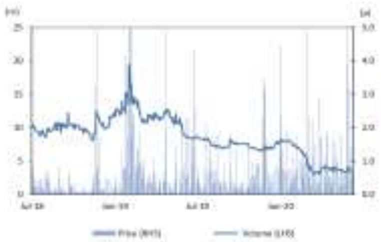
Deltic Energy Plc (formerly Cluff) (DELT.L)

Deltic confirms Shell's well commitments

Corporate

Current price	0.675p
Sector	Oil & Gas
Code	DELT.L (CLNR)
AIM	AIM

Share Performance



	1m	3m	12m
DELT.L	-13.3%	-21.2%	-62.3%

Source: Thomson Reuters, Allenby Capital

Share Data

Market Cap (£m)		9.5
Shares in issue (m)		1,406
52 weeks	High	Low
	1.75p	0.625p
Financial year end		31 December

Source: Company Data, Allenby Capital

Key Shareholders

IPGL (Michael Spencer)	16.8%
Canaccord Genuity	13.8%
Lombard Odier	8.1%
Janus Henderson	6.7%
Fiske	4.0%
James Caird Asset Man.	3.9%

Source: Company Data, Allenby Capital

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Deltic Energy's recent operational update, importantly, confirms the commitment of its JV partner, Shell, to drill the promising Pensacola and Selene prospects in the SNS (Southern North Sea) gas basin. Drilling the former now appears likely in the second half of 2021 and will be followed by Selene in mid-2022. Significantly, we expect major news flow over the next three months or so. This will relate to the results of the 3-D seismic shot on Pensacola by Shell in August 2019, a possible well decision and the awards of acreage under the 32nd North Sea Licencing Round. As noted in our May note, the marked contango in North Sea forward prices is more significant for investment than the currently depressed spot prices. Deltic's share of Pensacola and Selene well costs plus G&A through mid-2022 is well underpinned by the sizeable cash position.

- **P2252** (Pensacola) in which Deltic has a 30% non-operated interest, is located c.75 km east of the Tees estuary and contains the Pensacola Zechstein reef play. P50 resources have been assessed by Deltic at a significant 309 bcf of gas. The full suite of results from 2019's seismic shoot should be available by August. Deltic has indicated that a firm drilling decision is anticipated by end November 2020 with an exploration well following in H2 2021. Zechstein reef plays towards the northern frontier of the SNS have attracted considerable interest of late given the discoveries in 2019 of Darach (on test 3,500 b/d plus gas) and the sizeable West Newton onshore Yorkshire oil and gas discovery. Deltic's share of well costs is £3-4.5m, according to the company.

- **P2437 (Selene)** is located c.100km east of the Humber estuary in the prolific Leman Sandstone fairway. The licence is owned 50:50 by Shell and CLNR and contains the Lower Leman Selene prospect. Deltic has indicated that it is the largest untested structure in the Leman fairway. Selene has estimated P50 resources of 291 bcf and is considered relatively low-risk with a GCOS of 39%. Crucially, Selene is close to underutilised Shell owned infrastructure which is linked to the Bacton terminal on the Norfolk coast. It is also drill ready. Drilling has been deferred from our earlier expectation of 2021 to mid-2022. Shell is scheduled to finance 75% of well costs. Deltic estimates its share of well costs at £4.5m.

- **Financials**: Deltic has reported a cash position of £13.2m at end March 2020. We continue to look for cash of about £12m at end FY20 assuming full year G&A of around £1.4m and £0.5m mainly for OGA (Oil and Gas Authority) licence costs with minimal additional project outlays. Based on the drilling scenario indicated above and similar rates of G&A and ongoing licence related expenditure end year 2021 cash would decline to £6.2m. We forecast modest net debt of £0.22m for FY22, assuming Selene drilling.

- **Valuation:** We are leaving our valuation estimates unchanged from our January 2020 note. Our GCOS valuation across the portfolio is £116m or 8.3p/share. In a success case for the three most advanced projects Pensacola, Selene and Dewar our valuation is £234m or 16.7p/share. This reflects a farm down to 50% for the Dewar working interest and a valuation quotient of $5.0/boe. Our valuations assume a more favourable commodity price backdrop than presently prevailing.

