

Deutsche Rohstoff AG

Germany / Raw materials
 Frankfurt
 Bloomberg: DR0 GR
 ISIN: DE000A0XYG76

Update

RATING
BUY

PRICE TARGET
€ 26.90

Return Potential 37.3%
 Risk Rating High

SUBSTANTIAL UPSIDE POTENTIAL AT CURRENT OIL PRICE

DRAG continues to invest in the expansion of oil and gas production at its North American subsidiaries Cub Creek Energy (79.9% owned), Elster Oil & Gas (93% owned) and Salt Creek Oil & Gas (90.2% owned). DRAG has great potential at the current oil price in our view. Providing that oil remains at or above the current level, we forecast DRAG will generate EBITDA of €147m in 2019 – 4% above current enterprise value. However, the first half of 2017 serves as a reminder of the capacity of oil price volatility to slow investment programmes. In H2/16 Cub Creek Energy planned to drill 30 new wells during 2017. Cub Creek will complete 23 of these wells this year but only 7 will go into production. We maintain our Buy recommendation but lower the price target from €34.00 to €26.90. The reduction in our price target stems both from lower near term production than we had previously forecast and the use of a 12% discount rate (we previously used 10%) to reflect restricted visibility regarding the oil price and investment plans in the medium term.

We model another 48 wells at Cub Creek following recent drilling The first nine horizontal wells at Cub Creek Energy's (CCE) north east Wattenberg project began producing from the Vail Pad in November 2016 and a further 12 horizontal wells came on line at the Markham Pad in January 2017. In mid-September DRAG reported that a further 7 horizontal wells had begun production from the Haley Pad and that drilling of a further 16 horizontal wells had been completed at the Litzenberger Pad. Production from the Litzenberger Pad is expected to start in Q1 2018. All of these are one-mile lateral wells. Provided that the oil price remains around the current level or better, we expect DRAG/CCE to begin production at a further 48 further one-mile lateral equivalent horizontal wells over the next two years (see figure 1).

Twenty well programme at Elster 11 one-mile lateral horizontal wells are currently producing at Elster Oil & Gas (EOG). In July DRAG announced that Elster will be participating in a 20 well drilling programme. (p.t.o.)

FINANCIAL HISTORY & PROJECTIONS

	2014	2015	2016	2017E	2018E	2019E
Revenue (€m)	22.87	1.90	9.17	48.24	80.81	155.83
Y-o-y growth	28.8%	-91.7%	383.4%	426.1%	781.2%	223.0%
EBIT (€m)	88.73	3.36	-0.50	20.03	40.36	45.97
EBIT margin	387.9%	176.9%	-5.4%	41.5%	49.9%	29.5%
Net income (€m)	25.17	1.16	0.10	8.10	19.15	20.64
EPS (diluted) (€)	4.80	0.23	0.02	1.60	3.78	4.08
DPS (€)	0.50	0.55	0.60	0.70	1.00	1.00
FCF (€m)	82.10	-12.11	-57.26	-16.46	-61.12	-26.15
Net gearing	-63.7%	-40.5%	59.8%	59.9%	105.6%	111.0%
Liquid assets (€m)	92.82	71.04	28.09	36.92	28.50	26.13

RISKS

Risks include negative movements in the oil price and other raw materials prices, dry well risk, mechanical failure, loss of key personnel.

COMPANY PROFILE

Deutsche Rohstoff AG (DRAG) is a resources company with a portfolio of properties in oil/gas, so-called high tech metals such as tin and tungsten, base metals and rare earths. The business model is based on production in well explored areas in politically stable countries. DRAG is based in Mannheim, Germany.

