

Saturn Oil & Gas Inc.

Canada / Oil & Gas

TSXV, Canada; Frankfurt, Germany; OTCQX, US

Bloomberg: SOIL CN, SMKA GR, OILSF US

ISIN: CA80412L8832

Update

RATING**PRICE TARGET**

Return Potential

Risk Rating

BUY**CAD 6.30**

173.9%

High

Q3 RESULTS VALIDATE VIKING ACQUISITION

The Viking acquisition (consolidated from 6 July 2022) was the main driver of a 49.7% rise in Saturn's output to 10,965 boepd between Q2/22 and Q3/22. The acquisition was financed by a CAD200m expansion of the company's senior term loan and by a CAD75m equity issue. Despite a ca. 75% rise in the share count, Saturn still succeeded in raising adjusted funds flow (operating cashflow less decommissioning expenditure) per share by 53% to CAD0.69. This success was attributable to lower royalties and operating costs at the acquisition relative to the existing business, as well as the very well-timed hedging of the newly purchased production at mid-year. We forecast that a full year's contribution from the Viking acquisition, as well as continued drilling at both the Oxbow and Viking assets will push EBITDA up by a further 60% to CAD261m in 2023 (company guidance: CAD252m). We also continue to expect the current net debt position of CAD252m to become net cash of CAD177m by YE2025. However, while we retain our Buy recommendation, we have lowered the price target from CAD7.00 to CAD6.30. The reduction reflects the impact on unhedged production (2023E: 48%; 2024E: 61%; 2025E: 70%) of the average 6% fall in the oil futures curve to YE2025 since our most recent note of 4 November.

Q3/22 results benefitted from lower unit costs/reduced losses on derivatives Production jumped 49.7% between Q2/22 and Q3/22 to 10,965 boepd (see figure 1 overleaf). Petroleum/natural gas sales grew at a slower clip (+28.6%) to CAD105.7m because of a 15% decline in the average commodity price to CAD104.8/BOE. However, revenue after royalties climbed 33.5% to CAD93.8m because of a 34.3% decline in unit royalties occasioned by the Viking acquisition. Royalties at the Viking acquisition are lower than at pre-acquisition Saturn because a higher proportion of the newly purchased wells are on crown land where initial production is royalty-free. As figure 1 overleaf shows, unit net operating costs were also 11.9% lower in Q3/22 compared with Q2/22. Here too the decline was due to the addition of the new Viking wells.

FINANCIAL HISTORY & PROJECTIONS

	2020	2021	2022E	2023E	2024E	2025E
Revenue (CAD m)	7.16	98.16	318.52	371.16	403.94	399.90
Y-o-y growth	n.a.	1270.6%	224.5%	16.5%	8.8%	-1.0%
EBITDA (CAD m)	5.31	34.63	162.68	260.78	290.48	300.09
EBITDA margin	74.2%	35.3%	51.1%	70.3%	71.9%	75.0%
Net income (CAD m)	-7.76	-65.06	90.30	182.24	192.02	203.02
EPS (diluted) (CAD)	-0.66	-3.36	2.02	3.05	3.22	3.40
DPS (CAD)	0.00	0.00	0.00	0.00	0.00	0.00
FCF (CADm)	0.80	-9.98	21.27	131.25	132.78	143.75
Net gearing	n.a.%	n.a.	151.6%	29.4%	-6.4%	-24.3%
Liquid assets (CAD m)	0.57	2.42	8.21	24.59	78.92	193.38

RISKS

Risks to our price target include a fall in the oil price, lower than expected production rates, inflation in well-development costs.

COMPANY PROFILE

Saturn has assembled a portfolio of free-cash flowing, low-decline, light oil-weighted operated assets in Southeastern and West Central Saskatchewan. The assets include a deep inventory of drilling opportunities across multiple zones and the company's strategy also encompasses the targeting of accretive, complementary opportunities.

