



DRILLING DOWN

THE OVERVIEW OF PERFORMANCE AND PROSPECTS
OF AIM OIL AND GAS COMPANIES IN 2013

MARCH 2014

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KEY FINDINGS

- 2013 was another difficult year for AIM listed oil and gas companies, with market valuations falling in both absolute terms and relative to the wider market.
- The decline in the AIM Oil and Gas index was greater than for oil prices and lasted for longer. Whereas oil prices declined by 10% from the start of the year to the low point in April before starting their recovery, the index declined by 20% to its low point in June.
- The aggregate market capitalisation of AIM's oil and gas companies declined by 4% from £13.8 billion at the end of 2012 to £13.2 billion at the end of 2013. After the turbulence of the 2007 – 2010 period, when total market value fluctuated from a trough of £3.6 billion in 2008 to a peak of £16.9 billion in 2010, aggregate market caps have been relatively stable, with total market value fluctuating between £13 billion and £14 billion.
- IPO fundraisings in 2013 of £54m were 59% lower than in 2012. This is a stark contrast to the wider AIM market, which saw a 51% increase in IPO proceeds in 2013.
- Secondary issues were down 15% to £365m in 2013. This is the fourth year in a row that further equity funding on AIM had declined. In contrast, the wider AIM market saw an increase of 11% in further issues in 2013.
- Despite the challenging climate for the sector, the number of oil and gas companies on AIM remained broadly stable. The net reduction of two companies was partly a result of M&A activity, suggesting an ongoing period of consolidation within the sector.



THE LONG FREEZE IN THE CAPITAL MARKETS, WHICH HAD EXISTED SINCE THE FINANCIAL CRASH IN 2008 STARTED TO THAW IN 2013. ALTHOUGH ECONOMIC GROWTH CONTINUED TO STRUGGLE FOR TRACTION IN THE FIRST HALF OF THE YEAR, AN UNEXPECTEDLY STRONG RECOVERY STARTED IN A NUMBER OF WESTERN ECONOMIES IN THE SECOND HALF, NOTABLY IN THE UK AND THE US.

Oil prices largely reflected these wider economic developments. After declining by 10% over the first few months of the year, they started a slow recovery in April and ended the year in line with their starting position of approximately US\$110 per barrel.

Despite this improvement in outlook, AIM listed oil and gas companies have still found it tough to raise finance and progress their projects. In our third annual review of the performance of AIM listed oil and gas companies, we examine how they have fared in comparison to the overall AIM market and the FTSE more generally. We also assess the trends in the size, number and market caps of AIM listed oil and gas companies, highlight those that have seen the most dramatic changes in fortune during the year, and review the level of fundraising activity in the sector.

MARKET PERFORMANCE

A DIFFICULT YEAR

2013 WAS A YEAR OF UNDER-PERFORMANCE FOR AIM LISTED OIL AND GAS COMPANIES RELATIVE TO THE REST OF THE MARKET.

Figure 1 shows that, whereas the AIM 100 and FTSE 100 indices rose by 21% and 12% respectively over the year and, in broad terms, followed a similar pattern, the AIM Oil & Gas index declined by 8%. In addition, whereas the low point for the AIM 100 index was only 3% below its starting position and the FTSE 100 index never fell below its starting position, the AIM Oil & Gas index had declined by 20% by June before recovering in the second half of the year.

