BUY

Current Price	$0.39
Target Price	$1.96

Ticker:		PVD
Sector:		Energy
Shares on Issue (m):		92.3
- fully diluted (m):		126.5
Market Cap ($m):		36.5
Market Cap Diluted ($m)		50.0
Net Cash ($m)*:		13.0
Enterprise Value ($m):		37.0
* estimate		
52 wk High/Low:	$0.89	$0.25
12m Av Daily Vol (m):	0.26	

Valuation	Risked	Risked	Unrisked
	$m	$/s	$/s
Toubkal	260.0	2.06	27.40
Jbel Tadrart	101.1	0.80	19.04
Gabon	11.3	0.09	10.73
Cash	17.0	0.13	0.13
Debt	-4.0	-0.03	-0.03
Corp Admin	-15.0	-0.12	-0.12
Options / Partly	6.2	0.05	0.05
Total	**376.5**	**2.98**	**57.20**

*Toubkal risked @ 7.5% vs IER 31%, Tadrart risked @ 5% vs IER 19%

In A$ unless otherwise stated

Share Price Graph

Wednesday, 29 May 2013

Pura Vida Energy

Return of the Mack

Analyst| Dave Wall

Quick Read

Pura Vida is back on track, with a strengthened balance sheet and a funding strategy that will focus on sourcing of future capital from industry via farm-out rather than the depressed equity market. The Company was able to accomplish this earlier this year when it achieved an excellent farm-out offshore Morocco where it will receive $15m in cash within weeks and a $215m expenditure carry on two wells in early 2014. Replication of this strategy offshore Gabon is considered likely given the prospectivity of the acreage and the increased level of regional industry activity.

Event & Impact | Positive

Sources of Capital: Pura Vida recently raised $12m ($8m equity and $4m debt) and reduced its debt position from $6m to $4m. Poor timing, coincident with general share market decline for small resource companies, meant that this was done at the heavily discounted price of $0.39, with the stock having traded as high as $0.95 late last year.

An internal review has highlighted that industry is a better source of capital than equity markets in the current environment. The farm-out offshore Morocco yielded $15m in cash and $215m in expenditure carry. In light of this, the Company has indicated it will farm-down its interests in Gabon, prior to acquiring expensive 3D seismic (removing $15m in funding requirement from CY2013). Past costs, including $9m signature bonus and purchase of existing seismic for $2.5m, are likely to be partially reimbursed.

Gabon Farm-Out – Can They Do It Again?: Gabon is far more mature as a petroleum province than Morocco and the level of industry activity is also very high, with many high impact wells being drilled over the next 12 months, commencing now. Whilst Mazagan, in Morocco, is drill ready, the Nkembe Block, offshore Gabon, requires additional 3D seismic to image the potential in the pre-salt. This means that a farm-out is likely to be on the basis of 3D and a well.

What Does PVD Look Like in 6 Months?: We expect several significant catalysts over the next 6 months, such as: contracting of a rig to drill offshore Morocco, receipt of $15m from the Plains farm-out, drilling by others offshore Morocco from August, drilling by others offshore Gabon from now, Resource upgrade at Gabon and a farm-out offshore Gabon. In addition to this, PVD will be on the cusp of drilling the 1.5 billion barrel Toubkal prospect that, if successful, could add >$25 per share. Conviction of significant share price appreciation prior to drilling is high.

Recommendation

After a sharp pullback in price, PVD is significantly undervalued despite being in a much stronger position financially and having grown the asset base. Significant catalysts are expected over the course of the year along with a large re-rating in share price. We rate PVD as a Buy with a price target of $1.96.

Highlights

Background

1.5 billion barrel prospect to be drilled early next year offshore Morocco

The Company listed in February 2012 (at $0.20) on the back of its 10,900km^2 Mazagan Permit offshore Morocco where it had 3,570km^2 of 3D seismic. After reprocessing and reinterpretation, PVD was able to high grade the potential of permit. Subsequently, this was independently confirmed and upgraded by DeGolyer and MacNaughton, with gross potential of 7.1 billion barrels of oil estimated on the permit. The lead prospect, Toubkal, has greater than 1.5 billion barrels of mean potential. Concurrently, a wave of industry activity took place, involving farm-ins and permit acquisitions in surrounding acreage from the likes of Kosmos, Genel, Cairn, Galp, Plains and Chevron.

