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Deutsche Rohstoff Buy

Germany | Oil & gas **Beta Profile:** MOMENTUM QUALITY **MCap: EUR135.7m**

Target Price:	EUR 40.00
Current Price:	EUR 26.70
Up/downside:	49.8%
Market data:	16 November 2022

Bloomberg: DR0 GR	Reuters: DR0G.DE
Free float	90%
Avg. daily volume (EURm)	0.7
YTD abs performance	31.5%
52-week high/low (EUR)	33.50/19.25

Sustained price levels, higher production and earnings – CMD feedback

Key points:

- The best is yet to come for DRAG, as it will increase its average yearly production from 6,000 BOEPD in 2019-21 to 9,000 BOEPD in 2022-24.
- The group has an attractive risk profile, given its low-risk operations in fields which have already been explored and the cooperation with major US oil players, in combination with the lucrative economic efficiency due to the current price levels.
- DRAG should continue to benefit from the structural trends, as the current environment is pointing towards sustained price levels and global undersupply.

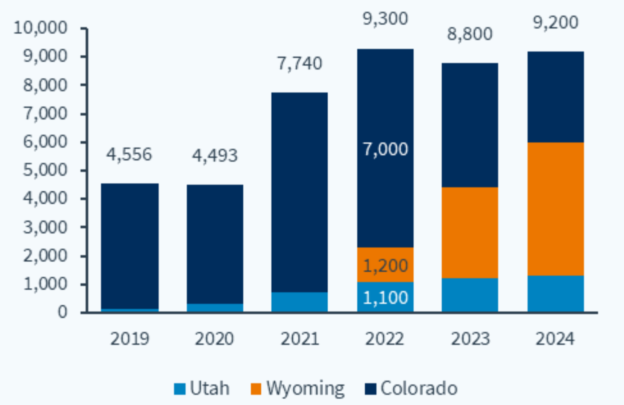
CMD divided into three parts: DRAG's operations and perspectives, economic efficiency, and the global oil market

- The company hosted its second digital CMD with CEO Jan-Philipp Weitz and CFO Henning Döring. The two-hour event comprised the development and perspectives for Deutsche Rohstoff AG in the US oil and gas market, followed by an overview of the economic efficiency and profitability drivers of drilling wells, including a comparison of DRAG's drilling operations in Wyoming and Colorado.
- The CMD was complemented by a discussion regarding the supply and demand situation in the global oil market and the potential impacts – including from political players – on the oil price.
- Management illustrated how the technological improvement over the past decade in the drilling and production of oil wells has led to a fourfold increase of BOE after eleven months from a single well.
- Due to its proximity to significantly larger US oil and gas companies, DRAG is in good company with its operations in Colorado, Utah, and Wyoming, as it is able to assess the mostly public information from its competitors regarding efficiency or how many wells can be located next to each other. DRAG only drills wells where it is very likely that production is economically viable.
- Overall, DRAG's operations thus have a very attractive risk profile, as the information provided by its peers enables the group to operate at low risk given the lack of uncertainty. The chances of dry drilling or total loss are thus very limited and in most cases the ROI is achieved in the following years.
- Given major US oil companies' budget constraints, DRAG with its more than ten years' experience is an attractive and established partner, and it appears that these partnerships (as with Oxy) are a win for both sides.

Production set to increase to higher levels over 2022-24E with high cash flow generation

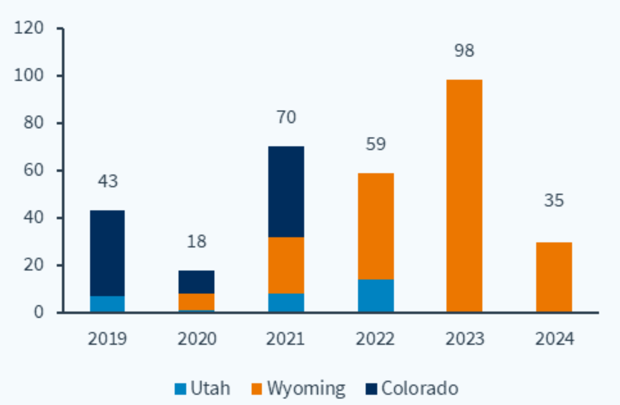
- DRAG's second CMD was geared towards educating current and potential shareholders about the group's US oil & gas operations as well as its outlook regarding production, drilling, investments, and subsequent earnings.
- The group will increase focus on Wyoming, where it currently holds a 70% stake in 20 wells, which are expected to produce 1,200 BOEPD in 2022. DRAG's assets in Colorado (87 operating wells with a 60% stake) are expected to produce 7,000 BOEPD in 2022 and will be overtaken as the group's largest production driver in the coming two years by its assets in Wyoming. In total, the group aims to increase BOEPD on average to 9,000 per year in 2022-24 (up from 6,000 BOEPD in 2019-21) by investing c. EUR70m per year.
- Below we show management's 2022-24 production and capex estimates, which are rough estimates and could differ slightly from the actual figures, as we have copied them from a graph provided in the presentation.

