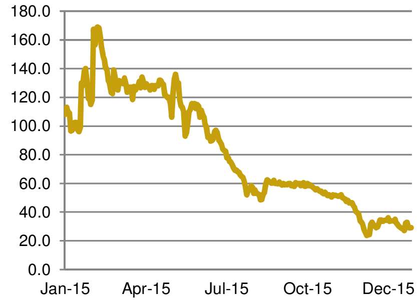
OIL & GAS FLASHNOTE

San Leon Energy (SLE LN)

26 August 2016

Stock Data (Including Placing Shares)	
Placing Price:	45p
Market Cap (M):	£199.4
Free float	96.2%

Price Chart



Company Summary

San Leon Energy is an exploration and production company with assets in Nigeria, Poland, Morocco, Ireland and Albania.

OML 18 acquisition

Event

San Leon Energy ("San Leon", "SLE" or the "Company") has announced that it has raised £170.3m (US$221.4m) in an equity placing (subject to shareholder approval) to complete the acquisition and restructuring of various interests in OML 18, located onshore Nigeria (the "Transaction"). On completion of the Transaction, SLE will have an initial indirect 9.72% economic interest in the licence, which as at May 2016 was reported as producing c.60mboepd and has significant future growth potential. At the 45p placing price, San Leon will have a post money market capitalisation of circa £200m.

Based on forecasts from the Petrovision Energy Services ("Petrovision") CPR and model, and assumptions on income from the provision of rig services, the Transaction could generate US$530m of cash flows to the Company by 2020. SLE is committing to distribute 50% of available Nigerian free cash flow to shareholders for the next five-year period by way of dividends and/or share buybacks providing a substantial potential yield.

Cash distributions from OML 18 to SLE are underpinned by the excellent performance of the asset to date (oil production has increased five-fold in the past year), future low risk production growth (production is forecast to reach 200mboepd in 2020), low operating costs, a substantial hedging position for 2016 and 2017 at US$95/bbl, a disproportionate cash sweep and a corporate guarantee from Midwestern Oil & Gas ("Midwestern"). SLE will also have the right to provide oilfield services to the operator of OML 18 with a significant contract value based on expected capex of around US$1.5bn over the next 5 years.

In aggregate, these cash streams have an NPV10 to SLE of US$514m indicating the Transaction will be highly value accretive to shareholders. A right of first refusal to participate in other future upstream and downstream projects alongside Eroton Exploration & Production ("Eroton") and Midwestern provides additional reinvestment opportunities.

Based on projected 2017 cash flows net to San Leon of $102.3M and the committed distribution policy, San Leon would be valued on an earnings multiple of just 2.6x and a yield of 19% at the 45p placing price. Whilst these numbers exclude corporate overheads and there are a number of other factors to evaluate, we would consider these ratios out of line for typical AIM listed Oil & Gas producers and believe a significant rerating above the 45p placing price in the next few years is possible.

William Arnstein
Tel: +44 (0)20 3463 5020
william.arnstein@brandonhillcapital.com
www.brandonhillcapital.com

OML 18

Background

OML 18 is located in the Southern Niger Delta close to the Shell-operated Bonny export terminal to the East and Port Harcourt to the North. The block covers an area of 1,035km^2 and includes nine oil and gas discoveries – Akaso, Alakiri, Asaritoru, Awoba, Bille, Cawthorne Channel, Orubiri, Krakama and Buguma Creek. Four of the fields are currently producing.

Existing oilfield infrastructure includes 165 wells, seven flow stations, three gas processing plants, a non-associated gas processing plant and various gathering facilities with an installed capacity of 220mbopd (170mbopd currently operational) and 270mmcfpd. Oil is exported to the Bonny Terminal via the Nembe Creek Trunkline and gas is primarily sold to the Notore Petrochemical Plant to the north east.

