



**Valeura Energy Inc.**

**Fourth Quarter 2018 Results Conference Call**

**TRANSCRIPT**

**Calgary, March 19, 2019:** The following is a transcript of the Valeura Energy Inc. Fourth Quarter 2018 Results Conference Call, held at 11:00AM ET on March 14, 2019. An audio replay of the call is available with the webcast link:

<https://event.on24.com/wcc/r/1938046/559D5CA7E1328CDCEA05EE6E6247F220>

**Speakers:**

Sean Guest, President & Chief Executive Officer, Valeura  
Steve Bjornson, Chief Financial Officer, Valeura

**Participants:**

Stephane Foucaud, Analyst, GMP FirstEnergy  
Chen Lin, Analyst, Lin Asset Management  
Colin Smith, Analyst, Panmure Gordon  
Garrett Ursu, Analyst, Cormark Securities

---

***Operator***

Good morning, ladies and gentlemen, and welcome to the Valeura Fourth Quarter 2018 Results Conference Call. At this time, all lines are in a listen-only mode.

Following the presentation, we will conduct the question-and-answer session. If at any time during this call you require immediate assistance, please press \*, 0 for the Operator.

This call is being recorded on Thursday, March 14, 2019.

And I would now like to turn the conference over to Sean Guest, President and CEO. Please go ahead.

***Sean Guest, President & Chief Executive Officer, Valeura***

Thank you, Operator. So my name is Sean Guest. I'm the President and Chief Executive Officer of Valeura. Joining me here in Calgary today are Steve Bjornson, our CFO; Heather Campbell, our Financial Controller; and Robin Martin, Investor Relations Manager.

Before getting started, I'd like to draw your attention to our general disclaimer, which is provided on our corporate website and in our updated corporate presentation, which is on our website and available by link to those of you joining through the webcast.

I'd also like to point out the advisories regarding forward-looking statements and non-GAAP measures used in this discussion.

As of this morning, we filed our financial and operating results for Q4 2018, as well as our reserves and resource report for the year ended December 31, 2018. They're available on SEDAR and on our website.

So to get started today, I'll touch on the highlights from our press release and then hand over to Steve, who will take you through a financial review. After Steve, I'll provide an update on operations and activities, and will then take any questions you might have.

So starting off, 2018 as a whole was a challenging year for Turkey, given the federal elections, followed by the devaluation of the Turkish lira and an increase in inflation; a lot of volatility. Q4 in contrast was a relatively quieter quarter for Turkey from a news flow point of view, and with that we saw a recovery of the Turkish lira and a period of financial stability.

As I look back at 2018, though, there are two points that I want to make related to Turkey. First, we continue to see a stable and secure operating environment on the ground in Northwest Turkey. We have good relationships with the regulators and government agencies we depend on for permitting and approvals, as well as the local communities where we work on a daily basis.

Second, while the Turkish lira devalued sharply midyear, at Valeura we've actually seen an increase in our realized gas prices of 37 percent in 2018 in Canadian dollars, such that in Q4 we realized over \$9. These high prices have continued into 2019. And I want to emphasize this again, as I believe many of our shareholders are concerned in our ability to realize full value for our gas because the price is set in Turkish lira.

We continue to see the Turkish regulator and price authority BOTAS regularly adjusting gas prices so that the pricing remains similar to the cost of gas in the European region. That's an important relationship as we look forward to the long-term value of our gas resource in Turkey.

So touching on a few highlights, and as required by the TSX, our reserves were evaluated by our auditor D&M. At year-end 2018, we have 2P volumes of nearly 7.4 million barrels equivalent. That number is down 6 percent from the prior year, but that's really reflecting our 2008 produced volumes. Of note is that the value of the remaining reserves is up 35 percent from the prior year, given the higher gas prices in Turkey and in the region.

Our average production for Q4 of 623 barrels equivalent a day was roughly flat compared to Q3 2018, but we ended the year at a higher rate of 777 barrels equivalent a day. Given continued maintenance and workovers by our staff in Turkey, we've been able to roughly maintain this level of production into the start of Q1 2019.