PVD free carried on uplift potential of >$27 per share

Plenty of drilling by others offshore Morocco and Gabon could re-rate in the interim

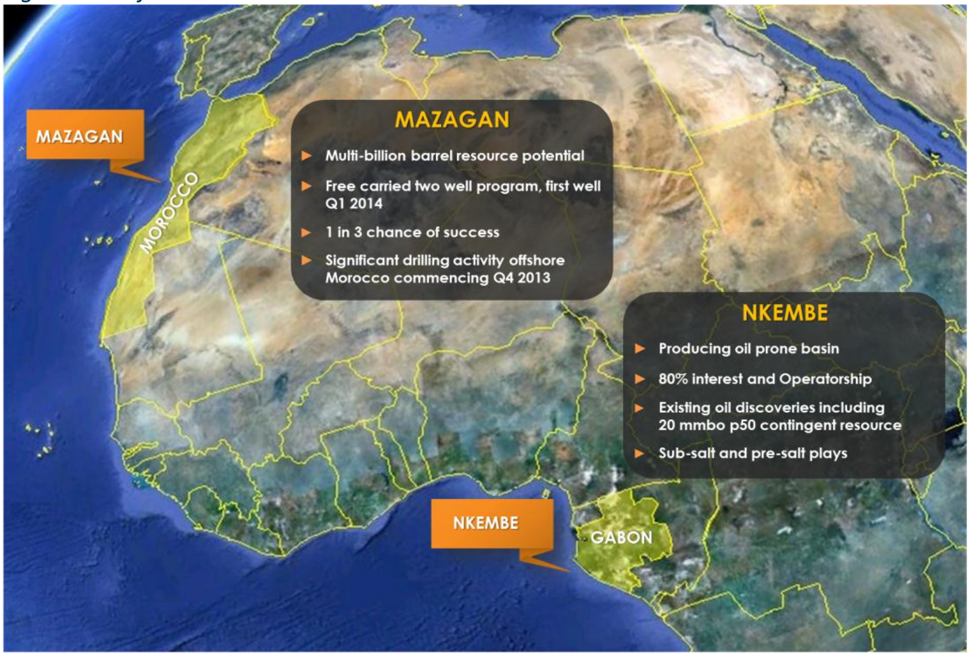
The above events, coupled with an expectation of a farm-out, created a perfect storm and saw the share price rise to as high as $0.95 by the end of 2012. The farm-out itself, to Plains Exploration, was completed early in the new year of 2013 and saw what looked like “buy the rumour, sell the fact” with a pullback in share price to $0.70. This occurred even though the farm-out was above expectation with $15m in cash back as well as $215m carry on two wells.

Gabon Resource upgrade and farm-out expected prior to year end

We also interpret that the pullback was partially related to perceived funding risk, as the Company also acquired its offshore Gabon interest for US$9m and issued short term debt funding of $6m to cover part of this cost. The expenditure program for Gabon in 2013, whilst discretionary, also included potential for a $15m 3D seismic shoot for which funding had not been secured. Given market conditions (i.e. worse than Global Financial Crisis levels for junior resources), these factors contributed to further share price decline, especially as there was an expectation that the $15m from the Morocco farm-out would be receipted sooner.

Funding risk now mitigated with proforma net cash of $17m after funds received from farm-out in late June

Figure 1: Project Locations



Source: Pura Vida

Funding to be sourced from industry rather than depressed equity markets -> dilution minimised

The Company recently raised $8m and reduced its debt from $6m to $4m. We expect that funds from the Morocco farm-out will be in the bank in 4-6 weeks. The Board has also clarified its funding strategy and indicated that it will seek to source funds from Industry rather than equity or debt markets. Medium term funding risk has now been mitigated, in our view, with the expectation of a proforma cash balance (net of debt) of $17m with no committed expenditure in the near term.

So the funding risk that contributed to the sell-off (albeit largely in line with the broader junior resources sector) is now gone. Additionally, the Company has increased value via its Gabon acquisition. PVD has 80% of the Nkembe Permit offshore Gabon and, like Morocco, the country is experiencing a wave of increased industry activity related to interest in a new play type in the pre-salt, which could yield several billion barrels of oil. Drilling by others is underway now and a farm-out is likely this year.

