Rialto Energy: Reviving the gazelle

Market Cap: $280mm

RIA AU / LN – NR
£0.25
3-May-2012

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Company overview: Rialto Energy is an Australian and UK AIM listed E+P with assets in Côte d'Ivoire, Australia and potentially Ghana. Its principal asset is the CI-202 block in Cote d'Ivoire, where it has an 85% interest (pre government back-in). The block contains 4 under appraised discoveries, namely: Gazelle, Hippo, Bubale and Addax, with total contingent resources of 116mmboe. Rialto is working to convert the contingent resources to 2P reserves, starting with 55mmboe associated with the Gazelle discovery, with a view to developing the field and achieving first production by end-2013 or early 2014. The company could potentially tie-in the other discoveries to the Gazelle production facilities, allowing for rapid monetisation. In addition to offering development opportunities, Block CI-202 also offers exploration upside, with 811mmboe of prospective resources identified. Rialto also has a 12% interest in the WA-399-P shallow water permit, offshore Western Australia, where it may participate in drilling the 42mmboe Gazelle oil prospect later this year. A discovery could unlock £0.05/sh of value. Ghana could be a game changer for Rialto; the company is currently seeking ministerial approval which will allow it to take ownership of a 20% interest in the deepwater Accra block. If granted approval, Rialto could participate in drilling a 500mmboe "Jubilee" type prospect called Starfish in 3Q12. We do not give Rialto any value for the prospect; however a discovery could be worth £0.66/sh on an unrisked basis. We expect ministerial approval to be granted or refused imminently. With a $90mm cash balance, Rialto is adequately funded for its near term work programme. We expect the company to fund the Gazelle development, which we estimate will cost $400mm, and future related work programmes in Côte d'Ivoire through a combination of a farm-out, debt facility and / or an equity offering.

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Rialto Energy

Net Asset Valuation ($ mm)	Value ($mm)	Per share	Per Share
Cash	$90	£0.08	A$0.11
Back cost provision (Ghana farm-in)	-$15	-£0.01	-A$0.02
Options	$22	£0.02	A$0.03
IFC convertibles	$8	£0.01	A$0.01
Working Capital	-$8	-£0.01	-A$0.01
1P: Net Asset Value	**$98**	**£0.08**	**A$0.12**
Unbooked but discovered assets slated for development:			
Côte d'Ivoire - Gazelle	$154	£0.13	A$0.19
2P: Booked + Unbooked value	**$252**	**£0.22**	**A$0.32**
Exploration potential:			
Côte d'Ivoire - Chouette / Hippo North	$25	£0.02	A$0.03
Côte d'Ivoire - Hippo / Bubale / Addax	$258	£0.22	A$0.32
Australia - WA-399-P	$6	£0.01	A$0.01
3P: Booked + Unbooked + Exploration value	**$542**	**£0.46**	**A$0.68**
New development:			
Total 4P Unrisked			
4P: Booked, development, exploration, and new development:	**$862**	**£0.74**	A$1.08
Diluted Shares		764	
	$/£	1.53	
	$/A$	1.04	

Investment points: Rialto trades at £0.25/sh versus our 3P NAV of £0.46/sh (85% upside) and our 4P NAV of £0.74/sh. Our un-risked 3P NAV is £1.36/sh.

- **Fast track development:** Rialto is working to appraise and develop the 55mmboe (24% oil) Gazelle discovery. It expects first production by the end of 2013/early 2014 (25mboepd at peak production), following an ongoing 2 well appraisal programme.
- **Low cost development:** The Gazelle platform is to be designed with sufficient spare capacity (32mboepd nameplate), which will allow the company to tie-in the nearby Hippo, Bubale and Addax discoveries with minimal incremental capex.
- **Exploration upside:** Rialto has identified 811mmboe of prospective resources across 14 prospects on the CI-202 block. The company will drill the 91mmboe Chouette prospect (25% CoS) in 3Q12, which could unlock £0.31/sh of value.
- **Fully funded for near term work:** With $90mm of cash, Rialto is funded for its near term work programme, comprising 3 firm wells in Côte d'Ivoire.
- **Strong management team:** Rialto is managed by a strong team of professionals. Furthermore, members of the team have operational experience and relationships in West Africa, which could be leveraged in the development of the Gazelle field.