MARKET DATA

As of 13 Oct 2017

Closing Price	€ 19.59
Shares outstanding	5.06m
Market Capitalisation	€ 99.18m
52-week Range	€ 16.13 / 26.45
Avg. Volume (12 Months)	14,703

Multiples	2016	2017E	2018E
P/E	970.5	12.2	5.2
EV/Sales	15.5	2.9	1.8
EV/EBITDA	22.2	3.3	1.9
Div. Yield	3.1%	3.6%	5.1%

STOCK OVERVIEW



COMPANY DATA

As of 30 Jun 2017

Liquid Assets	€ 39.49m
Current Assets	€ 50.06m
Intangible Assets	€ 38.92m
Total Assets	€ 190.23m
Current Liabilities	€ 12.03m
Shareholders' Equity	€ 66.90m

SHAREHOLDERS

Management	9.7%
BASF-VC	6.3%
Free float	84.0%



14 wells with a lateral length of 2 miles and 6 wells with a lateral length of 2.5 miles will be drilled from two pads. The equivalent number of one-mile lateral wells is 43. EOG's working interest in these wells will be 24% and its share in the overall USD104m investment will amount to USD25m. We model an April 2018 production start (see figure 1).

Eleven new wells to start production at Salt Creek by end 2017 In late 2016 Salt Creek Oil & Gas (Salt Creek) acquired a working interest of ca. 8% in 60 producing wells and 90 infill development wells which are expected to be drilled within the next 4 years. The assets are located in the Bakken and Three Forks plays of the Williston Basin in North Dakota. The wells are also not operated by DRAG/Salt Creek but by large, well-known companies including Hess, EOG Resources, Statoil, Whiting and XTO. Salt Creek has received well proposals from a number of different operators so far this year. We expect six wells to start production in November and a further five in December. We model the start of production at a further 32 wells in 2018 and 10 in 2019 (see figure 1). All of these wells are two-mile laterals.

Figure 1: Recent and forecast well production starts

Cub Creek				Elster				Salt Creek			
Production start date	No 1-mile lateral equivalent wells	Working interest	End year no. wells	Production start date	No 1-mile lateral equivalent wells	Working interest	End year no. wells	Production start date	No 2-mile lateral equivalent wells	Working interest	End year no. wells
Dec-16	9	98%	9	Oct-15	5	45%	5	Nov-17	6	8%	
Jan-17	12	74%		Sep-16	6	45%	11	Dec-17	5	8%	71
Sep-17	7	78%	28	Apr-18	43	24%	54	May-18	8	8%	
Apr-18	16	80%						Aug-18	14	2%	
Dec-18	24	80%	68					Dec-18	10	8%	103
Jul-19	24	80%	92					Jun-19	10	8%	113

Source: DRAG; First Berlin Equity Research estimates

We expect CAPEX to exceed €100m in both 2018 and 2019 DRAG ended H1 2017 with net debt of €42.5m (comprised of cash and financial assets of €47.1m and combined bank and bond debt of €89.6m). Net gearing was 63.5%. We expect DRAG's share of CAPEX at the three north American oil and gas subsidiaries discussed above to amount to €44.8m this year. Cashflow benefited from the receipt of the expected USD13.1m (€11.1m) tax refund at mid-year but we expect a free cash outflow after dividends of €16.5m for 2017. In July DRAG announced a USD25m floating rate (currently ca. 4%) credit agreement with a leading US energy lender. The company also placed another €7.5m of its 2021 bond. We expect CAPEX to be around €111m and €139m in 2018 and 2019 respectively as the investment programmes at Cub Creek, Elster and Salt Creek gather pace. On our forecasts cashflows will be sufficient however to ensure that net gearing peaks at 111% in 2019.

Our 2017 EBITDA forecast is in line with guidance, revenue below DRAG published H1/17 results at the end of September showing revenues of €32.1m and EBITDA of €23.5m. H1/16 revenues and EBITDA were minimal because EOG was the only one of the three north American oil and gas subsidiaries in production for most of 2016. On 8 May management issued guidance for full year 2017 revenue of €55-65m and EBITDA of "at least €40 million." This forecast was based on assumptions including the following:

- production start at the Haley wells in August
- no contribution from the Litzenberger wells until 2018
- the start of production at 10 Salt Creek wells by the end of this year
- an average oil price of USD 50/barrel
- a EURUSD exchange rate of 1.08

Our 2017 EBITDA forecast of €42.4m is in line with guidance. But our 2017 revenue forecast of €48.2m is below guidance because since 8 May the oil price and the EURUSD exchange rate have averaged USD47.9/barrel and 1.16 respectively. In addition production at the Haley wells did not start until the second week of September.



