NG Energy International Corp.

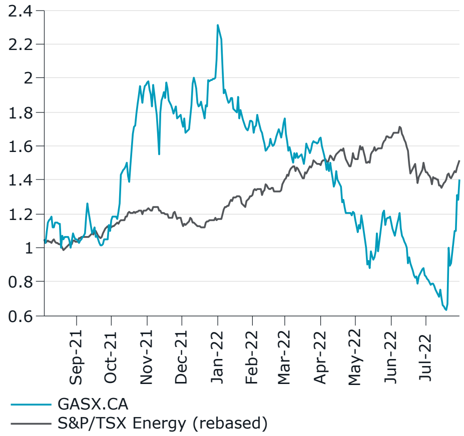
Latin America Research – Energy

2 August 2022

Rating	Price Target
SPECULATIVE BUY	C$1.40
GASX-TSXV	Price C$1.28

Market Data

52-Week Range (C$) :	0.60 - 2.33
Avg Daily Vol (000s) :	137.69
Shares Out. (M) :	125.0
Market Cap (C$M) :	175.0
Dividend /Shr (US$) :	0.00
Dividend Yield (%) :	0.0



Source: FactSet

Priced as of close of business 2 August 2022

NG Energy International (GASX-TSXV) is a Canadian-listed company involved in O&G exploration and production in Colombia, where it has working interests in the Maria Conchita, SINU-9, and Tiburon blocks. The company is focused on natural gas.

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Encouraging results, but that is just half the job

Today, NG Energy provided additional information on Magico-1

NG Energy provided an update on its recently drilled well, Magico-1, located in the SINU-9 block in the department of Cordoba. As we have mentioned previously, this well was drilled in a very prospective area just a few kilometers away from Canacol's (CNE-TSX | Not Rated) Nelson field (Figure 4). It was known that the well had been successful, but today's press release brought more information around testing.

GASX performed two successful Drill Stem Tests (DST) and a commingled test in three prospective zones, all located within the Cienaga de Oro (CDO) formation (the same formation that Canacol targets). Importantly, the well tested over 15MMcf/d of dry gas on a commingled production for a total net pay of 76 feet, and there are still additional zones to be tested. While we still need to wait for pressure transient analysis, the results are very encouraging so far. Figures 1-3 present three case scenarios based on different initial outputs, and the IRRs and payback periods look promising.

However, we note that a successful well is just half of the job at SINU-9. As we argued in our initiation report, the company still needs to build infrastructure in order to sell the gas into the market. GASX might have at least two alternatives worth mentioning:

1. Building a plant from scratch such as in Maria Conchita, something that could take ~12 months and could cost more than US$35M (considering a 40MMcf/d plant);
2. Connecting to Canacol's facilities which are just 25km away, which could take only ~6 months and cost ~US$2.5M.

While the second option might sound quicker and easier, the question is whether Canacol would be interested in receiving NG Energy's production in exchange for a fee. We note that CNE does have the spare capacity (~60MMcf/d) to start receiving production right away.

Additionally, after finishing the analysis, NG Energy expects to continue with the spudding of the "Brujo" well in the same block, just 10km away from Magico. The company has already received approval from the ANH and has enough cash to self-fund the drilling.

Share performance and rating

Over the past three weeks, NG Energy has rallied from C$0.70/share to C$1.28/share, an 83% rise. We believe that the market has started to price in the positive updates around the drilling campaign and supporting comments coming from government officials such as the incoming Minister of Finance, Jose Antonio Ocampo. During a recent interview, he highlighted Colombia's low gas reserves and that this will be a priority, considering the strategic role that natural gas will have in the energy transition (something we discussed here).

We maintain our SPECULATIVE BUY rating and C$1.40/share price target, as we wait for more information around the discovery and a clearer path on SINU-9 marketing strategy.

For important information, please see the Important Disclosures beginning on page 4 of this document.

Figure 1: Magico-1 at 15MMcf/d

SINU-9 Type-Well	15MMcf/d
D&C Cost per well, in US$M	$6.50
Initial Production, in MMcf/d	15
EUR, in Bcf	35
Working Interest	72%
Royalty Rate	26%
Decline Rate	15%
Gas Price, US$/MMBtu	5.00
After-Tax IRR	115%
Payback (months)	10

Source: Company Reports, Canaccord Genuity estimates

Figure 2: Magico-1 at 20MMcf/d

SINU-9 Type-Well	20MMcf/d
D&C Cost per well, in US$M	$6.50
Initial Production, in MMcf/d	20
EUR, in Bcf	35
Working Interest	72%
Royalty Rate	26%
Decline Rate	15%
Gas Price, US$/MMBtu	5.00
After-Tax IRR	160%
Payback (months)	7

