

Action Note

Equity Research

May 6, 2020

Energy Producers - Junior & Intermediate

TORC Oil & Gas Ltd.

(TOG-T) C\$1.21

Q1/20 Beat; Divi Suspended, Production Shut-ins, Guidance Withdrawn

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Event

Last night, TORC announced its Q1/20 financial and operating results, the suspension of the dividend, and updated the 2020 guidance (including the suspension of production guidance).

Impact: MIXED

Q1/20 production of 28.5 mBOE/d was in line with TD (28.4 mBOE/d) and consensus (28.3 mBOE/d); CFPS of \$0.21 was ahead of TD (\$0.19) and consensus (\$0.20). The outperformance relative to our estimates was largely due to higher realized pricing and hedging gains.

2020 capex guidance is reduced to \$75mm, with \$65mm having been already spent in Q1/20 due to the uncertainty associated with current supply/demand fundamentals. TORC is not the first to materially reduce spending guidance in this environment, and we are confident that it will not be the last. The current commodity price outlook does not justify new development in the near term, and even challenges the economics of maintaining existing production. TORC also announced the shutting-in of 4.0 mBOE/d of production at this point, or 14% of corporate production.

TORC is in a position of having assembled an extremely attractive decline profile in the low-20% range, and we estimate that Q4/20E production could average ~24 mBOE/d assuming current shut-ins are layered back in during H2/20. This sets the company up for an extremely attractive maintenance capital level of ~\$110mm in 2021, which under our current US\$40/bbl WTI assumption, will equate to a 79% payout and generate \$30mm in free cash flow.

The monthly dividend was significantly reduced on March 16 to \$0.06/share annually, and is now being completely suspended, a prudent move, in our view. The current dividend equated to a nominal annualized cash outflow of \$13mm, which is not significant, but supports management's focus on preserving the balance sheet through the current uncertainty. We believe that this sets the company up to revisit this dividend policy once things improve.

TD Investment Conclusion

In our view, TORC has the asset base, the balance sheet, and the management discipline to successfully navigate the challenges currently facing the oil and gas complex. The dividend and capex cuts were prudent and necessary. Our estimates improve on a more constructive outlook for 2021, driving an increase in our target price to \$1.90 (from \$1.80).



Company Profile

TORC Oil & Gas Ltd. is engaged in the acquisition, development, and production of oil and natural gas in the Western Canadian Sedimentary Basin. The company primarily focuses on Cardium development opportunities in WC AB, a low-decline Mississippian asset in SE SK, and the Torquay light oil play, also in SE SK.

| | |
|----------------------------------|-----------------------------------|
| Recommendation: | BUY |
| Risk: | HIGH |
| 12-Month Target Price: | C\$1.90↑ Prior: C\$1.80 |
| 12-Month Dividend (Est.): | C\$0.00 |
| 12-Month Total Return: | 57.0% |

Market Data (C\$)

| | |
|-------------------------|-----------------|
| Current Price | C\$1.21 |
| 52-Week Range | \$0.41 - \$4.96 |
| Mkt Cap (f.d.) (\$mm) | \$269.0 |
| Mkt Cap (basic) (\$mm) | \$269.0 |
| Float Cap (\$mm) | \$186.6 |
| Current Dividend | \$0.00 |
| Dividend Yield | 0.0% |
| Avg. Daily Trading Vol. | 3,833,556 |

Financial Data (C\$)

| | |
|-------------------------|----------|
| Fiscal Y-E | December |
| Shares O/S (f.d)(mm) | 222.3 |
| Shares O/S (basic) (mm) | 222.3 |
| Float Shares (mm) | 154.2 |
| Net Debt (\$mm) | \$403.7 |
| Net Debt/Total Cap | 42.8% |
| NAVPS | \$1.94 |

Estimates (C\$)

| Year | 2018A | 2019A | 2020E | 2021E |
|-------------------|-------|-------|-------|-------|
| CFPS (f.d) | 1.36 | 1.37 | 0.20 | 0.63 |
| CFPS (f.d) (old) | - | - | 0.23 | 0.61 |
| Oil & NGLs (mb/d) | 22.3 | 25.1 | 22.1 | 21.7 |
| Gas (MMcfd) | 18.2 | 19.6 | 17.1 | 16.6 |
| MBOE/d | 25.3 | 28.3 | 25.0 | 24.5 |