Catalysts

- **Flow tests**: Rialto is drilling 2 wells to appraise the Gazelle discovery. Drilling was halted on the first well, to rectify a mechanical problem, and has since resumed. We expect results by mid-June; a flowrate >2.5mboepd will be positive.
- **Gazelle reserves:** A successful appraisal programme will allow Rialto to initially convert 55mmboe of contingent resources associated with the Gazelle discovery to 2P reserves. We would expect the reserves to be certified by 3Q12.
- **Further reserves**: Rialto may also be able to convert 61mmboe of resources associated with the Hippo, Bubale and Addax discovery to reserves if it submits a field development plan and is granted an exploitation permit by the government.
- **Gas sales agreement**: We expect Rialto to finalise a gas offtake agreement with the government of Côte d'Ivoire in 2Q12. Providing certainty that gas produced from Gazelle will be monetised.
- **FEED award and completion**: We expect Rialto to award a FEED contract for the Gazelle field development in 2Q12. The FEED should take at least 3 months to complete.

Important Disclosures start at page 5 of this report

- **Farm-down:** A farm-out to a well-funded partner will reduce Rialto's $400mm (TPHe) capex requirement and increase confidence in the development plan. We expect Rialto to complete a farm-out, after the FID, in 3Q12. We believe a company such as Dragon Oil (DGO LN – A) would be a good fit.
- **Debt raise**: A combination of a gas sales agreement and certified 2P reserves will make the Gazelle project suitable for debt financing. Rialto has initiated discussions with "reserve base lenders"; a decision could be made by September.
- **Ghana option:** Rialto is working to secure ministerial approval which will allow it to take a 20% interest in the Accra block, offshore Ghana. If approved, Rialto could participate in drilling a 500mmboe prospect in 3Q12, potentially worth £0.66/sh.
- **Chouette prospect**: Rialto will be drilling the 91mmboe oil prospect in Côte d'Ivoire in 3Q12, a discovery could unlock up to £0.31/sh of value.
- **Australia Well**: Rialto may also participate in the 42mmboe Gazelle well, offshore Australia. Success could unlock £0.05/sh of value.

Risks

- **Gas commercialisation:** Although Rialto and the government of Côte d'Ivoire have signed a MoU on gas commercialisation, the parties are yet to sign a binding gas sales agreement. This is an important element in the Gazelle field development, given the high gas content (76% gas) associated with the discovery.
- **Future funding:** Rialto will need $400mm to develop the Gazelle field. This leaves the company at the mercy of the capital markets, debt providers and / or potential farm-in partners, which may provide funding under unfavourable terms. We use a 50% chance of commercialisation to factor this into our valuation.

3P NAV sensitivity to oil and gas price

Gas Price Variation ($/mcf)	Oil Price Variation ($/bbl)						
	$80.00	$90.00	$100.00	$110.00	$120.00	$130.00	$140.00
$3.00	£0.32	£0.33	£0.33	£0.34	£0.34	£0.35	£0.35
$4.00	£0.41	£0.41	£0.42	£0.42	£0.43	£0.43	£0.44
$5.00	£0.49	£0.50	£0.50	£0.51	£0.51	£0.52	£0.52
$6.00	£0.58	£0.58	£0.59	£0.59	£0.60	£0.60	£0.60
$7.00	£0.66	£0.67	£0.67	£0.67	£0.68	£0.68	£0.69
$8.00	£0.74	£0.75	£0.75	£0.76	£0.76	£0.77	£0.77

Source: TPH

Financial position: In March 2012, Rialto formally concluded an arrangement to receive an equity investment of $20mm from the International Finance Corporation (IFC), a subsidiary of the World Bank. As a consequence Rialto's share count was increased by 63.7mm, bringing the total share count to ~764mm, on a diluted basis. As a result of the new investment, Rialto now has a cash balance to $90mm and is adequately funded for its near term work programme comprising 3 wells in Côte d'Ivoire ($78mm gross – TPHe). We estimate a field development Capex for $400mm and we believe Rialto will be able to obtain the necessary funding through a combination of a working interest farm-out; a reserve based lending facility, secured against the field, and a possible equity offering.