Year End: 31 December (£'000)	2018	2019	2020E	2021E	2022E
PBT	(1,659)	(2,360)	(1,401)	(1476)	(1,528)
EBITDA	(1,532)	(1,589)	(1,443)	(1,468)	(1,520)
NET OP. CASH FLOW	(1,523)	(1,413)	(1,347)	(1,372)	(1,399)
NET CASH	1,426	13849	12057	6186	(217))

Allenby Capital acts as Nomad & Broker to Deltic Energy Plc (formerly Cluff) (DELT.L).

Please refer to the last page of this communication for all required disclosures and risk warnings.

Other assets

P2352 (Dewar): Deltic has a 100% working interest in P2352 which is situated in the CNS (Central North Sea) Graben, a prolific oil and gas condensate producing zone. It contains the Dewar Forties sandstone liquids prospect about 240 km east of Aberdeen. Dewar has significant P50 resources of 39.5mm barrels and is relatively low-risk with GCOS (geological chances of success) of 39.5%. It is located in close proximity to the BP-operated Marnock-Skua field and the ETAP (East Trough Area) infrastructure. Industry reports suggest ETAP reserves of over 500mm boe. High quality 3-D seismic has been shot over Dewar and all work commitments on the licence have been undertaken. According to Deltic, Dewar is drill ready. Water depths are modest at about 90m so a jack-up rather than a more expensive semi-submersible rig can be used for drilling. Deltic puts the dry-hole costs at £17-20m gross.

Deltic commenced a farm-out process for Dewar in July 2019. Significant interest has been shown by established operators and the Company remains in dialogue with a number of parties. In the current commodity price environment, however, Deltic believes that a commercially attractive farm-out deal is unlikely to be struck, at least in the short-term. Given the proximity to infrastructure and assuming resources of around 40mm barrels, Dewar's economics could be attractive as oil prices recover from current depressed levels. Interestingly, Deltic has indicated it is attempting to increase its CNS exposure through its 32nd Round licence applications.

P2428 (Cupertino) and P2424 (Cortez): Deltic has a 100% working interest in P2428 and P2424 which are located in the SE-NW trending Carboniferous sandstone fairway towards the northern boundary of the SNS gas basin. The zone is also prospective for overlying Permian Leman sandstone and Zechstein carbonate reef plays and Triassic sandstones. The fairway contains some of the largest gas fields in the SNS such as Breagh (Ineos), Pegasus (Spirit Energy) and Cygnus (Spirit Energy) with reserves of 500 bcf plus.

P2428 lies about 60 km northeast of Breagh and a similar distance north of Pegasus. It contains the Cupertino structural lead. Initially the targets are Carboniferous sandstone and Zechstein carbonate reef reservoirs. The current P50 resource estimate for P2428 is a highly significant 820 bcf and the GCOS is 27%, a moderate risk factor at this relatively early stage of exploration. Deltic believes that P2428 has multi-tcf resource potential. In the second half of 2019 Deltic reprocessed legacy 2-D seismic and has been appraising prospectivity.

P2424 lies immediately to the east of the Breagh field and contains the Cortez Carboniferous sandstone lead. The licence also contains a Triassic Bunter sandstone prospect and a technical discovery. Currently Deltic P50 resource estimate for P2424 is 656 bcf while the GCOS is 31%. As for P2428, Deltic believes that P2424 could have multi-tcf resource potential. Deltic commenced a legacy 2-D seismic reprocessing exercise in April 2020 with results expected in September 2020.

The company has indicated that licences P2428 and P2424 have already attracted significant interest from E&P concerns. This, we believe, is indicative of the location close to major sources of production and successful exploration activity. Subject to seismic evaluation work supporting hypotheses on exploration prospectivity, Deltic is planning a farm-out programme for P2428 and P2424 in late 2020. Following the completion of 2-D seismic reprocessing, licence work commitments on the two licences will have been satisfied.

P2435 (Blackadder): Deltic has a 25% working interest in the Parkmead operated P2435. The licence is located in the heart of the SE-NW trending Leman sandstone fairway approximately 50 km due west of P2437 (Selene). It contains the Blackadder prospect and the Bob technical discovery. All work commitments were completed on P2435 in 2019. In line with its policy of assigning resources to high priority projects such as Pensacola and

Selene, Deltic has announced that all discretionary spending relating to P2435 has been deferred or cancelled for the time being.

