

# Sun Resources

# SUR

LOW RISK BY-PASSED OIL IN COASTAL LOUISIANA

## Capital Structure

| ASX Code: SUR  |                   |
|----------------|-------------------|
| Shares         | 756 m.            |
| Options        | 589 m. @ 0.9cts   |
| Con note       | \$ 1 m.           |
| Price          | \$ 0.40 cts / shr |
| Market Cap     | \$ 3.0 m.         |
| Net cash (est) | -\$ 0.9 m.        |
| EV (est)       | \$ 3.9 m.         |
| EV/2C          | \$ 9.8 per boe    |
| EV/2C + Pros   | \$ 3.3 per boe    |

Source: Strachan Corporate

## Valuation Metric

| Asset                | Value          |               |
|----------------------|----------------|---------------|
|                      | Success        | Risked        |
|                      | \$m.           |               |
| Bowsprit             | 5.4            | 2.9           |
| Bowsprit Prospective | 12.2           | 3.0           |
| Net Cash             | (0.9)          | (0.9)         |
| ITM Options          | 1.2            | 1.2           |
| New Issue            | 1.0            | 1.0           |
| Corporate            | (1.2)          | (1.2)         |
| <b>TOTAL</b>         | <b>\$ 17.8</b> | <b>\$ 6.0</b> |

Source: Strachan Corporate

## Board

|                 |                   |
|-----------------|-------------------|
| Ian McCubbing   | Chairman          |
| Alex Parks      | Managing Director |
| William Bloking | Non-Exec Director |

## Opinion

Sun holds strong valuation leverage to success at the Bowsprit oilfield re-develop project in shallow, Gulf of Mexico coastal waters where ~1 mmboe of Contingent Resources plus a further 2 mmboe of Prospective Resources has been estimated.

Sun has a 50% WI but may farm-down to 30%-35% for funding.

Use of horizontal well completion technology could see initial production of 2,000 bbls per day of premium grade light crude, with success delivering substantial cash flow over a 3-7 year operating life.

Peter Strachan

## Investment Drivers

- ◆ **MODERATE RISK OILFIELD RE-DEVELOPMENT:** The Bowsprit oil project involves redevelopment of ~1 mmboe of estimated Contingent Resources and assessment of +2 mmboe of Prospective Resources. With a market capitalisation of ~\$3 million, Sun's 50% working interest (WI) in the project offers considerable financial leverage to success. Strachan Corporate assesses a potential net present value of over \$25 million to Sun's current 50% WI in the event of success and a current risked value of \$6 million for Contingent and Prospective Resources after farming down to fund appraisal.
- ◆ **FUNDING FLEXIBILITY WITH STRONG EQUITY POSITION:** Sun has capacity to farm-out project equity for funding, retaining a significant 30% to 35% exposure to the project.
- ◆ **LOW COST, COASTAL WATERS LOCATION:** The Bowsprit project is located close to transport and production infrastructure in coastal waters of <4 metres depth. Based on measured reservoir characteristics and the performance of nearby wells, the company's consultants estimate that barge-mounted drilling of a new well with 450 metres of horizontal completion should initially flow at 2,000 BOPD and produce ~650,000 bbls of oil over three years at an all-up capital cost of below US\$15/bbl.
- ◆ **LEVERAGE TO PROSPECTIVE RESOURCE:** Assuming Sun farms-out 35% of its WI at Bowsprit, Strachan Corporate estimates that a Prospective Resource of 1 mmboe has a success value of \$12.2 million and a risked value of \$3 million assuming a 35% probability of success. At its current WI level, the stock has an EV of just \$2.60 per boe of 2C+Prospective Resource, which might be seen as half fair value.
- ◆ **RAPID PAYBACK:** Modelling of possible Bowsprit production by the company indicates that a well would produce net free cash flow of A\$31 million over three years. If it retains a 33% WI after funding, Strachan Corporate estimates that Sun would achieve net income of ~\$10 million from one well.
- ◆ **EXPERIENCED MANAGEMENT:** The company is led by a new team with a strong resource industry background.