While, we're pleased with the results from our shallow production, our operational focus in 2018 was on appraisal of the deep unconventional play. These appraisal activities have continued on plan into 2019, and we continue to be encouraged by what we are seeing in all the data acquired to this point.

We currently have operations ongoing at three deep well sites. At the Yamalik-1 discovery well, we are preparing the well for production logging to increase our understanding of the flow potential of different zones that were originally stimulated in the well.

At Inanli-1, we will be undertaking a Diagnostic Fracture Injectivity Test as the first step prior to really finalizing the complete stimulation and testing program.

And meanwhile at Devepinar-1, the appraisal well is drilled to just above the objective Kesan sections, and there's already been clear indications of overpressured gas at the base of the section we've just drilled.

On a corporate front, we ended the year with 60 million of working capital, which is more than we had after our Q1 raise, and we are progressing towards an additional listing of the Company's shares in the UK. And I'll speak more to this in a moment.

So with that, I'm going to hand over to Steve to walk through a financial review.

Steve?

***Steve Bjornson, Chief Financial Officer, Valeura***

Thanks, Sean. Hi, everyone. Financial and operating results for Q4 are summarized in a table at Pages 2 and 3 of the press release we issued this morning.

The headline from a finance standpoint is that our balance sheet remains in excellent shape. We have no debt, and working capital is sitting at 59.5 million. In fact, our working capital has grown at the close of 2018 from the 55.4 million equity financing in the first quarter of 2018.

As we continue planning out the appraisal program, I'm confident that we have sufficient resources to fully fund our portion of spending through the end of 2019 and beyond. We are in good financial position.

Remaining costs for the Inanli-1 appraisal well, namely the completion program, are being carried by our partner, Equinor, as part of their farm-in agreement. I'm pleased to say that drilling operations, which are operated by Valeura, were concluded on budget, and we're working hard to keep the completion program on budget too. As of Devepinar-1, we are now participating according to our working interest share, which is 31.5 percent.

And so just to reiterate, we've got sufficient financing for this and fully financed through the remainder of the capital program for 2019, which includes Devepinar-1 drilling, completion, and testing along with further capital spending for the BCGA in 2019.

So as Sean mentioned, our conventional gas production continues with average production of 623 boes a day in Q4, which generated revenue of 3.15 million. While production was down 5 percent over the prior quarter, revenue was up by 31 percent, reflecting the higher prices we saw in Q4.

Natural gas price realizations were 9.06 an Mcf, which by no means is a record for our business in Turkey, but is in stark contrast to the prevailing prices in North America. We have a very valuable business in Turkey, and I believe that results like this will illustrate it well.

Not surprisingly, we achieved strong operating netbacks in the fourth quarter of 32.48 per boe, which is 38 percent higher than in Q3.

So with that, I'll hand it back to Sean.

***Sean Guest***

Thanks, Steve. I'd now like to give a little more colour on our current operations and activities.

By way of reminder, our focus is on appraising and de-risking our basin-centred gas play. The way we intend to do this is by: one, demonstrating that overpressured gas is pervasive across our lands; and that two, we can achieve commercial flow for Yamalik.

We believe there is more that we can learn from the Yamalik-1 exploration well. And for that reason, we've gone back to the well and are currently preparing to log individual intervals that were stimulated by production logging testing. What this will tell us is the rates of inflow and specific products on an interval-by-interval basis. We expect the results of that production logging over the next few weeks.

Inanli-1, our first appraisal well, which was drilled to nearly 4,900 metres in January, encountered a large column of 1,615 metres of high net to gross gas-bearing sandstones, and we identified at least four intervals of interest worthy of fracking and testing.

We're getting into the initial phase of the completion program now with the DFIT near the bottom of the well. The DFIT test is expected to occur over the next few weeks, but I caution our listeners that these data are not on its own exciting, but will be used mainly to finalize the selection of equipment and finalize the full completion program, which is then expected to start around the end of April.

