Dana Gas Q2 2017 Investor Call transcript

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Corporate Participants

Caroline Berzi
CI Capital – Equity Research Analyst

Mohammed Mubaideen
Dana Gas – Head of Investor Relations

Dr Patrick Allman-Ward
Dana Gas – Chief Executive Officer

Christopher Hearne
Dana Gas – Chief Financial Officer

Iman Hill
Dana Gas – Technical Director

Presentation

Operator
Good morning, good afternoon, and good evening everybody. This is Caroline Berzi and on behalf of CI Capital, I am pleased to welcome you to the Dana Gas Second Quarter 2017 Results conference call. With us from Dana Gas, we have CEO Dr Patrick Allman-Ward, CFO Chris Hearne, Technical Director, GM/UAE and President Egypt, Iman Hill and Head of Investor Relations Mohammed Mubaideen. With no further delay, I will now pass you on to Mohammed Mubaideen to outline the presentation.

Mohammed Mubaideen
Many thanks, Caroline. Welcome to the call everyone.

[Disclaimer]

I will now hand over the call to Dana Gas CEO, Dr Patrick Allman-Ward to start the presentation, which will be concluded with a Q&A session.

Dr Patrick Allman-Ward

Thank you, Caroline and Mohammed for the introduction. I welcome you all to our second quarter and first half earnings call. Without further ado, let us turn to slide 5. I will talk you through our achievements for the quarter before handing over to Chris for a run-through of our financials and Iman on our country operations.

Let me start with our operational performance. June saw us temporarily shut down our El Wastani gas plant in Egypt for planned maintenance. The repair and maintenance work lasted for nine days and was carried-out successfully, on time and on budget, with an outstanding HSSE record of no incidents and no environmental spills. However, this did have a direct impact on our second quarter production output. Chris will talk in more detail on this shortly. But despite this one-off reduction in production, first half 2017 group production was 67,550 boepd, 6% higher year-on-year, driven by greater production output from Egypt.

In April, as previously mentioned, we successfully concluded our first international condensate sale. The 150,000 barrels of Wastani condensate cargo was sold for $7 million in hard currency and was a direct result of the Gas Production Enhancement Agreement that we put in place with the relevant Egyptian government agencies in August 2014. A second cargo was sold in early July. This was for 157,000 barrels of condensate at a total price of US$ 7.0 million.

In terms of our financials the results have been very positive. Our half-year numbers are $222 million in revenues and $23 million in net profit, compared to $178 million and $13 million in H1 2016, an increase of 25% and 77%, respectively. The increase in revenue was due to greater production and higher realised hydrocarbon prices. In conjunction with lower financing and other expenses, the resulting net profit increased.

We continue to focus on managing our costs. During the first half we reduced our operational costs by 7%. G&A costs, which we successfully reduced by 43% during 2016, remain flat in H1 2017 in keeping with the same period last year so we are managing to hold the gains.

Our cash in hand as of 30 June is $337 million as compared to year-end balance of $302 million. It is higher, in large part due to the $110 million industry payment received from the Egyptian government and from collections in Kurdistan Region of Iraq, which totalled $55 million. The group collected a total of $198 million in the first half of 2017. Strong Q2 collections helped lower our group receivables position at period end to $900 million as compared to $999 million at the end of the first quarter of 2017.

However, Dana Gas Egypt has financial commitments (accounts payable) of $60 million that have accumulated during the last 18 months of drilling activity related to the GPEA investment program that need to be repaid. Furthermore, we have plans to drill three exploration wells on Block 1 in Egypt in the fourth quarter as part of our concession activity commitment.

We also need to maintain the necessary financial strength and depth to sustain ourselves through the short to medium-term cash collection challenges that the Company faces until it recovers its affirmed receivables and thereby to realise the enormous value of our assets.

There is one point I would like to discuss regarding our Zora Gas Field project before handing over to Chris. The field is currently delivering approximately 10 mmscfd sales gas to Sharjah power station and producing 100 bbl/day of condensate. Production has continued to decline from 3,250 boepd in June 2016 to 1,650 boepd by the end of the second quarter this year. A detailed geo-technical study was carried out which has identified reservoir deliverability as the primary reason for this underperformance. We have now received the preliminary results of our Field Development Plan, which indicates that at current gas prices any further well intervention is unlikely to be economically viable. As a result, this will need to be taken into consideration when we undertake our annual reserves audit towards year-end and will be factored into the final decision that will have to be taken on the asset in due course.