Source: Sun

## Background

*Reenergised with low cost oil project*

Sun Resources has acquired a 50% working interest (WI) in a joint venture over permits in the Breton Sound, 70 kilometres south of New Orleans in coastal water depths of 2-4 metres. The company is in joint venture with Singapore based company Pinnacle Exploration Pte Ltd.

*New Board & management*

Sun Resources consolidated its shares and has strengthened its Board with the appointment of experienced oil & gas professionals. The company now aims to establish a strong cash flow at a low cost oil operation from which it can leverage into the many opportunities that have arisen following three years of weak oil and gas pricing and development activity.

## Breton Sound Bowsprit Lease 50% WI

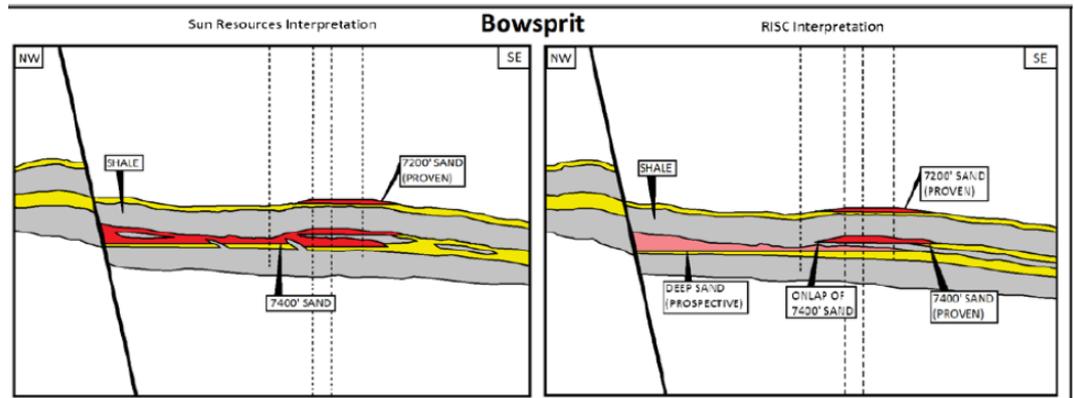
*Low cost operating environment for by-passed oil*

The Breton Sound region is estimated to have produced over 134 mmbbls of oil and 650 Bcf of gas, largely from deeper sediments over about 35 years up until the late 1990's. In earlier times, thin shallower zones with oil & gas were considered sub-commercial with technology then available and at commodity prices prevailing up until production ceased in 1998.

*Estimated 18 mmbbls of oil initially-in-place at Bowsprit structure sets up-side target for 4.5 mmbbls of recoverable oil*

Interpretation of modern 3D seismic data indicates sands that vary in thickness between 6 and 16 metres at 2,195 metres (7,200 sand) and 2,256 metres (7400 sand).

### Sun's Bowsprit reservoir interpretation



*Significant up-dip Prospective oil target seen on modern 3D data*

Gas in the shallower 7200 sand is obvious on seismic data and conforms to a hydrocarbon trap which is interpreted to indicate the presence of gas, possibly over oil and water. This shallower sand has an estimated 2C gas potential of 0.2 Bcf to Sun's WI, contingent on deliverability from a horizontal well completion. A fault to the north uplifts the underlying 7400 sand to the level of the 7200 sand. The 7400 sand is the project's primary focus. It has previously produced oil from vertical wells and abuts a thick shale sequence at a defining fault to the north. Sun interprets the broader 7400 sand to be an inter-bedded zone of two major sands and shales. The 7400 sand is interpreted to hold total 2C oil of just under 1 million barrels plus gas, which is 0.38 mmbbls of oil plus 0.42 Bcf of gas to Sun's account, again contingent on deliverability via a horizontal well completion.

