

Stock Data

Share Price: 0.12p
Market Cap: £4.5m
Shares in issue: 3,764.5m

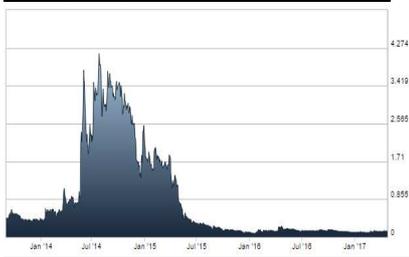
Company Profile

Sector: Oil & Gas
Ticker: ROSE.L
Exchange: AIM

Activities

Multi-asset natural resources company with oil and gas interests in the US in addition to precious metals and uranium assets in Mexico and the US.

Share price performance



Source: LSE

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Rose Petroleum plc

Rose Petroleum is a multi-asset natural resources company with major interests in the US and Mexico. The group holds a substantial oil and gas acreage position in the Paradox Basin in Utah where a planned 3D seismic survey will target a major clastic sandstone play in H2 2017. Rose's mining activities are focused on toll milling third party ore at the group's crushing and floatation mill (SDA Mill) in Mexico. However, longer terms plans for this asset are likely to change given that Rose recently entered into negotiations with Magellan Gold Corp for the sale of the SDA Mill.

Rose plans to conduct a 61 sq. mile 3D seismic survey on its acreage in the Paradox Basin in Utah in September 2017. The shoot will focus on identifying potential drill targets in the Cane Creek interval and other clastics of the Paradox Formation which are proven productive intervals in the wider Paradox Basin. The US Bureau of Land Management (BLM) is currently working with the company to finalise Rose's Environmental Assessment (EA) document as part of the permitting process for the seismic survey. The BLM is close to submitting the EA for the public comment period and assuming a positive outcome, Rose expects to receive the permit in June 2017.

Rose's 3D seismic survey will earn the company a 75% interest in the Paradox Basin acreage portfolio which Ryder Scott estimates could contain recoverable prospective resources of over 1.1 bn barrels of oil and nearly 2.2 TCF of gas net to Rose's interest.

At the end of 2015, Rose suspended its mining operations at Mina Charay in northwest Mexico due to depressed commodity prices and high transportation costs. This has enabled the company to focus on toll milling third party ore at its nearby 100% owned crushing and floatation mill (the SDA Mill).

Rose has indicated that the mill could deliver an operating profit in 2016 although long terms plans, including establishing joint venture mining partnerships to accelerate mill throughput could be put on hold given that Rose recently entered into an MOU with Magellan Gold to potentially sell the SDA Mill for US\$1.5m in cash and shares.

Rose's uranium interests in the US are currently being held on care and maintenance and the progress regarding the group's other Mexican mining interests is subject to further funding. However, following a US\$1.2m investment in Rose from Earth Source LLC in May 2016, the group has established a subsidiary, Rose Gypsum Limited, in order to exploit exciting opportunities in the Cuban gypsum market.

Rose Gypsum was set up to participate in a tendering process to manufacture a range of gypsum based products for the Cuban construction industry. The subsidiary is tendering to become the sole manufacturer of gypsum products in Cuba. Although there is no guarantee of a successful outcome to this tender, we believe that prospects have improved over the course of the current year as existing embargo restrictions continue to loosen.

Although exposure to both the oil and mineral resources commodity cycles has necessitated a re-examination of the group's asset base and strategic aims over the last 18 months, Rose's immediate activities in the US, Mexico and Cuba are largely funded. We expect that accelerated news flow has the potential to re-energise the share price as the group achieves its core milestones over 2017.

Oil and gas assets

Rose Petroleum's core oil and gas asset is located in the Paradox Basin in Utah, USA. The company's current focus is to complete the permitting for a 61 sq. mile 3D seismic shoot in this hydrocarbon province where Rose is earning a 75% working interest in over 90,000 net acres and is targeting the Paradox Clastics Formation in the Cane Creek Clastics play.