MARKET DATA

As of 10 Jan 2023

Closing Price	CAD 2.30
Shares outstanding	59.84m
Market Capitalisation	CAD 137.63m
52-week Range	CAD 2.01 / 3.80
Avg. Volume (12 Months)	229,082

Multiples	2021	2022E	2023E
P/E	n.a.	1.1	0.7
EV/Sales	3.9	1.2	1.0
EV/EBIT	11.1	2.4	1.5
Div. Yield	0.0%	0.0%	0.0%

STOCK OVERVIEW



COMPANY DATA

As of 30 Sep 2022

Liquid Assets	CAD 31.04m
Current Assets	CAD 91.29m
Intangible Assets	CAD 5.09m
Total Assets	CAD 593.59m
Current Liabilities	CAD 220.44m
Shareholders' Equity	CAD 155.04m

SHAREHOLDERS

PenderFund Capital Management	7.3%
Broadbill Energy, Inc.	1.0%
James Payne	0.9%
John Jeffrey	0.4%
Free float and other	90.4%

**Figure 1: Q3/22 vs. Q2/22 results**

	Q2/22A	Q3/22A	% Δ
Production (boepd)	7,324	10,965	49.7%
Petroleum/natural gas sales (CAD 000s)	82,230	105,728	28.6%
Revenue after royalties (CAD 000s)	70,216	93,769	33.5%
Petroleum/natural gas sales (CAD/boe)	123.39	104.81	-15.1%
Royalties (CAD/boe)	19.12	12.57	-34.3%
Net operating expenses (CAD/boe)	27.08	23.86	-11.9%
Realised loss on derivatives (CAD/boe)	46.31	17.18	-62.9%
Adjusted funds flow (CAD 000s)	14,562	39,956	174.4%
Adjusted funds flow per basic share (CAD)	0.45	0.69	53.3%

Source: Saturn Oil & Gas Inc.

The average age of the Viking wells is lower than that of the Oxbow wells, which accounted for over 90% of Saturn's Q2/22 production. A well's output declines as its ages. This means that production per well is higher and unit cost lower at Viking than at Oxbow. In addition, along with hydrocarbons, Oxbow also extracts a high quantity of water. Indeed, water accounts for around 97% of a typical Oxbow well's volume. Processing and reinjecting this water increases unit costs. Water accounts for under 10% of production at Viking by volume.

Figure 2: H2/22 impact of hedging of Viking acquisition production

	Av. H2/22 volume (b/d)	Average oil price hedged (USD)
Post-acquisition hedging	7,777	78.49
Hedging of acquisition	2,782	102.65
Pre-acquisition hedging	5,096	57.11

Source: Saturn Oil & Gas Inc.

Positive influence of mid-year hedging The biggest positive influence on the Q3/22 vs. Q2/22 comparison stemmed from lower realised derivative losses. The Viking assets were acquired unhedged. Hedging of Viking production at mid-year (close to the peak in the oil price) raised the average level of the company's H2/22 oil price hedges by 37% from USD57.11 to USD78.49, thereby greatly reducing the differential between the company's derivatives and market pricing. West Texas Intermediate averaged USD91.63 in Q3/22 and USD108.77 in Q2/22.

Figure 3: Oil production hedged as % total oil and NGL production

Period	Av. volume (b/d)	% of oil and NGL production	Average oil price hedged (USD)
2022 H2	7,777	72%	78.49
2023	6,674	52%	69.80
2024	5,556	39%	62.73
2025	4,620	30%	64.32
2026	2,046	12%	67.37

Source: Saturn Oil & Gas Inc.



The changes to our forecasts shown in figure 4 reflect the impact on unhedged production (see figure 3) of the average 6% fall in the oil futures curve to YE2025 since our most recent note of 4 November.