Share performance: Rialto's share price is down 15% year on year to A$0.40/sh. However, the company's share price drifted further downward during the intervening period, reaching a nadir of A$0.24/sh in December 2011, due to the lack of material catalysts. The announcement of the IFC investment, the establishment of definitive work programme and the publication of a revised competent person's report for Block CI-202 in Côte d'Ivoire has focused attention on the name, and this is reflected in the recent performance; Rialto is up 65% year to date.

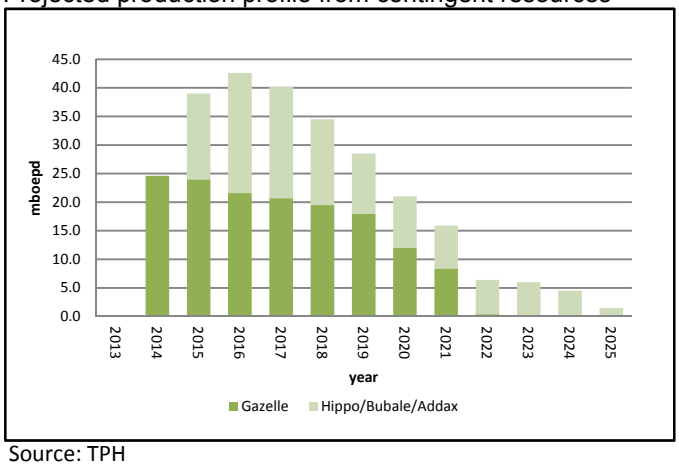
Management: Rialto is managed by a team of experienced industry professionals. Managing Director, Jeff Schrull, has 25 years of industry experience, including 19 years with Chevron. Importantly, he spent 4 years working in West Africa, building Addax Petroleum's business on the continent. The COO, Charles Nieto, is a Petroleum Engineer and has held senior management as well as technical positions at Shell, Enterprise Oil and most recently Stratic Energy. Patrick Garo is the CFO and has over 20 years of experience in the oil and gas space; he was previously the CFO at Perenco. Petroleum geologist, Ian Bulley, is the exploration manager and has worked for a variety of companies including Amoco, Hunt oil, Tullow Oil and Hardman Resources. Dean Criddle is the company's Geophysicist; he spent 16 years working on variety of exploration and development projects for Chevron.