Figure 2: Changes to our forecasts

All figures in € 000s	2017E	2017E	Δ	2018E	2018E	Δ	2019E
	New	Old		New	Old		New
Revenues	48,243	100,420	-52.0%	80,812	155,977	-48.2%	155,827
EBITDA	42,363	84,928	-50.1%	73,403	131,689	-44.3%	146,822
Depreciation and amortisation	22,336	22,490		33,041	38,080		100,851
Operating income (EBIT)	20,028	62,438	-67.9%	40,362	93,609	-56.9%	45,971
Net financial result	-4,737	-3,548		-5,281	-3,808		-7,381
Pre-tax income (EBT)	15,291	58,889		35,081	89,800		38,590
Income taxes	-5,352	-20,611		-12,278	-31,430		-13,506
Net before minorities	9,939	38,278		22,802	36,258		25,083
Minority interests	-1,839	-6,703		-3,652	-10,050		-4,442
Net income after mins.	8,100	31,575	-74.3%	19,151	48,321	-60.4%	20,642
EPS (€)	1.60	6.24	-74.3%	3.78	9.54	-60.3%	4.08

Source: DRAG; First Berlin Equity Research estimates

Our 2017 revenue forecast is only half the previous level because oil price volatility earlier this year caused a delay in DRAG's drilling schedule. We had previously expected CCE to be producing from 56 one-mile equivalent lateral wells by the end of 2017 and 120 by the end of 2018 this year. Our current forecasts for 2017 and 2018 are 28 and 68 respectively. We expect DRAG to make up much of the ground lost in 2017 and 2018 in 2019.

Figures 3, 4 and 5 show our valuations of CCE, Elster and Salt Creek.

Figure 3: DCF Valuation of CCE*

USD 000s	2017E	2018E	2019E	2020E	2021E	2022E	2023E	2024E	2025E
Production (working interest): barrels of oil equivalent (000s)	1,742	2,241	4,520	5,254	3,094	2,328	1,901	1,622	1,423
Oil price period end (WTI -USD/barrel)	50.00	50.00	50.00	50.00	50.00	50.00	50.00	50.00	50.00
No. 1 mile-lateral equivalent wells period end	28.0	68.0	92.0	116.0	116.0	116.0	116.0	116.0	116.0
Net revenue (working interest after royalty and ad valorem tax)	47,063	61,605	156,663	179,114	100,858	74,085	59,783	50,441	43,715
EBITDA	42,177	56,384	149,112	169,996	92,121	65,547	51,191	41,809	35,063
EBIT	21,985	33,839	45,590	125,046	64,914	44,818	34,129	27,170	22,169
NOPLAT	14,290	21,996	29,634	81,280	42,194	29,132	22,184	17,661	14,410
Tax Rate (%)	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%
Depreciation	20,192	22,544	103,521	44,950	27,206	20,730	17,061	14,638	12,894
CAPEX	28,566	84,736	128,000	0	0	0	0	0	0
Working capital expenditure	-5,559	-2,181	-14,259	-3,368	11,738	4,016	2,145	1,401	1,009
Free cashflow	357	-42,377	-9,104	122,862	81,139	53,877	41,391	33,700	28,313
PV free cashflow (12% discount rate)	174	-36,947	-7,087	85,394	50,353	29,852	20,477	14,886	11,166
Sum PV free cashflows	206,471								

