

Action Note

Equity Research

August 6, 2020

Energy Producers - Junior & Intermediate

Kelt Exploration Ltd.

(KEL-T) C\$1.73

Q2/20 Miss; Focus Remains on Well-Capitalized Pro-forma Entity

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Event

Kelt announces Q2/20 financial and operating results.

Impact: NEUTRAL

Q2/20 production of 30.4 mBOE/d was in line with TD (30.3 mBOE/d) and consensus (29.5 mBOE/d); CFPS of \$0.06 was below TD (\$0.09) and consensus (0.08). Operating costs of \$9.62/BOE were notably higher than our forecast of \$8.50/BOE.

We believe investor focus will be on the pro-forma Kelt once the Inga Montney sale to ConocoPhillips closes late August. Kelt will have no debt, 15.9 BOE/d of pro-forma production (38% liquids), and significant upside in the 374,528 net acreage in the Montney across Alberta and BC. Kelt also plans to develop the growing Charlie Lake light oil play, where it has exposure to 74,719 net acres.

11 Montney wells behind pipe provide ability to add 7.5-8.5 mBOE/d of production to offset declines and potentially show some growth into 2021. Kelt has 5 wells at Wembley (four drilled and completed and one DUC) and another 6 wells at Oak of which 2 are drilled and completed but the remaining are DUCs. In our view, the Wembley/Pipestone Montney could be one of the fastest growing Montney plays in the WCSB, with the potential for significant oil and condensate-weighted economics in a return to a more normalized commodity price environment, see Montney Rocks Centre Stage at Wembley (and Pipestone) for details ([link](#)).

TD Investment Conclusion

Although production was in line and CFPS was a miss, we do not view the quarter as being material given the sale of the Inga Montney to ConocoPhillips for \$510 in cash as announced in July. Our thesis continues to be focused on Kelt's track record of acquiring undeveloped land, proving up its resource, and monetizing these assets when appropriate. The sale completely eliminates Kelt's debt, and allows the company to fund its growth initiatives at Wembley (and to a certain extent Oak). We believe investors will continue to be rewarded through Kelt's exploration initiatives through a much better capitalized entity that still has access to a tremendous Montney resource both in BC and Alberta. Our estimates are largely unchanged and our target remains \$2.75; we reiterate our BUY recommendation.

Recommendation:	BUY
Risk:	HIGH
12-Month Target Price:	C\$2.75
12-Month Dividend (Est.):	C\$0.00
12-Month Total Return:	59.0%

Market Data (C\$)

Current Price	C\$1.73
52-Week Range	\$0.67 - \$5.00
Mkt Cap (f.d.) (\$mm)	\$325.1
Mkt Cap (basic) (\$mm)	\$325.1
Float Cap (\$mm)	\$239.8
Current Dividend	\$0.00
Dividend Yield	0.0%
Avg. Daily Trading Vol.	2,323,573

Financial Data (C\$)

Fiscal Y-E	December
Shares O/S (f.d)(mm)	187.9
Shares O/S (basic) (mm)	187.9
Float Shares (mm)	138.6
Net Debt (\$mm)	\$(34.5)
Net Debt/Total Cap	(6.1)%
NAVPS	\$3.26

Estimates (C\$)

Year	2018A	2019A	2020E	2021E
CFPS (f.d)	1.01	0.98	0.26	0.35
CFPS (f.d) (old)	-	-	0.28	-
Oil & NGLs (mb/d)	11.6	13.9	10.4	7.4
Gas (MMcfd)	92.5	96.7	79.7	60.2
MBOE/d	27.0	30.0	23.6	17.5

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

Year	2018A	2019A	2020E	2021E
Q1	0.25	0.27	0.15	0.09
Q2	0.25	0.24	0.06	0.07
Q3	0.25	0.21	0.02	0.08
Q4	0.25	0.25	0.03	0.10

Valuations

Year	2018A	2019A	2020E	2021E
EV/DACF	3.1x	3.8x	5.1x	5.1x
P/NAV MG	-	53.0%	-	-

Supplemental Data

Year	2018A	2019A	2020E	2021E
WTI (US\$/bbl)	64.83	57.03	38.00	41.00
AECO (C\$/mcf)	1.53	1.79	2.00	2.50
FX (US\$/C\$)	0.77	0.75	0.73	0.74
H. Hub (US\$/mcf)	3.13	2.56	2.00	2.65

All figures in C\$, unless otherwise specified



Company Profile

Kelt Exploration Ltd. is a Canadian oil and natural gas exploration, development, and production company with properties concentrated in the Montney area of Alberta and northeast British Columbia.