Strategy

Since the inception of Cluff Natural Resources, Deltic has had an exploration focus primarily in the SNS gas basin. Interestingly, in its recent operational update Deltic has indicated that it is considering acquiring non-operated oil producing assets in the North Sea. The catalyst for this new strategic thrust is the investment opportunities that could conceivably arise from the currently depressed commodity price backdrop. Potentially, major operators could accelerate the disposal of perceived marginal assets in the current circumstances. Deltic's aim would be to secure a source of cash flow to support the financing of exploration activity.

Conceptually, we believe, the strategy of acquiring preferably long-life assets (no near-term dismantling costs) in a mature basin such as the North Sea is plausible. Assuming no major capital commitments other than for routine maintenance, such oil assets can be very cash generative. Typically, the variable costs of production and transportation to an on-shore terminal are modest even in relation to the currently depressed Brent price of about $40/barrel. The problem perhaps for a buyer is acting quickly enough before commodity and asset prices have recovered to more normal levels.

Cost cutting measures

In the light of the depressed commodity price environment and the ongoing Covid-19 crisis, Deltic has undertaken a review of its G&A overhead and project spending. The key objective is to ensure that the financing of its priority projects, Pensacola and Selene, is comfortably underpinned. The review resulted in the following actions:

- A review of the entire asset portfolio resulting in investment only in core projects.
- Deferral or cancellation of expenditure in non-core projects requiring third party support.
- Deferral of contingent work programmes related to technical and commercial studies requiring external consultants. The exception is work related to Pensacola and Selene.
- Reduction of headcount and removal of all retained contractors.
- Reduction of staff budgeted costs.
- Exercise of a break clause on the lease of the Westminster corporate office and relocation from end May to smaller, lower cost space in Waterloo.

Deltic has indicated that the above has resulted in a 25% reduction in G&A and investment related spending compared with the 2020 budget. According to the company, cash expenditure on this basis in 2020 is now expected to be below £2m. Our forecast for 2020 is £1.85m reflecting £1.34m for the operational outflow and £0.51m for OGA licence costs. Additional project-related outlays will be minimal.

Cash position

At end 2019 Deltic reported a cash position of £13.85m. During the first quarter of 2020 there was an outflow of £0.65m to £13.2m, according to the company. Over the balance of the year we would expect a significant decline in the monthly outflow reflecting cost-cutting measures and policy decisions to reduce project-related expenditure. Our end 2020 cash forecast is £12.06m which is slightly higher than that given earlier in 2020 of £12.02m. Assuming that Pensacola and Selene are drilled as intimated by Deltic, we would expect to see cash fall to £6.19m by end 2021 while at end 2022 we believe a swing to a modest net debt position is possible. We forecast one of £0.22m. Our cash flow forecasts reflect the following:

- Annual operational cash outflows of £1.3-1.4m
- Deltic's share of well costs of £4m for Pensacola and £4.5m for Selene in line with company indications. Note regarding Selene, Deltic benefits from an element of free-carry given that its working interest in the project is 50%.
- Project-related expense in addition to the two Shell joint-venture wells of approximately £0.5m pa mainly for OGA licence costs with minimal additional project outlays.

Our 2022 forecast of modest end year net debt of £0.72m is consistent with Deltic's indication that it potentially has sufficient cash to finance its share of two exploration wells through mid-2022.

Commodity prices

International oil and gas prices plunged to multi-year lows in both nominal and real terms in April/May 2020. This reflected slumping demand in response to public policy measures around the globe to shut-down the market economy in the wake of the Covid-19 crisis and lagging supply trends. During April, Brent plumbed a low of $9.1/barrel on 21st after having traded at about $70/barrel at the beginning of 2020. It should also be noted that the former was considerably below the $34/barrel low that Brent traded in late 2008 at the height of the then financial crisis. The UK benchmark NBP (National Balancing Point) gas price was trading at about 12p/therm in April and dropped to under 10p/therm ($0.75/boe) in May. Since the recent lows, prices particularly for oil, have climbed with Brent reaching over $40/barrel in early June. Towards mid-June the NBP benchmark had recovered modestly to about 12p/therm.

While operators can generate cash operationally at $40/barrel Brent this is not the case for gas producers at current prices. Significantly for Brent and especially the NBP the forward curves are in contango with futures prices higher than spot. The NBP futures curve is, in fact, in contango for all dates through the mid-2020s with a seasonal peak at this time of around 45p/therm. The Brent forward curve shows prices at the backend in the mid 2020's of about $52/barrel.