Independent consultant, Ryder Scott has reported that the acreage could contain net un-risked prospective recoverable resources of over 1.1 billion barrels of oil and up to 2.2 TCF cubic feet of gas (see later table). There is also extensive infrastructure in place which the management believes can support the economics of a development project in the current tough market conditions.

Rose's strategy is to undertake a 3D seismic shoot in order to firm up drill target identification focusing on naturally fractured areas. This would then be followed by exploration drilling to probe the interception of the natural fractures. This has been demonstrated previously to be a successful strategy for former Paradox Basin operator, Fidelity Exploration and Production, in this highly over pressured hydrocarbon play.

Location of the Paradox Basin



Source: Virtus Oil & Gas Corp

Fidelity exits the exploration sector

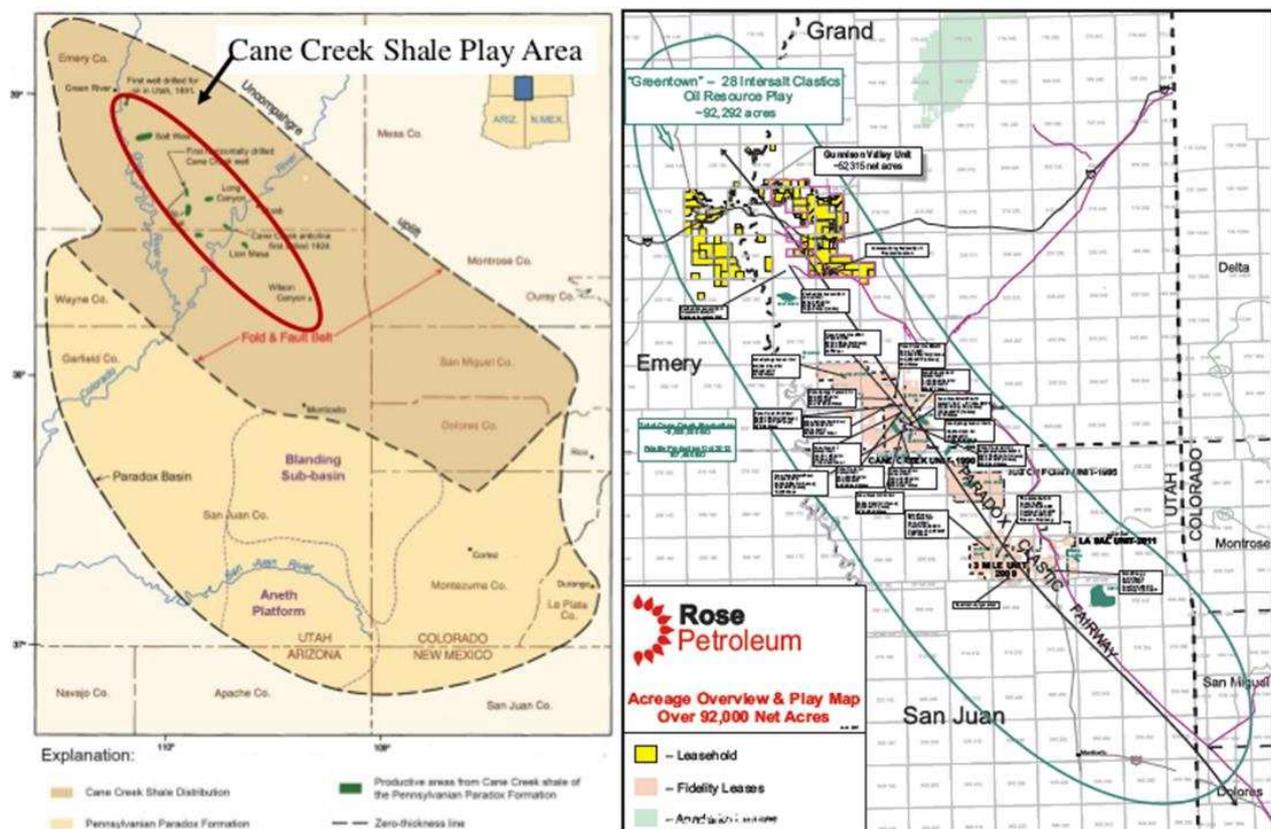
Prior to disposing of its entire oil and gas exploration portfolio in November 2015, Fidelity Exploration and Production operated in several US onshore locations including the Paradox Basin where it was one of the most active operators targeting the Cane Creek Clastics formation. Fidelity's acreage is located close to Rose's lease blocks in a south-south-easterly direction.