I will discuss and provide an update on the arbitration and sukuk later on. I will now pass on to Chris to take you through the financial results in more detail.

Chris Hearne
Thank you, Patrick and welcome, everyone.

Let us start on slide 7, I am pleased to report that we have remained profitable during the second quarter and that the Company's overall first half performance has been strong.
During the second quarter, we reported Gross Revenue of $104 million and a Net Profit of $12 million, as compared to $96 million and $7 million respectively in Q2 2016.
Our first half Gross Revenue was $222 million and Net Profit was $23 million, increases of 25% and 77% respectively, compared to H1 2016.
The solid increase in our half-year profitability is based on several factors:
Firstly, a 25% increase in gross revenue which is due to higher production in Egypt and also to higher realised hydrocarbon prices.
Secondly, to an increase in our profit entitlement in KRI.
Thirdly, to the positive impact of our cost management program, which we have had in place since 2014, and which has helped us further optimise our operating costs during the first half of the year by 7%.
Fourthly, to a $5 million increase in the Other Income segment.
Lastly, a reduction in finance costs by $8 million or 18% as a result of settling the Zora and other loans during the period.
This increase was however partly offset by a reduction in investment and finance income.

Turning to slide 8, The first graph, top left, gives the Company's production numbers for the first half 2017 as compared with the equivalent number in 2016.
Production increased 6% to 67,550 boepd. The increase was mainly driven by the strong production performance in Egypt, where production was up 13% and consistent

performance in KRI, which continued to produce steadily at 25,900 boepd. Only the UAE continues to lag for the reasons mentioned by Patrick earlier.
The second graph, top right, shows the average production number on a quarterly basis, Q2 2017 versus Q2 2016. Due to lower production at Zora and KRI, group production dropped by 2% to 65,400 boepd on a quarter-by-quarter basis.
The next graph, bottom left, gives the average realised prices achieved during the quarter. On a half-year comparable basis, H1 2017 realised prices averaged $44 per barrel for condensate and $32 per barrel of oil equivalent (boe) for LPG. This compares to $32 and $28 boe respectively in 2016.

Now on to slide 9,Here we present the Company's OPEX and CAPEX.
In the first half of the year, OPEX dropped by a further 7% to $25 million and G&A remained steady at $7 million as compared to the same period in 2016.
We continue to manage our cost base efficiently. I think it is worth reminding everyone that our 2016 G&A and OPEX costs were down 43% and 7% respectively from the year before.
We also continue to balance our expenditures with our collections in Egypt. With the additional monies coming in during the second quarter, our priority remains to settle our creditors who have continued to work with us over the last 18 months to deliver the GPEA program. Accumulated liabilities in Egypt at the end of H1 2017 amount to $60 million.

Moving on to slide 10, which covers the Company's liquidity position, The Group collected a total of $198 million during the first half of the year, which has allowed us to report strong positive free cash flow of $142 million as compared to an outflow of $32 million in the first half 2016. However, the majority of the collection received from the industry payment, will be used to pay down creditors amounting to $60 million, and to fund further spending required for the Block 1 drilling activity being planned for Q4 2017. Iman will explain this in more detail shortly.
Our cash at the period end stood at $337 million. This is an increase of 11% on year-end 2016 and follows the collection $198 million during the first half of the year. Cash preservation remains critical to the Company – our short to medium-term cash collection continues to remain challenging. We continue to focus on this and managing our costs, especially with the financial commitments in Egypt as outlined previously.
In order to reflect the Company's legal position in connection with the sukuk we have reclassified the Sukuk from Borrowings to Capital received on issuance of Sukuk. The final outcome of the ongoing litigations would likely result in a significant liability for the Sukukholders to repay the Company for excess 'on account profit payments', based on a lawful reconciliation of the matter.