Exhibit 1: OML 18 fields

Source: San Leon Energy

OML 18 is operated by Eroton Exploration & Production ("Eroton"), which acquired a 45% participating interest in the licence from Shell, Total and Agip in March 2015 for a total consideration of US$1.1bn. NNPC owns the remaining 55% interest in the licence. The licence is due to expire on 1 July 2019, however under current legislation, an extension will be granted provided the lessee has paid oil rent and royalties and has performed all obligations under the lease.

The Eroton consortium partly funded the acquisition cost with a US$663m seven year RBL. Interest on the US$380m ‘A’ facility is charged at 90 day LIBOR plus 9.5% and on the US$283m ‘B’ facility at 90 day LIBOR plus 9.0%. Repayments on the RBL commenced in December 2015 with future payments due on a quarterly basis. Insurance is in place to repay outstanding balances on the RBL in the unlikely event the licence is not extended.

At the time of the Eroton acquisition a reserves report by RPS Energy attributed 2P reserves of 407mmbbl and 3Tcf of gas to OML 18. A more recent CPR by Petrovision has increased reserves by over a third to

576mmbbl and 4.2Tcf reflecting the strong production performance. Additional contingent resources are estimated at 203mmbbl and 1.6Tcf, while there is also considerable exploration potential (471mmbbl and 1.6Tcf are attributed to the top 20 ranked prospects on a risked basis). Importantly, San Leon negotiated the acquisition on the basis of the old reserve numbers so will immediately benefit from the reserves upgrades.

Production

Since 1970 cumulative production from OML 18 is estimated to have totalled approximately one billion barrels of oil and 1.8Tcf, with peak production of 140mboepd achieved in the 1970's and 1990's. Production in more recent years has ranged from 20-30mbopd and fell to a low of just 5mbopd in January 2015 after the Akaso and Cawthorne facilities went offline.

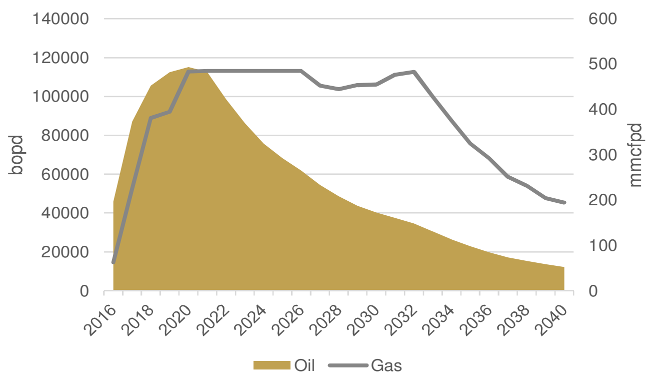
Since becoming operator in March 2015, Eroton has increased oil production to approximately 50mbopd (April 2016). Gas production contributes a further 57mmcfpd (10mboepd). Production has benefitted from high uptime and the results of a well intervention programme, which has so far largely been limited to quick fixes above ground.

Production is expected to continue growing during the next few years as the operational focus shifts to the subsurface, with a multi-well re-entry and workover programme planned, followed by drilling of new wells starting in 2017.

A conceptual development plan devised by Petrovision envisages 76 new wells (50 oil wells and 26 gas wells) are required to fully exploit the existing developed and undeveloped reservoirs and to accelerate recovery. It should be noted that a development plan has not been finalised by the operator and the eventual approved plan could accommodate an alternative work programme. The condition and integrity of the existing wells to be re-entered is also unknown providing a risk to nearer term forecasts.

Based on the Petrovision plan, production from OML 18 is forecast to average 64mboepd in 2016 before rising to more than 200mboepd in 2020. Oil production is forecast to peak at 120mbopd (all figures exclude the effects of downtime and losses estimated at 14% in 2016, and reducing over time with facilities upgrades). Capex for the 2P development plan is estimated at around US$1.8bn and is fully funded by production. Life of field opex is estimated at US$13/bbl and <US$10/bbl between 2018 and 2021.

