



May 8, 2017

Maglan Capital increased in value by 7.17% (net of all fees) during the month of April.

For 2017, Maglan Capital has increased 6.99% (net).

Madalena Energy (MVN; MDLNF)

After an initial 25%+ bump to start the year, Madalena Energy's stock has been quiet recently. However, the industry and the region have been on fire (in a good way), with no signs of slowing down. This bodes very well for Madalena.

Macro Elements

President Mauricio Macri has continued to prove that he is leading one of the most stable governments and one of the brightest economies in South America. In that vein, in early April, S&P upgraded Argentina's long-term credit rating from B- to B. While the upgrade still leaves Argentina's credit rating in high-yield territory, it nonetheless represents a vote of confidence in the reforms that Pres. Macri has undertaken since taking over from the previous government, which left behind an economy on the brink of collapse. After contracting around 2.3% in 2016, Argentina's economy is expected by S&P to grow by 3%, on average, over the next three years.

In March, as part of a plan to attract new investment in the country's energy exploration and development, the Government of Argentina announced an immediate 10% increase in the wellhead price of natural gas (\$3.77/mmbtu in April (from \$3.42)). Furthermore, the country set out a schedule of pricing, with an increasing premium, through 2019¹.

¹ \$4.19 in Oct 2017; \$4.68 in April 2018; \$5.26 in Oct 2018; \$5.96 in April 2019; \$6.80 in Oct 2019. The foregoing is for existing production. There is a separate pricing scheme for "new production" On January 12, 2017, Macri

With respect to both oil and gas production, although current government incentives/premiums are helping support interest and investment, the eventual and planned goal is to have the industry supported independently by open-market prices. To that end, YPF recently announced that its horizontal well break-even costs have fallen below \$40/barrel. In relation, YPF has cut its average horizontal well cost ~50% to \$8.2mm in Q4/16 from \$16.6mm in 2014. The majority of the cost savings are as a result of improved drilling and completion efficiencies which reduced the average time for a new well to 15 days from 40 days.

Industry Developments and Transactions

Recently, Energy Minister, Juan Jose Aranguren, ball-parked the total spend on drilling pilot projects in 2017 in Neuquen (Vaca Muerta) at \$6-8B. Furthermore, the expectation is \$12-15B in investments in 2018, and \$20B annually from 2019 onward. More explosively, if the pilot projects move from “pilot” phase to “development” phase, they will lead to an additional \$125B of investment over 10 years. There are 700 unconventional wells scheduled to be drilled in Argentina, which would likely *increase by a factor of 10* when projects move to development.

In early May, the *Wall Street Journal* highlighted the emphasis by worldwide energy majors, like Exxon, Chevron, BP, Total and Shell, on the Vaca Muerta, making an effort to replicate the US shale boom in Argentina’s Vaca Muerta, which could potentially carry as much oil and gas as the largest basins in Texas or North Dakota.²

In recent weeks, the announcement of additional deals in the Vaca Muerta have come fast-and-furious.

- YPF announced a \$500mm shale development with PAE, Total and Wintershall.
 - Total’s CEO said on April 27 that the company will invest \$500mm over three to four years to develop a shale-gas field in Argentina. The CEO said there are giant resources of non-conventional gas in Argentina.
- Schlumberger, known as a drilling services provider, is investing \$390mm to jointly develop Vaca Muerta property owned by YPF.³
- Pluspetrol, the third-biggest oil producer in Argentina, announced an investment of \$160mm in a Vaca Muerta pilot gas project.⁴ Pluspetrol started its testing in 2016, and is expected to complete the 35-well pilot project by 2020. If the results find resources economically viable for production, the company will consider continuing with the development of the block with an investment of \$350mm.

announced natural gas pricing incentives for production from new wells with \$7.50/mmbtu through 2018, \$7.00 in 2019, \$6.50 in 2020 and \$6.00 in 2021.

² https://www.wsj.com/articles/big-oil-gets-in-early-on-argentina-shale-1493890202?mod=wsj_streaming_stream

³ <http://www.reuters.com/article/argentina-ypf-schlumberger-idUSL1N1HK0X2>

⁴ <https://www.platts.com/latest-news/natural-gas/puntadeleste-uruguay/argentina-pluspetrol-to-invest-160-mil-in-vaca-21578341>

- Oil trading firm, Mercuria, announced an investment into Andes Energia, to finance drilling activities in Vaca Muerta⁵
- YPF is prepared to raise \$1B from assets sales of non-core assets- Metrogas (natural gas distributor), OPESSA (service station business), and Profertil (fertilizer business), to fund increased oil and gas exploration and development

Madalena

The recipe for success for Madalena is clear:

- Reduce fixed costs. Particularly, consolidate management and financial reporting into Buenos Aires
- Develop shale assets with large, sophisticated partners, with a focus on gas (over oil)
- Self-develop conventional assets

With regard to the company's shale assets, the initial results of the first well drilled jointly with Pan-American in Coiron Amargo Sur Este should be available shortly. Solid results could catapult the value of the block and, thereby, the value of Madalena's share-price.

Maglan Capital is an event-driven investment fund with a concentrated portfolio of investments across the capital structure of small- and mid-cap companies with core focus on financial distress, restructuring and operational turnaround.

We appreciate your support and confidence in our team.

Best regards,

Steven Azarbad, *Chief Investment Officer* and David D. Tawil, *President*

⁵ <http://timesofindia.indiatimes.com/business/international-business/oil-producer-andes-energia-gets-60-mln-financing-from-mercuria/articleshow/57917525.cms>