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Exhibit 1. Q2/20 Summary

Production	Q2/20A	Q1/20E	Variance	Netbacks (\$/BOE)	Q2/20A	Q1/20E	Variance
Oil (bbl/d)	8,824	9,093	-3.0%	Gross Revenue	16.23	16.18	0.3%
NGLs (bbl/d)	5,066	4,969	1.9%	Hedging Gains (Losses)	4.62	5.00	-7.7%
Natural Gas (mcf/d)	98,853	97,440	1.5%	Royalties	(0.84)	(0.65)	29.4%
Corporate (BOE/d)	30,366	30,302	0.2%	Transportation Costs	(3.65)	(3.80)	-3.9%
% Liquids	46%	46%		Operating Costs	(9.62)	(8.50)	13.2%
Financial				Operating Netback	6.74	8.23	-18.2%
Cash Flow (\$mm)	11.7	16.2	-27.6%	General & Administrative	(0.66)	(0.71)	-7.2%
CFPS (fd)	0.06	0.09	-27.6%	Interest Expense	(1.64)	(1.63)	1.1%
E&D Capex (\$mm)	27.8	18.0	54.3%	Cash Taxes/Other	(0.20)	(0.04)	460.8%
Total Capex (\$mm)	27.8	18.0	54.3%	Cash Netback	4.23	5.86	-27.8%
Net Debt (\$mm)	465.5	448.1	3.9%				

Source: Company reports, TD Securities Inc. estimates

Outlook

We have updated our forecast to reflect Q2/20 results and additional minor adjustments to our estimates.

Exhibit 2. Estimate Revisions

Production	Q3/20E			2020E			2021E		
	Revised	Previous	Variance	Revised	Previous	Variance	Revised	Previous	Variance
Oil (bbl/d)	4,034	4,067	-0.8%	6,697	6,789	-1.4%	5,027	5,016	0.2%
NGLs (bbl/d)	2,562	2,577	-0.6%	3,661	3,653	0.2%	2,407	2,446	-1.6%
Natural Gas (mcf/d)	59,592	59,929	-0.6%	79,668	79,707	0.0%	60,173	61,151	-1.6%
Corporate (BOE/d)	16,528	16,633	-0.6%	23,636	23,726	-0.4%	17,463	17,654	-1.1%
% Liquids	40%	40%		44%	44%		43%	42%	
Financial									
Cash Flow (\$mm)	3.0	3.3	-7.4%	48.4	53.0	-8.6%	65.2	65.3	-0.2%
DACF (\$mm)	4.8	4.9	-1.7%	59.3	63.6	-6.8%	65.2	65.3	-0.2%
CFPS (fd)	0.02	0.02	-7.5%	0.26	0.28	-8.7%	0.35	0.35	-0.3%
Capex (\$mm)	15.0	22.5	-33.3%	156.0	156.2	-0.1%	90.0	90.0	0.0%
Total Capex (\$mm)	(495.0)	(487.5)	1.5%	(384.1)	(383.9)	0.1%	90.0	90.0	0.0%
Net Debt (\$mm)	(34.5)	(42.5)	-18.9%	(20.9)	(26.3)	-20.5%	3.9	(1.6)	-341.0%
% Undrawn Credit	100%	100%		100%	100%		100%	100%	
Netbacks (\$/BOE)									
Gross Revenue	20.18	20.19	0.0%	20.49	20.43	0.3%	25.43	25.33	0.4%
Hedging Gains (Losses)	(2.82)	(2.81)	0.6%	1.19	1.31	-8.8%	0.00	0.00	-
Royalties	(0.85)	(0.85)	0.0%	(0.93)	(0.86)	7.2%	(1.14)	(1.14)	0.4%
Transportation Costs	(3.00)	(3.00)	0.0%	(3.37)	(3.41)	-1.3%	(3.00)	(3.00)	0.0%
Operating Costs	(9.00)	(9.00)	0.0%	(9.80)	(9.44)	3.8%	(10.00)	(10.00)	0.0%
Operating Netback	4.51	4.53	-0.6%	7.58	8.02	-5.4%	11.29	11.19	0.9%
General & Administrative	(1.28)	(1.27)	0.6%	(0.88)	(0.89)	-1.4%	(1.00)	(0.99)	1.1%
Interest Expense	(1.17)	(1.06)	10.6%	(1.26)	(1.23)	2.4%	0.00	0.00	-
Cash Taxes/Other	(0.07)	(0.07)	0.6%	0.14	0.20	-26.9%	(0.06)	(0.06)	1.1%
Cash Netback	1.99	2.14	-6.8%	5.59	6.10	-8.3%	10.22	10.13	0.9%

Source: Company reports, TD Securities Inc. estimates

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Valuation

Kelt is currently trading at a P/NAV_{MG} of 53% and an EV/2020E DACF multiple of 5.1x; these compare with averages of 63% and 6.6x, respectively, for Montney-focused peer group under coverage.