Exhibit 2: OML 18 2P production forecast (after deduction of downtime and losses)



Source: Petrovision

Beyond these forecasts there are a number of additional opportunities to add further value for San Leon. These include:

- De-watering and enhanced oil recovery
- Commercialisation of contingent resources
- Exploration success
- Oil price recovery and higher domestic gas prices (US$1.5-2.0/mcf assumed by PetroVision)
- Award of pioneer tax status
- Right of first refusal on future upstream and downstream deals originated by Eroton or Midwestern

Cash flows

The table below shows cash flows from the Petrovision CPR 2P case for OML 18 split between repayments/interest on the loan notes and dividends from BidCo, along with potential cash flows from oilfield services. Distributions to San Leon shareholders (set at 50% of overall cash flows) are also outlined.

Exhibit 3: San Leon cash flows estimates

US$m	2016e	2017e	2018e	2019e	2020e
BidCo loan payments	32.5	74.5	66.6	53.8	12.2
BidCo dividends	3.0	2.3	6.2	88.6	75.0
Oilfield services	0.0	25.5	31.7	25.2	33.3
Total SLE cash flows*	**35.5**	**102.3**	**104.4**	**167.5**	**120.6**
Shareholder distributions*	17.8	51.1	52.2	83.8	60.3

Source: Petrovision, San Leon Energy, *subject to other potential Nigerian deductions

The table clearly demonstrates that the most important cash flows in the near term are the loan note interest (at 17% coupon) and repayments contributing more than 50% of cash flows in each of the first three years. Based on our own calculations (not shown) we believe this funding mechanism, while complex, is value enhancing for SLE adding an estimated US$140m in cash flows compared to a straight 40% share of BidCo profits.

That said, the CPR calculations show a modest cash shortfall for loan note repayments in 2016-2017 totalling US$11.7m. Such shortfalls are cleared by the end of 2017. The corporate guarantee with Midwestern envisages and provides protection for this and ensures repayment of the loan note within four years. San Leon management are highly confident that sufficient safeguards are in place, including cash flows from the 25mbopd Umusadege field and pipeline tariff, and if necessary payment in equity.

Overall, cash flows to San Leon are forecast to total US$530m between 2016 and 2020 and US$924m out to 2040, generating an unrisked NPV10 of US$514m (US$341m net of acquisition costs). For shareholders this offers exposure to a quality and high value asset and potential San Leon shareholder distributions (share buy backs or dividends) of more than US$250m in the first five years, providing a substantial yield.

Summary of the Transaction

On 22 January 2016, San Leon announced a series of proposed transactions and shareholder agreements that, if successfully executed, would result in the company securing an initial 9.72% indirect economic interest in OML 18. The total cost of the Transaction to SLE is US$173m equating to an effective acquisition cost of US$2.2/boe (based on Petrovision 2P reserves estimates).

Whilst somewhat complicated, the deal structure was arranged in a manner to enable San Leon to complete the acquisition of its interest in OML 18 in sequential stages. With a vote of approval by SLE shareholders at the September 2016 EGM and completion of the proposed placing, San Leon will be able complete the acquisition of its 9.72% indirect economic interest, and benefit from the revenues generated to date by the asset.

On completion, San Leon will hold its indirect interest in OML 18, through a 40% shareholding in a special purpose entity ("BidCo") formed with Midwestern as a partner, for the purpose of acquiring the asset. BidCo is funding the acquisition through the issuance of Loan Notes, which will all be held by San Leon on completion. The US$173m Loan Notes and 17% per annum coupon will be repaid over four years.