Source: DRAG; First Berlin Equity Research estimates

Figure 4: DCF Valuation of Elster*

USD 000s	2017E	2018E	2019E	2020E	2021E	2022E	2023E	2024E	2025E
Production (working interest): barrels of oil equivalent (000s)	217	841	537	365	284	236	203	180	161
Oil price period end (WTI -USD/barrel)	50.00	50.00	50.00	50.00	50.00	50.00	50.00	50.00	50.00
No. 1 mile-lateral equivalent wells period end	11.0	54.0	54.0	54.0	54.0	54.0	54.0	54.0	54.0
Net revenue (working interest after royalty and ad valorem tax)	4,668	22,699	13,817	9,178	7,042	5,762	4,947	4,342	3,863
EBITDA	3,912	20,838	12,549	8,094	5,900	4,604	3,762	3,139	2,648
EBIT	2,383	14,123	8,248	5,164	3,613	2,703	2,123	1,690	1,346
NOPLAT	1,549	9,180	5,361	3,356	2,348	1,757	1,380	1,098	875
Tax Rate (%)	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%
Depreciation	1,529	6,715	4,300	2,930	2,287	1,901	1,640	1,449	1,302
CAPEX	9,984	14,976	0	0	0	0	0	0	0
Working capital expenditure	-300	-2,705	1,332	696	320	192	122	91	72
Free cashflow	-7,207	-1,786	10,994	6,983	4,956	3,850	3,142	2,638	2,249
PV free cashflow (12% discount rate)	-3,519	-1,557	8,558	4,853	3,075	2,133	1,554	1,165	887
Sum PV free cashflows	20,042								

Source: DRAG; First Berlin Equity Research estimates



Figure 5: DCF Valuation of Salt Creek*

USD 000s	2017E	2018E	2019E	2020E	2021E	2022E	2023E	2024E	2025E
Production (working interest): barrels of oil equivalent (000s)	217	443	578	642	677	656	486	385	324
Oil price period end (WTI -USD/barrel)	50.00	50.00	50.00	50.00	50.00	50.00	50.00	50.00	50.00
No. 2 mile-lateral equivalent wells period end	71.0	103.0	113.0	133.0	153.0	160.0	160.0	160.0	160.0
Net revenue (working interest after royalty and ad valorem tax)	6,161	12,671	16,512	18,355	19,336	18,732	13,882	10,991	9,246
10% ad valorem tax	685	1,408	1,835	2,039	2,148	2,081	1,542	1,221	1,027
Direct op. costs (working interest)	915	1,180	1,473	1,746	1,994	2,200	2,235	2,235	2,235
Overhead costs	499	629	513	513	835	1,018	938	880	848
EBITDA	4,747	10,862	14,526	16,096	16,508	15,514	10,709	7,877	6,164
EBIT	3,218	4,147	10,226	13,165	14,221	13,613	9,070	6,428	4,861
NOPLAT	2,092	2,696	6,647	8,558	9,243	8,849	5,895	4,178	3,160
Tax Rate (%)	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%
Depreciation	1,529	6,715	4,300	2,930	2,287	1,901	1,640	1,449	1,302
CAPEX	6,233	11,467	10,667	5,333	10,667	3,733	0	0	0
Working capital expenditure	-524	-977	-576	-276	-147	91	728	434	262
Free cashflow	-3,137	-3,033	-296	5,878	717	7,107	8,263	6,061	4,724
PV free cashflow (12% discount rate)	-1,532	-2,644	-230	4,086	445	3,938	4,088	2,677	1,863
Sum PV free cashflows	17,378								

Source: DRAG; First Berlin Equity Research estimates

* our valuation models for CCE, Elster and Salt Creek extend to 2034 but for reasons of space we show numbers only out to 2025

VALUATION SUMMARY

We maintain our Buy recommendation but lower the price target from €34.00 to €26.90

The sum of the parts model in figure 6 summarises our valuation of DRAG's most important assets. The reductions in our valuations of CCE, Elster and Salt Creek reflect the use of a 12% discount rate to value cashflows at these assets. In our previous reports we used 10%, which is a 10% discount is the standard value used by consultants such as Ryder Scott to value oil and gas reserves. We have switched to 12% in the current report to reflect restricted visibility regarding the oil price and oil industry investment plans in the medium term. Our valuation of Elster is also influenced by a reduction in the forecast pace of new well starts. We now forecasts 54 one mile equivalent horizontal wells at Elster by the end of 2019 compared with 62 previously.