Arguably, the trend in the forward curve is more important for assessing project viability than the spot price. The contango in the forward curves for both Brent and the NBP reflects the assumption of a return to normal demand patterns as Covid-19 restrictions on the market economy are relaxed and ultimately lifted and actual and potential constraints on supply of ultra-depressed commodity prices. Supply constraints are not simply a function of investment cutbacks but also the increasing marginalisation of existing production capacity following an extended period of historically depressed prices and weak economics. In the case of the Southern North Sea gas basin we know that on both sides of the east/west divide production is in secular decline as indeed it is in the giant on-shore Groningen gas field in the Netherlands. There is the potential for a widening gas supply deficit emerging in the southern North Sea basin in the coming years, although this could admittedly be filled by more long-distance supplies of pipeline gas from central Asia and the Norwegian Sea and LNG.

Our expectation for the balance of 2020 is for crude oil prices to trend higher. This reflects the market moving into deficit as demand continues to gather momentum as major economies return to the semblance of normality and supply lags due in part to the OPEC+ production accord and in part cutbacks induced by adverse economics in North America and elsewhere in the world. The historically large inventory position will, however, probably slow the pace of recovery. We look for Brent to average $39/barrel in 2020 and $50/barrel in 2021. In the case of the NBP price, we also see this trending higher in 2020 and 2021, albeit from a very depressed level. Our average price forecasts for these two years are 23p/therm and 35p/therm respectively. A key issue for the NBP price near to medium term is the availability of foot loose LNG in the North Sea basin.

Risks

We see the key risk surrounding Deltic at this juncture as being an extended period of historically depressed oil and gas commodity prices resulting in a deferral of Shell's drilling plans. The most likely reason for such a development would be a continuation of the Covid-19 pandemic in virulent form into 2021 and 2022. This would clearly have bearish implications for energy demand and the supply-demand balances for oil and gas. Futures curves could be markedly flatter than at present thereby reducing the attraction of investment in long cycle projects.

Partially mitigating uncertainty over commodity prices, particularly in the case of Selene, is Shell's availability of infrastructure in close proximity to the potential project. This relates to the Clipper gas gathering platform and associated pipeline network. The gas processing terminal a Bacton on the Norfolk coast which is linked to Clipper and operated by Shell also has spare capacity. The upshot is that from an offshore gas field development perspective Selene, could offer attractive economics assuming that any discovery has sufficient critical-mass at prevailing prices towards the back-end of the futures curve. It might also be added that without development of new fields in the Leman fairway Shell could be faced with major expense related to decommissioning offshore facilities.

Name change

At the AGM on June 4, 2020 the company name was changed from Cluff Natural Resources to Deltic Energy Plc (DELT: AIM). The name change reflects the evolution of the company from early stage exploration to a more operational phase associated with drilling activity. Owing to Covid related delays, Deltic has yet to receive the relevant certificate with the new name from Companies House. Until this occurs the company will continue to be called Cluff Natural Resources for legal purposes.

Exhibit 1: Deltic Energy risked valuation summary

	Working interest post farm-in	Net un-risked P50 resources		Net risked P50 resources		Valuation quotient	Un-risked valuation	Risked valuation adj for working interest		
Project	%	bcfe	mmboe	bcfe	mmboe	$/boe	$m	$m	£m	p/share
SNS licence P2252	30	157	26	47	8	2.5	65.4	19.4	15.2	1.1
SNS Licence P2437	50	193	32	77	13	2.5	80.4	32.2	25.2	1.8
SNS P2424, P2428	50	738	123	214	36	2.0	246.0	71.4	55.7	4.0
SNS P2435	25	34	6	18	3	2.0	11.3	6.1	4.7	0.3
CNS 30th Round licences P2352	50	119	20	47	8	2.5	49.4	19.75	15.4	1.1
Total		**1240**	**207**	**404**	**67**		**452.4**	**148.8**	**116.3**	**8.3**

Source: Allenby Capital. Exchange rate: US$1.28; Conversion: 6000 cf/boe

Note: Working interests for P2252 and P2437 are post the Shell farm-outs.