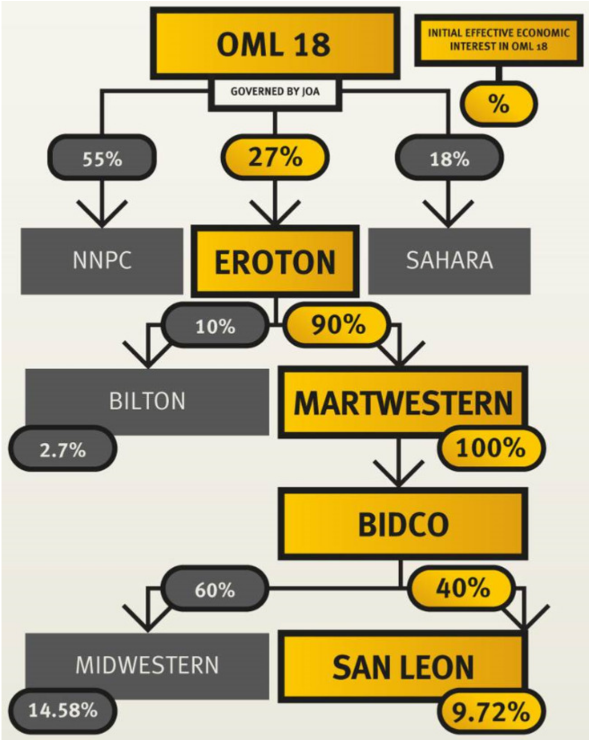
The Loan Notes to BidCo were originally funded on a temporary basis by funds managed by Toscafund, a major shareholder in SLE. On completion of its placing SLE will acquire the Loan Notes and accrued interest from Toscafund.

BidCo' interest in OML 18 will be secured by acquiring 100% of the shares held by three parties in Martwestern Energy. To date BidCo has completed the purchase of an 83.57% interest in Martwestern Energy (40% from Mart Resources, 40% from Midwestern and 3.57% from Suntrust), with the remaining 16.43% to be acquired from Suntrust following completion of the SLE placing. The final stage of the transaction will be financed with the issue of a further US$57.5m of Loan Notes to SLE.

In addition to earning a 40% interest in BidCo, San Leon will also receive an enhanced cash sweep and the right to provide oilfield services to the operator of OML 18. The cash sweep will allow San Leon to receive at least 65% of net cash flows from BidCo's share of OML 18 production proceeds until transaction debt plus a 17% coupon has been repaid. San Leon will also receive a corporate guarantee from Midwestern.

Following a restructuring of Eroton, the economic interests in OML 18 will be as outlined in exhibit 5 on page 6. Eroton will be 50% owned by Martwestern (100% owned by BidCo) and 50% by Bilton, a community carry vehicle. Martwestern is entitled to a 90% share of distributions, and Bilton is entitled to 10% until certain production and economic thresholds are exceeded, at which time rights to distributions will be as per shareholding interest and SLE's indirect economic interest will decline below 9.72%.

Exhibit 5: Revised structure of OML 18 economic interests



Source: San Leon Energy

Use of proceeds

Exhibit 5: Use of proceeds

	US$m
Acquisition of US$115.5 million of Loan Notes (and associated accrued interest) and warrants issued by BidCo from Toscafund	127.0
Subscription for new Loan Notes issued by BidCo	57.5
Payment of accumulated interest and fees to Suntrust	4.0
Payment of current Creditors	17.7
Transaction Costs	7.0
General working capital	4.5

Source: San Leon Energy

San Leon board changes

On completion of the transaction, San Leon will appoint Mutiu Sunmonu (former MD of Shell Petroleum Development Company) as Non-Executive Chairman, Ewen Ainsworth (former Finance Director of Gulf Keystone Petroleum) as Finance Director, and Mark Phillips and Nick Butler as Non-Executive Directors. The other executive board members will be Oisin Fanning, Joel Price and Alan Campbell.

Research Disclosures

William Arnstein

Will is a CFA charterholder and has more than 10 years' experience as a sell-side equity research analyst having previously worked at Dresdner Kleinwort, Jefferies International and finnCap. In his last role, he co-founded the Oil & Gas franchise at finnCap and later became Head of Oil & Gas, where he also coordinated corporate finance and corporate broking in addition to his responsibilities as a Research Director. During his career, Will has worked closely with many international E&P companies, both listed and private, evaluating assets across the globe and has developed particular expertise in petroleum economics and asset valuation. In 2010, Will was awarded No.1 stock picker for the European energy sector in the FT/Starmine Awards.