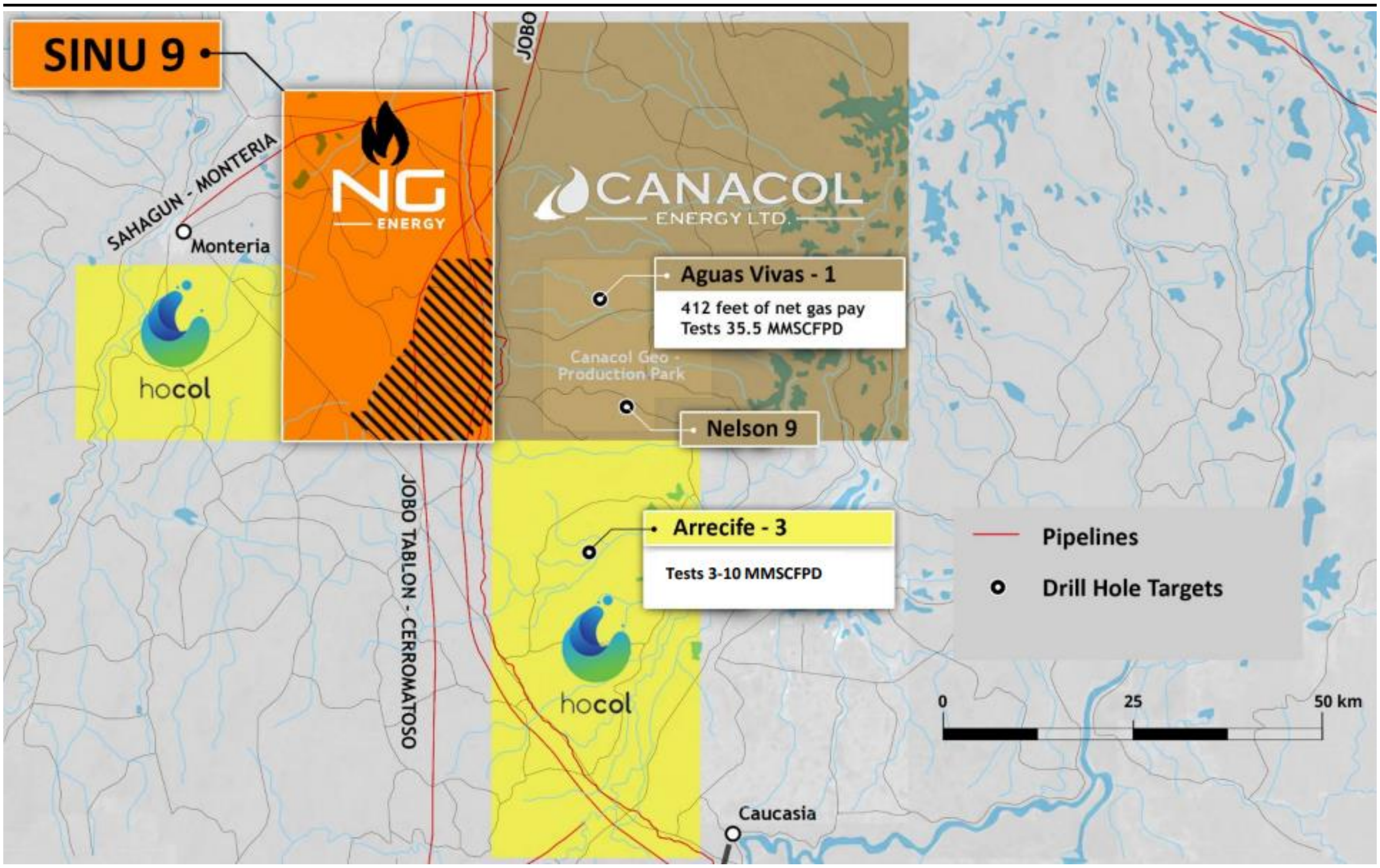
Source: Company Reports, Canaccord Genuity estimates

Figure 3: Magico-1 at 25MMcf/d

SINU-9 Type-Well	25MMcf/d
D&C Cost per well, in US$M	$6.50
Initial Production, in MMcf/d	25
EUR, in Bcf	35
Working Interest	72%
Royalty Rate	26%
Decline Rate	15%
Gas Price, US$/MMBtu	5.00
After-Tax IRR	150%
Payback (months)	6

Source: Company Reports, Canaccord Genuity estimates

Figure 4: SINU-9 map



Source: Company Reports

NG Energy International Corp.