Based on the data we currently have from Inanli-1, we expect to frack at least four zones, and this program will continue for a couple of months. As we previously announced, if we see something interesting from the fracked results, we are prepared to test individual zones for longer periods of several weeks. And will, wherever possible, test through our existing production infrastructure so that we're able to sell the gas to our customers. We expect to announce results as and when we have material information to share.

The next appraisal well, Devepinar-1, is ongoing. Those of you who've been watching our announcements know that this was spudded last month. Now this well is a big step-out from the prior BCGA wells approximately 20 kilometres to the west, and will really test the extent of the BCGA to the western side of the basin.

It's early days for Devepinar-1, but drilling is going well and we are at the intermediate casing point just above the target Kesan formation. We already have confirmation of high-pressure gas entering the wellbore. We'll release more information when we're able to.

What we learn from the drilling, logging, and testing of Yamalik, Inanli and Devepinar will greatly advance our understanding of this play.

Now to be clear, the appraisal wells we are currently drilling are only vertical wells, and are designed to give us an understanding of how the quality of our BCGA play varies vertically through more than a kilometre of gas-charge section that we have drilled to date, and laterally across the whole area of the basin we control.

In normal course in our industry, one wants many of these vertical wells with production data to build a vertical and lateral model of the play and to identify the best zones in the best areas. These would then be targeted for horizontal wells.

In our planning with our partners, we believe that these steps do not have to run in a serial mode. But with good results in 2019, the notional plan for 2020 would already be drilling horizontal wells to understand the production potential, while at the same time progressing with continued vertical appraisal drilling across a whole area.

This is very important to the horizontal wells, as we know from looking across basins in North America that horizontal wells will deliver much higher production than seen in vertical wells. The production rates in horizontal wells will be multiples or many multiples of what you see in vertical production.

It's an exciting time for our BCGA play, and we're moving ahead as quickly as we can, given that we're at the early phases of learning and appraisal.

So a couple other points I'd like to touch on related to the BCGA play. You will note that D&M ... that the D&M prospective resource report was updated to year-end 2018. This was not a requirement for the TSX, but we did require this update to include in our prospectus and filing to support the UK listing. That was the sole reason for undertaking the update, and unfortunately also drove the timing of that report in that it was as of December 31, 2018.

And as of December 31, 2018, the effective date of the report, the new information available to D&M was the Yamalik-1 long-term production test and the drilling data from a portion of Inanli that was drilled as of year-end. And having reviewed the Yamalik-1 production data and the limited data from Inanli, D&M concluded that there was not sufficient new information that would justify a change in either the volumes that they associate with the play or the risk of success on that play.

Accordingly, the numbers remain unchanged from end 2017, which showed Valeura with 10.1 Tcf of estimated working interest unrisks mean prospective resource of natural gas.

I'd also like to make a comment on the value. In very simple terms, if you look at the current market cap of Valeura at 250 million, you subtract the value of the cash that we have in bank and our audited 2P reserves value, the total value the market is attributing to this whole play that we have is approximately US\$75 million.

Now again, I'm not pointing to the exact value that we have here. What I'm pointing to is the vast difference between what the market is ascribing to the asset and to what we, our external auditors and our analysts, see as the potential of this play.

So another point is that we're stepping up our efforts to have the Valeura story heard by a broader audience of investors. In November, we released that the Company was planning to undertake an additional listing of our shares in London, and that this would be a Q1 2019 activity with timing linked to our year-end results. Today, we released our year-end financials and reserves.

A London listing is the right move for the Company and our existing shareholders. We believe that we'll be able to attract increased institutional following and more research coverage in the London market. A Turkish gas story is much better understood in Europe.

To emphasize this point, when we raised capital 12 months ago, almost all of the money came out of London. Looking at a 12-month period around our raise at that time, the total amount of equity raises for international oil and gas companies in Toronto was US\$60 million. Valeura was 45 million of that. In the equivalent period in London, more than \$2 billion was raised.

So at this point, I can confirm to you that we are proceeding with the documentation and filing for an additional listing in London, and that this will be on the main board of the London Stock Exchange.

I can confirm to you that the Company does not intend to raise any capital at the time of this listing, and there will be no dilution to the existing shareholders.

