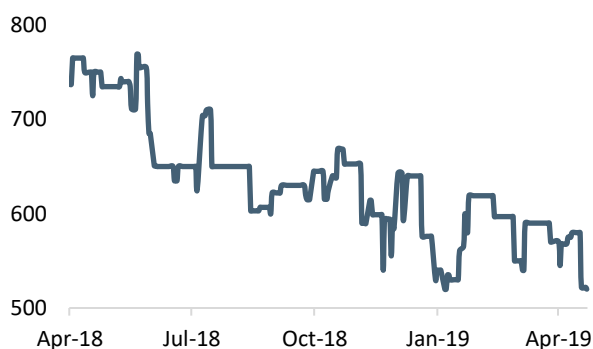


Rating	STRONG BUY
Price	₦520.00
FVE	₦782.15
52-week range	₦515.10-769.00
Market Cap. (₦'bn)	305.991
1-month Avg. Vol	58,176
Curr. PE	5.65x

SEPLAT:NL - Share Price Trend



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Seplat Plc. (SEPLAT.NL)

Stock Report

Still Cheap Despite Short-Term Drags

- We update our views on Seplat Petroleum Development Company Plc. (Seplat) following release of FY 18 and Q1 19 financial results. We have revised our earnings estimates lower, following (1) reduced tax credit forecast over the horizon period and (2) increase in our estimated cost per boe. A culmination of our adjustments resulted in a reduction of our 2019E EPS to \$0.31, compared to our previous estimate of \$0.43 and FY 2018 of \$0.25.
- Based on the foregoing, we revise our FVE on Seplat lower to ₦782.15 from ₦952.8, which still translates to a **STRONG BUY** rating. Seplat currently trades at a P/E and P/CF of 5.7x and 1.8x, a discount to Bloomberg's MENA peers of 6.6x and 4.2x, respectively. That said, the ANOH gas project (which we are yet to incorporate in our model) has potential to significantly boost earnings in the medium term, thus, an upside to our estimates. On the flip side, a decline in oil price below \$50/bbl. portends a downside risk to our estimates.
- Further in the report, we also give further details on the ANOH gas project as communicated by management during the last conference call.

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- **Quick look at Q1 19 numbers** Seplat recorded a decline in revenue over Q1 19 by 10% QoQ to \$159.5 million, following reduction in oil revenues which offset growth in the gas segment. Revenue in the oil segment fell 21% QoQ to \$118 million, reflecting the slowdown in production which dropped 14% QoQ to 21.8kbpd and the decline in average oil prices (-4% QoQ to \$61.7/bbl). Meanwhile, gas revenue jumped 46% QoQ to \$41.8 million supported by increase in both gas production (+14% QoQ to 143mmscfd) and price (+31% QoQ to \$3.24/mmcf) from the low base in Q4 18. Speaking with the company's representative, we understand that the slowdown in oil production -- despite improvement in uptime to 85% -- was a result of recent years of faltering capex spend (3-yr avg.: \$58 million) which led to reduced drilling activities. That said, a faster decline in production cost by 16% QoQ to \$78 million, compared to revenue, supported expansion in gross margin by 308bps to 51.1%. Further straining earnings in the period, was increased over lift in the period and loss on derivatives. Overall, PBT was lower 70% QoQ to \$19 million, while a higher tax credit of \$13 million led to a slower decline in PAT (-53% QoQ) to \$33 million. On a positive note, there was improvement in the cashflow position to \$644 million in Q1 19 from \$581 million in FY 18. This makes for enough legroom for management to meet the 2019 capex guidance of \$200 million which is to support the busy work schedule aimed at drilling of 12 oil wells in both eastern and western assets over 2019 (details below).

Production boost on the horizon, but with fruition from H2 2019

- Going further into 2019, we revise our forecast working interest production lower to 49,765boepd from our previous estimate of 51,100boepd (2018: 49,867boepd). We expect the pullback in production to stem from lower oil output which we now estimate to average 23,960bpd over 2019 (previously 26,200bpd), offsetting our increased forecast for gas production to 155mmscfd (previous estimate: 149mmscfd). However, it is worth stating that our projection remains within management's guidance to overall production of 49,000 – 55,000boepd.

