



Resources Stocks Down Under

🗉 *Don't be so humble - you are not that great.* 🗉

- Golda Meir (1898-1978), Former Israeli Prime Minister

CALIMA ENERGY

Taking giant steps without reaping the rewards

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Stocks Down Under rating: ★★☆☆

ASX: CE1
Market cap: A\$82.6M

52-week range: A\$0.097 / A\$0.26
Share price: A\$0.13

It has been 15 months since we last looked at Calima Energy (ASX: CE1). Calima was just another small cap explorer until an M&A deal helped it take the leap from explorer to producer. Calima's share price is down 37% in 2022, largely tracking the oil price, which peaked in February as Russia invaded Ukraine, followed by a gradual decline in the second half of the year. But what has this company been up to all this time? And what is to come in 2023?

Share price chart



Source: Tradingview

Jumping from explorer to producer

Calima has three projects in Canada: Throsby and Brooks in the province of Alberta, and Montney in British Columbia. It owned Montney prior to 2021 and was trying to bring it into production. Throsby and Brooks were already producing gas, but lower than expected oil-prices and a high debt burden caused then-owner Blackspur Oil Corp to bite the dust and sell itself. Brooks and Throsby were acquired with a combined 2P (proven and probable) resource of 22m barrels with an oil-gas split of 71-29%. And these assets made a significant difference to Calima.

Calima closed FY20 (which for this company is the calendar year) with just \$356k in oil and natural gas sales. In FY21, revenue rose to \$47.7m and it made \$21.6bn in EBITDA, but it made a \$32m net loss due to an impairment. There's only one analyst covering Calima who expects \$135m in revenue (up 187%), \$69.4m in EBITDA (up 221%) and \$0.07 EPS in FY22. These estimates provide valuation multiples of just 1x EV/EBITDA and 0.84x P/E. If Calima can achieve these figures, this company is a no-brainer at this price. But are things on track?

Is it on track?

Based on its 1HY22 results, the company is on track to reach these figures. It made \$68m in revenue, \$40.4m in EBITDA and a net profit of \$13.2m. However, these figures excluded hedge losses of \$13.5m. Including

them, the company was barely break even on a free cash flow basis. It also projected a mere \$5.3m impact from hedge losses for 2HY, a figure that will likely prove to be an underestimation. The saving grace is that the company's hedging positions unwind at the end of the calendar year, so this will not be a medium to long term issue for the company.

From an operational perspective, it produced and sold 705,461 barrels of oil equivalent (boe), a figure up 18% over 2HY21. The production was split 60-40 between Brooks and Throsby. It is anticipating the sale of 776,087 boe, thereby projecting an annual total of 1.48m all up, or 4,059 boe per day.

Montney still to come

What about Montney? Calima Energy is still looking to bring it into production, most likely partnering with another major company. The company claims there has been interest in some kind of deal, i.e. a farm-in, joint venture or an outright sale. Once in production, which is anticipated to occur 2025, it is hoping to supply LNG Canada's C\$40bn LNG facility.

However, it told its shareholders that it 'sees no need to enter into transactions on less than optimum terms', given Europe's natural gas crisis and the potential opportunity to help with it. Calima estimates that there is 213.3 MMCFG (Metric Million Cubic Feet of Gas) and 10.1m barrels of light oil and natural gas liquids of Contingent Resources. All it is waiting for is the funding. We can appreciate the company wanting a good deal for shareholders. Yet we think they can't be too picky, but it seems it is acting that way right now.

Can Calima recover?

Let's look at Calima's most recent quarterly update (for Q3). On the positive side, it paid a \$2.5m capital return to shareholders and its hedge losses were down 66% - meaning its free cash flow was up 58% from \$3.7m to \$5.8m - and production was 10% higher quarter-on-quarter to 382,910boe. However, oil prices meant that revenues fell 19% from \$37m to \$30.1m, earnings (pre-amortisation) fell 11% from \$14.1m to \$12.5m. It has also slightly reduced its anticipated sales for the full year. Oil sales were cut from 972k to 937k and natural gas from 2.96mcf (million cubic feet) to 2.89mcf. It also reduced its estimated realised oil price to A\$97.72 a barrel.

Although shareholders have not sold off the company further in the last few months, it remains 34% lower than 12 months ago. We do not rule out the prospect of the company recovering, but we don't think this can happen just by production figures. We think there are only two catalysts for the company: Increasing oil and gas prices, and a deal with Montney. Neither of these are impossible, but we cannot see either happening in the near term - albeit the latter only because the company has been overly picky on a deal when it shouldn't have been. If it does secure a deal, we think it is unlikely to be as lucrative as it would've been some months ago. Yet by 2025, the difference may not matter much if it can supply LNG Canada.

Ultimately, we think that even if it takes some time to realise the upside, it will come eventually. We think the blow from falling oil prices will not be too substantial if recent updates are anything to go by. We acknowledge risk averse investors may want to wait until Calima secures a partnership for Montney, or to confirm that it can meet consensus estimates. In our view, it is inevitable that a deal will come. Combined with CE1's current valuation, we are giving it four stars as a result.



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