CFPS (f.d) Quarterly Estimates (C\$)

| Year | 2018A | 2019A | 2020E | 2021E |
|------|-------|-------|--------|-------|
| Q1 | 0.32 | 0.34 | 0.21 | 0.13 |
| Q2 | 0.37 | 0.36 | (0.07) | 0.15 |
| Q3 | 0.44 | 0.33 | (0.01) | 0.17 |
| Q4 | 0.23 | 0.33 | 0.08 | 0.18 |

Valuations

| Year | 2018A | 2019A | 2020E | 2021E |
|----------|-------|-------|-------|-------|
| EV/DACF | 4.6x | 3.5x | 11.1x | 4.1x |
| P/NAV MG | - | 62.5% | - | - |

Supplemental Data

| Year | 2018A | 2019A | 2020E | 2021E |
|-------------------|-------|-------|-------|-------|
| WTI (US\$/bbl) | 64.83 | 57.03 | 30.00 | 40.00 |
| AECO (C\$/mcf) | 1.53 | 1.79 | 1.95 | 2.60 |
| FX (US\$/C\$) | 0.77 | 0.75 | 0.72 | 0.73 |
| H. Hub (US\$/mcf) | 3.13 | 2.56 | 2.15 | 2.70 |

All figures in C\$, unless otherwise specified

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Exhibit 1. Q1/20 Summary

| Production | Q1/20A | Q4/19E | Variance | Netbacks (\$/BOE) | Q1/20A | Q4/19E | Variance |
|--------------------------|---------------|---------------|-------------|--------------------------|--------------|--------------|-------------|
| Oil (bbl/d) | 23,672 | 23,382 | 1.2% | Gross Revenue | 41.37 | 40.64 | 1.8% |
| NGLs (bbl/d) | 1,582 | 1,648 | -4.0% | Hedging Gains (Losses) | 0.74 | 0.00 | - |
| Natural Gas (mcf/d) | 19,568 | 20,480 | -4.5% | Royalties | (6.83) | (7.11) | -4.0% |
| Corporate (BOE/d) | 28,515 | 28,444 | 0.3% | Transportation Costs | (1.10) | (1.25) | -11.6% |
| % Liquids | 89% | 88% | | Operating Costs | (13.44) | (13.00) | 3.4% |
| Financial | | | | Operating Netback | 20.74 | 19.28 | 7.6% |
| Cash Flow (\$mm) | 46.6 | 42.9 | 8.5% | General & Administrative | (1.29) | (1.39) | -7.4% |
| CFPS (fd) | 0.21 | 0.19 | 8.3% | Interest Expense | (1.28) | (1.30) | -1.2% |
| E&D Capex (\$mm) | 64.7 | 65.0 | -0.5% | Cash Taxes/Other | (0.22) | 0.00 | - |
| Total Capex (\$mm) | 68.0 | 65.0 | 4.5% | Cash Netback | 17.96 | 16.59 | 8.2% |
| Net Debt (\$mm) | 382.7 | 387.2 | -1.2% | | | | |

Source: Company reports, TD Securities Inc. estimates.

Outlook

We have updated our estimates to incorporate the updated capex guidance and the suspension of the dividend. We have also made additional minor adjustments to our forecast.