Figure 4: Changes to forecasts

All figures in CAD'000	2022E			2023E			2024E			2025E		
	new	old	%Δ	new	old	%Δ	new	old	%Δ	new	old	%Δ
Revenue after royalties	318,520	336,149	-5.2%	371,156	410,669	-9.6%	403,940	422,930	-4.5%	399,899	412,222	-3.0%
Realised gain/(loss) on derivatives	-76,838	-82,882	n.a.	-19,032	-38,252	n.a.	-21,550	-28,295	-23.8%	-8,350	-11,722	-28.8%
Unrealised gain/(loss) on derivatives	45,654	-34,536	n.a.	0	0	n.a.	0	0	n.a.	0	0	n.a.
Other income	11,351	4,082	178.1%	0	0	n.a.	0	0	n.a.	0	0	n.a.
Operating and transportation costs	80,702	80,491	0.3%	79,612	79,612	0.0%	79,300	79,300	0.0%	78,066	78,066	0.0%
General and administrative	8,256	8,233	0.3%	11,033	11,033	0.0%	11,908	11,908	0.0%	12,691	12,691	0.0%
Exploration and evaluation expiries	698	698	0.0%	0	0	n.a.	0	0	n.a.	0	0	n.a.
Share-based payments	697	697	0.0%	700	700	0.0%	700	700	0.0%	700	700	0.0%
EBITDA	208,334	132,694	57.0%	260,779	281,072	-7.2%	290,483	302,727	-4.0%	300,092	309,043	-2.9%
EBITDA before unrealised gain/(loss) on derivatives	162,680	167,230	-2.7%	260,779	281,072	-7.2%	290,483	302,727	-4.0%	300,092	309,043	-2.9%
EBIT	171,360	94,094	82.1%	209,294	229,587	-8.8%	233,339	245,583	-5.0%	240,868	249,819	-3.6%
Financing costs	81,689	81,744	-0.1%	27,052	27,297	-0.9%	12,621	12,739	-0.9%	7,510	7,587	-1.0%
Foreign exchange gain	623	623	0.0%	0	0	n.a.	0	0	n.a.	0	0	n.a.
Gain on debt extinguishment	6,883	6,883	0.0%	0	0	n.a.	0	0	n.a.	0	0	n.a.
Unrealised (gain)/loss on warrant liability	-2,414	-2,414	0.0%	0	0	n.a.	0	0	n.a.	0	0	n.a.
Gain on acquisitions	-5,723	-5,723	0.0%	0	0	n.a.	0	0	n.a.	0	0	n.a.
Transaction costs	0	0	n.a.	0	0	n.a.	0	0	n.a.	0	0	n.a.
Pretax profit	90,302	12,981	595.6%	182,242	202,289	-9.9%	220,718	232,844	-5.2%	233,357	242,232	-3.7%
Deferred income tax recovery	0	0	n.a.	0	0	n.a.	-28,693	-30,270	-5.2%	-30,336	-31,490	-3.7%
Net profit	90,302	12,981	595.6%	182,242	202,289	-9.9%	192,024	202,575	-5.2%	203,021	210,742	-3.7%

Source: First Berlin Equity Research estimates

Buy recommendation maintained but price target reduced from CAD7.00 to CAD6.30

Figure 5 shows the effect of the lower oil futures curve on our valuation of Saturn's Oxbow and Viking wells. Our valuation of the new and existing Oxbow wells, as well as of the existing Viking wells falls. Our valuation of the new Viking wells rises slightly because of the transfer of Q3/22 CAPEX to net debt. We now see fair value for the Saturn share at CAD6.28. We maintain our Buy recommendation but lower the price target from CAD7.00 to CAD6.30.

Figure 5: Sum of the parts valuation model

CAD 000s	New	Old	Δ %
DCF valuation existing Oxbow wells	188,581	197,358	-4.4%
DCF valuation new Oxbow wells	295,098	309,269	-4.6%
DCF valuation existing Viking wells	214,044	243,890	-12.2%
DCF valuation new Viking wells	91,882	85,591	7.4%
Sum of DCF well valuations	789,605	836,108	-5.6%
Proforma net debt	112,394	91,200	23.2%
Asset retirement liability	54,562	47,953	13.8%
Asset retirement deposit	21,101	21,021	0.4%
Net asset value	643,750	717,976	-10.3%
Proforma no. shares	102,500	102,500	0.0%
Value per share (CAD)	6.28	7.00	-10.3%