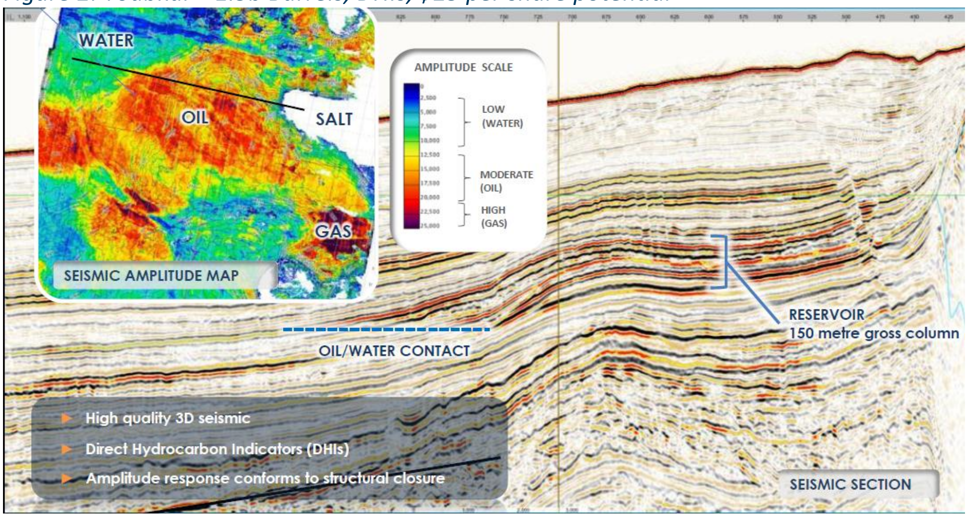
Multiple catalysts will make PVD a different looking company in 6 months – high conviction of share price increase

We expect several significant catalysts over the next 6 months, such as:

- contracting of a rig to drill offshore Morocco
- receipt of $15m from the Plains farm-out
- drilling by others offshore Morocco from August
- drilling by others offshore Gabon from now
- resource upgrade at Gabon
- farm-out offshore Gabon

In addition to this, PVD will be on the cusp of drilling (free carried) the 1.5 billion barrel Toubkal prospect that, if successful, could add >$27 per share.

Figure 2: Toubkal – 1.5b Barrels, DHIs, $25 per share potential



Source: Pura Vida

Morocco (PVD 23% post farm-out)

Toubkal – 1.5b Barrels, DHIs, Free Carried

Toubkal – a world class prospect with 1.5b barrels of potential and a 1 in 3 chance of success

The 1.5b barrel Toubkal Prospect is shown above in Figure 2. Independent estimation for the chance of success is >30% due to Direct Hydrocarbon Indicators (DHIs) interpreted from 3D seismic. Assuming $10 per bbl NPV, Pura Vida's share of a successful outcome would be worth ~$3.5b, or $27.40 (fully diluted).

Drilling By Others

Up to 10 wells to be drilled over next 12 months offshore Morocco by credible international operators

Over the next 12 months, up to 10 wells are scheduled to be drilled by Kosmos, Cairn, Genel, Galp and Plain (with PVD). Newsflow is expected to commence from Q3, with the spud of the first wells by Genel and Cairn. Whilst these will test a different play, investor interest in the region is likely to increase. Pura Vida is currently scheduled to drill in Q1 2014 and we expect that a rig contract will be announced in the near term.

Farm-out $$ Expected within Weeks

Receipt of farm-out funds of $15m could re-rate in risk averse market

Low risk of transaction closing so chance for opportunistic buying now

Early in 2013, PVD executed a farm-out agreement with Plains Exploration for $15m in cash and $215m in carry for the drilling of two wells. The funds will be deposited on completion of Ministerial sign off, which we understand is progressing. Timing is hard to predict; however, our best guess is that the funds will be receipted around June 30. Given the nervousness in the market, this could be the beginning of the re-rating for PVD so getting set now is advised for the more opportunistic.

Pre-Drill Value Expectation

Peers trade at multiples of PVD's current market cap prior to drilling of high impact wells – PVD more leveraged than any other ASX listed company we have seen

Expected Monetary Value is calculated (in its most simple form) by multiplying out the potential value by the chance of success. This results in a valuation for PVD, based on Toubkal alone, of $1b. Typically, companies will trade at a discount to this valuation. Our observation of the ASX listed peers indicates that Pura Vida should trade in excess of $200m market capitalisation prior to drilling. This indicates a pre drill price target of ~$1.60.