Figure 6: Sum of the parts model

€m	New	Old
Cub Creek Energy (DRAG's stake 79.9%)	138.8	152.3
Elster Oil & Gas (DRAG's stake: 93.0%)	15.7	46.0
Salt Creek Oil & Gas (DRAG's stake: 90.2%)	13.2	31.9
Almonty (13.1% equity stake plus CAD8.8m in convertible debentures, promissory notes)	15.4	11.7
Tin International (DRAG's stake: 61.5%)	1.5	0.2
Rhein Petroleum (DRAG's stake: 10%)	2.0	2.0
Ceritech (DRAG's stake: 67.9%)	1.0	1.0
Devonian Metals (DRAG's stake: 47%)	0.0	0.0
Hammer Metals (DRAG's stake: 17.8%)	1.0	1.4
Holding company costs	-10.0	-10.0
Total enterprise value	178.5	236.5
Cash and financial assets	47.1	10.8
Debt	89.6	74.1
Net cash and financial assets (30.06.2017E)	-42.5	-63.3
Total equity value	135.9	173.2
No shares (m)	5.06	5.06
Equity value per share (€)	26.9	34.2

Source: First Berlin Equity Research estimates



INCOME STATEMENT

All figures in € 000s	2014A	2015A	2016A	2017E	2018E	2019E
Revenues	22,871	1,897	9,170	48,243	80,812	155,827
EBITDA	114,160	4,933	6,374	42,363	73,403	146,822
Depreciation and amortisation	25,434	1,578	6,874	22,336	33,041	100,851
Operating income (EBIT)	88,726	3,355	-500	20,028	40,362	45,971
Net financial result	-4,065	-3,912	-1,454	-4,737	-5,281	-7,381
Non-operating expenses	0	0	0	0	0	0
Pre-tax income (EBT)	84,661	-557	-1,953	15,291	35,081	38,590
Taxes	-30,645	1,086	2,028	-5,352	-12,278	-13,506
Minority interests	-28,845	626	28	-1,839	-3,652	-4,442
Net income / loss	25,171	1,155	102	8,100	19,151	20,642
EPS (in €)	4.80	0.23	0.02	1.60	3.78	4.08
Ratios						
EBIT margin on revenues	387.9%	176.9%	-5.4%	41.5%	49.9%	29.5%
EBITDA margin on revenues	499.1%	260.0%	69.5%	87.8%	90.8%	94.2%
Net margin on revenues	110.1%	60.9%	1.1%	16.8%	23.7%	13.2%
Tax rate	36.2%	195.0%	103.8%	35.0%	35.0%	35.0%
Y-Y Growth						
Revenues	28.8%	-91.7%	383.4%	426.1%	67.5%	92.8%
Operating income	n.m.	-96.2%	n.m.	n.m.	101.5%	13.9%
Net income/ loss	n.m.	-95.4%	-91.2%	7825.8%	136.4%	7.8%



BALANCE SHEET

All figures in € 000s	2014A	2015A	2016A	2017E	2018E	2019E
Assets						
Current assets, total	98,203	79,267	51,874	50,919	59,781	97,534
Cash and cash equivalents	92,821	71,041	28,090	36,919	28,497	26,134
Inventories	38	55	139	280	626	1,428
Receivables	106	2,831	7,794	10,080	22,524	51,407
Prepayments	190	276	495	840	1,877	4,284
Other current assets	726	4,530	15,105	2,800	6,257	14,280
Deferred tax assets	4,322	534	251	0	0	0
Non-current assets, total	36,493	48,786	141,598	163,133	241,270	271,498
Intangible assets	12,279	17,501	40,614	39,614	38,614	37,614
Land and buildings	0	0	0	0	0	0
Producing oil plants	0	5,314	76,172	98,514	173,921	210,907
Exploration and evaluation	1,647	1,596	3,493	4,518	7,975	9,671
Plant and machinery	513	444	173	224	395	479
Other equipment	94	119	103	133	235	285
Equity investments	11,456	11,822	12,542	12,542	12,542	12,542
Loans to other investors			913	0		0
Securities classified as fixed assets	10,504	11,990	7,588	7,588	7,588	0
Total assets	134,696	128,053	193,472	214,052	301,051	369,032
Shareholders' equity & debt						
Current liabilities, total	4,675	4,230	33,904	25,116	20,817	47,512
Bank debt	414	7	0	0	0	0
Bond debt	0	0	0	15,800	0	0
Accounts payable	217	957	29,915	2,795	6,245	14,254
Other current liabilities	4,044	3,266	3,989	6,521	14,572	33,258
Long-term liabilities, total	63,147	57,955	75,243	86,860	158,900	178,900
Bond debt	57,111	51,555	66,705	58,400	88,400	108,400
Bank debt	5,993	6,400	8,538	28,460	70,500	70,500
Other long term liabilities	43	0	0	0	0	0
Provisions	1,540	1,089	5,308	2,000	2,000	2,000
Minority interests	2,331	2,566	9,698	11,537	15,189	19,630
Shareholders' equity	60,157	59,274	56,423	85,539	101,145	117,989
Consolidated equity	62,488	61,840	66,121	97,075	116,334	137,620
Deferred tax liabilities	2,846	2,939	12,896	3,000	3,000	3,000
Total consolidated equity and debt	134,696	128,053	193,472	214,052	301,051	369,032
Ratios						
Current ratio (x)	21.01	18.74	1.53	2.03	2.87	2.05
Quick ratio (x)	21.00	18.73	1.53	2.02	2.84	2.02
Financial leverage	-63.7%	-40.5%	59.8%	59.9%	105.6%	111.0%
Book value per share (€)	11.94	11.77	11.20	16.98	20.08	23.42
Net cash (debt)	39,807	25,069	-38,652	-58,153	-122,815	-152,766
Return on equity (ROE)	106.6%	0.9%	0.1%	12.2%	21.4%	19.8%



