunity with Darwin LNG expansion an option". This is the most concrete statement we have seen to date about a possible development of Poseidon, and bodes well for Karoon's contingent milestone payments of up to US\$200m, which we wrote about in detail in our [February](#) update.

IMPORTANT INFORMATION:

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