

#### Stock Data

Share Price:	4.35p
Market Cap.:	£69.45m
Shares in issue:	1,596.50m
52 week high/low:	8.15p/3.75p

#### Company Profile

Sector:	Oil & Gas
Ticker:	ZPHR
Exchange:	AIM

#### Activities

Zephyr Energy plc ('Zephyr', 'the Group') is an independent oil and gas E&P Group with a strategic focus on carbon-neutral hydrocarbon development projects in the Rocky Mountain region of the US.

[www.zephyrplc.com](http://www.zephyrplc.com)

#### 5-year share price performance



Source: [LSE](https://www.lse.com)

Past performance is not an indication of future performance.

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TPI acts as joint broker to Zephyr Energy plc.

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## Zephyr Energy plc

Zephyr yesterday provided an operational update for its State 36-2 LNW-CC well (the 'State 36-2 well' or 'the Well') at the Group's flagship project in the Paradox Basin, Utah. Following completion of workover operations on 7 April 2023, apparent failure of a Full Opening Safety (or 'TIW') Valve at surface led to a significant well control incident. Despite multiple attempts by the rig crew to secure the Well, hydrocarbons were released from the wellbore in an uncontrolled manner. Importantly, all personnel were safely evacuated without injury and relevant authorities were notified, as a result of which a specialist well control team (recommended by the Group's insurers) was deployed. On Monday the Well was successfully brought back under control, following which well pad remediation steps immediately commenced. While the remediation process is not expected to present any technical challenges, management will now re-evaluate every aspect of the upcoming production test, including any associated well work needed to help ensure a successful test (which is now understandably delayed but at present expected to get underway in the coming weeks). On a positive note, Zephyr does maintain comprehensive Well Control Insurance with potential to cover the bulk of all direct and indirect costs incurred during this incident, while the extent of gas and condensate flow witnessed during the three days of continuous uncontrolled blowout builds confidence that Zephyr does indeed have a very large well on hand.

### Apparent failure of a safety valve led to a well control incident

Occurring toward the end of operations last Friday, a problem was identified when preparing to release excess drilling fluids (or 'mud'), with the TIW Valve encountering a significant build-up of pressure. As the rig crew attempted to transfer back to surface reserve tanks, a Well Kick resulted in formation fluids flowing up the wellbore in an uncontrolled manner, leaving the Blowout Preventor ('BOP') unable to choke off the excessive flow

Start-up issues are of course not particularly unusual when such emerging plays break new ground. Senior management were on site within one hour of the incident, overseeing strict safety routines that ensured the pad was rapidly abandoned with no injuries or casualties. All relevant authorities were notified and a specialist well control team (recommended by the Group's insurers) was deployed in order to bring the Well under control as quickly as possible. This was effected the following Monday using the principle that sufficiently high pressure (or 'hydrostatic head') of 'kill mud' can be created to overcome the underlying pressure of the formation fluids, whereupon it was immediately sealed. Once stabilised, the clean-up and wash-down got underway, with the original TIW Valve also being replaced.

### Well Control Insurance expected to cover most of the costs

Being familiar with such unpredictable events, Zephyr's operations are covered by comprehensive Well Control Insurance. Although finalisation of negotiations is likely to take some time, it is expected that its policies will cover the bulk of all equipment and pad damage costs, as well as expenses

related to site remediation. Zephyr may have duty to pay some relatively minor excess charges, while also incurring additional charges related to possible facilities modification required to cope with the excess pressure, any additional work that may be needed to the well itself plus fees related to retaining the rig crew for a longer than expected period.

Representatives from Utah state regulators that attended the site appeared satisfied with actions taken to date.

### **Restart of State 36-2 well's production testing expected in coming weeks**

Rig, drill pad and wellbore remediation is not expected to present any technical challenges although additional well work may be required once further evaluation has been undertaken. Although it is unclear at this time as to the total volume of gas and condensate released, surface impacts appear to be limited to an immediate area around the pad, and management plans to conduct a confirmatory environmental survey in the near term. Possibly taking a little longer, Zephyr's Board is expected to review each and every aspect of the production facilities, the Well itself and operational procedure to help ensure a successful production test (which is now understandably delayed but at present expected to get underway in the coming weeks) given the significant pressure events witnessed to date. Altogether this is likely to result in a few weeks delay before State 36-2 well's production testing gets underway, although we do not view the delay as material in the long run.

The event itself, although challenging from a safety and environmental standpoint, provided yet a further boost to the Group's confidence that it has a significant well on hand with State 36-2. Being an uncontrolled event, there was of course no facility to measure the flow of gas and condensate over the three days, although it clearly left an impression that the Group has a large well on hand capable of producing exceptional volumes of both natural gas and high-API gas condensate (that typically trades on a price/bbl slightly above WTI). The fluid mix itself is likely to be similar to that seen during State 16-2 well's own production test, although being somewhat further south it may possibly produce a slightly higher proportion of gas condensate. Once underway, workover operations and production testing are likely to take four weeks to complete. The outcome will undoubtedly be eagerly awaited.

Production test results from the State 36-2 well, along with results from that on the State 16-2 well, will be integrated into Zephyr's overall reservoir model and will help define the next steps for the Paradox project development, including the sizing of related gas infrastructure and the associated capital expenditure. Targeting first commercial gas sales during Q4 2023, the Group needs to complete the recommissioning of its recently acquired Powerline Road gas processing plant (with handling capacity yet to be determined). From that point, Zephyr will remain at the mercy of Dominion with regard to completing the refurbishment of their 16-inch infrastructure, regarding which TPI understands positive discussions have already taken place and construction of the Dominion pipeline extension is currently underway.

### **Potential Contingent & Prospective Resources worth well in excess of US\$1 billion**

Zephyr's active land management strategy appears to be delivering a defensible and growing portfolio of development opportunities, something which is increasingly difficult to replicate in today's regulatory and political environment. Following the events of the past few days, management's immediate focus remains on restarting State 36-2 LN-CC's production testing, followed by safely completing the Well and the recommissioning of a recently acquired processing plant before being tied-in to gas infrastructure. It remains on schedule to be generating first revenues before the end of 2023.

Publication of the Group's Competent Person's Report ('CPR') 2022 on 26 April 2022, highlighted Zephyr's substantial remaining potential in the Paradox Basin. While the range of values illustrated in Sproule's report presently remain very wide, recognising also that there are still significant underlying technical/operational risks to be surmounted, Zephyr's management and exploration team have demonstrated a high level of intuition along with the capacity to meet and optimise such challenges through carefully calculated process. The fully funded drilling programme now underway will enable further delineation and increase overall understanding of the Paradox asset base.

Management continues to assess potential upside and will shortly determine additional steps with a view to delivering increases in all reserve and resource classes during 2023.

Significantly in this respect, funding for the development of the Paradox Project will be provided from the Group's Williston Basin non-operated assets, for which a further positive quarterly update is expected to be released quite shortly. In February 2023, it reiterated its FY 2023 production forecast of 1,550 to 1,750 boepd from the Williston project (net to Zephyr). It also noted that eight additional producing wells from its existing portfolio were expected to be brought online during the following six months, which were expected to more than mitigate decline rates typical of Williston Basin production. The Group has hedged 157,000 barrels of oil over the next 15 months (starting 1 January 2023) at a weighted-average price of US\$86.89 per barrel and is expecting significant additional production volumes by the end of March 2023 from the new Slawson wells coming online and will continue to evaluate its commodity price risk management strategy on a regular basis.

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