Oil production capacity is expected to improve by the end of the year if the proposed drilling schedule – which will result in the addition of 12 new oil wells – pulls through as guided by management during the last conference call. Specifically, we expect 6 new Ohaji South wells, 4 Sapele shallow wells and 2 Ovhor oil wells, which will add ~30mbpd in gross production capacity by the end of the year. However, payoffs of these capex investments are more likely to trickle in from H2 19 (more in 2020) but not enough to offset the depressed production we envisage over H1 19. Meanwhile, we remain optimistic on stable gas production over the year with increase also expected at the tail end of the year upon completion of the Oben booster compression scheduled for completion in Q3.

- Meanwhile, we increase our oil price forecast for 2019 to \$60/bbl. (previously \$50/bbl.) and slightly adjust our gas price lower to \$3.06/mmscfd (previously \$3.7/mmscfd). A culmination of the foregoing, together with our expectation on production will result in an increase to our 2019E revenue forecast to \$656 million (previous estimate: \$633 million) – oil: \$493 million and gas: \$164 million.
- ***Increased cost per boe forecast weighs on margin.*** We increased our 2019E forecast production cost per boe to \$7,008 (previously \$5,727) which resulted in total production cost of \$349 million (previous estimate: \$292 million). This stemmed from increased estimate for depreciation, following our now upbeat expectation of capex to \$224 million, which translates to higher value of assets. Excluding depreciation, forecast production cost per boe would be nearly unchanged at \$4,670 (previous estimate: \$4,680). Accordingly, our 2019E gross margin reduced to 46.8% (previous estimate: 53.8%, 2018: 52.4%).
- ***Toned down tax credit expectation.*** Weighing heavily on our earnings forecast is our adjustment to expected tax credit over the forecast horizon. Over 2019, we now estimate tax credit of \$61 million (previous estimate: \$79.6 million), considering recent results and upon further clarification. That said, we note that with unutilized capital allowance of \$397 million in deferred tax assets as at Q1 19, there is enough legroom for Seplat to earn more in tax credits, depending on tax assessments made by the relevant tax authorities.
- Consequently, coalescing our adjustments leads to a downward revision to our 2019E PAT forecast to \$184 million from previous estimate of \$252 million and 2018 PAT of \$147 million. This translates to EPS of \$0.31 from \$0.25 in 2018.

Valuation remains compelling, with potential upsides

- Based on the foregoing, we revise our FVE lower **to ₦782.15 from ₦952.81**. Our revised target price equates to implied forward 2019 P/E of 7x, a discount to Bloomberg's Middle East and Africa peer of 12.5x. Meanwhile, further upside to earnings lie in **the ANOH gas project (details below), which is set to kick in from 2021 and could give significant boost to earnings from its gas business.** We await further clarification on this before incorporating this to our model. On the flip side, downside risk to earnings is a nosedive in oil prices below \$50/bbl. compared to our \$60/bbl. projection over 2019. That said, we retain a **BUY** rating on the stock.

The ANOH Gas project

- During the previous conference call, management gave details on the ANOH Gas project, following the sanction of the financial investment decision (FID) earlier in January. The gas project comprises upstream and midstream units, with Seplat holding 20% and 50% working interest respectively.
 - The upstream segment will comprise 6 production wells with expected gross production of over 500MMscfd wet gas and required capex spend of \$200 million, of which \$40 million will accrue to Seplat. In the mid-stream unit, AGPC will own and operate a gas processing plant with initial capacity of 300MMscfd and required capex of \$700 million -- \$420 million funded via equity (\$210 million apiece to Seplat and NGC) and \$280 million raised via debt.
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Summary of Results and Forecasts - \$'000