Source: First Berlin Equity Research estimates



INCOME STATEMENT

All figures in CAD '000	2020A	2021A	2022E	2023E	2024E	2025E
Revenue after royalties, net processing income	7,162	98,164	318,520	371,156	403,940	399,899
Realised gain/(loss) on derivatives	2,033	-16,038	-76,838	-19,032	-21,550	-8,350
Unrealised gain/(loss) on derivatives	243	-74,570	45,654	0	0	0
Other income	0	256	11,351	0	0	0
Operating costs	1,882	42,392	99,372	138,275	153,473	159,060
Transportation cost	0	1,107	3,193	4,903	5,442	5,640
Operating and transportation costs	1,882	43,499	80,702	79,612	79,300	78,066
General and administrative	1,310	3,802	8,256	11,033	11,908	12,691
Exploration and evaluation expiries	0	0	698	0	0	0
Share-based payments	689	452	697	700	700	700
EBITDA	5,557	-39,941	208,334	260,779	290,483	300,092
EBITDA before unrealised gain (loss) on derivatives	5,314	34,629	162,680	260,779	290,483	300,092
Depletion, depreciation, amortisation	4,523	16,226	36,974	51,485	57,144	59,225
EBIT	1,034	-56,167	171,360	209,294	233,339	240,868
Financing costs	10,182	17,977	81,689	27,052	12,621	7,510
Foreign exchange gain	-319	-220	623	0	0	0
Gain on debt extinguishment	-138	-1,032	6,883	0	0	0
Unrealised (gain)/loss on w warrant liability	-933	87	-2,414	0	0	0
Gain on acquisitions	0	-7,790	-5,723	0	0	0
Transaction costs	0	2,469	0	0	0	0
Pretax profit	-7,758	-67,658	90,302	182,242	220,718	233,357
Deferred income tax recovery	0	2,597	0	0	-28,693	-30,336
Net profit	-7,758	-65,061	90,302	182,242	192,024	203,021
Ratios						
EBITDA margin ex unrealised derivative gains/losses	74.2%	35.3%	51.1%	70.3%	71.9%	75.0%
Net margin on revenues	-108.3%	-66.3%	28.4%	49.1%	47.5%	50.8%
Tax rate	0.0%	-3.8%	0.0%	0.0%	12.5%	12.5%
Expenses as % of revenues						
Operating costs	26.3%	43.2%	31.2%	37.3%	38.0%	39.8%
Transportation cost	0.0%	1.1%	1.0%	1.3%	1.3%	1.4%
General and administrative	18.3%	3.9%	2.6%	3.0%	2.9%	3.2%
Y-Y Growth						
Revenues	n.a.	1270.6%	224.5%	16.5%	8.8%	-1.0%
EBITDA before unrealised gain (loss) on derivatives	n.a.	551.7%	369.8%	60.3%	11.4%	3.3%
Net income	n.a.	n.a.	n.a.	101.8%	5.4%	5.7%