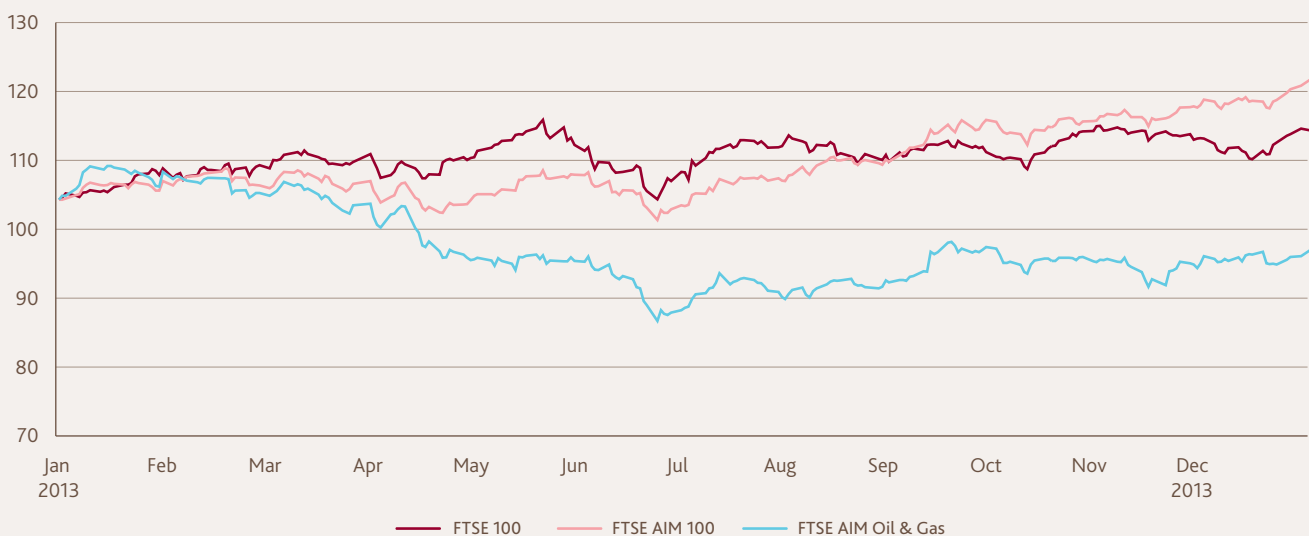
A broadly similar performance was noted in *Extracting Insights*, our review of the performance of AIM listed mining companies for the year to June 2013. This highlights that resource companies in general have found it difficult to build value in recent years.

This trend is also highlighted by a review of these indices over the last five years (see Figure 2). Although the AIM Oil & Gas index outperformed the AIM 100 index and, in particular, the FTSE 100 index for most of this period, it fell substantially over the last 12 months to finish below the AIM 100 index. Although it was still 15% above the FTSE 100 at the end of the five year period, this is a small margin considering it had increased over five times faster by early 2011.

Interestingly, given the strong weighting of oil and gas companies in the AIM 100 (representing 22% in terms of market cap at the end of 2013), the AIM 100 index finished up over the year. This shows how strongly other AIM 100 companies performed in 2013.

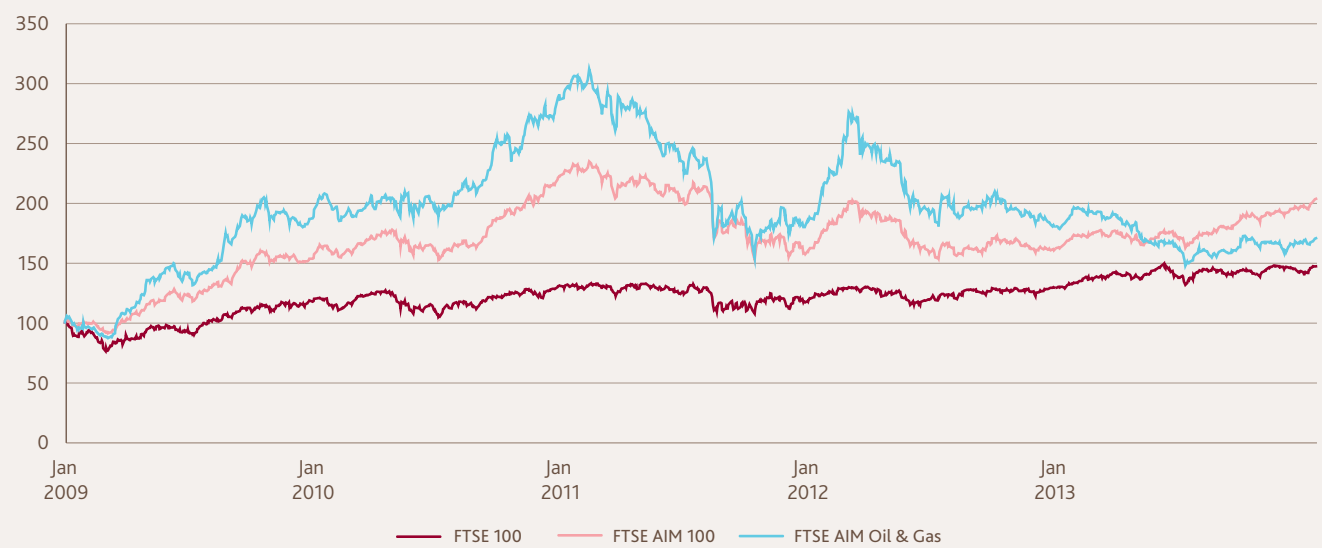
In broad terms, the AIM Oil and Gas index has followed a similar pattern to oil prices in 2013, with a general decline in the first half of the year, followed by a recovery in the second half as shown in Figure 3. However, the extent of the decline for the AIM Oil and Gas index was greater than for oil prices and lasted for longer. Whereas oil prices declined by 10% from the start of the year to the low point in April before starting their recovery, the index declined by 20% to its low point in June. As a result, the AIM Oil & Gas index ended the year 8% lower than at the start, whereas oil prices had recovered to their starting position of approximately US\$110 per barrel.