Tel: +44 (0)20 3463 5020
william.arnstein@brandonhillcapital.com

Investment Analyst Certification

All research is issued under the regulatory oversight of Brandon Hill Capital Limited. Each Investment Analyst of Brandon Hill Capital Limited whose name appears as the Author of this Investment Research hereby certifies that the recommendations and opinions expressed in the Investment Research accurately reflect the Investment Analyst's personal, independent and objective views about any and all of the Designated Investments or Relevant Issuers discussed herein that are within such Investment Analyst's coverage universe.

Brandon Hill Capital Limited provides professional independent research services and all Analysts are free to determine which assignments they accept, and they are free to decline to publish any research notes if their views change.

Research Recommendations

Brandon Hill Capital uses a five-tier recommendation system for stocks under coverage:

Buy	Recommendation implies that expected total return of at least 15% is expected over 12 months between current and analysts' target price.
Trading Buy	Recommendation implies that the analysts' expected total return over the short term compared against the target price is positive.
Hold	Recommendation implies that expected total return of between 15% and zero is expected over 12 months between current and analysts' target price.
Trading Sell	Recommendation implies that the analysts' expected total return over the short term compared against the target price is negative.
Sell	Recommendation implies that expected total return expected over 12 months between current and analysts' target price is negative.

Research Disclaimers

Research disclosure as of 26 August 2016

Company Name	Disclosure
San Leon Energy (SLE LN)	1,2,5,7,8,9

Investment Research Disclosure Legend:

1. In the past 12 months, Brandon Hill Capital Limited or its affiliates have had corporate finance mandates or managed or co-managed a public offering of the Relevant Issuer's securities or received compensation for Corporate Finance services from the Relevant Issuer.
2. Brandon Hill Capital Limited expects to receive or intends to seek compensation for Corporate Finance services from this company in the next six months.
3. The Investment Analyst or a member of the Investment Analyst's household has a long position in the shares or derivatives of the Relevant Issuer.
4. The Investment Analyst or a member of the Investment Analyst's household has a short position in the shares or derivatives of the Relevant Issuer.
5. As of the month end immediately preceding the date of publication of this report, or the prior month end if publication is within 10 days following a month end, Brandon Hill Capital Limited and / or its affiliates beneficially owned 1% or more of any class of common equity securities of the Relevant Issuer.
6. A senior executive or director of Brandon Hill Capital Limited or a member of his or her household is an officer, director or advisor, board member of the Relevant Issuer and / or one of his subsidiaries.
7. Brandon Hill Capital Limited acts as corporate broker for the Relevant Issuer.
8. The Investment Analyst who is responsible for the preparation of this Investment Research is employed by Brandon Hill Capital Limited, a securities broker-dealer.
9. The Investment Analyst who is responsible for the preparation of this Investment Research has received (or will receive) compensation linked to the general profits of Brandon Hill Capital Limited.

Disclaimer: Important Information

This document is not independent and should not be relied on as an impartial or objective assessment of its subject matter. Given the foregoing, this document is deemed to be a marketing communication and as such has not been prepared in accordance with legal requirements designed to promote the independence of investment research and Brandon Hill Capital Limited is not subject to any prohibition on dealing ahead of dissemination of this document as it would be if it were independent investment research.

This document has been issued by Brandon Hill Capital Limited for information purposes only and should not be construed in any circumstances as an offer to sell or solicitation of any offer to buy any security or other financial instrument, nor shall it, or the fact of its distribution, form the basis of, or be relied upon in connection with, any contract relating to such action. This document has no regard for the specific investment objectives, financial situation or needs of any specific entity. Brandon Hill Capital Limited and/or connected persons may, from time to time, have positions in, make a market in and/or effect transactions in any investment or related investment mentioned herein and may provide financial services to the issuers of such investments. The information contained herein is based on materials and sources that we believe to be reliable, however, Brandon Hill Capital Limited makes no representation or warranty, either express or implied, in relation to the accuracy, completeness or reliability of the information contained herein. Opinions expressed are our current opinions as of the date appearing on this material only. Any opinions expressed are subject to change without notice and Brandon Hill Capital Limited is under no obligation to update the information contained herein. None of Brandon Hill Capital Limited, its affiliates or employees shall have any liability whatsoever for any indirect or consequential loss or damage arising from any use of this document.

