



52-wk Range: £0.10-0.32
 12 month target £0.50

Market Cap (M): £59.3
 EV (M): £145.6

Oil & Gas

Grin and bear it

Summary

Max Petroleum Plc is an independent Oil and Gas exploration company with an initial focus in the Republic of Kazakhstan. The Group owns a 100% interest in the Blocks A&E and Astrakhanskiy oil and gas licence areas covering 13,500 km².



Key Metrics

Shares Outstanding (M): 439.4
 Current Price (GBP): £0.135

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Event

Max Petroleum Plc announced today that the Court of Cassation, an appellate court of the Republic of Kazakhstan, has upheld a tax claim brought against the Company by local Kazakh tax authorities regarding the timing of certain tax deductions made by the Company prior to 1 January 2009. The Tax Claim resulted from a routine tax audit of the Company for calendar years 2005 to 2008 and involves a dispute over the timing of recovery (i.e. depreciation) of the Company's costs capitalised to its oil and gas properties for tax years prior to Kazakhstan's adoption of a new tax code in 2009. In summary, the Company began depreciating its capitalised costs when it began producing crude oil in accordance with the terms of its subsoil use licence and the Kazakh legislation in place at the time the licence was executed. The local tax authorities, however, have asserted that the Company should only begin depreciating its capital costs upon the formal declaration of a commercial discovery to the Kazakh authorities. As a result, the local tax authorities have disallowed a total of \$35 million in depreciation deductions taken by the Company during calendar years 2006 through 2008, resulting in an assessment of additional taxes, interest and penalties of \$15.6m. The Company continues to believe the Tax Claim is without merit and will appeal the Court of Cassation's decision to the Supreme Court of the Republic of Kazakhstan as soon as possible. The Company expects the Supreme Court appeals process to take between two to six months. In the event it is unsuccessful, the Company expects to recover the economic benefit of the contested deductions in future years.

Due to the Court of Cassation's decision, however, the local tax authorities now have the right to require payment of the Tax Claim prior to the ruling of the Supreme Court. The Company has applied for, and is in current discussions with, the appropriate local tax authorities to spread any required payments over a longer term period of up to twelve months. The Company intends to fund any near-term payments due on the Tax Claim from cash flow from operations, borrowings under its Credit Facility with Macquarie Bank Limited, and the offset of current VAT receivables from the Kazakh government. If the Company is successful in its appeal to the Supreme Court, any payments made on the Tax Claim would be refundable to the Company or creditable against other current tax obligations.

Comment

The worse cash flow impact scenario would be for the Supreme Court to require immediate payment of the disputed tax liability and subsequently uphold the decision of the Court of Cassation. It would mean an immediate payment of US\$15.6m that Max Petroleum could and would cover from the existing Macquarie debt facility, and no subsequent reimbursement. The impact on FDC risked NAV of a debt increase of that magnitude is -1p.

However even this impact would be partly offset by future depreciation tax shield on the unrecovered depreciation for the 2006-2008 period.

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The Company will file an application to the Supreme Court of Kazakhstan in the next week or two and should get a ruling within 2-6 months. We understand that in a similar case the Supreme Court has overruled the local tax authorities recently and if Max Petroleum were to be successful any potential payment that could be required immediately would then be recovered after the ruling.

Clearly the stock could do with a better news flow, given the lack of success from the drill bit recently.

Recommendation

Buy rating and target price unchanged.

Research Disclosures

Lionel Therond

Lionel has worked at Fox-Davies since April 2009. Prior to this, he had 13 years experience as an investor at JPMorgan Asset Management and had previously spent 10 years in the Oil&Gas industry at Shell. Lionel graduated in Geology and Geophysics (MSc) before gaining an MBA at Insead; he is also a CFA charterholder.

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Research disclosure as of 02 June 2010

Company Name	Disclosure
Max Petroleum (MXP)	7

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Company	Ticker	Recommendation	Date	Target Price	Last Price
Oil & Gas					
Ascent Resources	AST LN Equity	BUY	22.04.10	£0.20	£0.04
Borders & Southern Petroleum	BOR LN Equity	BUY	01.02.10	£1.50	£0.68
Circle Oil	COP LN Equity	BUY	27.05.10	£0.90	£0.35
Desire Petroleum	DES LN Equity	HOLD	29.03.10	£1.00	£0.87
Enegi Oil	ENEG LN Equity	SELL	17.05.10	£0.10	£0.24
Falklands Oil & Gas	FOGL LN Equity	BUY	01.02.10	£4.00	£1.88
Gulf Keystone	GKP LN Equity	BUY	25.05.10	£2.00	£0.75
Gulfsands Petroleum	GPX LN Equity	HOLD	04.05.10	£3.00	£2.57
Hardy Oil & Gas	HDY LN Equity	BUY	26.05.10	£3.00	£1.69
Matra Petroleum	MTA LN Equity	BUY	26.05.10	£0.07	£0.02
Max Petroleum	MXP LN Equity	BUY	02.06.10	£0.50	£0.14
Petrokamchatka	PKP CN Equity	HOLD	14.01.10	C\$0.15	C\$0.05
Po Valley	PVE AU Equity	BUY	29.04.10	A\$1.50	A\$0.39
Range Resources	RRL LN Equity	BUY	17.12.09	£0.08	£0.04
Rockhopper Exploration	RKH LN Equity	HOLD	07.05.10	£1.10	£2.68
San Leon Energy	SLE LN Equity	BUY	02.06.10	£0.80	£0.18
Sterling Energy	SEY LN Equity	HOLD	01.02.10	£1.50	£1.12
Tower Resources	TRP LN Equity	HOLD	23.03.10	£0.02	£0.01
Victoria Oil & Gas	VOG LN Equity	BUY	21.04.10	£0.09	£0.03

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