CASH FLOW STATEMENT

All figures in € 000s	2014A	2015A	2016A	2017E	2018E	2019E
EBIT	88,726	3,355	-500	20,028	40,362	45,971
Depreciation and amortisation	25,434	1,578	6,874	22,336	33,041	100,851
EBITDA	114,160	4,933	6,374	42,363	73,403	146,822
Changes in working capital	1,524	-4,625	-5,809	-15,055	-5,782	-13,421
Interest paid	-4,263	-3,912	-1,413	-4,737	-5,281	-7,381
Tax paid/received	-29,091	1,086	1,724	5,748	-12,278	-13,506
Profit/loss from sale of Tekton Energy	-103,605	0	0	0	0	0
Other adjustments	2,299	3,712	2,038	0	0	0
Operating cash flow	-18,976	1,194	2,914	28,320	50,061	112,513
Investing cash flow	101,073	-13,307	-60,177	-44,783	-111,179	-138,667
Free cash flow	82,097	-12,113	-57,263	-16,463	-61,118	-26,154
Dividends, share buybacks	-38,929	-3,100	-2,714	-3,038	-3,544	-3,797
Equity financing	0	0	1,126	0	0	0
Debt financing	0	0	39,233	27,417	72,040	20,000
Debt repayment	-8,540	-6,182	-22,148	0	-15,800	0
Other	999	-2,712	-3,981	913	0	7,588
Financing cash flow	-46,470	-11,994	11,516	25,292	52,696	23,791
Other	0	0	2,246	0	0	0
Change in cash and equivalents	35,627	-24,107	-43,501	8,829	-8,422	-2,363
FX/consolidation effects	11,131	2,327	550	0	0	0
Cash and cash equivalents, start of the year	46,063	92,821	71,041	28,090	36,919	28,497
Cash and cash equivalents, end of the year	92,821	71,041	28,090	36,919	28,497	26,134
EBITDA/share (in €)	21.70	0.97	1.26	8.37	14.51	29.02
Y-Y Growth						
Operating cash flow	n.m.	n.m.	144.1%	871.9%	76.8%	124.8%
Free cash flow	n.m.	n.m.	n.m.	n.m.	n.m.	n.m.
EBITDA/share	5954.7%	-95.5%	29.2%	564.6%	73.3%	100.0%

FIRST BERLIN RECOMMENDATION & PRICE TARGET HISTORY

Report No.:	Date of publication	Previous day closing price	Recommendation	Price target
Initial Report	22 July 2010	€7.45	Buy	€13.20
2...22	↓	↓	↓	↓
23	5 October 2016	€21.40	Buy	€27.00
24	12 December 2016	€23.91	Buy	€31.00
25	20 February 2017	€23.66	Buy	€34.00
26	Today	€19.59	Buy	€26.90

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