FIGURE 1: STOCK MARKET INDICES 2012 AND 2013 (REBASED)



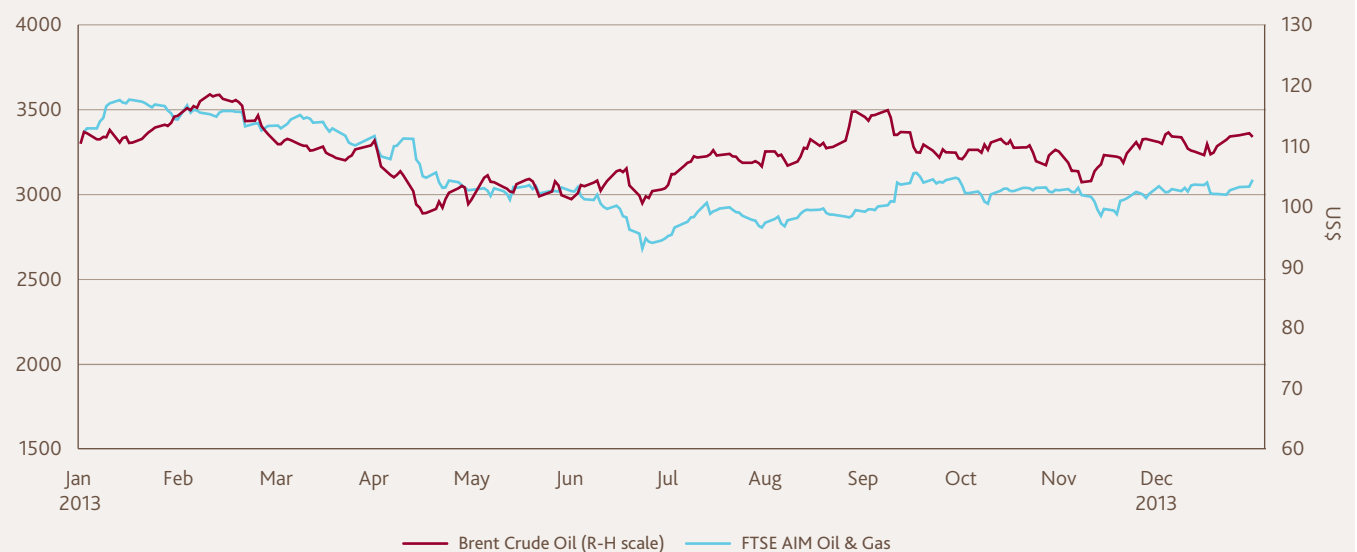
Source: Bloomberg

FIGURE 2: STOCK MARKET INDICES – 5 YEAR (REBASED)



Source: Bloomberg

FIGURE 3: COMMODITY PRICES



Source: Bloomberg

CONTINUED STABILITY

THERE HAS BEEN LITTLE CHANGE IN THE NUMBER OF OIL AND GAS COMPANIES ON AIM OVER THE LAST FEW YEARS, AT JUST OVER A HUNDRED. HOWEVER, THE YEAR END FIGURE WAS DOWN TO 104 COMPANIES, TWO LESS THAN THE PREVIOUS RECORD OF 106.

