SAYER ENERGY ADVISORS

Viewpoint

An Oil and Natural Gas Industry Newsletter

Spring 2022

Is the SpinCo Returning?

A recent trend we have witnessed in the Canadian oil and natural gas industry is the return of the SpinCo structure as part of a transaction involving the sale of all of the issued and outstanding shares of an oil and natural gas company. The SpinCo structure involves the seller spinning out certain lands and production into a separate entity concurrent with the sale of all of the issued and outstanding shares of the company.

The SpinCo structure was very common in the early to mid-2000's when oil and natural gas royalty income trusts ("RITS") were very active on the merger and acquisition ("M&A") front. At that time, RITS were focused on acquiring producing properties with low-risk development potential and the exploration and production companies would then sell their producing properties to RITS in a corporate sale and concurrently "spin out" these growth type assets into a separate entity.

In addition, a number of oil and natural gas companies which previously converted into RITS in the early 2000's also created SpinCo's as part of these reorganizations. Companies such as **Crew Energy Inc.** and **NuVista Energy Ltd.** were the resulting SpinCo's created out of the reorganizations of **Baytex Energy Ltd.** and **Bonavista Petroleum Ltd.** respectively into RITS in 2003.

Late last week, **Tamarack Valley Energy Ltd.** announced that it had entered into an agreement to acquire all of the issued and outstanding shares of privately-held **Rolling Hills Energy Ltd.** for total consideration of approximately $93.0 million consisting of $46.5 million in cash and the issuance of 9,276,623 common shares of Tamarack Valley. Rolling Hills main producing properties are located in the Jarvie area of Alberta and are producing from the Clearwater Formation. As part of the transaction, shareholders of Rolling Hills will also receive 0.387 of one common share in a newly created Clearwater growth focused company ("NewCo"). NewCo will operate as a private company and will be led by existing members of the Rolling Hills management team. NewCo will retain certain of Rolling Hills' Clearwater lands totaling approximately 193,000 net acres and estimated production of 700 bbls/d of oil.

In late March, **Leucrotta Exploration Inc.** announced that it had entered into an arrangement agreement with **Vermilion Energy Inc.** pursuant to which Vermilion will acquire all of the issued and outstanding shares of Leucrotta for total consideration of approximately $477.0 million excluding value assigned to the newly formed Montney company **Coelacanth Energy Inc**. As part of the transaction, the shareholders of Leucrotta will receive $1.73 in cash per Leucrotta share held, plus 1.0 common share of Coelacanth and 0.1917 of one Coelacanth common share purchase warrant. Each Coelacanth warrant will entitle the holder to acquire one Coelacanth share at an exercise price of $0.27 per share at any time on or before 30 days following the closing of the transaction.

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Coelacanth is anticipated to be a new junior energy company led by Mr. Robert Zakresky as President and CEO and certain members of Leucrotta's current management team. Coelacanth will be a growth-oriented entity with assets focused in the Montney Formation in the Two Rivers area of northeastern British Columbia. At the time of closing, Coelacanth is forecast to have approximately 400 boe/d of production, over 140 net sections of Montney land and approximately $80.0 million in cash (subject to the completion of certain equity financings and the exercise of Coelacanth warrants mentioned above).

It should be noted that Leucrotta was formed through a SpinCo structure back in 2014 when **Crocotta Energy Inc.** was acquired by **Long Run Exploration Ltd.** for approximately $394.0 million. As part of the transaction, each common share of Crocotta was exchanged for 0.415 of a common share of Long Run, 1.0 common share of Leucrotta and 0.2 of a Leucrotta common share purchase warrant. Each whole Leucrotta warrant entitled the holder to acquire one common share of Leucrotta at an exercise price of $1.70 per share at any time on or before 30 days following the closing of the transaction.

The Crocotta assets which were spun out to Leucrotta were focused in the Montney Formation in the Dawson-Sunrise area of northeastern British Columbia. At the time of the transaction, Leucrotta had approximately 2,300 boe/d of production, over 60 net sections of Montney land and approximately $67.0 million in cash. We expect this recent trend with the SpinCo type transaction to continue as it is a structure that could be used in the current M&A market to bridge a value gap between buyer and seller and provide additional returns to shareholders. In addition, this structure also allows existing management teams such as Rolling Hills and Leucrotta a platform to start over again in popular plays such as the Clearwater and Montney, rather than starting from scratch.

Written by Tom Pavic
Sayer Energy Advisors
Originally Appeared in the Daily Oil Bulletin on April 27, 2022

Merger and Acquisition Report

Stay informed, stay current, stay active.