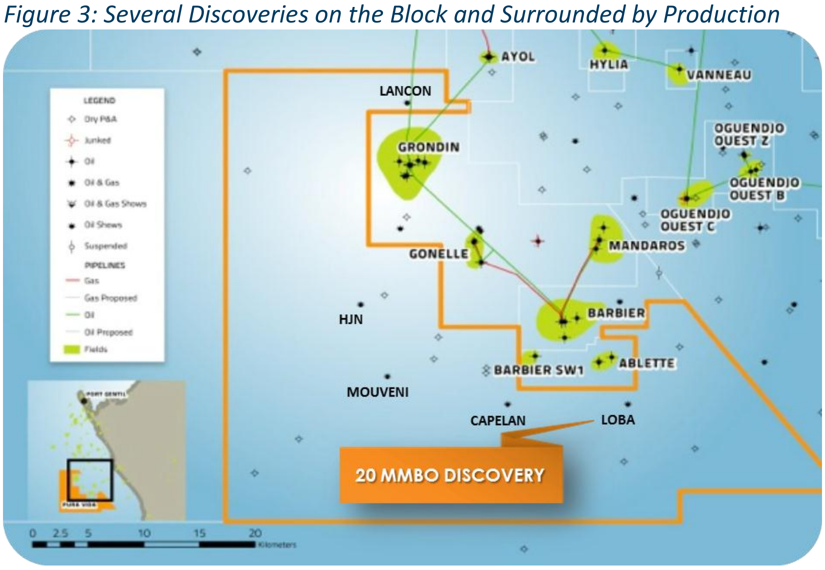
Gabon (PVD 80%)

Nkembe – Large, Mature but with Huge Undefined Upside Potential

Gabon has significant value but not the focus of investors – this could change very quickly

Pura Vida acquired the Nkembe permit in January 2013 and paid a US$9m signature bonus. The signature bonus is an indicator of the maturity of the permit, which has several existing small discoveries (above the salt layer – "post salt"). Work commitments on the block in the near term are minimal; however, the Company is eager to commence a new 3D shoot to help define potential beneath a thick salt layer in a play targeted by others in the region ("pre-salt"). Importantly, this seismic is now likely to be funded by others via a farm-out arrangement.