The trend in the number of oil and gas companies and aggregate year end market cap since 2006 is shown in Figure 4.

There were eight leavers and six joiners in 2013, representing a similar level of churn as in 2012. However, the net reduction of two in the number of oil and gas companies was the first such reduction since 2009.

Six of the eight leavers were the result of takeovers, mergers or the disposal of projects. These six companies were in addition to the five that left in 2012 as a result of M&A activity, suggesting an ongoing period of consolidation within the sector.

The average market cap of the leaving companies in 2013 (as at the previous year end) was £47 million. Four of the six companies acquired had market caps in excess of £50 million as at 31 December 2012, which suggests that most of the M&A activity in 2013 was for positive reasons rather than being distressed sales.

Of the six joiners, four were straight IPOs, one was a secondary listing of a TSX company and one was a transfer from the ISDX Growth market.

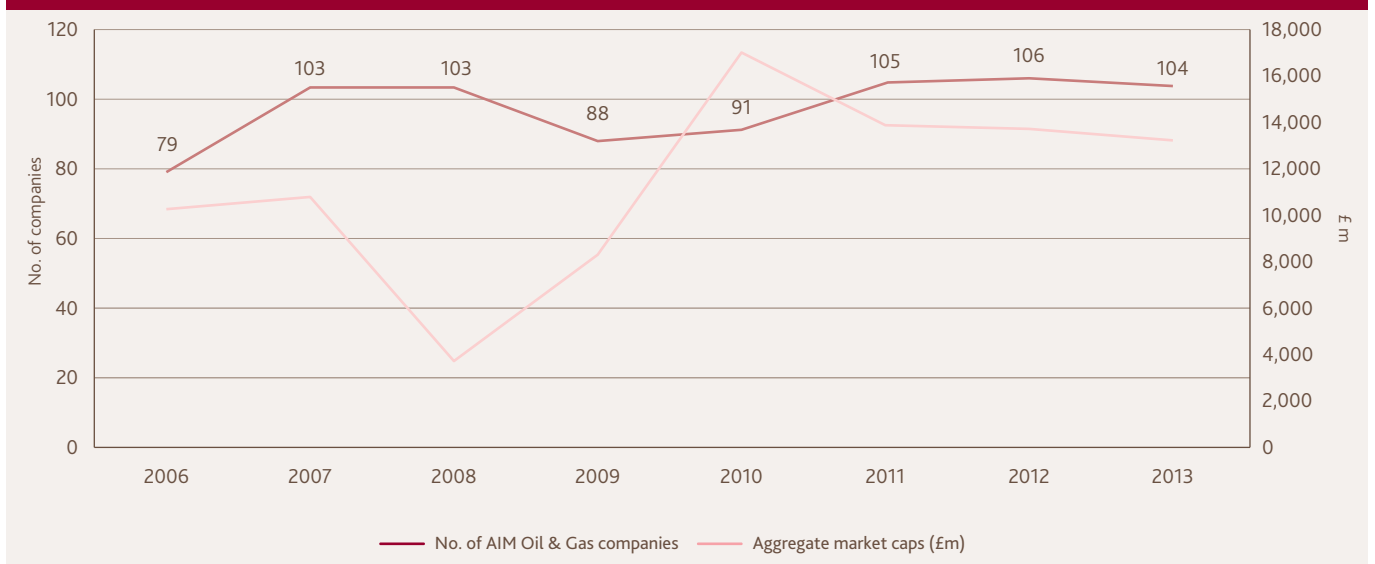
Although all of the joiners raised funds on joining AIM, they only raised a total of £54 million, with Lekoil (£32 million) and Falcon Oil and Gas (£17 million) being the only companies to raise substantial funds. This compares to £186 million and £131 million being raised from IPOs in 2011 and 2012 respectively (albeit that 2012 included £118 million raised by one company, Eland Oil and Gas).