Turning to slide 11, which provides a summary of the Company's Receivables and Collections at the period end. Egypt's trade receivables balance has decreased to $189 million from $265 million at the end of 2016 as we collected $135 million in the first half.
Our collection to billing rate in Egypt and KRI, for the first half 2017, was 229% and 115% respectively.
KRI's trade receivables are also decreasing slightly and our total receivable there now stands at $707 million. Our share of collections for the period stood at $55 million, partly as a result of collecting regular payments on the $100 million Peremptory Order as well as receiving full entitlement on our liquid sales. The KRG has paid our Pearl Consortium $82

million, of which our share is $29 million, against the Peremptory Order as at 30 June 2017.
Overall, in the first half of 2017, we received just a fraction under $200 million in receivables, thereby reducing total group receivables to $900 million as compared to $982 million at the end of 2016.
On that positive note, I will hand you over to Iman who will provide an operational overview.

Iman Hill
Thank you, Chris, let me start with Egypt on page 13 and 14. I will begin with the planned shutdown of the El Wastani gas plant in June which was completed safely and successfully. There was a complete shutdown for five days for critical inspection and maintenance and a further partial shutdown for four days. The work was conducted by Egyptian contractors, which included 1,300 personnel working with WASCO, our joint venture operator. There were 105 planned activities including major repairs and inspections undertaken, and the work was concluded with no recordable incidents or environmental spills, reflecting our excellent, HSSE performance. Although this did affect our June production numbers, the shutdown was necessary for us to improve plant performance and allow us to maintain production at just under 40,000 barrels per day until the end of the year.

Secondly, one of our critical projects, the south Faraskur compression project is nearing completion, with start-up planned during the third quarter. This project is tied into the El Wastani gas plant and will add further production and help us maintain our production at the full plant capacity. We have also started preparation work on our North El Salhiya Block 1 drilling campaign. This will commence during the fourth quarter when we will drill three onshore wells; North El Basant, East/South Abu El Naga-1 and Bahy-2. The company owns 100% of the concession area, any exploration success, and future production can be easily monetised through tieback to our existing infrastructure. Separately, work is progressing on our North El Arish Block 6 offshore concession in the Eastern Nile Delta. We are preparing to drill an exploration well at the beginning of 2018. In July, we sold a cargo of 157,000 barrels of condensate for $7 million. This is the second cargo exported by Dana Gas under the GPEA. In the second half of the year, we have also received $135 million in payment from the Egyptian Government. We continue to have high-level discussions with officials to secure further payments.

Turning to slide 15, Kurdistan has remained unchanged. Our average annual production was just under 26,000 boepd for the first half of the year. There is nothing further to report or update at this time.
Wrapping up with Zora on slide 16, as Patrick explained, the draft field development plan indicates that any further well intervention is not currently economically viable. We will continue to operate Zora for as long as possible before a final decision is taken on the future of the asset.

Thank you for your time and now back to Patrick to say a few more words.

Dr Patrick Allman-Ward

Thank you, Iman. Thank you, Chris.

Please turn to **slide 17** where I provide you with a brief overview and summary of the Arbitration cases and Sukuk.

Regarding the arbitration cases, we continue to wait for the final judgement regarding the NIOC damage claims and this is now expected towards the end of 2017 or in the first half of next year. In relation to the KRG, we continue to press ahead with recovering the money owed to us from the second and third Partial Final Awards, and have prepared for the final damages claim that will be heard in London in September.

With regard to the Sukuk, the Company made a public statement to Sukukholders on the 6th July and has kept the market updated since then through regular disclosures on the ADX and press releases. The transcript of the call to Sukukholders and the texts of all the ADX disclosures and press releases can all be found on the Company website. Due to the existence of ongoing legal proceedings we will not be making any further statements regarding the Sukuk on this call and we will not be taking any Q&A related to this subject. However, if any Sukukholder has any questions, they are welcome to submit these in writing to Mohammed Mubaideen and we will try to provide answers subject to legal advice.

Let me now summarize the discussion so far with reference to slide 19.

- Overall, the second quarter has been solid.
- Our operational performance has been steady in our two key production areas and we successfully completed a highly successful planned shutdown in Egypt with minimal disruption and no HSE or environmental incidents.
- Our collections were strong this quarter – with an industry wide payment from Egypt making important contributions to our collections. However, we remain cautious about the timing and scale of future collections given our past experience and therefore we continue to maintain a strategy of cash conservation.
- We remain excited about the potential for medium-term growth opportunities in Egypt and the development of our world-class assets in KRI over the medium to long term.
- Our NIOC damages claim should be forthcoming in the next ten months and the final phase of our damages claim related to the KRG arbitration will be heard in September.

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