*Re-development of proven, conventional light sweet oil from good quality reservoir*

The project also has strong exploration appeal. Total interpreted Best Prospective oil plus estimated Contingent Resources amount to 2.33 mmbbls of oil plus gas, with Prospective Resources to Sun's account amounting to 0.86 mmbbls of oil plus 0.83 Bcf of gas in the 7400 sand, with upside to 3 mmbbls of oil plus 4.4 Bcf of gas to Sun's account.

*Estimated breakeven oil price of US\$30/bbl*

Sun and its partner plan to drill a well with a 450 metre horizontal section to test flow rates. JV partners estimate an all-up cost of US\$3.2 million for an initial appraisal well, with subsequent development wells estimated to cost US\$3 million each.

*Horizontal well completion should significantly enhance oil flow rate*

Given an estimated high average reservoir porosity of 25% to 30% and permeability of 50-150 milli-Darcy, the company estimates that with an appropriate well completion, an initial flow rate of over 2,000 BOPD from each well is possible, delivering an estimated ultimate recovery of ~650,000 barrels from an individual well.

## Bowsprit Resources

Targeting 1.5 mmboe & up to 4.8 mmboe

| SUN's WI             | 1C         | 2C          | 3C          |       |
|----------------------|------------|-------------|-------------|-------|
| Contingent           | 0.06       | 0.49        | 1.07        | mmboe |
|                      | <b>Low</b> | <b>Best</b> | <b>high</b> |       |
| Prospective          | 0.06       | 1.00        | 3.78        | mmboe |
| C'gent & Prospective | 0.12       | 1.48        | 4.85        | mmboe |

Source: Sun & RISC

Assessment of Continent Resources and Prospective upside will narrow once data from an initial appraisal-development well has been delivered.

Sun sees potential to install up to five development wells at a cost of ~US\$15.3 million with initial production from each, constrained to 1,000 BOPD to extend field life. Bowsprit partners control the structure's peak, from which all of the oil in the trap is accessible, enabling production of over 3.5 mmbbls of oil from a structure that extends beyond the permit boundaries into open ground that other companies are unlikely to lease.

## SWOT Analysis

### Strengths

**SMALL AND NIMBLE:** Sun is unencumbered by a large corporate structure and can move swiftly to capture opportunities.

**LOW COST PROJECT CLOSE TO MARKET AND SERVICES:** The Bowsprit project has potential to be a low cost and high yielding project employing horizontal drilling in relatively thin, a conventional reservoir with premium crude product.

**APPLICATION OF NEW WELL COMPLETION TECHNOLOGIES:** Sun's focus on conventional reservoirs and the application of off-the-shelf, modern drilling and completion technologies in a low cost environment appear more likely to succeed than a focus on unconventional resources.

**LOW DRILLING COST:** Use of low cost, niche barge drilling rig has limited exposure to rig rate increases.

### Weaknesses

**UNDERFUNDED:** Sun will need to attract funding to support both project development and its corporate working capital.

**OVERCOMING PREVIOUS PERFORMANCE:** Even though Sun has been completely restructured, existing shareholders may remain stale bulls.

### Opportunities

**LACK OF RECENT CAPEX:** Three years of falling capital expenditure in the oil and gas business, along with a focus on unprofitable unconventional projects has left plenty of conventional project development opportunities open for junior companies.

### Threats

**GEOLOGICAL & ENGINEERING:** Risks associated with drilling and well completion as well as uncertainties surrounding geology will always come into play for resource development.

However, field has flowed oil previously and engineering risk is mitigated by use of standard technology.

**COMMODITY PRICING:** The price of oil and gas is out of the company's control but project break-even oil price is low.

## Valuation

Premium grade oil attracts US\$3 premium to WTI

Oil from this location will attract a premium of about \$3/bbl above the prevailing WTI crude marker price so that after transport costs, the received price should reflect the WTI marker price.

State royalty is levied at 21% and severance tax of 12.5% is charged after the project recoups its drilling costs.