Figure 3: Several Discoveries on the Block and Surrounded by Production



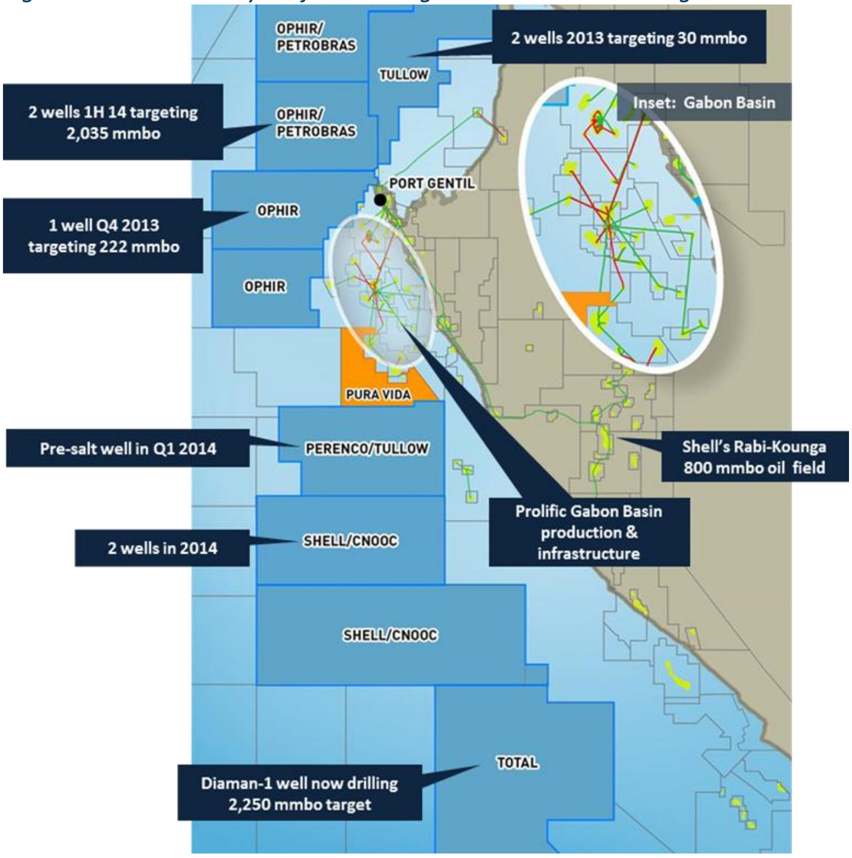
Source: Pura Vida

Drilling By Others

5 wells planned in the near term targeting pre-salt potential

As can be seen below, Pura Vida is surrounded by Majors and large Independents. There has been a recent renaissance in activity offshore Gabon, with 6 wells planned over the next 12 months by Ophir (partnered with Petrobras), Total (with Marathon), Tullow (with Perenco in the adjacent block to PVD) and Shell (with CNOOC). Small discoveries in the pre-salt have already been made by Harvest, high grading the potential for finding oil in larger structures.

Figure 4: Surrounded by Majors Chasing Pre-Salt – Brazil Analogue



Source: Pura Vida

Farm-out Before Year-End

Farm-out strategy clarified -> funding risk gone

In line with the clarified strategy to source capital from industry, PVD plans to farm-out its 80% interest in Gabon. This is likely to occur prior to year end and may involve funding of 3D seismic with an optional well and some cash back. Given the level of interest regionally and the Company's track record of execution of farm-out, we are confident that a decent farm-out can be achieved in a timely manner.

Pre-Salt Potential

Billion barrel prospects to be drilled in the pre-salt could result in significant re-rating

Whilst the pre-salt discoveries at Tortue and Ruche by Harvest in the pre-salt are relatively small (< 50mmbbl combined), the geological model has been de-risked. Ophir has identified two large prospects, North Cluster and Padouck Deep, that have mean recoverable potential of 885 and 1,150 million barrels of oil, respectively. Drilling on these larger prospects is scheduled for late this year. Total is currently drilling the 2.25 billion barrel Diaman-1 prospect on the block to the south of Shell.

Small Contingent Resource could be upgraded - large Prospective Resource also expected

Contingent Resource

Figure 3 shows that there are four discoveries on the Nkembe Block. PVD has identified Contingent Resources of 20 million barrels at one of these, Loba. Assessment of the potential at Loba and the other discoveries is ongoing; however, upside seems likely.

Valuation and Recommendation

Risk reward more skewed than we have ever seen before – based on Toubkal alone

Our valuation for Pura Vida remains based predominantly on the Toubkal Prospect. We assume:

- 1.5b barrels mean recoverable potential
- 7.5% chance of success
- $10 NPV per bbl
- 23% working interest

Correction will occur and conviction of significant uplift in price is high

This results in a valuation of $2.06 fully diluted on a risked basis. The upside potential is in excess of $27.00. We have never seen a company trade at the current level of divergence between the share price and upside potential, which implies that the chance of success for the well is 1.5%. Typically, companies will trade at an implied 10% chance of success valuation prior to drilling. On the ASX there also seems to be a cap of ~$250m market cap. If PVD were to trade at an implied 1 in 10 ratio (even though the independent expert estimates 1 in 3 chance of success), this would imply a $2.70 share price. At $250m market cap a share price of $1.98 is implied.

Even if PVD trades at a substantial discount to these historical peer metrics (which have been remarkably resilient to broader market sentiment), the share price is highly likely to be a multiple of the current share price ahead of drilling in Q1 2014.

Our summary valuation is detailed below (note we have ascribed little value to Gabon at this stage but will look to do so once more detail is known on the potential Resource).

Figure 5: Summary Valuation

Valuation Summary*	$m	$/sh
Toubkal	260	2.06
Jbel Tadrart	101	0.80
Gabon	11	0.09
Cash	17	0.13
Debt	-5	-0.04
Corp Admin	-15	-0.12
Options / Partly Paids	6	0.05
Total	**375**	**2.97**

*Toubkal risked at 7.5% COS vs expert estimate of 31%

Source: Pura Vida

Buy with price target of $1.96

We recommend PVD as a Buy with a price target of $1.96, which is a 33% discount to our risked valuation of $2.97. Our unrisked valuation, based on the two likely drill targets offshore Morocco is in excess of $40.

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The analyst has a beneficial interest in the shares of Pura Vida.

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