This report has been approved in the UK by Brandon Hill Capital Limited solely for the purposes of section 21 of the Financial Services and Markets Act 2000. In the UK, this report is directed at and is for distribution only to persons who (i) fall within Article 19(1) (persons who have professional experience in matters relating to investments) or Article 49(2) (a) to (d) (high net worth companies, unincorporated associations, etc.) of the Financial Services and Markets Act 2000 (Financial Promotions) Order 2005 (as amended) or (ii) are professional clients or eligible counterparties of Brandon Hill Capital Limited (all such persons together being referred to as “relevant persons”). This report must not be acted on or relied up on by persons in the UK who are not relevant persons.

Neither this report nor any copy of part thereof may be distributed in any other jurisdictions where its distribution may be restricted by law and persons into whose possession this report comes should inform themselves about, and observe any such restrictions. Distribution of this report in any such other jurisdictions may constitute a violation of UK or US securities law, or the law of any such other jurisdictions.

Investments in general involve some degree of risk, including the risk of capital loss. The services, securities and investments discussed in this document may not be available to nor suitable for all investors. Investors should make their own investment decisions based upon their own financial objectives and financial resources and, if in any doubt, should seek advice from an investment advisor. Past performance is not necessarily a guide to future performance and an investor may not get back the amount originally invested. Where investment is made in currencies other than the investor’s base currency, movements in exchange rates will have an effect on the value, either favourable or unfavourable. Levels and bases for taxation may change. When we comment on AIM or ISDX shares you should be aware that because the rules for those markets are less demanding than the Official List of London Stock Exchange plc, the risks are higher. Furthermore, the marketability of these shares is often restricted.

Brandon Hill Capital Limited and/or its associated companies may from time-to-time provide investment advice or other services to, or solicit such business from, any of the companies referred to in this document. Accordingly, information may be available to Brandon Hill Capital Limited that is not reflected in this material and Brandon Hill Capital Limited may have acted upon or used the information prior to or immediately following its publication. In addition, Brandon Hill Capital Limited, the directors and employees thereof and/or any connected persons may have an interest in the securities, warrants, futures, options, derivatives or other financial instrument of any of the companies referred to in this document and may from time-to-time add or dispose of such interests. Neither the whole nor any part of this material may be duplicated in any form or by any means. Neither should any of this material be redistributed or disclosed to anyone without the prior consent of Brandon Hill Capital Limited. Brandon Hill Capital Limited is authorised and regulated by the Financial Conduct Authority and is a member of the London Stock Exchange.

Brandon Hill Capital Limited may distribute research in reliance on rule 15a-6(a)(2) of the Securities and Exchange Act 1934 to persons that are major US Institutional investors, however, transactions in any securities must be effected through a US registered broker-dealer. Any failure to comply with this restriction may constitute a violation of the relevant country’s laws for which Brandon Hill Capital Limited does not accept any responsibility. By accepting this document, you agree that you have read the above disclaimer and to be bound by the foregoing limitations/restrictions. Please note that unless otherwise stated, the share price used in this publication is taken at the close of business for the previous day.

Brandon Hill Contact List

International Sales

Oliver Stansfield

Tel: +44 20 3463 5061
Email: oliver.stansfield@brandonhillcapital.com

Alex Walker

Tel: +44 20 3463 5018
Email: alex.walker@brandonhillcapital.com

Research

William Arnstein

Tel: +44 20 3463 5020
Email: william.arnstein@brandonhillcapital.com

Peter Rose

Tel: +44 20 3463 5034
Email: peter.rose@brandonhillcapital.com

Corporate Finance & Broking

Jonathan Evans

Tel: +44 20 3463 5016
Email: jonathan.evans@brandonhillcapital.com

Wei Jiao

Tel: +44 20 3463 5019
Email: wei.jiao@brandonhillcapital.com

Robert Beenstock

Tel: +44 20 3463 5023
Email: robert.beenstock@brandonhillcapital.com