Working interest for P2435 is actual as of June 2019

Working interests for P2424, P2428, P2352 assume a farm-down from 100%

Per share calculation based on 1,405.96 shares in issue

Exhibit 2: Valuation success case

	Working interest post farm-in	Net un-risked P50 resources		Valuation quotient	Net un-risked valuation		
Prospect	%	bcfe	mmboe	$/boe	$m	£m	p/share
Pensacola	30	93	15.5	5.00	77.5	61	4.3
Selene	50	146	24.3	5.00	121.3	95	6.8
Dewar	50	118.5	19.8	5.00	98.8	78	5.5
Total		**357**	**59.5**		**297.5**	**234.3**	**16.7**

Source: Allenby Capital, Exchange rate: US$1.28; Conversion: 6000 cf/boe

Note: Dewar working interest assumes a farm-down from 100%, working interests for Pensacola and Selene are post the Shell farm-outs, per share calculation based on 1,405.96m shares in issue, Dewar per share not diluted for CLNR share of drilling costs.

Exhibit 3: Summary financials: Year end 31 December (£000s)

INCOME STATEMENT	2017	2018	2019	2020E	2021E	2022E
Administrative Expenses	(1,592)	(1,661)	(1,709)	(1,451)	(1,476)	(1,528)
Impairment charge	0	1	(801)	0	0	0
Operating Profit	(1,592)	(1,660)	(2,510)	(1,451)	(1,476)	(1,528)
Finance Income/other	1	1	150	50	0	0
PBT	(1,590)	(1,659)	(2,360)	(1,401)	(1,476)	(1,528)
Taxation	-	-	-	-	-	-
Net Income	(1,590)	(1,659)	(2,360)	(1,401)	(1,476)	(1,528)
Comprehensive Loss	(1,590)	(1,659)	(2,360)	(1,401)	(1,476)	(1,528)
EBITDA	(1,473)	(1,532)	(1,589)	(1,443)	(1,468)	(1,520)
Avg. Shares Basic (m)	343.9	475.4	979.6	1,406.0	1,406.0	1,406.0
EPS (report) p	(0.46)	(0.35)	(0.24)	(0.32)	(0.10)	(0.11)

CASH FLOW	2017	2018	2019	2020E	2021E	2022E
Net Loss for the year	(1,590)	(1,660)	(2,360)	(1,401)	(1,476)	(1,528)
Change in receivables	54	7	(17)	30	0	0
Change in payables	(10)	2	21	(24)	0	0
Depreciation	5	8	120	8	4	4
Other	0	(2)	651	(50)	0	0
Share Based Payments	114	122	172	100	100	125
Net Operating cash flow	(1,428)	(1,523)	(1,413)	(1,337)	(1,372)	(1,399)
Acquisition of PPE	(2)	(10)	(6)	(5)	(3)	(3)
Exp and Eval assets additions	(224)	(665)	(896)	(500)	(4,500)	(5,000)
Other	1	0	(80)	50	0	0
Proceeds from farm-out			470	0	0	0
Proceeds from issue of shares	962	2,607	14,348	0	0	0
Net cash flow	(691)	409	12,423	(1,793)	(5,875)	(6,402)
Net cash/(debt)	1,017	1,426	13,849	12,057	6,186	(217)

BALANCE SHEET	2017	2018	2019	2020E	2021E	2022E
Intangible assets	775	1617	1128	1623	6119	11119
Property, Plant & Equipment	4	12	47	49	48	48
Other	54	0	0	0	0	0
Total Non-Current Assets	833	1,629	1,175	1,672	6,167	11,167
Receivables	89	82	130	100	100	100
Cash & Cash Equivalents	1,017	1,426	13,849	12,057	6,186	500
Total Current Assets	1,106	1,508	13,979	12,157	6,286	600
Total Assets	1,939	3,137	15,154	13,829	12,454	11,767
Non-Current Liabilities	0	0	0	0	0	0
Trade payables	112	269	173	175	175	175
Other payables	100	127	26	0	0	0
ST debt	0	0	0	0	0	717
Current Liabilities	213	396	199	175	175	892
Total Liabilities	213	396	199	175	175	892
Net assets	1,727	2,741	14,956	13,654	12,279	10,876
Net cash/(debt)	1,017	1,426	13,849	12,057	6,186	(217)
Shareholder Equity	1,727	2,795	14,956	13,654	12,279	10,876
Total Equity & Liabilities	1,939	3,191	15,154	13,829	12,454	11,767

Source: Company and Allenby Capital

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