Sayer's Canadian Oil Industry Merger and Acquisition Report gives you all the information you need to analyze individual transactions or the market as a whole. This quarterly report is a great reference tool for strategic decision-making. The analysis of individual transactions and industry activity allows readers to compare specific deals or overall market trends every quarter. From median prices to detailed information and metrics, the ***Canadian Oil Industry Merger and Acquisition Report*** ensures you know what the industry is really paying for Canadian oil and natural gas assets not just announced in the headlines.

The Canadian Oil Industry Merger and Acquisition Report is considered by our peers in the field to be the only reputable source for independent and complete information on merger and acquisition activity in the Canadian oil patch. The Merger and Acquisition Report offers the competitive edge to help you lead your company to success.

Annual Subscription: $1,600.00 + G.S.T.
Includes Four Quarterly Reports and the Annual Summary

To subscribe, please contact Lori Deagle
research@sayeradvisors.com or 403.266.6133

Sayer in the News...

Financial Post

Soaring Oil Prices May Not be Enough to Draw Investment Back to Canada's Oilpatch

Barbara Shecter
Published March 9, 2022

A push for cleaner energy and memories of past boom and bust cycles, is creating reticence among investors and producers.

The spike in oil prices driven by Russia's invasion of Ukraine and the sanctions imposed by Western nations in response has revived the debate over building up Canada's energy sector. But while the commodity lift has energy stocks soaring, it may not be enough to draw investment back to the oilpatch.

"If we ramp up production here, you're going to have an issue of getting it out to the world market," said Tom Pavic, president of Sayer Energy Advisors in Calgary.

"We still don't have Trans Mountain (pipeline) up and running, so that's going to be another year. And Keystone got kiboshed, so you just don't have enough ability to export all the oil and gas that we produce right now because of a lack of pipelines."

While politicians in Alberta are pushing Canada's oilpatch as a solution for the United States and parts of Europe looking for alternatives to Russian oil, sector observers say Canada's prospects of stepping up have been dampened by years of underinvestment. Combined with a push for cleaner energy and memories of past boom and bust cycles, this is creating reticence among investors and producers.

"The United States is clearly looking for alternate sources of crude oil, as indicated by the talks with Iran and Venezuela," said Kristina Hooper, chief global market strategist at Invesco. "Given Canada's close alliance with the United States and its robust production of crude oil, it would be a natural source of increased production," she added, noting that Canada increased its exports to the U.S. last year.

The challenge, however, is how quickly Canada can meet demand, given the geopolitical risks and alliances now driving business and trade decisions, she said.

There is also the challenge of attracting fresh, patient capital to fund long-term projects.

"A lot of funds are not investing in companies that are producing fossil fuels, so you're not seeing a lot of that capital flowing in," Pavic said. "And because of that … you're seeing a lot of discipline by the producers here where they're not — even though commodity prices are shooting up — they're not increasing their capital expenditure budgets."

He said that even if they were to change course and ramp up production — rather than pay down debt or return money to shareholders through share buybacks and dividends — the cost of getting the oil to the U.S. and European markets without the availability of additional pipelines would render it less competitive than alternatives.

"Typically, our oil trades at a discount to West Texas Intermediate … and then once our supply builds up, and we're not able to get it out to market, that differential widens," Pavic said.

J. Ari Pandes, an associate professor of finance at the University of Calgary's Haskayne School of Business, said countries such as Venezuela and Iran have an edge in that they have spare capacity and an ability to export their product, which has been hampered only by past sanctions.

Canada, on the other hand has a bit of spare capacity "on the margin, which will no doubt be in demand," he said.

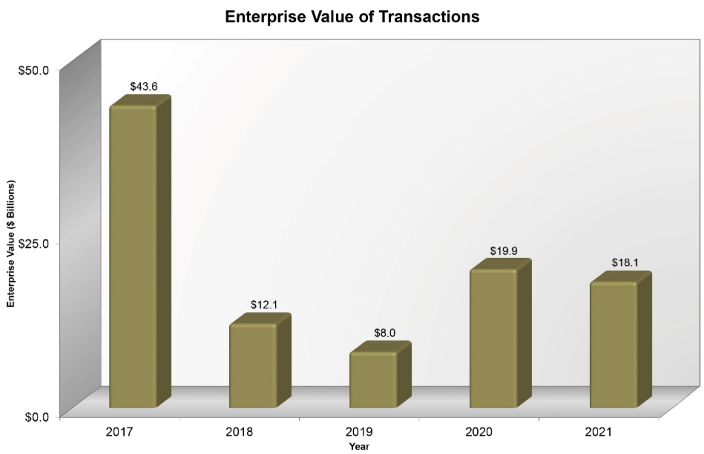
"But we can't immediately ramp up production to satisfy a major loss in Russian oil …. Part of this has to do with the lack of investment over the last eight years, plus limited take-away capacity."