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)
KEL	53%	53%	5.1x	5.1x	\$12,869	6.7x	-0.4x	322%	56%
AAV	68%	64%	4.6x	2.9x	\$12,632	3.1x	2.3x	132%	90%
ARX	77%	50%	4.8x	4.3x	\$19,132	3.8x	1.4x	70%	77%
BIR	60%	59%	7.0x	3.4x	\$15,910	2.4x	5.8x	202%	76%
CR	-	-	6.5x	5.7x	\$16,821	1.4x	9.1x	110%	70%
KEL	53%	53%	5.1x	5.1x	\$12,869	6.7x	-0.4x	322%	56%
NVA	33%	33%	4.1x	4.2x	\$14,727	1.1x	4.3x	122%	61%
POU	91%	91%	6.7x	5.5x	\$15,789	2.3x	6.5x	134%	61%
PONY	57%	57%	18.1x	4.3x	\$9,567	nmf	nmf	nmf	92%
TOU	82%	81%	4.9x	3.7x	\$16,926	4.0x	1.6x	92%	79%
VII	84%	80%	3.7x	3.7x	\$19,214	1.7x	2.6x	79%	43%
Montney Peer Group Avg.	67%	63%	6.6x	4.3x	\$15,359	2.9x	3.7x	140%	71%

*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 \$2.75 target price is based on a 6.0x 2021E EV/DACF multiple (50% weighting) and 1.0x our NAV_{MG} of \$3.26/share (50% weighting).

Key Risks to Target Price

The key risks associated with our target price include business risks of the company and industry, including, but not limited to: 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, we believe that the following key near-term risks are specific to Kelt: 1) premium valuation associated with management pedigree; 2) future acquisitions are an ongoing component of the business model and could materially affect future estimates; and 3) asset and production base are highly levered to Canadian natural gas pricing.