Asset summary

Country	Field	P50 gross reserves	Working interest	P50 WI reserves	EV/bbl (WI) $	Unrisked value $mm	Unrisked value £/share	Geological CoS	Commercialisation CoS	Gross risked dry hole cost	Total risked value $mm	Total risked value £/share	Risked as % of share price	Comments
Core/1P NAV		**n.a**	**n.a**	**n.a**	**n.a**	**n.a**	**n.a**	**n.a**	**n.a**	**n.a**	**n.a**	**n.a**	**n.a**	
Côte d'Ivoire	Gazelle	55	74.0%	41	$9.6	$392	£0.34	89%	50%	$26.0	$154	£0.13	49%	Appraisal programme in progress
Contingent/2P NAV		**55**	**74.0%**	**41**	**$9.6**	**$392**	**£0.34**	**89%**	**50%**	**$26.0**	**$154**	**£0.13**	**49%**	
Côte d'Ivoire	Chouette	91	74.0%	67	$5.3	$358	£0.31	25%	50%	$26.0	$25	£0.02	8%	Drilling in 3Q12
Côte d'Ivoire	Hippo/ Bubale / Addax	142	74.0%	105	$6.5	$681	£0.58	81%	50%	$26.0	$258	£0.22	81%	Discovered resources
Australia	WA-399-P	42	12.0%	5	$11.7	$60	£0.05	25%	50%	$11.7	$6	£0.01	2%	Prospect evaluation / drilling in 2H12
Risked exploration/3P NAV		**275**	**64.5%**	**177**	**$6.2**	**$1,099**	**£0.94**	**60%**	**26%**	**$63.8**	**$290**	**£0.25**	**91%**	
Ghana	Starfish	500	18%	90	$8.5	$766	£0.66	25%	50%	$67.5	$84	£0.07	26%	contingent on farm-in / drilling in 2H12
Côte d'Ivoire	Condor	141	74%	105	$6.5	$679	£0.58	81%	25%	$26.0	$119	£0.10	37%	Drilling in progress (gas prospect)
Côte d'Ivoire	Calao	68	74%	51	$5.3	$269	£0.23	25%	50%	$26.0	$14	£0.01	5%	Drilling in 2013 and beyond
Côte d'Ivoire	Autour	46	74%	34	$5.3	$179	£0.15	25%	50%	$26.0	$3	£0.00	1%	Drilling in 2013 and beyond
Côte d'Ivoire	Aigle	115	74%	85	$5.3	$451	£0.39	25%	50%	$26.0	$37	£0.03	12%	Drilling in 2013 and beyond
Côte d'Ivoire	Impala Updip	22	74%	16	$5.3	$85	£0.07	25%	50%	$26.0	$0	£0.00	0%	Drilling in 2013 and beyond
Côte d'Ivoire	Gazalle Downdip	11	74%	8	$5.3	$43	£0.04	25%	50%	$26.0	$0	£0.00	0%	Drilling in 2013 and beyond
Côte d'Ivoire	Faucon	167	74%	123	$5.3	$656	£0.56	25%	50%	$26.0	$63	£0.05	20%	Drilling in 2013 and beyond
Côte d'Ivoire	Impala Deep	7	74%	5	$5.3	$26	£0.02	25%	50%	$26.0	$0	£0.00	0%	Drilling in 2013 and beyond
Future prospects/4P NAV		**1076**	**48.0%**	**516**	**$6.1**	**$3,154**	**£2.70**	**37%**	**10%**	**$276**	**$320**	**$0.27**	**101%**	
1P														
1P+2P		**55**	**74.0%**	**41**	**$9.63**	**$392**	**£0.34**	**89%**	**50%**	**$26**	**$154**	**£0.13**	**49%**	
1P+2P+3P		**330**	**66.0%**	**218**	**$6.8**	**$1,491**	**£1.28**	**68%**	**33%**	**$90**	**$444**	**£0.38**	**140%**	

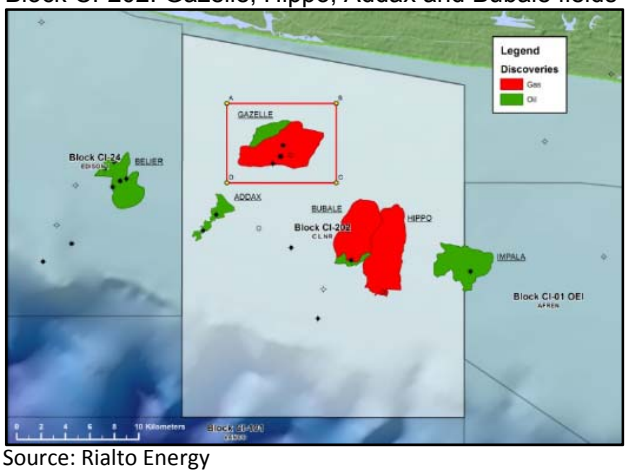
Côte d'Ivoire:

Projected production profile from contingent resources



Source: TPH

Block CI-202: Gazelle, Hippo, Addax and Bubale fields



Source: Rialto Energy

Rialto's main asset is the shallow water CI-202 Block, offshore Côte d'Ivoire. Rialto has an 85% interest in the block. The government of Côte d'Ivoire has a 15% interest in the block. The government also retains an 11% back-in right, which we assume it exercises, reducing Rialto's effective working interest to 74%. There have been 13 wells drilled on the block over a 26 year period; 12 of the wells encountered significant hydrocarbons and 9 recovered hydrocarbons to surface via DSTs. The block contains 4 under appraised discoveries (Gazelle, Hippo, Bubale and Addax) and has total contingent resources of 116mmboe (43% oil).

Rialto's current work programme is focused on converting 55mmboe (24% oil) of contingent resources associated with the Gazelle discovery to 2P reserves ahead of a planned final investment decision (FID), finalisation of a gas sales agreement and ultimately field development. We estimate Gazelle is worth £0.34/sh to Rialto on an unrisked basis, £0.13/sh on a risked basis. We apply a 50% chance of commercialisation to Gazelle as the company will require ~$400mm (TPHe) to fund the development and will most likely have to dilute its interest in the block, through a combination of a farm-out, debt raise and / or an equity offering.

We assume the other discoveries, Hippo, Bubale and Addax, will be tied back to the Gazelle facilities. We estimate the discoveries are worth £0.58/sh to Rialto on an unrisked basis, £0.22/sh on a risked basis, based on 142mmboe (11% oil) of contingent and prospective resources. Rialto will also test the 141mmboe (89% gas) Condor prospect during the Gazelle

appraisal programme, however we do not give Rialto any value for Condor in our 3P NAV, as we remain cautious of the company's ability to monetise future gas discoveries. Overall, in addition to the contingent resources, a further 811mmboe (63% oil) of prospective resources has been identified across 14 prospects. Near term, Rialto will drill the 91mmboe (92% oil) Chouette prospect in 3Q12. We estimate Chouette is worth £0.31/sh to Rialto on an unrisked basis, £0.02/sh on a risked basis. Rialto also plans to test several prospects on the block in 2013. We do not give the company any value for its future work programme, given its lack of medium term liquidity.

Australia: Offshore Western Australia, Rialto has a 12% interest in the WA-399-P permit. The block is situated within the hydrocarbon producing Carnarvon basin. Rialto and its partners on the block have indentified a 3D seismic supported prospect called Gazelle with gross mean prospective resources of 42mmboe (93% oil). The partners may elect to drill the Gazelle prospect late 2012 or early 2013, subject to the outcome of an on-going evaluation. We estimate the prospect is worth £0.05/sh to Rialto unrisked or £0.01 on a risked basis. The block is operated by Apache (APA US – A; 60% WI); APA produces oil from the nearby Pyrenees and Van Gogh fields. Other participants in the block are Jacka Resources (JKA AU – NR; 15% WI) and Carnarvon Petroleum (CNV AU – NR; 13% WI).

Ghana: Rialto has an agreement with Challenger Minerals Inc., to acquire a 20% paying interest (18% earning interest) in the Accra Block, offshore Ghana. However, the transfer of the working interest to Rialto is subject to Ministerial approval. The block is operated by Tap Oil (TAP AU – NR; 36% WI). Tap Oil has identified over the 3Bboe of unrisked prospective resources within the block, across multiple play types, including the Upper Cretaceous fan and Lower Cretaceous plays. Tap has high graded the 500mmboe (P50) Starfish prospect for drilling in 3Q12. Starfish is a "Jubilee" style Upper Cretaceous fan target. We do not give Rialto any value for Starfish in our 3P NAV, as the company is yet to be awarded an interest in block. However, we estimate it could be worth £0.66/sh, unrisked, or £0.07/sh on a risked basis to Rialto. We expect the Ministerial approval to be granted or refused imminently.

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Equal-weight / Hold	36	29%
Underweight / Sell	5	4%

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