Investment capital would be expected to come from players in private equity, which tend to take a patient view on investments, he said. However, private equity funds are holding back because of the environmental, social, and governance movement driving a push away from fossil fuels, Pandes said.

"At the end of the day energy investments are long-term, and so they, too, will be reluctant to invest in long-term traditional energy projects unless the companies can demonstrate and have a plan that fits in with the energy transition," he said. "This is why energy companies are returning cash to shareholders instead of reinvesting."

M&A Value Falls Slightly Year-Over-Year

The total enterprise value of merger and acquisition ("M&A") transactions in the Canadian oil and natural gas industry, dropped 9% in 2021 to $18.1 billion from $19.9 billion 2020.



There were three deals in 2021 valued at over a billion dollars which accounted for approximately 40% of the total M&A value. All three of which were corporate transactions. This compares to 2020, when there was only one deal valued at over a billion dollars. **Cenovus Energy Inc**.'s acquisition of **Husky Energy Inc**. in 2020 was valued at $15.0 billion and made up 75% of the total M&A value for the year.

The largest transaction in 2021 was **ARC Resources Ltd.**'s acquisition of **Seven Generations Energy Ltd.** for $5.1 billion. Seven Generations' main producing property was located in the Kakwa area of Alberta. At the time of the transaction, the combined company became Canada's largest condensate producer, third-largest natural gas producer, and sixth-largest upstream energy company. The combined company continued under the name ARC Resources Ltd. with expected average daily production of over 340,000 boe/d, consisting of approximately 138,000 bbl/d of liquids and approximately 1.2 Bcf/d of natural gas.

The second largest transaction in 2021 was **Tourmaline Oil Corp.**'s acquisition of **Black Swan Energy Ltd.** for $1.1 billion. Black Swan's main producing properties were located in the Aitken and Nig areas of northeastern British Columbia. Black Swan also held material Montney land positions in the Beg, Jedney, Laprise and the Sojer areas of northeastern British Columbia. With this acquisition, Tourmaline forecasted its production would increase to between 465,000 to 475,000 boe/d (78% natural gas).

The third largest transaction in 2021 was **Canadian Natural Resources Limited**'s acquisition of publicly-held **Storm Resources Ltd.** for just over $1.0 billion. Storm's main producing properties were located in the Fireweed, Nig Creek and Umbach areas of British Columbia. Storm's lands complemented Canadian Natural's interests in northeastern British Columbia and provided Canadian Natural synergies with its operations in the area. This was the second significant corporate acquisition Canadian Natural completed in northeastern British Columbia in the last two years as Canadian Natural also acquired all of the issued and outstanding shares of publicly-held **Painted Pony Petroleum Ltd.** in 2020 for $638.8 million. Painted Pony's main producing properties were located in the Beg, Blair, Daiber, Gundy, Kobes, Townsend and West Blair areas of British Columbia.

In recent years corporate transactions have dominated the M&A market and this was no different in 2021. There was approximately $18.0 billion in total enterprise value of large deals (over $5 million in value) in 2021 with corporate transactions accounting for $12.0 billion or 67%. Property deals made up the remaining $6.0 billion in total enterprise value. The split between corporate and property transactions is similar to what occurred in 2020 when corporate transactions made up a majority of the total M&A value.

The increase in commodity prices along with the continued lack of investment capital were the dominating factors that drove the M&A market in 2021. These factors led to a number of privately-held oil and natural gas companies being sold as illustrated by the aforementioned Tourmaline/Black Swan transaction. Other notable private oil and natural gas companies which were sold in 2021 were **Velvet Energy Ltd.** to **Spartan Delta Corp.** for approximately $754.0 million and **Anegada Energy Corp.** to **Tamarack Valley Energy Ltd.** for approximately $533.6 million.

There are a number of assets and companies that are currently on the market which may lead to strong M&A activity in 2022. Some notable offerings include **Imperial Oil Limited** and **ExxonMobil Canada,** which publicly announced their intention to pursue the sale of their interests in **XTO Energy Canada**. Imperial and ExxonMobil each own 50% of XTO which has assets located in various areas in central Alberta with production of over 32,000 boe/d (140 MMcf/d of natural gas and 9,000 bbl/d of oil and natural gas liquids). Also of note is **Enerplus Corporation,** which publicly announced its intention to initiate a divestment process for its Canadian assets. Enerplus' Canadian assets produce approximately 9,100 boe/d (84% oil and natural gas liquids).

