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Parkmead enters into transformational talks on key project

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There were several positives to note in the annual results from **Parkmead** (PMG:52.8p), a small-cap oil and gas exploration and development company led by 19 per cent shareholder Tom Cross, the founder and former chief executive of Dana Petroleum until its sale to the Korea National Oil Corporation in 2010.

Firstly, the company generated £2.2m of positive operating cash flow from its low-cost onshore gas portfolio in the Netherlands, and the Diever West gas field in particular, which came on stream three years ago and has been exceeding expectations ever since. These have an average operating cost of only US$15.6 (£12.1) per barrel of oil equivalent. Closing net cash of £23.8m was £800,000 ahead of analyst predictions and with the benefit of the fall in sterling since the end of the financial year, the pro-forma cash pile is now worth around £24.2m. Parkmead also owns a shareholding currently worth £6m in oil and gas producer **Faroe Petroleum** (FPM:155p), a company that received a cash offer from Norwegian oil and gas operator DNO ASA, and one that clearly highlights the potential for corporate activity in the sector. Parkmead has a £2.9m interest bearing loan receivable on its balance sheet, too.

In effect, these three assets back up £33m of Parkmead's £52m market capitalisation, meaning that the company's exploration activities across 30 licences in the North Sea, any one of which has potential to create substantial investment upside for shareholders, are in the price for just £19m. The most valuable are three licences in the Moray Firth that contain the Perth and Dolphin fields.

Bearing this in mind, I can reveal that a detailed engineering study carried out by Nexen Petroleum, a subsidiary of the China National Offshore Oil Corporation (CNOOC), has confirmed the technical feasibility of a potential subsea tie-back of Parkmead's Greater Perth Area (GPA) project to the Nexen-operated Scott platform and associated facilities in the UK Central North Sea. Parkmead has now entered into commercial discussions with the Scott field partners to explore terms for a tie-back of GPA to Scott. A tie-back has the potential to transform the GPA project both commercially and economically, by dramatically reducing the capital expenditure required to bring the GPA project onstream and by lowering the operating costs thereafter.

To put the potential valuation upside into perspective, analyst Colin Smith at house broker Panmure Gordon places a risked valuation of £50m, or 50.5p a share, on Parkmead's undeveloped oil resources, or £372m on an unrisked basis. It goes without saying that if the commercialisation of the GPA project via Scott makes substantial progress then there is likely to be significant upside to Parkmead's share price. For good measure, with the benefit of its low-cost onshore gas portfolio, Mr Smith at Panmure expects Parkmead to turn in a pre-tax profit of £1.2m in the current financial year to the end of June 2019, thus de-risking the investment case even further and providing additional operational cash flow to direct towards exploration activities.

So, having included Parkmead's shares, at 37p, in my **2018 Bargain Shares Portfolio**, and last rated them a buy at 50.5p ahead of news on the commercialisation of the GPA project **('Bargain Shares repeating buying opportunities', 29 Oct 2018)**, priced on a 36 per cent discount to Panmure Gordon's total risked net asset value (NAV) estimate of 85p a share I continue to see significant share price upside. Buy.