Chart 1: DRAG's yearly estimated BOEPD from CMD presentation



Source: DRAG, Kepler Cheuvreux

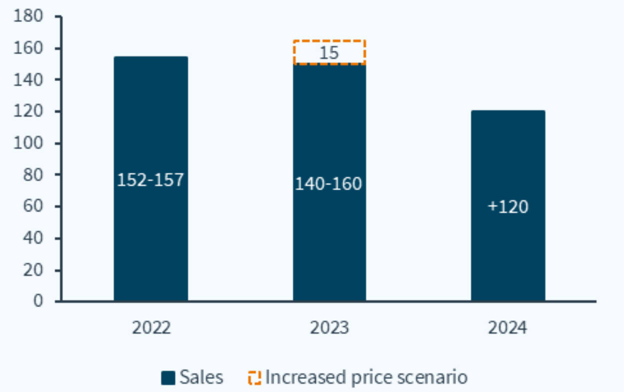
Chart 2: Capex by US state (EURm)



Source: DRAG, Kepler Cheuvreux

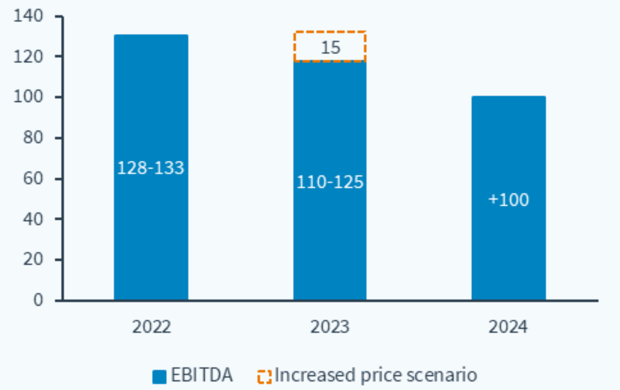
- Regarding sales and EBITDA, management has reiterated its FY 2022-24E guidance on the basis of a USD75 WTI price, which we show in the graphs below.
- Should the average WTI price be USD85 in 2023, management expects an additional EUR15m in sales and EBITDA.

Chart 3: FY 2022-24E sales guidance (EURm)



Source: DRAG

Chart 4: FY 2022-24E EBITDA guidance (EURm)



Source: DRAG

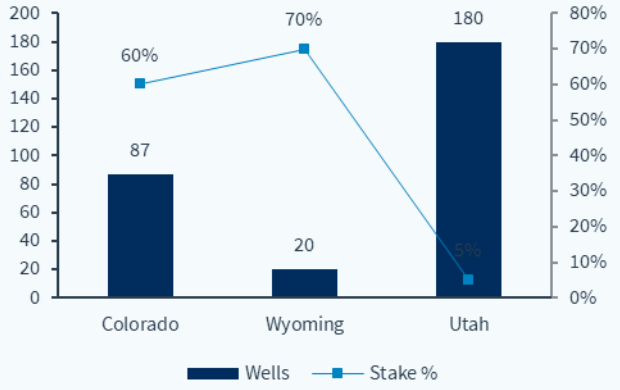
- DRAG has laid the foundation for a significant increase in potential wells going forward, which are not part of the production or sales and earnings guidance.
- As of 2022, the group operates 87 wells (7,000 BOEPD) and has a stake in over 200 non-operating wells. With its 60,000 acres in Wyoming, there is potential for 100 additional wells in the mid- to long term. DRAG has received over 20 permits for its acreage.
- In 2023, Cub Creek will add a total of five new operating wells (four net wells) in Wyoming, which could be increased to eight.
- Two areas of cooperation with Occidental with a total investment amount of c. USD150m until H2 2024 will see the development of 31 further wells.
- The next well site will be completed in Q1 2021 with an amount of USD30m (Huckleberry).
- The production from the first 30 days from its first wells with Oxy is within management's expectation; however, no figures have been disclosed yet.

Economic efficiency in Wyoming higher than in Colorado

- As pointed out above, DRAG will increase its focus on Wyoming (and Utah to a smaller extent) given its own 60,000 acres, its new operating wells, and its cooperation agreements with Oxy.