Exhibit 2. Estimate Revisions

| | Q2/20E | | | 2020E | | | 2021E | | |
|--------------------------|---------------|---------------|----------------|---------------|---------------|---------------|---------------|---------------|--------------|
| Production | Revised | Previous | Variance | Revised | Previous | Variance | Revised | Previous | Variance |
| Oil (bbl/d) | 19,470 | 14,993 | 29.9% | 20,745 | 16,479 | 25.9% | 20,395 | 20,431 | -0.2% |
| NGLs (bbl/d) | 1,302 | 1,056 | 23.3% | 1,385 | 1,159 | 19.4% | 1,341 | 1,387 | -3.3% |
| Natural Gas (mcf/d) | 16,103 | 13,118 | 22.8% | 17,127 | 14,406 | 18.9% | 16,591 | 17,236 | -3.7% |
| Corporate (BOE/d) | 23,456 | 18,235 | 28.6% | 24,984 | 20,040 | 24.7% | 24,501 | 24,691 | -0.8% |
| % Liquids | 89% | 88% | | 89% | 88% | | 89% | 88% | |
| Financial | | | | | | | | | |
| Cash Flow (\$mm) | (16.1) | (6.3) | -257.5% | 45.5 | 49.9 | -8.8% | 139.8 | 135.7 | 3.0% |
| DACF (\$mm) | (12.5) | (2.7) | -469.6% | 59.8 | 64.2 | -6.8% | 153.9 | 150.3 | 2.4% |
| CFPS (fd) | (0.07) | (0.03) | -255.0% | 0.20 | 0.23 | -9.2% | 0.63 | 0.61 | 2.7% |
| E&D Capex (\$mm) | 3.0 | 3.0 | 0.0% | 74.7 | 76.0 | -1.7% | 110.0 | 110.0 | 0.0% |
| Total Capex (\$mm) | 3.0 | 3.0 | 0.0% | 78.0 | 76.0 | 2.6% | 110.0 | 110.0 | 0.0% |
| Net Debt (\$mm) | 403.7 | 395.1 | 2.2% | 394.9 | 396.6 | -0.4% | 365.1 | 384.1 | -4.9% |
| % Undrawn Credit | 34% | 29% | | 35% | 29% | | 41% | 31% | |
| Netbacks (\$/BOE) | | | | | | | | | |
| Gross Revenue | 6.57 | 6.32 | 4.0% | 25.10 | 25.18 | -0.3% | 39.82 | 39.68 | 0.4% |
| Hedging Gains (Losses) | 4.51 | 5.33 | -15.2% | 1.43 | 1.44 | -0.3% | 0.00 | 0.00 | - |
| Royalties | (1.05) | (1.11) | -5.0% | (4.08) | (4.41) | -7.5% | (6.77) | (7.14) | -5.2% |
| Transportation Costs | (1.10) | (0.88) | 25.7% | (1.10) | (1.01) | 9.3% | (1.25) | (1.25) | 0.0% |
| Operating Costs | (13.25) | (9.10) | 45.6% | (13.30) | (10.48) | 27.0% | (13.00) | (13.00) | 0.0% |
| Operating Netback | (4.32) | 0.56 | nmf | 8.05 | 10.73 | -24.9% | 18.80 | 18.28 | 2.8% |
| General & Administrative | (1.29) | (2.17) | -40.6% | (1.27) | (1.98) | -35.9% | (1.34) | (1.61) | -16.6% |
| Interest Expense | (1.69) | (2.17) | -22.1% | (1.57) | (1.94) | -19.5% | (1.58) | (1.61) | -2.1% |
| Cash Taxes/Other | (0.26) | 0.00 | - | (0.24) | (0.00) | - | (0.25) | 0.00 | - |
| Cash Netback | (7.55) | (3.77) | -200.2% | 4.98 | 6.80 | -26.8% | 15.63 | 15.06 | 3.8% |

Source: Company reports, TD Securities Inc. estimates.

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Valuation

TORC is currently trading at a P/NAV_{MG} of 63% and an EV/2020E DACF multiple of 11.1x; these compare with averages of 99% and 5.1x, respectively, for the >60% oil-weighted production (2020E) peer group under coverage. In our view, investors should be more focused on the 2021E metrics, where TORC is currently trading at a discount to the peer group average. We believe that the company deserves to trade at a premium due to its relative asset quality and FCF potential.