Fidelity's parent company, MDU Resources sold part of Fidelity's oil and gas portfolio, which includes the Cane Creek Unit to joint venture partners, Kirkwood Resources and NERD Energy which operate under the banner of Wesco Operating Co. This disposal was driven by MDU's strategy to focus on its less cyclical utilities and construction businesses. Rose has noted that Kirkwood has plans to drill two wells in the Paradox Basin in 2017 and also conduct several workovers of existing wells.

The Cane Creek interval of the Paradox formation

Depicted in yellow, Rose's acreage in the Cane Creek Clastics play is located towards the northwest end of the Paradox Clastic hydrocarbon fairway as shown on the maps below.

Rose's licence interests in the Cane Creek Clastics play area



Source: Utah Geological Survey, Rose Petroleum

Resource estimates

Rose's acreage in the Cane Creek Clastics play is located towards the northwest end of the Paradox Clastic hydrocarbon fairway. Outlined overleaf are Ryder Scott's prospective resources estimates in regard to the Paradox Formation. Although these estimates encompass several reservoir intervals in the Paradox Formation, major development activity to date has focused on the proven and productive Cane Creek reservoir. Rose notes that Fidelity E&P established pay in 10 of the clastic sands and Ryder Scott attributed reserves in a total of 15 of the clastic intervals.

Paradox formation resource estimates net to Rose Petroleum

OIIP (mmbbls)				GIIP (BCF)			
P90	P50	P10	Mean	P90	P50	P10	Mean
15,876	19,139	23,008	19,230	26,005	32,999	41,300	33,395
Estimated ultimate recovery (mmbbls)				Estimated ultimate recovery (BCF)			
Low	Best	High	Mean	Low	Best	High	Mean
452	933	1,995	1,115	874	1,888	3,914	2,187

Source: Ryder Scott (April 2014)

Geology of the Cane Creek Clastics Formation

In May 2014, the Utah Geological Survey (UGS) conducted an in depth study of the Paradox Basin focusing on the Cane Creek Clastics formation in particular. The aim was to gain insight into the properties of the formation and further define the characteristics of the reservoir. This study is of direct relevance to Rose given that the UGS drew substantially on Fidelity's work in the area.

The UGS reports that the Paradox Basin sediments indicate up to 29 clastic cycles related to alternate periods of marine flooding and evaporation events. Clastic rocks deposited during these cycles are composed of fragments, or clasts, of pre-existing minerals and rock. These clastic cycles compose of inter-bedded dolomite, dolomite siltstone, anhydrite and crucially, organic rich shale. Cane Creek to one of these major shale groups and is believed to be part of cycle number 21.

The Paradox Basin Formation is estimated to be up to 5,000 feet thick and the Cane Creek Clastics is believed to be deeper in the northern part of the basin where Rose's acreage is located. The majority of current production in the formation is in the central area of the basin called the Big Flat area where Fidelity's original leases are located.

As can be seen clearly from the map on the previous page, the Cane Creek fairway trends northwest to southeast and averages 90 feet thick across three clear intervals (A,B and C). In some areas the gross formation is over 120 feet thick. Of particular interest is the B reservoir interval with organic rich shale and natural open fractures bounded by anhydrite seals within the A and C intervals. Union Pacific Resources has reported that the total organic content of the B interval in its Remington 21-1H well was an average 12% over a 29 feet interval which is exceptionally high, although the logs reported that there were no open fractures in the formation.

It should be noted that the UGS has concluded that historical exploration and production activity has focused on the central section of the Cane Creek clastic and the production potential to both the south and the north where Rose's acreage is located is largely unknown. However, we believe that the completion of Rose's 3D seismic survey which will commence in September 2017 has the potential to reveal a significant amount of new information.