The M&A market early in 2022 has seen steady activity with a number large transactions announced to date. The most significant transaction announced so far in the first quarter of 2022 was **Vermilion Energy Inc.** announcing its intention to acquire **Leucrotta Exploration Inc.** for approximately $477.0 million. The number of companies and assets currently available on the market coupled with appreciating commodity prices could lead to more consolidation and thus increased M&A activity for the remainder of 2022.

Written by Ben Rye
Sayer Energy Advisors
Originally Appeared in the Daily Oil Bulletin on March 30, 2022

Current Disposition Packages Available through Sayer Energy Advisors

- Property Divestiture
- Swan Hills, Alberta
- 268 boe/d (256 bbl/d, 70 Mcf/d)
- Bid Deadline: May 12, 2022

- Water Disposal Divestiture
- Grande Prairie, Alberta
- Bid Deadline: May 12, 2022

- Property Divestiture
- Southeastern Saskatchewan
- 189 bbl/d of oil
- Bid Deadline: June 2, 2022

Visit our website at www.sayeradvisors.com for more information

Sayer in the News...

Calgary Herald

Varcoe: As Revenues Surge, Canadian Producers can 'Choose More Things Off the Menu' - Including Acquisitions

Chris Varcoe
Published March 29, 2022

'There isn't going to be one single strategy for what companies do with their cash flow these days'

Like a customer sitting down at a restaurant, Canadian petroleum producers are faced with several options as energy prices continue to rise and revenues climb.

Vermilion Energy announced Monday it has acquired junior producer Leucrotta Exploration for $477 million in cash, its second major acquisition within four months, giving it an entry into the Montney formation.

Many producers have spent the past year focused on paring down debt and returning money to investors through increased dividends and share buybacks.

However, with oil and natural gas prices continuing to climb this year, companies have more alternatives ahead and can pursue several paths at once.

"There isn't going to be one single strategy for what companies do with their cash flow these days," said Michael Tims, vice-chair of Matco Investments.

"Because commodity prices are stronger than what people originally envisioned and the cash flows are much larger, they can — to a degree — choose more things off the menu.

"They don't have to just solely increase the immediate returns to shareholders. They can also, if they want, spend more on existing assets and they can look at acquisitions."

Since the start of the year, oil prices have risen by 40 per cent. Oil closed Monday just below US$106 a barrel for West Texas Intermediate crude, while U.S. benchmark gas prices remain high, closing at US$5.54 per million British thermal units.

The Canadian industry is expected to see record revenues of $225 billion and after-tax cash flow of $143 billion, according to ARC Energy Research Institute.

Vermilion, which operates in both Europe and Western Canada, has largely prioritized strengthening its balance sheet since oil prices crashed in early 2020 and its net debt topped $2 billion.

In November, it announced a $556-million deal to acquire a bigger stake in the Corrib natural gas project, located off the coast of Ireland. It has now agreed to pay Leucrotta investors $1.73 per share, plus they will receive a share in a new junior energy company.

Leucrotta produces about 4,400 barrels of oil equivalent (boe) per day in the Montney region of Alberta and British Columbia. Vermilion expects to increase output from the properties to about 13,000 boe per day next year.

The Calgary-based company said it would increase its exploration and development budget for the year to $500 million, as it invests $75 million on its new assets.

However, president Dion Hatcher said Vermilion is still going to cut its debt levels down to $1.2 billion in the second half of the year, and will reduce net debt below $1 billion by the end of 2022, three years ahead of its initial schedule.

"As we achieve these debt targets, we will evaluate options to increase (the) return of capital, which could include an increase to the base dividend, share repurchases, further debt reduction, or special dividends," he told analysts during a conference call.

Leucrotta CEO Rob Zakresky said the transaction will see Vermilion acquire part of the junior producer's Montney lands, including property that's developed and has energy infrastructure in place.

A new junior company, led by Zakresky, will be spun out and develop properties in the Two Rivers area of northeastern British Columbia, with Vermilion acquiring about 12.5 per cent of the new corporation for about $14 million.

"It just made sense. (Vermilion) is a large company and better capitalized and can draw the value forward on a piece of it," Zakresky said in an interview. "We are going to go back out and try to build back value into the piece we have left for our shareholders."