The average market capitalisation of the joiners was £22 million at 31 December 2013 but this would have been even lower without Lekoil (£206 million) and Falcon Oil & Gas (£100 million). Despite these two companies, the average is considerably lower than the equivalent average in 2011 and 2012 of £30 million and £55 million respectively.

The aggregate market capitalisation of AIM's oil and gas companies ticked down by 4% to £13.2 billion. After the turbulence of the 2007-2010 period, when total market value fluctuated from a trough of £3.6 billion in 2008 to a peak of £16.9 billion in 2010, the aggregate market cap has since been relatively stable, with total market value fluctuating between £13 billion and £14 billion.

The average market cap per company fell from £130 million per company to £127 million. This minor reduction reflects the low average size of new joiners relative to the leavers. However, the average market cap per company remains in line with the pre-crisis average in 2006 of £130 million.

FIGURE 4: AIM OIL & GAS COMPANIES – NUMBERS AND MARKET CAPS



Source: London Stock Exchange and BDO analysis

TOP TEN FOCUS

2013 WAS ANOTHER YEAR OF STABILITY FOR THE TOP 10 AIM LISTED OIL AND GAS COMPANIES. THE AVERAGE MARKET CAP OF THE TOP 10 WAS £835 MILLION, WHICH WAS ONLY 3% DOWN ON THE PRIOR YEAR AND BROADLY IN LINE WITH 2011 (£840 MILLION).

There were only two changes to the composition of the top 10, with the top seven places all remaining unchanged in terms of both company and order.

Compared to AIM listed mining companies that we review in our *Extracting Insights* publication, it is notable that the composition and order of the oil and gas top 10 is much more consistent. Seven of the current top eight (the exception being Amerisur Resources) have been in the top 10 since 2010, which was the first year of our top 10 list.

The two new companies were Ithaca Energy and Quadrise Fuels International, which both joined the top 10 on the back of large increases in their market caps, the reasons for which are not obvious. They replaced Providence Resources and Faroe Petroleum whose market caps both declined. Ithaca Energy and Quadrise Fuels

International saw the two largest increases in market cap of any AIM listed oil and gas company, whereas Providence Resources suffered the largest fall in market cap.

Having moved up from third in 2012, Indus Gas retained its position in top spot, despite a fall in its market cap of £255 million, the second largest absolute reduction behind Providence Resources (£256 million). Indus Gas has its principal interests in an oil and gas exploration and development project in Rajasthan, India. It also retains its position as the second largest company of any sector on AIM by market cap, with Gulf Keystone Petroleum, Energy XXI and Coastal Energy being in third, fifth and sixth position respectively.

Bankers Petroleum saw the third largest increase in market cap of £144 million. This, together with the reduction in Coastal Energy's market cap of £173 million (the third largest reduction of any AIM listed oil and gas company) helped to close the gap between it and the big four from £918 million to £601 million.

In terms of the development cycle of companies in the top 10, there was no overall change, with eight out of the 10 being production companies at the end of 2013, in line with the profile at the end of 2012.

THE 10 LARGEST COMPANIES BY MARKET CAP AS AT 31 DECEMBER 2012 AND 2013

Table 1: Largest companies by market cap

A1 31 December 2013	£m	%	At 31 December 2012	£m	%
Indus Gas	1,629	-14	Indus Gas	1,885	44
Gulf Keystone Petroleum	1,545	0	Gulf Keystone Petroleum	1,551	-4
Energy XXI (Bermuda)	1,235	-12	Energy XXI (Bermuda)	1,398	1
Coastal Energy	1,214	-12	Coastal Energy	1,387	38
Bankers Petroleum	613	31	Bankers Petroleum	469	-27
Amerisur Resources	601	30	Amerisur Resources	463	202
Rockhopper Exploration	438	0	Rockhopper Exploration	439	-37
Green Dragon Gas	375	4	Providence Resources	400	292
Ithaca Energy	358	74	Green Dragon Gas	362	-56
Quadrise Fuels International	346	251	Faroe Petroleum	292	-11

Source: London Stock Exchange and BDO analysis

RISERS AND FALLERS

THE MAIN MOVERS

OF THE 98 COMPANIES STILL LISTED ON AIM BY THE END OF DECEMBER, THERE WERE 65 FALLERS AND 33 RISERS.