Production in the Cane Creek interval

UGS states that there are five producing fields in the Cane Creek formation which has produced over 5.4 million barrels since the 1960s. One of the most prolific wells in the formation is the Cane Creek 12-1 well drilled by Fidelity in 2012 in the Big Flat field. This well produced over 437,000 barrels (averaging 1,199 bopd) in 2013 alone making it the most productive well in the area by a significant margin.

Other producing wells which are concentrated in the central area of the play include the old vertical well, Long Canyon-1 which has been producing since 1962 and has cumulative production in excess of 1.1 million barrels of oil. This well produced c.7 bopd as recently as 2013.

Kane Springs Fed 10-1 on the Hell Roaring Field is a vertical well producing since 1992 and has recorded over 642,000 bbls of cumulative oil production to date. In addition, the Fidelity-drilled, Kane Springs 27-1 also has recorded cumulative production of over 500,000 bbls oil.

Fidelity produced nearly 1.0 mmbbls from the Cane Creek formation in 2013 from an aggregate 15 wells. In addition to the prolific 12-1 well, other wells including CCU 18-1, CCU 36-1 and CCU 26-3 which came on stream in 2013 demonstrated initial flow rates of 800 – 1,200 bopd. As can be inferred from the production data from wells drilled prior to 2013 and the accepted characteristics of shale oil production, wells in the Cane Creek formation have a considerably more aggressive production decline curve compared to wells drilled in conventional oil reservoirs.

Current status

Prior to the completion of the disposal of its oil and gas assets, Fidelity was the most active operator in the Paradox Basin and average Q1 2015 production in the basin was 2,100 bopd. Rose is determined to employ the same optimal strategy that worked well for Fidelity prior to 2015 in that a 3D seismic shoot is used to identify prime drilling targets focusing on potential features of natural fracturing together with structural features which would promote the best areas of a fracture network. Due to the success of this process, most of the wells have not required fracture stimulation which is likely to reduce capital expenditure substantially.

Rose's internal estimates demonstrate that at an oil price of only US\$55 per barrel wellhead pricing and a single well drilling cost of US\$10m, the internal rate of return (IRR) of the well would be around 25% with a pay-back period of just over two years, all other things being equal.

Rose notes that the permitting process is a very time consuming activity due to the requirement for a large number of cultural and environmental studies in the shoot area. However, the bulk of seismic programme has been managed under a turnkey contract by third party consultant, Dawson Geophysical Inc. and most of the permitting process has already been achieved barring any further design changes from the Public Comment period.

Due to the governmental and regulatory restrictions, the 3D seismic shoot is scheduled to commence in H2 2017. The Bureau of Land Management (BLM) has made assurances to Rose that the permits will be granted so as to be received well within the timeline for the planned shoot.

BLM supports EA Study

The US Bureau of Land Management (BLM) is in the process of working with Rose and its contractors to edit the Environmental Assessment (EA) document language to ensure compliance with new land use doctrine. As such, the document is expected to be ready for the public comment period submission by May 2017.

Following completion of the public consultation period, there will be a period of response to any questions raised by the public, following which the application will be put forward for final approval. If this process is successful, the company expects to receive the permit by the end of June 2017.

Additional comments will not delay seismic shoot

On 7 March 2017, Rose announced that the 15 day public consultation period for its 3D seismic shoot permit had formally begun. Following the completion of this period, and based on comments received, the company was informed by the BLM that certain questions raised in the comments received should have been addressed by the BLM in the original EA that supports the permit application. Consequently, Rose has amended the shoot design to accommodate the points raised and resubmitted the documents to the BLM for its review.

Once this review is complete, the revised and updated EA will be published and made available for a further 15 day public consultation period. The BLM has assured Rose that the revised timing of the granting of the permits will not impact the commencement of the proposed shoot in H2 2017.

Lease extension

On 22 March, Rose announced that the company had been granted a five year extension on State lands within the Gunnison Valley Unit within its Paradox Basin acreage position. Rose received confirmation from the School and Institutional Trust Lands Administration (SITLA) that it had granted an extension of five years for all eight State leases that form part of the Gunnison Valley Unit, otherwise known as the Federal Unit.

