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Canacol Energy

Oil & gas

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Expanding gas resource base

In September 2016, Canacol added a second drilling rig in the Lower Magdalena Basin targeting the addition of c 100bcf of recoverable resource to its 2P 390bcf (end 2015) gas reserve base. More gas resource is expected to underpin new sales contracts and a planned increase in productive capacity from 100mmcfd to 190mmcfd. Recent successes at Oboe-1 (28bcf), Nispero-1 and Trombon-1 (Nispero/Trombon combined 40bcf pre-drill) and a five-year rolling 64% exploration success rate gives us confidence in Canacol's ability to meet its resource expansion target. Management estimates a 2P gas value under long-term contract of US$1.17bn, relative to Canacol's EV of US$823m (30 June net debt).

Exploration success and Q416 drilling activity

Four successful gas discoveries year-to-date have added material resource and net production; this momentum is expected to continue in Q416 with four more wells planned before year end: Nelson-6 gas exploration (31bcf prospective), Nelson-8 gas development (14bcf proved undeveloped), Clarinete-3 gas development (25bcf proved undeveloped) and Mono Capuchino-1 oil exploration (9mmbbls prospective). Gas prospects have been significantly de-risked through AVO analysis, driving up basin-wide exploration success rates, while well costs remain low at US$4.0-6.5m despite subsurface depths of up to 10,000ft. Well costs have benefitted from significant improvements in drilling efficiency over the last 12 months. Low well costs and high success rates enable Canacol to generate peer-leading risked returns on exploration spend.

Strong cash generation and sales growth

Contractual oil and gas sales averaged 18,908kboed in Q316 (80% gas), up 81% y-o-y helped by the successful Promigas pipeline expansion in April 2016. Increased gas production and reduced costs have helped netback margins of 86% or US$4.56/mcf. Management expects increased production and reduced unit costs to enable Canacol to deliver group 2016 EBITDAX of c US$135m at prevailing oil prices. Canacol's fixed price gas contracts mitigate impact from oil volatility with c 86% of production insensitive to oil. As a result of increased production and strong cash generation, the consolidated leverage ratio is expected to fall from 3.8x net debt to 12m trailing EBITDAX at December 2015 to 1.9x* December 2016.

Valuation: Trading below gas value

Management estimates a 2P gas value under a long-term contract of US$1.17bn, relative to an EV of US$823m. Relative to consensus Canacol trades at c 0.4 times consensus RENAV and c 0.9 times Core NAV.

Consensus estimates

Year end	Revenue (US$m)	EBITDA (US$m)	Net income (US$m)	Capex (US$m)	FCF (US$m)
12/14	206.1	103.0	9.9	(132.9)	(54.9)
12/15	149.0	56.4	(106.0)	(190.5)	(126.1)
12/16e	153.7	104.9	(30.6)	(84.5)	(10.0)
12/17e	233.1	186.4	71.0	(91.9)	18.2

Source: Bloomberg. Note: *Management forecasts and estimates

Price	C$4.58
Market cap	C$791m
	C$/US$ 0.76

Share price graph

Share details

Code	CNE
Listing	TSX
Shares in issue	172.8m

Business description

Canacol Energy has secured 2.5m net acres of prospective acreage across Colombia and Ecuador. 2P reserves stand at 79mmboe, 82% gas. Gas production is ramping up to meet domestic demand, with Canacol forecasting 16-17kboed of net production in 2016.

Bull

- High, sustainable netbacks.
- Growing resource base supported by 64% five-year exploration success rate.
- Option on high impact oil/shale oil as crude prices recover.

Bear

- Currently reliant on third-party operated pipeline infrastructure for gas transport.
- Shale oil exploration remains early stage.
- Step-change in gas production contingent upon new pipeline infrastructure.

Analysts

Sanjeev Bahl	+44 (0)20 3077 5742
Ian McLelland	+44 (0)20 3077 5756
Will Forbes	+44 (0)20 3077 5749

oilandgas@edisongroup.com

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