This shows that the difficult market conditions were widely felt and not restricted to a few companies.

Seven of the current top 10 saw some of the most significant movement – in both directions. Four of the top five risers all finished the year in the top 10 – while the four biggest fallers had all been in the top 10 at the end of 2012. This correlation between top 10 and the largest risers and fallers has been a consistent theme ever since we started our reviews in 2011.

Eight of the 10 largest fallers in 2013 are now in the production phase, in contrast with last year when there was an even split between exploration/development and production companies. Given the risks inherent in this sector, this shows that volatility can be experienced at any point in the exploration and production cycle.

There were several company specific factors that contributed to the share price performances of the companies below, particularly for the largest increases in market caps. In general there was no obvious reason for the majority of reductions noted below. This suggests that wider sector concerns were the main reasons for the poor performance of AIM oil and gas stocks.

THE LARGEST INCREASES AND DECREASES IN MARKET CAP IN 2013

Table 2: Increase/Decrease in market cap

Risers	£m	Fallers	£m
Quadris Fuels International	247	Providence Resources	(256)
Ithaca Energy	152	Indus Gas	(255)
Bankers Petroleum	144	Coastal Energy	(173)
Petroceltic International	141	Energy XXI (Bermuda)	(164)
Amerisur Resources	138	Gulfsands Petroleum	(71)
Trinity Exploration & Production	87	Bowleven	(70)
Tower Resources	85	Regal Petroleum	(66)
Nighthawk Energy	57	Maple Energy	(63)
Parkmead Group	52	Antrim Energy	(55)
Falkland Oil & Gas	47	Lansdowne Oil & Gas	(46)

Source: London Stock Exchange and BDO analysis

FUNDING

FEW POSITIVE SIGNS

ALTHOUGH COMPANY NUMBERS AND MARKET CAPS WERE RELATIVELY STABLE IN 2013, FUNDING CONTINUED TO BE DIFFICULT.

We set out in Figure 5 the trend of IPO and secondary fundraisings over the last four years.

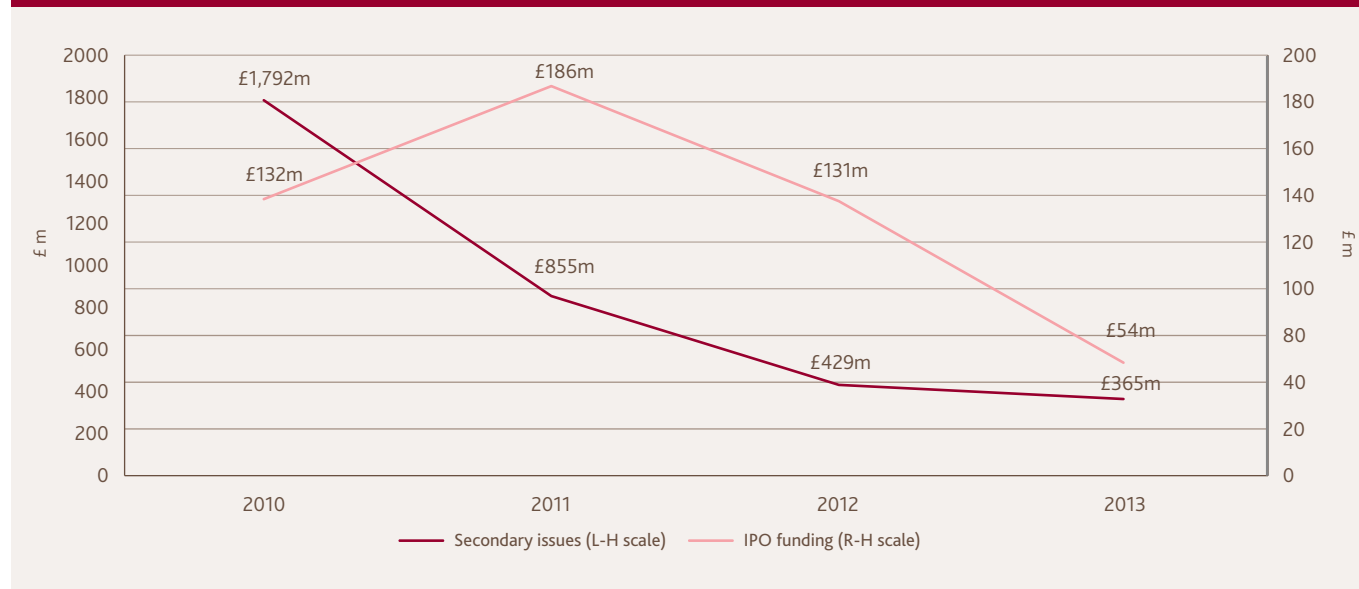
Secondary issues were down 15% to £365 million in 2013. This is the fourth year in a row that equity fundraisings on AIM had declined and is in contrast to the wider AIM market, which saw an 11% increase in further issues from £2.45 billion in 2012 to £2.72 billion in 2013.