The Federal Unit, which comprises a substantial proportion of Rose's overall 90,000 acre position in the Paradox Basin, consists of almost 64,483 acres of which Rose is earning a 75% working interest in approximately 52,316 net acres. Of this net acreage position, over 6,257 acres is SITLA land and 43,031 acres is US BLM land, the entity which recently accepted Rose's EA Study (see above). The balance of 3,027 acres is private fee land.

Although the SITLA land has no bearing on the overall Federal Unit itself, this lease extension does preserve Rose's ability to develop the State land as well as the BLM acreage once the 3D seismic shoot is completed later this year.

Mexican mining assets

Third party toll milling

At the end of 2015, Rose announced that it had suspended mining operations at the Mina Charay project in northern Sinaloa in northwest Mexico due to high transportation costs and depressed commodity prices. Since this decision was made, the group has focused on toll milling third-party ore at its 100% owned crushing and floatation mill located at San Dieguito de Arriba (SDA Mill) which processes ore from two separate mines.

During H1 2016, the mill processed 8,664 tonnes of ore and a further 4,252 tonnes were processed in July and August 2016. These volumes have been sufficient to cover all direct mill operating costs and Rose is confident that increased tonnages over H2 2016 will be maintained, potentially delivering an operating profit from this business unit in the second half of 2016.

The mill at San Dieguito de Arriba (SDA)



Source: Rose Petroleum

Potential sale of milling operations

In March 2017, Rose entered into an MOU with Magellan Gold Corporation for the potential disposal of the SDA Mill and associated assets, licences and agreements for a total consideration of US\$1.5m. Under the terms of the agreement, Magellan has been granted a 90-day option to purchase the SDA Mill for a non-refundable US\$50,000 deposit which has already been paid by Magellan. This option can be extended for a further 60 days upon the payment of an additional US\$100,000 which would be credited against the final purchase price should a sale be agreed. The total purchase price of US\$1.5m is payable as US\$1.0m in cash with the balance of US\$0.5m in restricted Magellan stock.

Completion of the disposal of the SDA Mill is subject to several conditions including due diligence, an audit of SDA's financial statements and the completion of a financing by Magellan. The deal would also be subject to approval by Rose's shareholders at a general meeting of the company and as such, there can be no assurances that the sale of the mill will be completed.

In the event that sale of the SDA Mill does not occur, Rose will continue with its efforts to progress away from third-party toll milling and establish joint venture mining partnerships to increase mill throughput and benefit from the upturn in the gold price in order to boost group cash flow. The management has identified a number of past producing high grade gold projects that could provide feed for the SDA Mill if agreeable terms can be established with the mine project owners.

The Crushing circuit and Floatation process at the SDA mill



Source: Rose Petroleum

Recovery of Mexican IVA

Rose is currently pursuing the recovery of IVA (value added tax) and tax totalling MX\$16.5m, equivalent to c.US\$868,000 (assuming a current exchange rate of MX\$19.00 to US\$1.00) from the Mexican tax authority, Servicio de Administracion Tributaria (SAT). Rose has been in discussions with SAT regarding the reclamation of the sums owed to Minerales VANE SA de CV, the subsidiary of Rose that owns the SDA Mill. This claim dates back to 2013. Rose has made significant progress in this process over the past few months and the management is confident of a positive outcome.

Rose received a total of MX\$6.0m (c.US\$315,000) in March which was significantly more than the MX\$4.2m that the management anticipated that it would recover. This was followed by a further MX\$3.16m (c.US\$167,500) during April bringing the total recovered to date to approximately MX\$9.17m (US\$486,000) including MX\$774,476 (US\$41,000) of inflation adjustments.

The company is continuing the process of recovering the remaining MX\$8.8m (cUS\$466,400) from SAT excluding inflation adjustment payments. It should be noted that proposed disposal of the SDA Mill will have no impact on the potential recovery of this IVA for the Group.