Exhibit 3. Relative Valuation

| | P/NAV _{BD} | P/NAV _{MG} ^{***} | EV/DACF* | | EV/BOEPD | P/CF | D/CF | Payout** | % Gas |
|-----------------------------|---------------------|------------------------------------|--------------|-------------|-----------------|-------------|--------------|-------------|------------|
| | | | (2020E) | (2021E) | (2020E) | (2020E) | (2020E) | (2020E) | (2020E) |
| TOG | 73% | 63% | 11.1x | 4.1x | \$26,573 | 5.9x | 8.7x | 202% | 11% |
| BNE | 310% | 310% | 19.6x | 7.9x | \$35,854 | 15.1x | 117.2x | 964% | 33% |
| BTE | - | 15% | 8.6x | 4.8x | \$27,183 | 2.3x | 12.9x | 167% | 19% |
| CPG | 102% | 102% | 6.0x | 5.9x | \$30,833 | 2.1x | 5.1x | 120% | 10% |
| SGY | 93% | 89% | 8.9x | 6.0x | \$28,159 | 3.5x | 15.2x | 190% | 16% |
| TOG | 73% | 63% | 11.1x | 4.1x | \$26,573 | 5.9x | 8.7x | 202% | 11% |
| TVE | 47% | 46% | 3.4x | 2.5x | \$16,651 | 1.8x | 2.0x | 103% | 37% |
| VII | 67% | 65% | 4.0x | 3.3x | \$16,586 | 1.4x | 3.6x | 105% | 42% |
| WCP | 97% | 97% | 6.3x | 4.9x | \$30,003 | 2.8x | 4.7x | 104% | 15% |
| Average Oil-Weighted | 111% | 99% | 5.1x | 5.5x | \$26,309 | 3.5x | 16.2x | 198% | 25% |

*EV based on forecast year-end net debt and shares outstanding, **Payout = (Capex+Dividend-DRIP)/CF.

***Our modified growth NAV (NAV_{MG}), assumes free cash flow (i.e. after 2P FDC, interest, G&A and dividends) is reinvested in company specific internal development opportunities for up to a five year period.

Source: Company reports, TD Securities Inc. estimates.

Justification of Target Price

Our \$1.90 target price is based on a 5.0x 2021E EV/DACF multiple (50% weighting) and 1.0x our NAV_{MG} of \$1.94/share (50% weighting).

Key Risks to Target Price

Key risks associated with our target price include business risks of the company and industry, including the loss of key employees; drilling success; volatile commodity prices; operating costs; capital cost overruns; product supply and demand; financing/access to capital; government regulations; legislation; royalties; taxes; exchange rates; interest rates; and environment and weather concerns.

In addition to industry risks, the key near-term risks specific to TORC include 1) production base highly levered to Canadian light oil pricing; 2) exploration risk in southern Alberta; 3) mixed operatorship on southeast Saskatchewan assets; and 4) there is no guarantee that the current bank credit facilities will be renewed at current levels or that undrawn credit capacity will be available to repay other creditors in the future.

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Exhibit 4. Summary

| Company Overview | | | | |
|------------------------------|--------|--------|--|--|
| Market Capitalization (\$mm) | \$269 | | | |
| Net Debt (\$mm) | \$404 | | | |
| Enterprise Value (\$mm) | \$673 | | | |
| Current Price | \$1.21 | | | |
| 52 Week Low/High | \$0.41 | \$4.96 | | |
| Current Yield | 0.0% | | | |

| Production | 2018A | 2019A | 2020E | 2021E |
|---------------------------------|---------------|---------------|---------------|---------------|
| Crude Oil (bbl/d) | 20,943 | 23,507 | 20,745 | 20,395 |
| NGLs (bbl/d) | 1,365 | 1,556 | 1,385 | 1,341 |
| Total Liquids (bbl/d) | 22,308 | 25,062 | 22,130 | 21,736 |
| Natural Gas (mcf/d) | 18,183 | 19,588 | 17,127 | 16,591 |
| Total Production (BOE/d) | 25,338 | 28,327 | 24,984 | 24,501 |
| % Gas | 12% | 12% | 11% | 11% |
| Production Hedged (%) | - | - | 7% | - |

| Growth | 2018A | 2019A | 2020E | 2021E |
|---------------------------------|-------|-------|-------|-------|
| Y/Y Production Growth | 21% | 12% | -12% | -2% |
| Y/Y Production Per Share Growth | 11% | 5% | -13% | -2% |
| Y/Y DAPPS Growth | 5% | -2% | -41% | -15% |

| Pricing Assumptions | 2018A | 2019A | 2020E | 2021E |
|--------------------------|---------|---------|---------|---------|
| WTI (US\$/bbl) | \$64.83 | \$57.03 | \$30.00 | \$40.00 |
| Edmonton Par (C\$/bbl) | \$69.14 | \$69.06 | \$29.75 | \$48.00 |
| WCS (C\$/bbl) | \$49.90 | \$58.12 | \$19.50 | \$34.25 |
| Nymex (US\$/mcf) | \$3.13 | \$2.56 | \$2.15 | \$2.70 |
| AECO (C\$/mcf) | \$1.53 | \$1.79 | \$1.95 | \$2.60 |
| Exchange Rate (US\$/C\$) | \$0.77 | \$0.75 | \$0.72 | \$0.73 |