If only those raising more than £1 million are taken into account (i.e. ignoring small amounts raised through the exercise of share warrants and so forth), 32 companies raised additional equity at an average of £11.3 million each. In 2012, these numbers were 34 and £12.5 million, while in 2011 there were 36 and £23.7 million. This suggests that, although similar numbers of companies have raised funds over the last three years, investors appear to be increasingly reticent to invest substantial sums in each project.

The difficult fundraising climate is reflected by the relatively small amount of IPO fundraisings in 2013, which at £54 million were 59% lower than in 2012. This is a stark contrast to the wider AIM market, which saw a 51% increase in IPO proceeds from £643 million in 2012 to £974 million in 2013. This is consistent with the fortunes of mining companies, whose IPO fundraisings were lower in 2013 than the wider AIM market.

Although 2013 was a year of recovery for capital markets in general, it would appear that oil and gas companies are still experiencing difficulties in raising equity finance, whether through secondary or IPO issues.

FIGURE 5: AIM OIL & GAS FUNDRAISING TRENDS



Source: London Stock Exchange and BDO analysis

The largest secondary issue in 2013 was £76 million for Lekoil. Raised in several tranches, but mainly in November 2013, these funds were for completing the drilling and testing of existing wells, further exploration, refinancing and general working capital purposes. These funds were in addition to the £32 million it raised at IPO in 2013. In total, Lekoil's equity fundraising in 2013 of £108 million accounted for 26% of all oil and gas funds raised during the year.

Madagascar Oil raised £50 million in February 2013 to strengthen its financial position, complete the Tsimiroro Steam Flood Pilot and carry out further exploration activity on its other exploration interests. Wentworth Resources raised funds in two tranches, the largest of which was in October (£24 million), to enable it to carry out its planned work activities in Mozambique and Tanzania and for working capital purposes.



THE 10 LARGEST SECONDARY ISSUES DURING 2013, TOGETHER WITH THE LARGEST ISSUES IN 2012 BY WAY OF COMPARISON

Table 3: Largest further issues

Years ended 31 December further issues	£m	Year ended 31 December 2012	£m
Lekoil	76	Falkland Oil & Gas	48
Madagascar Oil	50	Borders & Southern Petroleum	46
Wentworth Resources	28	Xcite Energy	41
Victoria Oil & Gas	23	Chariot Oil & Gas	31
Igas Energy	23	President Energy	27
Parkmead Group	19	Amerisur Resources	26
Bowleven	13	Range Resources	20
Serica Energy	12	Red Emperor Resources	20
Range Resources	12	New World Oil & Gas	17
Tower Resources	10	Madagascar Oil	17
	267		293
Others	98	Others	136
	365		429