BALANCE SHEET

All figures in CAD '000	2020A	2021A	2022E	2023E	2024E	2025E
Assets						
Current assets, total	1,399	28,915	55,910	78,893	138,187	252,133
Cash	569	2,415	8,214	24,592	78,918	193,385
Accounts receivable	739	20,039	29,351	33,416	36,473	36,153
Deposits and prepaid expenses	44	6,461	18,344	20,885	22,796	22,596
Financial derivatives	47	0	0	0	0	0
Long-term assets, total	38,915	192,191	481,720	535,955	597,811	657,586
Exploration and evaluation assets	4,485	4,485	4,485	4,485	4,485	4,485
Property, plant and equipment	33,425	162,909	452,438	506,673	568,529	628,304
Rights-of-use assets	565	3,776	3,776	3,776	3,776	3,776
Deposit	440	21,021	21,021	21,021	21,021	21,021
Financial derivatives	0	0	0	0	0	0
Total assets	40,314	221,106	537,630	614,848	735,997	909,719
Shareholders' equity & debt						
Current liabilities, total	31,935	95,084	196,719	163,379	125,464	94,631
Accounts payable	5,147	28,850	66,040	75,185	82,064	81,344
Senior term loan	0	33,582	118,287	74,051	30,429	0
Promissory note	479	0	0	811	0	0
Revolving notes	26,134	0	0	0	0	0
Lease liabilities	175	933	3,501	4,440	4,079	4,395
Financial derivatives	0	31,719	8,892	8,892	8,892	8,892
Long-term liabilities, total	4,773	156,328	188,939	114,275	82,896	83,730
Senior term loan	0	31,473	104,479	30,429	0	0
Term notes	0	24,104	0	0	0	0
Revolving notes	0	0	0	0	0	0
Promissory note	853	784	811	0	0	0
Convertible notes	2,038	2,197	2,280	0	0	0
Decommissioning obligations	415	47,296	47,296	47,296	47,296	47,296
Lease liabilities	435	2,814	9,240	11,718	10,767	11,601
Warrant liability	1,032	4,856	4,856	4,856	4,856	4,856
Financial derivatives	0	42,804	19,977	19,977	19,977	19,977
Shareholders' equity	3,606	-30,306	151,971	337,193	527,637	731,358
Total consolidated equity and debt	40,314	221,106	537,630	614,848	735,997	909,719
Ratios						
Current ratio (x)	0.04	0.30	0.28	0.48	1.10	2.66
Quick ratio (x)	0.04	0.24	0.19	0.36	0.92	2.43
Net debt	29,545	93,472	230,383	99,136	-33,643	-177,389
Net gearing	819.3%	n.a.	151.6%	29.4%	-6.4%	-24.3%
Equity ratio	8.9%	-13.7%	28.3%	54.8%	71.7%	80.4%
Book value per share (CAD)	0.31	-1.57	3.40	5.65	8.84	12.25
Return on equity (ROE)	n.a.	n.a.	148.4%	74.5%	44.4%	32.3%



CASH FLOW STATEMENT

All figures in CAD '000	2020A	2021A	2022E	2023E	2024E	2025E
OPERATING ACTIVITIES						
Net loss for the year	-7,758	-65,061	90,302	182,242	192,024	203,021
Depreciation, depletion and amortisation	4,523	16,226	36,974	51,485	57,144	59,225
Deferred income tax recovery	0	-2,597	0	0	0	0
Share-based payments	689	452	697	700	700	700
Unrealised (gain) loss on financial derivatives	-243	74,570	-45,654	0	0	0
Unrealised (gain) loss on warrant liability	-933	87	-2,414	0	0	0
Unrealised foreign exchange (gain) loss	191	21	623	0	0	0
Gain on acquisition	0	-7,790	0	0	0	0
Gain on debt extinguishment	-138	-1,032	6,883	0	0	0
Non-cash financing expenses	7,019	10,259	0	0	0	0
Non-cash transaction costs	0	611	0	0	0	0
Other income	0	-256	0	0	0	0
Decommissioning expenditures	0	-53	0	0	0	0
Change in non-cash working capital	-2,499	-26,722	15,994	2,541	1,911	-200
Other	0	0	-5,723	0	0	0
Operating cash flow	851	-1,285	97,682	236,968	251,779	262,746
INVESTING ACTIVITIES						
Property, plant and equipment	-51	-8,694	-76,410	-105,720	-119,000	-119,000
Free cash flow	800	-9,979	21,272	131,248	132,779	143,746
Property acquisition	0	-82,297	-250,093	0	0	0
Exploration and evaluation	-1,077	0	0	0	0	0
Change in non-cash working capital	-226	3,135	0	0	0	0
Investing cash flow	-1,354	-87,856	-326,503	-105,720	-119,000	-119,000
FINANCING ACTIVITIES						
Net proceeds from senior term loan	0	84,064	157,711	0	0	0
Debt issue costs	-474	-4,105	0	0	0	0
Repayment of senior term loan	0	-18,140	0	-118,287	-74,051	-30,429
Proceeds from share issuance	0	32,200	91,278	0	0	0
Share issue costs	0	-2,325	0	0	0	0
Lease payments	-202	-964	0	0	0	0
Repayment of promissory note	-352	-784	0	0	-811	0
Repayment of long term notes	0	0	-24,104	0	0	0
Proceeds from stock option exercise	0	50	0	0	0	0
Proceeds from revolving notes, net	990	0	0	0	0	0
Change in non-cash working capital	0	991	0	0	0	0
Financing cash flow	-38	90,987	224,885	-118,287	-74,862	-30,429
Other	0	0	9,735	3,417	-3,591	1,150
Change in cash during the year	-541	1,846	5,799	16,378	54,326	114,467
Cash, start of the year	1,110	569	2,415	8,214	24,592	78,918
Cash, end of the year	569	2,415	8,214	24,592	78,918	193,385
Y-Y Growth						
Operating cash flow	n.a.	n.m.	n.m.	142.6%	6.3%	4.4%
Free cash flow	n.a.	n.m.	n.m.	517.0%	1.2%	8.3%
EBITDA/share	n.a.	n.m.	n.m.	n.m.	n.m.	n.m.