| Corporate Netback (\$/BOE) | 2018A | 2019A | 2020E | 2021E |
|----------------------------|----------------|----------------|---------------|----------------|
| Revenue | \$58.50 | \$56.22 | \$25.10 | \$39.82 |
| Hedging | (\$0.35) | \$0.00 | \$1.43 | \$0.00 |
| Royalties | (\$10.27) | (\$9.70) | (\$4.08) | (\$6.77) |
| Transportation | (\$1.30) | (\$1.30) | (\$1.10) | (\$1.25) |
| Operating | (\$12.65) | (\$13.04) | (\$13.30) | (\$13.00) |
| Operating Netback | \$33.93 | \$32.18 | \$8.05 | \$18.80 |
| G&A | (\$1.33) | (\$1.26) | (\$1.27) | (\$1.34) |
| Interest Expense | (\$1.37) | (\$1.41) | (\$1.57) | (\$1.58) |
| Cash Taxes and Other | (\$0.59) | (\$0.18) | (\$0.24) | (\$0.25) |
| Cash Flow Netback | \$30.64 | \$29.32 | \$4.98 | \$15.63 |

| Per Share Metrics | 2018A | 2019A | 2020E | 2021E |
|---------------------------------|--------|----------|----------|----------|
| WA Outstanding Shares (diluted) | 208.5 | 222.1 | 222.7 | 222.3 |
| CFPS (diluted) | \$1.36 | \$1.37 | \$0.20 | \$0.63 |
| EPS (diluted) | \$1.67 | (\$0.17) | (\$4.50) | (\$0.28) |
| 2P NAV | | \$1.67 | | |
| Modified Growth NAV | | \$1.94 | | |

| Key Valuation Ratios | 2018A | 2019A | 2020E | 2021E |
|-----------------------------|---------|---------|--------|--------|
| P/CF (x) | 0.9x | 0.9x | 5.9x | 1.9x |
| EV/DACF (x) | 4.6x | 3.5x | 11.1x | 4.1x |
| EV/Production (\$000/BOE/d) | \$53.4 | \$39.2 | \$26.6 | \$25.9 |
| EV/1P Reserves (\$/BOE) | \$14.98 | \$12.29 | \$7.35 | \$7.02 |
| EV/2P Reserves (\$/BOE) | \$9.76 | \$8.01 | \$4.79 | \$4.58 |
| P/NAV (2P) | | 73% | | |
| P/NAV (Modified Growth) | | 63% | | |
| ROCE | 1% | -2% | nmf | -10% |

| Leverage | 2018A | 2019A | 2020E | 2021E |
|-------------------------------|-------|-------|-------|-------|
| Bank Debt (\$mm) | \$335 | \$304 | \$323 | \$293 |
| Term Debt (\$mm) | \$0 | \$0 | \$0 | \$0 |
| Net Debt (\$mm) | \$405 | \$343 | \$395 | \$365 |
| Net Debt-CF (x) | 1.4x | 1.1x | 8.7x | 2.6x |
| Credit Facility (\$mm) | \$500 | \$500 | \$500 | \$500 |
| % Drawn | 67% | 61% | 65% | 59% |
| Dividend PoR (%) (Pre-DRIP) | 12% | 14% | 38% | 0% |
| Dividend PoR (%) (Post-DRIP) | 6% | 10% | 38% | 0% |
| Corporate PoR (%) (Pre-DRIP) | 78% | 74% | 202% | 79% |
| Corporate PoR (%) (Post-DRIP) | 72% | 69% | 202% | 79% |

| Cash Flow Summary (\$mm) | 2018A | 2019A | 2020E | 2021E |
|-----------------------------------|----------------|----------------|---------------|----------------|
| Funds Flow from Operations | \$283 | \$303 | \$46 | \$140 |
| Debt-Adjusted Cash Flow | \$296 | \$318 | \$60 | \$154 |
| Investing Activities | | | | |
| Exploration and Development | (\$185) | (\$180) | (\$75) | (\$110) |
| Acquisitions/Divestitures | (\$292) | (\$8) | (\$3) | \$0 |
| Total Capital Expenditures | (\$477) | (\$188) | (\$78) | (\$110) |
| Financing Activities | | | | |
| Net Change in Debt | \$93 | (\$31) | \$19 | (\$30) |
| Dividends | (\$35) | (\$43) | (\$17) | \$0 |
| DRIP | \$17 | \$14 | \$0 | \$0 |
| Other / Share Issue Proceeds | (\$17) | (\$26) | (\$0) | \$0 |
| EBITDA | \$257 | \$302 | \$57 | \$146 |