Source: London Stock Exchange and BDO analysis

FUNDING

FEW POSITIVE SIGNS

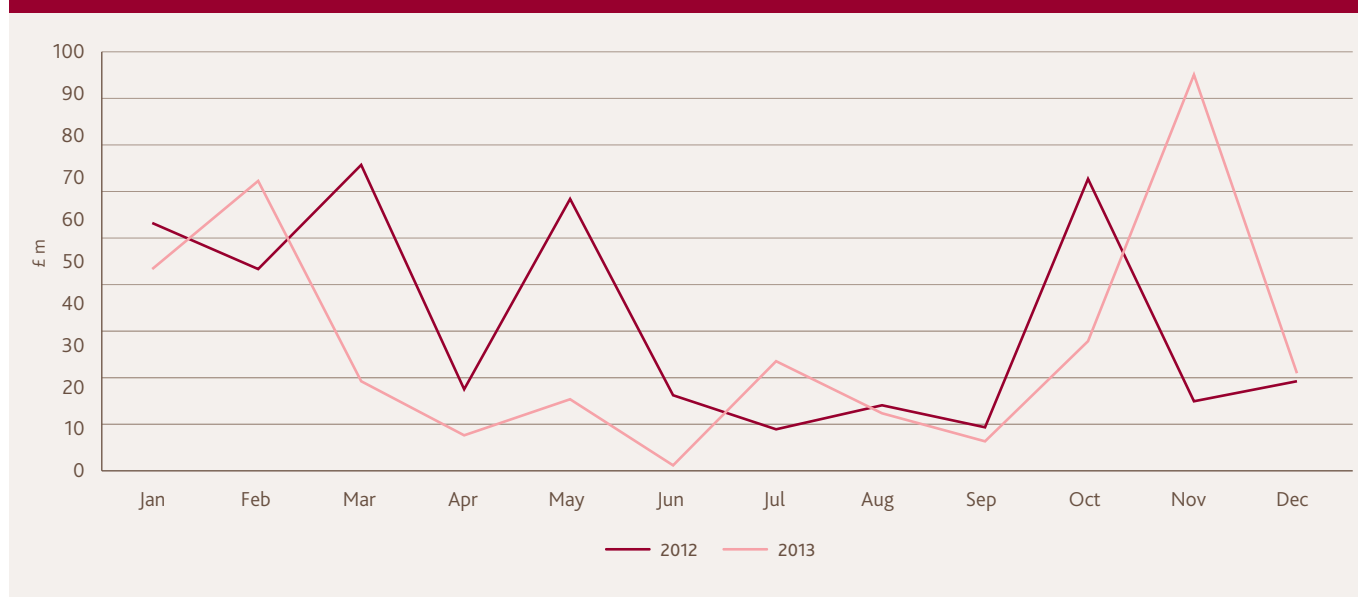
The monthly fundraising profile for AIM oil and gas companies for 2012 and 2013 is shown in Figure 6.

Secondary fundraisings were relatively evenly split between the first half of the year (46%) and the second half (54%), whereas in 2012 two thirds was raised in the first half.

The peaks in February and November 2013 include the secondary issues in respect of Madagascar Oil (£50 million) and Lekoil (£62 million) respectively.

It is encouraging to note that 41% of the secondary funds raised in 2013 were in the final quarter of the year. November was a particularly healthy month, with funds being raised by Bowleven (£13 million) and Serica Energy (£12 million) as well as Lekoil (£62 million). This was in line with the wider AIM market for which 43% of total secondary proceeds were in the final quarter. This reflects the general opening up of the capital markets to new investment and will hopefully usher in a more favourable climate in 2014, although it is too early in the year for any clear evidence to support this contention.

FIGURE 6: FURTHER ISSUES



Source: London Stock Exchange and BDO analysis

CONCLUSION

2013 WAS ANOTHER DIFFICULT YEAR FOR AIM LISTED OIL AND GAS COMPANIES COMPARED WITH THE WIDER AIM AND LISTED MARKETS. ALTHOUGH THERE WAS NO DRAMATIC DETERIORATION IN THE KEY STATISTICS FOR THE SECTOR, THERE WERE NEVERTHELESS DOWNWARD TRENDS IN MARKET CAPITALISATION AND THE VALUE OF IPO AND SECONDARY ISSUES. HOWEVER, ON A POSITIVE NOTE, A REASONABLE NUMBER OF COMPANIES DID MANAGE TO BUCK THIS TREND, WITH 33 COMPANIES RISING IN VALUE, INCLUDING FIVE SHOWING AN INCREASE IN MARKET CAP IN EXCESS OF £100 MILLION.



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