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PRICE TARGET DATES

Unless otherwise indicated, current prices refer to the closing prices of the previous trading day.

AGREEMENT WITH THE ANALYSED COMPANY AND MAINTENANCE OF OBJECTIVITY

The present financial analysis is based on the author's own knowledge and research. The author prepared this study without any direct or indirect influence exerted on the part of the analysed company. Parts of the financial analysis were possibly provided to the analysed company prior to publication in order to avoid inaccuracies in the representation of facts. However, no substantial changes were made at the request of the analysed company following any such provision.

ASSET VALUATION SYSTEM

First Berlin's system for asset valuation is divided into an asset recommendation and a risk assessment.

ASSET RECOMMENDATION

The recommendations determined in accordance with the share price trend anticipated by First Berlin in the respectively indicated investment period are as follows:

Category		1	2
Current market capitalisation (in €)		0 - 2 billion	> 2 billion
Strong Buy ¹	An expected favourable price trend of:	> 50%	> 30%
Buy	An expected favourable price trend of:	> 25%	> 15%
Add	An expected favourable price trend of:	0% to 25%	0% to 15%
Reduce	An expected negative price trend of:	0% to -15%	0% to -10%
Sell	An expected negative price trend of:	< -15%	< -10%

¹ The expected price trend is in combination with sizable confidence in the quality and forecast security of management.

Our recommendation system places each company into one of two market capitalisation categories. Category 1 companies have a market capitalisation of €0 – €2 billion, and Category 2 companies have a market capitalisation of > €2 billion. The expected return thresholds underlying our recommendation system are lower for Category 2 companies than for Category 1 companies. This reflects the generally lower level of risk associated with higher market capitalisation companies.

RISK ASSESSMENT

The First Berlin categories for risk assessment are low, average, high and speculative. They are determined by ten factors: Corporate governance, quality of earnings, management strength, balance sheet and financial risk, competitive position, standard of financial disclosure, regulatory and political uncertainty, strength of brandname, market capitalisation and free float. These risk factors are incorporated into the First Berlin valuation models and are thus included in the target prices. First Berlin customers may request the models.

RECOMMENDATION & PRICE TARGET HISTORY

Report No.:	Date of publication	Previous day closing price	Recommendation	Price target
Initial Report	4 November 2022	CAD2.83	Buy	CAD7.00
2	Today	CAD2.30	Buy	CAD6.30

INVESTMENT HORIZON

Unless otherwise stated in the financial analysis, the ratings refer to an investment period of twelve months.

UPDATES

At the time of publication of this financial analysis it is not certain whether, when and on what occasion an update will be provided. In general First Berlin strives to review the financial analysis for its topicality and, if required, to update it in a very timely manner in connection with the reporting obligations of the analysed company or on the occasion of ad hoc notifications.

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Legally required information regarding

- key sources of information in the preparation of this research report
- valuation methods and principles
- sensitivity of valuation parameters

can be accessed through the following internet link: <https://firstberlin.com/disclaimer-english-link/>

SUPERVISORY AUTHORITY: Bundesanstalt für Finanzdienstleistungsaufsicht (German Federal Financial Supervisory Authority) [BaFin], Graurheindorferstraße 108, 53117 Bonn and Marie-Curie-Straße 24-28, 60439 Frankfurt am Main

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