| CFPS (diluted) | 2018A | 2019A | 2020E | 2021E |
|----------------|--------|--------|----------|--------|
| Q1 | \$0.32 | \$0.34 | \$0.21 | \$0.13 |
| Q2 | \$0.37 | \$0.36 | (\$0.07) | \$0.15 |
| Q3 | \$0.44 | \$0.33 | (\$0.01) | \$0.17 |
| Q4 | \$0.23 | \$0.33 | \$0.08 | \$0.18 |
| Annual | \$1.36 | \$1.37 | \$0.20 | \$0.63 |

| Quarterly Production (BOE/d) | 2018A | 2019A | 2020E | 2021E |
|------------------------------|--------|--------|--------|--------|
| Q1 | 22,894 | 28,267 | 28,515 | 24,987 |
| Q2 | 23,059 | 28,326 | 23,456 | 24,137 |
| Q3 | 27,160 | 28,337 | 23,796 | 24,345 |
| Q4 | 28,163 | 28,378 | 24,191 | 24,542 |
| Annual | 25,338 | 28,327 | 24,984 | 24,501 |

Source: Company reports, TD Securities Inc. estimates.

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TD Securities Equity Research Disclosures

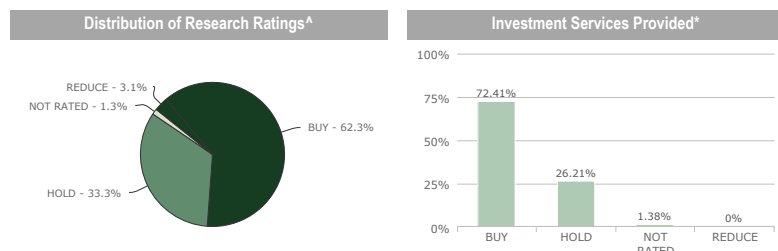
| Company | Ticker | Disclosures |
|---------------------|--------|-------------|
| TORC Oil & Gas Ltd. | TOG-T | 2, 4 |

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Current as of: May 6, 2020

[^] Percentage of subject companies under each rating category: BUY (covering ACTION LIST BUY, BUY and SPECULATIVE BUY ratings), HOLD, and REDUCE (covering TENDER and REDUCE ratings) and NOT RATED (covering UNDER REVIEW, SUSPENDED, and NOT RATED).

^{*} Percentage of subject companies within each of the four categories (BUY, HOLD, REDUCE, and NOT RATED) for which TD Securities Inc. has provided investment banking services within the last 12 months.

Definition of Research Ratings

ACTION LIST BUY: The stock's total return is expected to exceed a minimum of 15% (with higher thresholds for less liquid, more risky securities) over the next 12 months and it is a top pick in the Analyst's sector.

BUY: The stock's total return is expected to exceed a minimum of 10% (with higher thresholds for less liquid, more risky securities) over the next 12 months.

SPECULATIVE BUY: The stock's total return is expected to exceed a minimum of 30% over the next 12 months (with higher thresholds for less liquid securities); however, there is material event risk associated with the investment that could result in a significant loss.

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HOLD: The stock's total return is expected to be between 0% and 10%, (with higher thresholds for less liquid, more risky securities) over the next 12 months.

TENDER: Investors are advised to tender their shares to a specific offer for the company's securities or to support a proposed combination reflecting our view that a superior offer is not forthcoming.

REDUCE: The stock's total return is expected to be negative over the next 12 months.

SUSPENDED: Due to evolving circumstances, we can no longer generate what we consider a defensible target price and rating at the current time.

UNDER REVIEW: Our rating is under review pending additional information and/or analysis. The prior rating should not be relied on.

NOT RATED: We do not currently produce a recommendation and a target price on this security.

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Equity Research

May 6, 2020

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