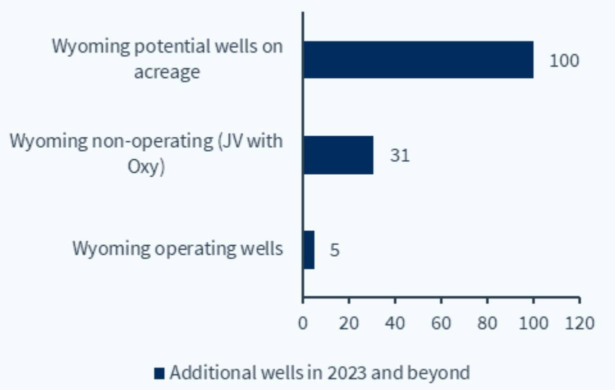
- In Wyoming, the single well economics are much more lucrative than in Colorado. While the drilling costs (and transport costs) are significantly higher in Wyoming (c. USD8.5-11.5m per well versus c. USD5m per well in Colorado), the increased cost base is overcompensated for by a higher production volume and flow rate, as the wells are drilled twice as deep in Wyoming. In addition, the share of oil is c. 70% in Wyoming compared to 40% in Colorado when a new well is drilled and production is commenced. As a result, the ROI is higher in Wyoming compared to Colorado, especially when the group will be able to generate scale effects.

Chart 5: Number of DRAG's operating and non-operating wells by US state



Source: DRAG

Chart 6: DRAG's additional and potential wells expected in 2023 and beyond



Source: DRAG

Part 3: What can investors expect from the oil and gas market going forward?

- To round off the CMD, management held a discussion regarding the current situation and the outlook for demand and supply in the global oil market.
- Management convincingly argued that the WTI price should remain at sustained levels due to the current global supply shortage.
- While a slowdown in demand, especially from China, could impact prices negatively, management suggests (and we agree) that the factors pointing towards a rather optimistic outlook outweigh the downside: 1) the regulatory environment in the US is comparatively positive; 2) the recent figures on a deceleration of inflation and declining producer prices can increase demand for oil; 3) OPEC's recent decision to cut oil supply; 4) the overall lower production in the US compared to pre-pandemic levels (620-640 active oil wells, which is 25% below pre-pandemic levels, and even lower compared to 2014 with over 1,900 active oil wells); 5) 70-80% of the global population have a lower prosperity level than in the US, which means the upside to higher demand for oil is significant in countries such as China, India and Africa, where the average person consumes c. 3,000-4,000 litres of oil per year (compared to 200,000-300,000 in the US); and 6) a lack of alternatives to substitute oil demand (except for e-mobility).
- Overall, a very informative and well-rounded CMD hosted by management with a strong outlook in the coming 12-24 months.

Appendix 1: Research framework

Last model update: 14 October 2022

Investment case

- As one of the few European companies offering direct exposure to US shale, DRAG has extensive experience as an operator in the field. There are a large number of manufacturing companies offering optimal opportunities for non-operative activities and participations.
- Assuming a c. 30% rate of success on the acquired acreage in Wyoming's Powder River Basin (up to 100 well locations), our play-by-play model suggests that this could lead to a sustainable high level of DRAG's oil & gas production in the medium term.
- The minority stake in Almonty Industries, which is expected to ramp up production at one of the largest tungsten mines outside China, should generate stable and long-term returns.

Catalysts

- Higher-than-assumed economic viability in Wyoming (50-100 potential net wells for BRE's part alone).
- Price movements in the WTI benchmark.
- Production start of Almonty's Sangdong mine in South Korea.

Valuation methodology

- Our valuation is based on an SOP of its oil & gas assets, Deutsche Rohstoff's minority investments in metals, and its investment portfolio.
- We value Cub Creek, Elster Oil & Gas and Bright Rock Energy/Salt Creek Oil and Gas using a 27-year NPV model with a 10% WACC.
- Under our current long-term WTI oil price assumption of USD68/bbl, our SOP points to a fair value of EUR40.0.

Risks to our rating

- Weaker-than-expected US dollar. Each USD0.05 move in our long-term EUR/USD assumption impacts our SOP by EUR1.5-2.0 per share.
- Lower demand leading to negative price movements in the WTI benchmark. Each USD3/bbl move in our long-term WTI oil price assumptions impacts our SOP by c. EUR1-2 per share.

Appendix 2: Company description

Deutsche Rohstoff is a Germany-based holding company that specialises in investing in resource projects. The current portfolio is mainly focused on the oil & gas sector, but it also holds minority stakes in high-tech metals such as tungsten. Its management team has longstanding expertise in the sector, and the group focuses on well-explored areas in the US.