### Risked Valuation matrix

| Prospect                    | Holding |     | Target |       | Total Value | SUR Value | Risk Cost | SUR Value | Risked Value |        |
|-----------------------------|---------|-----|--------|-------|-------------|-----------|-----------|-----------|--------------|--------|
|                             | %       | Rtn | Gas    | Oil   |             |           |           |           |              |        |
|                             | Now     |     | Bcf    | mmbbl | A\$m        | cts/shr   | \$m       | \$m.      | cts/shr      |        |
| <b>Bowsprit 2C</b>          | 50%     | 33% | 0.4    | 0.4   | 5.4         | 0.45      | 70%       | 0.9       | 2.9          | 0.24   |
| <b>Bowsprit Prospective</b> | 50%     | 33% | 0.8    | 0.9   | 12.2        | 1.02      | 35%       | 1.3       | 3.0          | 0.25   |
| <b>Net Cash</b>             | 100%    |     |        |       | (0.9)       | (0.07)    |           |           | (0.9)        | (0.07) |
| <b>ITM Options</b>          |         |     |        |       | 1.2         | 0.10      |           |           | 1.2          | 0.10   |
| <b>New Issue</b>            |         |     |        |       | 1.0         | 0.08      |           |           | 1.0          | 0.08   |
| <b>Corporate</b>            |         |     |        |       | (1.2)       | (0.10)    |           |           | (1.2)        | (0.10) |
| Source: Strachan Corporate  |         |     |        |       | \$17.8      | 1.48      | 2.2       | \$6.0     | 0.50         |        |

*\$3.9 m worth of 1 cent options may be attractive if project performs as the company intends*

Risked valuation estimates assume insitu values of US\$16/bbl and US\$0.55/Mcf for 2P oil and gas respectively from this project and an AUDUSD of 0.755. Strachan Corporate estimates a 70% probability of converting Contingent Resources into Proven and Probable Reserves and assigns a 35% probability of successes to the project's Best Prospective Resources estimate.

Whilst currently out of the money, 192 million options converting at 0.6 cents in May 2019 are assumed to be taken up on the back of a future capital raising initiative and the JV's ability to attract a farm-in partner, willing to acquire at least a 34% interest in the project on a promoted basis.

## Board & Management

### Chairman

#### Ian McCubbing

Ian was appointed to the Board as a Non-Executive Director and Chairman in October 2016. He is a Chartered Accountant with more than 30 years' corporate experience, including as an investment banker.

He has extensive experience working with ASX 200 and other listed companies in senior finance roles. He is currently a Non-Executive Director of Avenira Limited, Swick Mining Services Limited, and is Chairman of Rimfire Pacific Mining NL.

### CEO & Managing Director

#### Alexander Parks

Alex has served as Director since February 2016. He has over 20 years' of experience in the oil and gas industry, commencing as a petroleum engineer with RPS Energy Australia in 1997. Alex has managed companies and projects in Australia, SE Asia, North America, New Zealand, Europe, FSU and North Africa, including onshore and offshore exploration, development, production and significant new ventures and transactions.

Alex has a Petroleum Engineering degree from Imperial College, London,

is a member of the Society of Petroleum Engineers (SPE), is a Member of both the Petroleum Exploration Society of Australia (PESA) and Australian Institute of Company Directors (GAICD). He is currently a Director of Tamaska Oil & Gas Ltd and he has previously held the positions of Chief Commercial Officer at Cue Energy Resources Ltd, CEO of Mosaic Oil NL, CEO of Otto Energy Ltd and Technical Director at RPS Energy.

### Executive Director

#### William Bloking

William is an energy industry professional with more than 40 years of experience in the oil and gas industry. He was previously President, Australia Asia Gas, for BHP Billiton Petroleum and prior to joining BHP Billiton he served in a number of senior executive roles in the USA, South America, Europe and Asia for ExxonMobil. He is currently Non-Executive Chairman of Nido Petroleum Limited and Torrens Mining Limited and he is a Non-Executive Director of Challenger Energy Limited. He has a Bachelor's Degree in Mechanical Engineering (Summa cum Laude) from the University of South Carolina in the USA and is a citizen of both the USA and Australia.

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