In a note, analyst Travis Wood of the National Bank of Canada said he was a bit surprised by the "frothy purchase price," but noted the core asset Vermilion bought is high quality. Shares in Vermilion fell $2 Monday to close at $27.20, while Leucrott's stock jumped 65 cents to close at $1.95.

The Montney is one of the most prolific oil and gas areas in the country. Wells in the region have the ability to pay out quickly, particularly as commodity prices rise.

And higher cash flow levels open up more choices for companies.

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Sayer in the...

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Rafi Tahmazian, a senior portfolio manager at Canoe Financial, which owns stock in Vermilion, said he wants to see petroleum producers stay focused on returning money to investors.

However, he isn't against Canadian companies spending more money on capital budgets or on mergers and acquisitions (M&A), as long as they can provide a strong rationale for such a strategy, such as consolidating assets in a core area to drive down costs.

"I want bigger, stronger businesses in Canada," he said. "I think the market is ready for these companies to do it, but not all ships are going to rise."

So far this year, oilpatch deal-making has been relatively slow to lift off.

Canadian producers have announced about $750 million in mergers and acquisitions this year, said Sayer Energy Advisors president Tom Pavic.

During the same period last year, M&A activity hit $7.4 billion, dominated by the $5.1-billion purchase of Seven Generations Energy by ARC Resources.

Pavic anticipates oilpatch acquisitions will pick up this year, noting several large packages of properties are already on the block, including Imperial Oil and ExxonMobil Canada marketing their joint ownership in XTOEnergy Canada — with assets in the Montney and Duvernay— and Enerplus Corp. looking to sell all of its Canadian oil and gas properties.

With producers in a stronger financial position today, two types of companies are emerging in the sector: those playing offence and those on defence, said analyst Jeremy McCrea with Raymond James.

Both can be winning strategies, but companies positioning themselves into the best plays should come out ahead within five to 10 years.

"Companies are still trying to figure out what is the best use of their capital," McCrea added.

"You can do more things. You get an appetizer now and get a dessert."

Sayer Announces VP Appointment

Sayer Energy Advisors announces the appointment of Ben Rye, P. Geo., to Vice-President effective April 1, 2022.

"Ben joined Sayer in 2012 and has spent the last three years as Manager, Geology & Business Development, with increasing responsibilities, playing an instrumental role in expanding the corporate advisory focus of the company," said Tom Pavic, President of Sayer.

Since 1987, Sayer has been providing a range of corporate advisory and research services relating to the energy sector for companies, governments and financial institutions across Canada and internationally.

Recent Transactions Completed by Sayer Energy Advisors

This announcement appears as a matter of record only.

TSE

has sold its interests in a number of ISO Containers

The undersigned acted as financial advisor to Top Speed for this transaction.

January 2022

SAYER ENERGY ADVISORS

This announcement appears as a matter of record only.

CHAIR RESOURCES INC.

has sold its interests in the Verger area of Alberta

The undersigned acted as financial advisor to Chair for this transaction.

February 2022

SAYER ENERGY ADVISORS

This announcement appears as a matter of record only.

Cor4 Oil Corp.

has sold certain of its interests in southern Alberta
to

Tallahassee EXPLORATION INC.

The undersigned acted as financial advisor to Cor4 for this transaction.

February 2022

SAYER ENERGY ADVISORS

This announcement appears as a matter of record only.

ASPENLEAF ENERGY LIMITED

has sold its interests in the Puskwa area of Alberta
to

BIGHORN Energy

The undersigned acted as financial advisor to Aspenleaf for this transaction.

March 2022

SAYER ENERGY ADVISORS

This announcement appears as a matter of record only.

Avalon Energy Ltd.

has sold all of its oil & natural gas interests
to

TENTH AVENUE PETROLEUM CORP.

for

$2.5 million

The undersigned acted as financial advisor to Avalon for this transaction.

April 2022

SAYER ENERGY ADVISORS

This announcement appears as a matter of record only.

BASERADO RESOURCES INC.

has sold its interests in the
Niton, Pembina and Wainwright areas of Alberta

The undersigned acted as financial advisor to Baserado for this transaction.

April 2022

SAYER ENERGY ADVISORS

This announcement appears as a matter of record only.

Burgess Creek Exploration INC

has sold its interests
in the Rosebank area of Saskatchewan

The undersigned acted as financial advisor to Burgess Creek for this transaction.

April 2022

SAYER ENERGY ADVISORS

This announcement appears as a matter of record only.

Certain oil and natural gas interests held by

SanLing ENERGY LTD.

have been sold through its receiver

pwc

The undersigned acted as financial advisor to PwC for these transactions.

April 2022

SAYER ENERGY ADVISORS