US activities

In April 2016, Rose entered into an agreement with privately held Burdett Gold LLC, to conduct exploration drilling on the Ardmore copper project which consists of 18 unpatented mining claims located north of Tucson in Arizona. Burdett assumed control of the claims and is the operator of the project and has commenced exploration work.

Rose also holds uranium assets, the majority of which are held in a 50/50 joint-venture with Anfield Resources Inc., covering properties in the breccia pipe (vertical cylindrical bodies of broken sedimentary rock) district of northern Arizona. Rose also owns 100% of the North Wash project in Utah which contains a resource of uranium and vanadium.

Currently, Rose's uranium assets are being held on care and maintenance while management reviews its options to develop the projects further.

Cuba – Rose Gypsum Limited

In May 2016, Earth Source LLC invested US\$1.2m in Rose to pursue opportunities in Cuba. A newly formed subsidiary, Rose Gypsum Limited was set up participate in a competitive and exhaustive tender process to manufacture calcined gypsum, interior panels, ceiling panels, plaster bags and other related gypsum based materials for the construction industry in Cuba.

Gypsum is a soft sulphate mineral composed of calcium sulphate dihydrate. It is widely mined and is used as a fertilizer and as the main constituent in many forms of plaster, blackboard chalk and wallboard.

In July 2016, Rose Gypsum was selected by the negotiation group of Empresa de Materiales de Construcción Ciego de Ávila (EMC), the local company responsible for the project, to proceed into the detailed negotiations phase. Rose Gypsum was selected on the grounds of its technical and professional expertise following its negotiations with both EMC and the Cuban Ministry of Construction (MICONS).

Rose has engaged global market leader Grenzebach BSH GmbH as chief engineering partner on the project. Grenzebach will supply a complete design and engineering package for the project.

Rose Gypsum is tendering to become the operator, distributor and manufacturer on the project with an overall profit share. If successful, Rose will become the sole manufacturer of gypsum related products operating in Cuba. Although there is no guarantee that a deal will be completed, the management is confident of a successful outcome especially as embargo restrictions associated with Cuba appear to be relaxing.

Financial summary

Prior to the beginning of 2016, Rose derived nearly all of its revenue from gold and silver mining activities in Mexico. However, the decline in the gold price since its peak in 2012 meant that the group reported substantial operating losses in 2014 and 2015 even after stripping out non-cash impairment charges related to its uranium assets (US\$3.1m in 2015) and oil and gas properties (US\$0.55m in 2015 and US\$0.97m in 2014) in the income statement.

After the cessation of mining in Mina Charay in Mexico in late 2015, the group's revenue base was focused on third party toll mining in Mexico over the first half of 2016. This led to significantly reduced revenue but also a considerable reduction in the group's cost of sales. The management also reduced central administrative costs in H1 by US\$0.6m implying an annual run rate of up to US\$1.2m of G&A savings for the full year.

Rose has no outstanding debt and cash at the end of June 2016 was US\$1.7m. Although we expect that most of this has since been absorbed by group administration costs, cash resources were boosted in October 2016 with a £1.0m equity raise (c.US\$1.24m at the prevailing exchange rate). This cash is earmarked for advancing joint venture projects associated with Rose's SDA mill in Mexico in order to boost short term cash flow.

It should be noted that, with regards to the company's core activities, the permitting process relating to oil exploration activities in the Paradox Basin is funded up to the grant of the permits and activities in Cuba are also funded following the investment in Rose by Earth Source Investment Inc. in May 2016. We do not expect that the group will expend any significant funds on its uranium assets over the next 12 months.

Financial performance since 2011

Year ended Dec (US\$000)	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	H1 2016
Revenue	3,678	5,759	5,710	3,097	4,320	414
Profit before tax	-1,529	54	-2,981	-5,865	-9,864	-455
Underlying profit before tax*	-1,072	54	-41	-4,896	-4,600	-1,873
Basic EPS (¢)	-0.46	-0.12	-0.58	-0.55	-0.45	0.01
Net cash (debt)	816	-290	327	8,408	2,399	1,724

Source: Rose Petroleum

*Calculated prior to impairment charges, share based payments, forex gains and loss on disposals

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