Rating: SPEC BUY
Target: $1.40

Canaccord Genuity Capital Markets

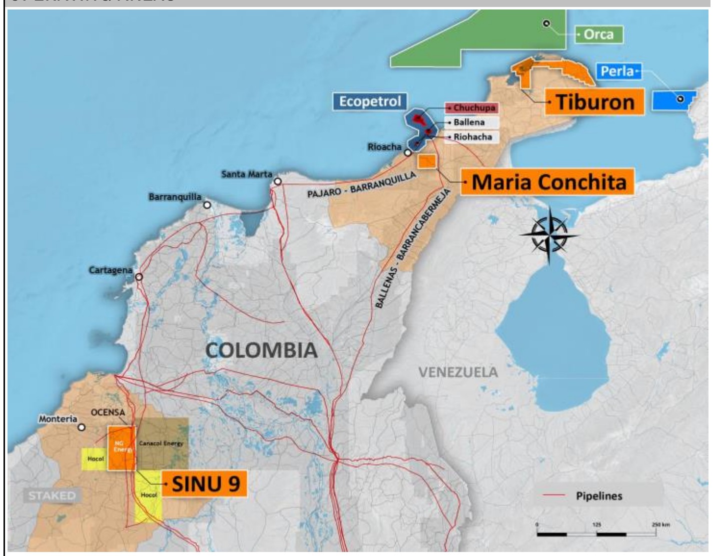
COMPANY STATISTICS

Price, C$		$1.28
Shares outstanding, #M:		122.6
Shares fully diluted, #M:		152.4
Market capitalization, C$M:		157
Enterprise value, C$M:		153
52-Week trading range, C$/share:	$0.60	$2.33
Average daily trading volume (000) (100 Day):		147
Projected 18-month return:		9%

FINANCIAL SUMMARY

	2021A	2022E	2023E
Gross Revenue, US$M	0.0	15.0	93.0
Royalties, US$M	0.0	3.1	22.4
Production Cost, US$M	0.0	5.0	26.4
SG&A, US$M	3.8	4.0	4.0
Other Opex, US$M	0.0	0.0	0.0
Adj. EBITDA, US$M	**-3.8**	**4.9**	**40.3**

OPERATING AREAS



VALUATION

	2021A	2022E	2023E
EV/EBITDA	-	16.93x	2.23x
EV/DACF	-	16.93x	2.23x
EV/BOED	-	$34.20	$21.00
Base NAV, C$			$1.52
P/NAV			0.84x
EV/EBITDA Target, C$			$1.25
P/DCFE			1.03x
Target P/NAV			0.92x
Target EV/EBITDA			1.12x

FINANCIAL SUMMARY

	2021A	2022E	2023E
FCF, US$M (EBITDA - Capex - Taxes - WK)	-9.1	-4.4	27.0
FCFPS - basic, US$/share	-0.07	-0.03	0.20
Capex, US$M	14.1	50.7	23.4
Dividends, US$M	0	0	0
Repurchases, US$M	0	0	0
Dividend + Repurchases, US$M	0	0	0
Dividend + Repurchases yield %	0.0%	0.0%	0.0%

RESERVES DATA (2P)

	2021A
Liquids (mbbls)	0.0
Natural Gas (mboe)	4.7
Total P+P (mboes)	**4.7**

PRODUCTION FORECAST

	2021A	2022E	2023E
Liquids (bbl/d)	0	0	0
Natural gas (boe/d)	0	500	2,623
Gross production (boe/d)	**0**	**500**	**2,623**
% Natural gas	0%	100%	100%

LEVERAGE

	2021A	2022E	2023E
Cash, US$M	5.3	7.9	20.9
Debt, US$M	13.6	13.6	13.6
Net Debt, US$M	8.3	5.7	-7.3
Net Debt to EBITDA	-	**1.7x**	**0.1x**

TOP HOLDERS

TOP HOLDERS	POSITION
Frank Giustra	17.0%
Serafino Iacono	9.6%
Gordon Keep	1.8%
Federico Restrepo	1.5%

COMMODITY PRICE ASSUMPTIONS

	2021A	2022E	2023E
WTI oil (US$/bbl)	95.7	87.8	73.1
Brent oil (US$/bbl)	99.0	90.0	75.0
NYMEX gas (US$/MMbtu)	5.0	4.1	3.9
Henry Hub (US$/MMbtu)	5.3	4.0	4.0
Colombian Gas Price (US$/MMbtu)	5.1	6.0	5.5
CAD/US$	1.27	1.26	1.25

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Investment Recommendation

Date and time of first dissemination: August 02, 2022, 18:14 ET

Date and time of production: August 02, 2022, 18:14 ET

Target Price / Valuation Methodology:

NG Energy International Corp. - GASX

We rate NG Energy with a SPECULATIVE BUY rating and a C$1.40/share price target. Our price target is the result of blending our Risked after-tax exploration NAV of C$1.52/share and a 3.5x target EV/EBITDA multiple to our 2023E EBITDA that results in a C $1.25/share.

