



Otto Energy Ltd (OEL.ASX)

Louisiana Light Sweet Spot

Event:

- We initiate research coverage on Otto Energy Ltd (OEL.ASX).

Investment Highlights:

- Otto Energy Ltd (OEL)** is an ASX listed company with producing conventional on- and offshore oil and gas assets in the Gulf of Mexico, including the South Marsh Island 71 (SM71, WI 50%), Lightning Field (WI 37.5%), and Green Canyon 21 (GC21, WI 16.7%).
- Poised to take advantage of improving price environment after delivery of sustained significant cost reductions.** Oil prices have continued a strong resurgence over CY21 with WTI up 50% up YTD, and demonstrating strength after trawling remarkable lows in April 2020. OEL's flagship GoM asset SM71 in particular underpins very strong near term cash generation from its liquid-rich, high margin project in a strong price environment.
- Robust economics from high margin production with quality premium product:** Significant margin with very low lifting costs, while only very modest capex required in the near to medium term to enable continued strong cash flow generation. Desirable Louisiana Light Sweet (LLS) crude oil product typically attracts 2-5% premium over WTI.
- Growth optionality supported by near term cash generation:** OEL's ambition is to lock in future growth opportunities targeting a diverse opportunity set including GoM distressed assets and technically driven GoM shelf salt domes.
- Cash of US\$8M at March 2021 end, with debt of US\$14M.** Combined with liquid investments in UK listed Pantheon Resources plc worth US\$12M due to its recent Alaska asset sales, the company is effectively net cash. Modest leverage can be serviced by strong cash flow generation in coming quarters, scheduled to be repaid in full by September 2022, if not earlier.

Earnings and Valuation:

- We forecast **FY21-23e earnings of US\$1M, US\$9M, and US\$13M, or EPS (US\$) of 0.0cps, 0.2cps, 0.3cps.** We forecast FY21-23e production of 1.1mmbob, 1.2mmbob, and 1.4mmbob.
- We derive a valuation of \$0.04 per OEL share,** underpinned by a NPV₁₀ of A\$192M for producing assets, assuming LT WTI oil of US\$62/bbl, natural gas of US\$3.00/mmbtu, and AUDUSD 0.74.

Recommendation:

- We initiate coverage of OEL with a **Buy recommendation and price target of \$0.04/share,** high margin cash generation for close to a decade of Reserve life.
- We think the market has been slow to recognise the material upside, with the current share price reflecting a low realised WTI outcome under 2P reserve with significant upside from continued stronger prices, cash generation, and maximising existing asset base. Very undemanding FY22e P/FCF of 3.1x.
- Catalysts for the stock** include: 1) continued production growth and operational improvements; 2) Reserve and production updates upgrades from production, development, and recompletion updates; 3) capital management updates; 4) GC21 updates; and 5) continued deleveraging.

Disclosure

The analyst does not own OEL securities.

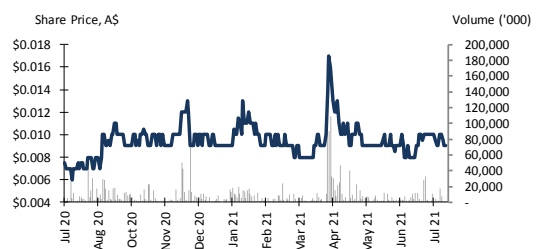
Foster Stockbroking and associated entities (excluding Cranport Pty Ltd) own 7,000,000 OEL shares.

Cranport Pty Ltd owns 36,625,112 OEL shares.

Foster Stockbroking provides equity capital markets and corporate advice to OEL and will receive consideration for this service.

Refer to end of report for details.

Recommendation	Buy			
Previous	N/A			
Risk	High			
Price Target (A\$/share)	\$0.04			
Previous	N/A			
Share Price (A\$)	\$0.009			
ASX Code	OEL			
52 week low - high (A\$)	0.006-0.017			
Capital structure				
Shares on Issue (M)	4,795.0			
Options and rights (M)	66.4			
Market Cap, undil. (A\$M)	43			
Net Cash/(Debt) (A\$M)	-8			
EV (A\$M)	51			
12mth Av Daily Volume ('000)	8,807			
Y/e Jun US\$	FY20a	FY21e	FY22e	FY23e
Sales, \$M	23.0	30.2	41.5	48.4
EBITDA adj. \$M	7.6	10.3	22.0	28.3
NPAT adj. \$M	-1.4	0.8	9.0	12.9
EPS adj c	0.0	0.0	0.2	0.3
PER (x)	nm	52.4	4.8	3.4
Dividend c	0.0	0.0	0.0	0.0
Board				
Mike Ustler	Executive Chairman and CEO			
John Jetter	Non-Executive Director			
Geoff Page	Non-Executive Director			
Paul Senyia	Non-Executive Director			
Major Shareholders				
Molton Holdings	48.1%			
Share Price Graph				



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