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Exhibit 4. Summary

Company Overview					Key Valuation Ratios				
Market Capitalization (\$mm)	\$325				P/CF (x)	1.7x	1.8x	6.7x	5.0x
Net Debt (\$mm) *	(\$35)				EV/DACF (x)	3.1x	3.8x	5.1x	5.1x
Enterprise Value (\$mm)	\$291				EV/Production (\$000/BOE/d)	\$22.6	\$24.7	\$12.9	\$18.8
Current Price	\$1.73				EV/1P Reserves (\$/BOE)	\$3.85	\$8.69	\$3.57	\$3.86
52 Week Low/High	\$0.67	\$5.00			EV/2P Reserves (\$/BOE)	\$2.02	\$4.64	\$1.91	\$2.06
Current Yield	0.0%				P/NAV (2P)		53%		
					P/NAV (Modified Growth)		53%		
					ROCE	2%	1%	267%	75%
Production					Leverage				
	2018A	2019A	2020E	2021E	Bank Debt (\$mm)	\$169	\$300	\$0	\$0
Crude Oil (bbl/d)	8,403	9,361	6,697	5,027	Term Debt (\$mm)	\$78	\$83	\$85	\$85
NGLs (bbl/d)	3,186	4,490	3,661	2,407	Net Debt (\$mm)	\$289	\$416	(\$21)	\$4
Total Liquids (bbl/d)	11,589	13,851	10,358	7,434	Net Debt-CF (x)	1.6x	2.3x	-0.4x	0.1x
Natural Gas (mcf/d)	92,502	96,658	79,668	60,173	Credit Facility (\$mm)	\$250	\$350	\$350	\$350
Total Production (BOE/d)	27,006	29,961	23,636	17,463	% Drawn	68%	86%	0%	0%
% Gas	57%	54%	56%	57%	Dividend PoR (%) (Pre-DRIP)	0%	0%	0%	0%
Production Hedged (%)	-	-	43%	-	Dividend PoR (%) (Post-DRIP)	0%	0%	0%	0%
					Corporate PoR (%) (Pre-DRIP)	158%	176%	322%	138%
					Corporate PoR (%) (Post-DRIP)	158%	176%	322%	138%
Growth					Cash Flow Summary (\$mm)				
	2018A	2019A	2020E	2021E	Funds Flow from Operations	\$186	\$180	\$48	\$65
Y/Y Production Growth	22%	11%	-21%	-26%	Debt-Adjusted Cash Flow	\$196	\$195	\$59	\$65
Y/Y Production Per Share Growth	18%	10%	-23%	-26%	Investing Activities				
Y/Y DAPPS Growth	16%	-13%	25%	-31%	Exploration and Development	(\$293)	(\$317)	(\$156)	(\$90)
					Acquisitions/Divestitures	\$7	\$2	\$540	\$0
					Total Capital Expenditures	(\$285)	(\$316)	\$384	(\$90)
					Financing Activities				
					Net Change in Debt	\$77	\$131	(\$300)	\$0
					Dividends	\$0	\$0	\$0	\$0
					DRIP	\$0	\$0	\$0	\$0
					Other / Share Issue Proceeds	\$37	\$17	(\$62)	\$0
					EBITDA	\$189	\$181	\$45	\$59
Pricing Assumptions					CFPS (diluted)				
	2018A	2019A	2020E	2021E	Q1	\$0.25	\$0.27	\$0.15	\$0.09
WTI (US\$/bbl)	\$64.83	\$57.03	\$38.00	\$41.00	Q2	\$0.25	\$0.24	\$0.06	\$0.07
Edmonton Par (C\$/bbl)	\$69.14	\$69.06	\$44.50	\$47.50	Q3	\$0.25	\$0.21	\$0.02	\$0.08
WCS (C\$/bbl)	\$49.90	\$58.12	\$32.00	\$35.25	Q4	\$0.25	\$0.25	\$0.03	\$0.10
Nymex (US\$/mcf)	\$3.13	\$2.56	\$2.00	\$2.65	Annual	\$1.01	\$0.98	\$0.26	\$0.35
AECO (C\$/mcf)	\$1.53	\$1.79	\$2.00	\$2.50					
Exchange Rate (US\$/C\$)	\$0.77	\$0.75	\$0.73	\$0.74					
Corporate Netback (\$/BOE)					Quarterly Production (BOE/d)				
	2018A	2019A	2020E	2021E	Q1	26,978	27,057	30,806	17,392
Revenue	\$37.25	\$34.53	\$20.49	\$25.43	Q2	26,121	30,314	30,366	16,715
Hedging	(\$0.60)	(\$0.08)	\$1.19	\$0.00	Q3	26,204	31,150	16,528	17,506
Royalties	(\$3.11)	(\$1.76)	(\$0.93)	(\$1.14)	Q4	28,711	31,262	16,995	18,231
Transportation	(\$3.92)	(\$4.62)	(\$3.37)	(\$3.00)	Annual	27,006	29,961	23,636	17,463
Operating	(\$9.11)	(\$9.18)	(\$9.80)	(\$10.00)					
Operating Netback	\$20.51	\$18.88	\$7.58	\$11.29					
G&A	(\$0.85)	(\$0.81)	(\$0.88)	(\$1.00)					
Interest Expense	(\$1.02)	(\$1.38)	(\$1.26)	\$0.00					
Cash Taxes and Other	\$0.21	(\$0.21)	\$0.14	(\$0.06)					
Cash Flow Netback	\$18.85	\$16.48	\$5.59	\$10.22					
Per Share Metrics									
WA Outstanding Shares (diluted)	184.4	184.7	187.9	187.9					
CFPS (diluted)	\$1.01	\$0.98	\$0.26	\$0.35					
EPS (diluted)	\$0.04	\$0.04	(\$3.04)	(\$2.49)					
2P NAV		\$3.26							
Modified Growth NAV		\$3.26							

* Estimated Q3/20 net debt, pro forma the Inga disposition.

Source: Company reports, TD Securities Inc. estimates



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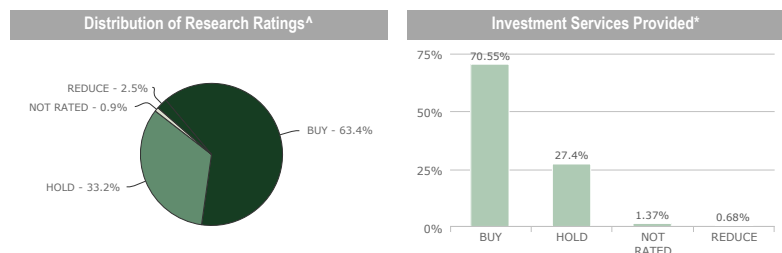
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Kelt Exploration Ltd.	KEL-T	2, 4, 9, 10

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Current as of: August 6, 2020

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Action Note

Equity Research

August 6, 2020

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