Risks to achieving Target Price / Valuation:

NG Energy International Corp. - GASX

- **Reliance on comparative data and testing results**: Our projections, such as hit rates, D&C costs and EUR figures, are based on peers' historical data, so any changes in these parameters could materially affect actual results. In addition, we are using the company's testing results, which could differ from actual production and decline rates.
- **Lack of infrastructure**: NG Energy does not have treatment and transportation infrastructure at SINU-9. In addition, it has limited capacity at Maria Conchita. Any delays with the construction of facilities could generate a bottleneck that would prevent the company from expanding volumes.
- **Exploration**: NG Energy is working on a very ambitious exploratory program in SINU-9, which will require intensive capital expenditures. While the first well has been successful, any dry wells could adversely affect the company's financials. Furthermore, even if the company finds new resources, we cannot be sure that they will be economically or commercially viable.
- **Reserves and Resources**: As happens with all companies within the sector, reserves and resources are estimates, and actual recoverable resources might be lower. In addition, reserves may be subject to downward or upward revisions based on several factors, including pricing.
- **Natural gas pricing**: Like every commodity-linked company, NG Energy is exposed to international pricing. Nevertheless, this is a minor risk considering that Colombia has historically shown higher prices compared to international markets. Additionally, this risk is tempered because firm contracts generally include fixed prices (indexed to CPI) for around 5 years.
- **Geographical concentration**: The company operations are located in Colombia and might be more sensible to local political and economic risks.
- **Environmental**: Oil and gas sites are inherently polluting and can harm the environment. Even if the company has implemented management programs to address the environmental impact of its operations, but we cannot predict accidents or other events that could result in increased remediation costs.
- **Local communities**: NG Energy invests significantly in managing relationships with its stakeholders, including local communities. Nevertheless, we have seen protests against O&G companies for various reasons. While such protests are generally peaceful, road blockades or disruptions to block operations can cause delays and increased expenditures. Guajira, in particular, is a region where the risk of social disruptions is significantly higher, in our view.
- **Limited liquidity**: We note that liquidity could be too narrow for some institutional players. Investors should carefully consider liquidity before investing in NG Energy.
- **Colombia security**: While a peace agreement was ratified in 2016, there has still been some violence directed at pipelines and infrastructure. Around 30 incidents were reported during 2021, down 38% YOY. As the ELN is still active, the risk of new attacks persists. GeoPark might have insurance against these acts, but a reoccurrence of such acts might be harmful to the company's operations.
- **Colombia macroeconomic and social situation**: The country has historically been one of the most stable jurisdictions in Latin America. Nonetheless, the fiscal deficit closed at around -7.4% during 2021, with consensus pointing to -5.5% for 2022 and -4.5%

for 2023, which might require more fiscal measures in spite of strong social opposition. The social unrest that took place in 2021 caused disruptions to supply chains and shut-ins of some wells, affecting companies including Frontera and Gran Tierra.

- **Colombia politics**: Gustavo Petro, a leftist candidate, won the presidency during the second round of general elections from June 19. Since then, companies within the space have suffered significant declines, which we believe that is related to Petro's remarks about his opposition to O&G. We recommend reading our note published on June 20, available here.
- **Regulations**: Colombia has taken significant positive steps to attract investment to the oil and gas industry, starting with the 2003 reforms. Nevertheless, we cannot rule out changes in technical or legal regulations, including increased royalty rates. This risk increases significantly under a government inclined to the left.
- **Emissions initiatives**: The global commitments to cut down emissions and the transition to a less carbon-intensive economy can reduce oil and gas demand. Additionally, Colombia has pledged to reduce 51% of its emissions by 2030, an effort that will require significant reductions for polluting sectors.

Distribution of Ratings:

Global Stock Ratings (as of 08/02/22)

Rating	Coverage Universe		IB Clients
	#	%	%
Buy	644	67.79%	34.63%
Hold	128	13.47%	14.84%
Sell	11	1.16%	18.18%
Speculative Buy	160	16.84%	40.62%
	950*	100.0%	

*Total includes stocks that are Under Review

Canaccord Genuity Ratings System

BUY: The stock is expected to generate risk-adjusted returns of over 10% during the next 12 months.

HOLD: The stock is expected to generate risk-adjusted returns of 0-10% during the next 12 months.

SELL: The stock is expected to generate negative risk-adjusted returns during the next 12 months.

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Risk Qualifier

SPECULATIVE: Stocks bear significantly higher risk that typically cannot be valued by normal fundamental criteria. Investments in the stock may result in material loss.

12-Month Recommendation History (as of date same as the **Global Stock Ratings** table)

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