ANNUAL								
Income Statement (\$'000)	2016A	2017A	2018A	2019F	2020F	2021F	2022F	2023F
Production								
Oil production (bopd)	9,479	17,900	25,670	23,960	28,660	28,960	29,260	29,560
Gas production (mmscfd)	95.0	114.0	145.0	155.3	172.4	175.8	179.3	183
Total (boepd)	26,796	36,900	49,768	49,765	57,304	58,177	59,061	59,957
Oil price (\$/bbl.)	40.4	50.4	70.1	59.7	50.0	50.0	50.0	50.0
Gas price (\$/mmscf)	3.0	3.0	2.9	3.1	3.0	3.0	3.0	3.0
Revenue								
Oil	148,757	328,206	590,503	492,577	494,694	498,425	503,588	508,751
Gas	105,460	123,973	155,637	163,549	178,497	181,539	185,170	188,874
	254,217	452,179	746,140	656,126	673,191	679,964	688,758	697,625
COGS	182,424	240,059	354,926	346,952	381,550	388,802	398,858	393,362
Gross Profit	71,793	212,120	391,214	309,173	291,642	291,163	289,900	304,263
Operating Cost	229,676	99,706	81,263	145,724	135,885	141,115	147,242	149,940
Operating Profit	157,883	112,414	309,951	163,449	155,757	150,048	142,659	154,322
Finance Income	59,017	4,335	9,905	9,453	10,834	9,243	8,470	7,719
Finance expense	73,900	72,752	56,492	50,189	35,643	30,029	24,631	16,188
PBT	172,766	43,997	263,364	122,713	130,947	129,261	126,498	145,854
Tax	6,672	221,233	-116,788	61,009	43,829	45,560	45,210	28,458
PAT	166,094	265,230	146,576	183,723	174,777	174,822	171,709	174,312
Balance Sheet (\$'000)	2016A	2017A	2018A	2019F	2020F	2021F	2022F	2023F
Oil & gas properties	1,224,400	1,286,387	1,301,220	1,543,192	1,653,782	1,759,126	1,851,379	1,934,961
Fixed Assets	1,516,073	1,764,789	1,668,466	1,890,900	2,005,601	2,115,363	2,211,931	2,299,726
Stocks	106,213	100,336	102,554	122,632	122,554	131,153	131,329	131,106
Trade debtors	390,694	310,345	136,393	119,939	123,058	124,296	125,904	127,525
Cash and other bank balances	159,621	437,212	584,723	498,658	461,602	401,625	392,600	419,659
Total Assets	2,179,273	2,614,630	2,526,565	2,652,869	2,733,970	2,794,015	2,883,774	3,000,465
Trade Creditors	261,528	410,593	284,565	250,235	256,744	259,327	262,681	266,062
Non-current Liabilities	463,847	431,407	601,976	519,472	522,861	526,319	529,845	550,942
Total liabilities	945,258	1,111,533	925,680	866,021	851,820	828,313	837,766	864,990
Shareholders' fund	1,234,015	1,503,097	1,600,885	1,786,847	1,882,150	1,965,702	2,046,008	2,135,475
Key Ratios	2016A	2017A	2018A	2019F	2020F	2021F	2022F	2023F
P/E (x)	-3.5	2.3	7.1	7.0	7.3	7.3	7.4	7.3
ROA	-13%	19%	9%	11%	10%	9%	9%	8%
ROE	-8%	10%	6%	7%	6%	6%	6%	6%
Net Margins	-65%	59%	20%	28%	26%	26%	25%	25%

EPS (\$)	-0.29	0.47	0.25	0.31	0.30	0.30	0.29	0.30
EBIT margins	-62%	25%	42%	25%	23%	22%	21%	22%
PBT margins	-68%	10%	35%	19%	19%	19%	18%	21%
Debt to Equity	53.8%	37.9%	27.8%	23.3%	20.7%	18.3%	17.6%	18%
Debt to Assets	30.5%	21.8%	17.6%	15.7%	14.3%	12.8%	12.5%	13%
BVPS (¥)	2.2	2.7	2.7	3.0	3.2	3.3	3.5	3.63

Source: ARM Research *unless otherwise stated

ARM ratings and recommendations

ARM now employs a two-tier rating system which is based on systemic importance of the security under review and the deviation of our target price for the stock from current market price. We characterize systemic importance as a function of a stock's ranking among the group of top 20 stocks by NSE market capitalization over a trailing 6-month period (minimum) to the review date. We adopt a 5-point rating system for this category of stocks and a 3-point rating system for stocks outside this group. The choice of top 20 stocks arises from the consideration that this group of stocks constitutes >75% of overall market capitalization and stocks outside this group are generally less liquid and individually account for <<1% of market capitalization. For stocks in both categories, the basis for ratings subject to target price deviation is outlined below:

TOP 20		NON-TOP 20	
Rating	Deviation	Rating	Deviation
STRONG BUY	>20%	BUY	>20%
OVERWEIGHT	10% — 20 %	NEUTRAL	5% — 20 %
NEUTRAL	0% — 10 %	SELL	<5%
UNDERWEIGHT	-5% — 0%		
SELL	<-5%		

RECOMMENDATION KEY	
Rating	Recommendation
BUY	Accumulate security to a substantial extent constrained only by portfolio diversification considerations
OVERWEIGHT	Accumulate security to an extent moderated by cognizance of its benchmark weight
NEUTRAL	Maintain status quo for security with respect to current holding—i.e. keep if already holding and don't buy otherwise—subject to reasonable portfolio constraints
UNDERWEIGHT	Minimize exposure to security taking cognizance of its index weighting
SELL	Sell-off security completely from portfolio

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