Management	Jan-Philipp Weitz, CEO | Henning Döring, CFO
Key shareholders	Free float: 89.96% | Management: 10.04% | Institutional investors: 20.00%

Appendix 3: share price perf.

Appendix 4: SWOT analysis

Strengths

- Solid oil and gas asset portfolio with an extensive drilling pipeline.
- Diversified portfolio
- Expert management with experience in resource-based activities

Weaknesses

- No control over non-operating wells
- Lower transparency compared to US oil and gas peers.
- The majority of mining investments are not producing yet.

Opportunities

- Efficiency gains in drilling could allow additional costs savings
- New land acquisitions
- Investments in electro mobility

Threats

- Price increases from field services companies leading to higher capex
- Direct competition from extractor Oil & Gas in land purchase.
- Euro/US dollar currency fluctuations

Appendix 5: Key financials

Last model update: 14 October 2022

Market data date: 16 November 2022

FY to 31/12 (EUR)	12/15	12/16	12/17	12/18	12/19	12/20	12/21	12/22E	12/23E	12/24E
Income Statement (EURm)										
Sales	1.9	9.2	53.7	109.1	41.2	38.7	73.3	152.7	142.0	108.3
% Change	-91.7%	383.4%	486.1%	102.9%	-62.2%	-6.1%	89.5%	108.3%	-7.0%	-23.7%
EBITDA adjusted	4.9	6.4	36.1	97.9	22.7	20.4	48.4	132.8	118.2	85.3
EBITDA adj. margin (%)	na	69.5%	67.2%	89.8%	55.2%	52.8%	66.0%	87.0%	83.3%	78.7%
EBIT adjusted	2.4	-0.5	5.3	32.7	5.6	-19.6	14.9	90.4	82.8	57.3
EBIT adj. margin (%)	na	-5.9%	9.9%	30.0%	13.7%	-50.8%	20.3%	59.2%	58.3%	52.9%
Net financial items & associates	-3.0	-1.4	-4.0	-6.2	-5.4	-6.4	-5.5	-6.3	-5.5	-5.5
Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Tax	1.1	2.0	6.4	-8.5	-0.1	6.4	-0.7	-17.7	-19.3	-12.9
Net profit from continuing operations	0.5	0.1	7.7	17.9	0.2	-16.1	26.4	66.5	57.9	38.8
Net profit from discontinuing activities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net profit before minorities	0.5	0.1	7.7	17.9	0.2	-16.1	26.4	66.5	57.9	38.8
Net profit reported	1.2	0.1	5.5	13.9	0.3	-15.5	24.8	63.0	55.9	37.1
Net profit adjusted	1.2	0.1	5.5	13.9	0.3	-19.0	7.1	63.0	55.9	37.1
Cash Flow Statement (EURm)										
Levered post tax CF before capex	1.2	2.9	37.8	68.7	13.9	14.0	51.8	107.2	113.8	83.1
Capex	-10.0	-66.1	-51.7	-66.2	-28.7	-36.8	-52.8	-61.0	-40.9	-60.0
Free cash flow	-8.8	-63.2	-13.9	2.5	-14.8	-22.9	-1.0	46.1	72.9	23.1
Acquisitions & divestments	-4.6	3.1	-2.0	0.1	-2.8	-3.9	-0.3	0.0	0.0	0.0
Dividend paid	-2.5	-2.7	-3.0	-3.2	-3.2	-0.5	0.0	-3.0	-4.1	-3.0
Others	-4.1	21.8	-8.8	31.1	-9.3	-15.1	16.8	0.0	0.0	0.0
Change in net financial debt	20.0	41.1	27.6	-30.5	30.1	42.3	-15.5	-43.1	-68.8	-20.1
Balance Sheet (EURm)										
Intangible assets	12.3	29.3	46.0	12.1	14.4	15.1	21.6	50.2	52.8	70.0
Tangible assets	12.6	91.2	102.2	114.8	147.0	119.4	157.2	176.2	178.0	189.4
Financial & other non-current assets	46.5	24.7	24.1	36.4	42.5	50.5	43.9	30.2	30.2	30.2
Total shareholders' equity	61.8	66.2	56.7	73.8	71.5	45.6	80.1	143.5	197.4	233.1
Pension provisions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Liabilities and provisions	66.2	127.4	156.9	151.0	207.4	161.1	184.9	194.8	214.1	227.1
Net debt	9.5	50.6	78.2	47.7	77.8	120.2	104.7	61.6	-7.2	-27.3
Net financial debt	9.5	50.6	78.2	47.7	77.8	120.2	104.7	61.6	-7.2	-27.3
IFRS 16 debt	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net working capital	1.1	-23.0	-9.3	-22.4	-29.3	-11.9	-19.0	-32.7	-52.0	-65.0
Invested capital	15.0	74.9	96.2	94.1	119.3	108.8	139.4	144.8	127.2	125.7
Per share data (EUR)										
EPS adjusted	0.23	0.02	1.10	2.74	0.06	-3.74	1.40	12.40	11.00	7.30
EPS adj and fully diluted	0.23	0.02	1.10	2.74	0.06	-3.74	1.43	12.73	11.30	7.50
% Change	-95.2%	-91.2%	5328.9%	150.0%	-97.8%	-chg	+chg	788.0%	-11.2%	-33.6%
EPS reported	0.23	0.02	1.10	2.74	0.06	-3.05	4.88	12.40	11.00	7.30
Cash flow per share	0.24	0.58	7.48	13.56	2.74	2.75	10.20	21.09	22.39	16.35
Book value per share	11.71	11.16	9.73	12.99	12.66	7.76	14.31	26.11	36.31	43.01
Dividend per share	0.55	0.60	0.65	0.70	0.10	0.00	0.60	0.80	0.60	0.60
Number of shares, YE (m)	5.06	5.06	5.06	5.06	5.08	5.08	5.08	5.08	5.08	5.08
Ratios										
ROE (%)	1.9%	0.2%	10.5%	24.1%	0.5%	-36.6%	12.7%	61.3%	35.3%	18.4%
ROIC (%)	15.7%	-0.8%	4.0%	22.3%	3.4%	-11.2%	7.8%	41.4%	39.6%	29.4%
ND(F+IFRS16) / EBITDA (x)	1.9	7.9	2.2	0.5	3.4	5.9	2.2	0.5	-0.1	-0.3
Gearing (%)	15.4%	76.4%	138.0%	64.7%	108.9%	263.6%	130.7%	42.9%	-3.6%	-11.7%
Valuation										
P/E adjusted	72.4	na	18.6	7.7	na	na	11.6	2.2	2.4	3.7
P/E adjusted and fully diluted	72.4	na	18.6	7.7	na	na	11.3	2.1	2.4	3.6
P/BV	1.4	1.5	2.1	1.6	1.3	1.2	1.1	1.0	0.7	0.6
P/CF	67.9	30.0	2.7	1.6	5.8	3.4	1.6	1.3	1.2	1.6
Dividend yield (%)	3.3%	3.5%	3.2%	3.3%	0.6%	0.0%	3.7%	3.0%	2.2%	2.2%
Dividend yield preference shares (%)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
FCF yield (%)	-9.8%	-72.1%	-15.5%	-1.5%	-18.2%	-46.4%	-3.1%	31.4%	52.2%	15.8%
EV/Sales	50.4	16.1	3.5	1.5	4.0	4.5	2.6	1.4	1.0	1.1
EV/EBITDA adj.	19.4	23.2	5.2	1.7	7.3	8.5	4.0	1.6	1.2	1.4
EV/EBIT adj.	39.6	na	35.6	5.0	29.4	na	13.0	2.3	1.7	2.1

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Deutsche Rohstoff	DE000A0XYG76	KEPLER CHEUVREUX and the issuer have agreed that KEPLER CHEUVREUX will produce and disseminate investment research on the said issuer as a service to the issuer

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Rating Breakdown	A	B
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Reduce	5%	0%
Not Rated/Under Review/Accept Offer	4%	7%
Total	100%	100%

Source: Kepler Cheuvreux
A: % of all research recommendations
B: % of issuers to which material services of investment firms are supplied

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The below table shows the history of recommendations and target prices changes issued by KEPLER CHEUVREUX research department (Equity and Credit) over a 12 months period.

Company Name	Date	Business Line	Rating	Target Price	Closing Price
Deutsche Rohstoff (EUR)	21/02/2022 05:48	Equity Research	Buy	36.00	24.30
	14/06/2022 04:40	Equity Research	Buy	40.00	31.00

Credit research does not issue target prices. Left intentionally blank.

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Reduce: There is an expected downside.

Accept offer: In the context of a total or partial take-over bid, squeeze-out or similar share purchase proposals, the offer price is considered to be fairly valuing the shares.

Reject offer: In the context of a total or partial take-over bid, squeeze-out or similar share purchase proposals, the offered price is considered to be undervaluing the shares.

Under review: An event occurred with an expected significant impact on our target price and we cannot issue a recommendation before having processed that new information and/or without a new share price reference.

Not rated: The stock is not covered.

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Location	Regulator	Abbreviation
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