On the exact timing of the commencement of trading in London, this will be related to the UK Listing Authority approval of the prospectus and the listing. Once the UKLA has granted the Company approval, the normal process is to issue an announcement of our formal intention to file, and then in normal course the Company would be trading about one week later.

So before I bring this to a close, I wanted to touch on one other issue. I'm sure you will all be aware of the debates going on globally about the positives and negatives of social media and the many recent abuses. This extends directly into investor information sharing websites. While the objectives of these websites are extremely valuable to the community in that they strive to provide a forum for information sharing between investors, they remain highly susceptible to misinformation, some of which is malevolent and designed to influence, and others is more innocence, just lacking real or fulsome data on which to draw conclusions.

We would caution our shareholders against believing information posted on these websites. As a company, we are bound by strict legal guidelines as to what we're able to share with you and ensuring that we are able to back up all statements with external advice. Anonymous bloggers have no such guidelines.

We appreciate our shareholders who contact us and make us aware of some of these posts. But to be clear, the Company will not engage on debate on these websites.

We remain open to our shareholders contacting us directly with their questions or concerns. And we remain open to people who feel that they have a geological background calling us and asking questions, but we also encourage all of our investors to seek professional investment advice.

So in summary, I'd just like to say this continues to be an exciting time for Valeura. We continue to find positive signs as we proceed through our evaluation program, and I believe we are doing the right things to demonstrate the value of our BCGA play and to unlock the value in the capital markets.

With that, I'd like to thank everyone for calling in this morning. And I'll now turn the call back over to the Operator to help us take any questions.

Thank you.

***Operator***

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. Should you have a question, please press the \*, followed by the 1 on your touch-tone phone. You will hear a three-tone prompt acknowledging your request and questions are polled in the order received. If you are using a speakerphone, please lift the handset before pressing any keys.

And your first question comes from Stephane Foucaud from GMP. Please go ahead.

***Stephane Foucaud, Analyst, GMP FirstEnergy***

Hi, Sean. Hi, guys. A simple one for me. Could you confirm that the Inanli test, well test will indeed start by the bottom and then progressing going up and, therefore, we probably start with the least exciting zones among the few that you plan to test? Thank you.

***Sean Guest***

Yeah. Thank you, Stephane. Good afternoon. Yes. With the way that you have to do the stimulation and fracking program, unfortunately as a company we would like to go to the very best zones and just start there. But no, you're correct in that we actually have to work from the bottom of the well up.

So the first test would be down at the lowest part of the well, which the way porosity naturally decreases with depth, those are likely to be some of the poorest reservoirs relative to each other, so we would expect better reservoirs near the upper part of the well.

But you're correct, we do need to start the testing at the bottom and then work our way up.

***Stephane Foucaud***

So in other words, if the result of the bottom—the full test at the bottom is not great then it's not really a big deal because the better zones are above. But if it's a very good result then it's very encouraging for the rest.

***Sean Guest***

That's very correct. And that was similar, as we saw in Yamalik where we had very good production from the deep.

***Stephane Foucaud***

Thank you.

***Operator***

Thank you. Your next question comes from Chen Lin from Lin Asset Management. Please go ahead.

***Chen Lin, Analyst, Lin Asset Management***

Hi, Sean. Thank you for taking my question. One ... first is that Yamalik, you said you're going to go back in to test the zones one-by-one. Are you planning to get ... to check the production data of the gas or find out where the water comes from? What's your plan there?

***Sean Guest***

Yes. To be clear, it's very hard to go back in and change how the well's been stimulated in the perforations that you have there. We have this all as commingled flow, so all the zones over 800 metres are all flowing

into the well together. So that's why it's very difficult to analyze the single bit of information, which is what you get out of the top and tell what's coming from what zone.

So what we're going to do is what we call production logging. So it's actually sending tools down the hole that are then capable of looking at each zone and what fluids are coming from each zone.

So that's the operation that we'll undertake. And it's been quite a complicated planning process on that because there are a number of different ways you can try and do this type of production logging. And it was only really recently last month that we came to an agreement with Equinor as to the best way to try and get information from the well. So we've gone back there, pulled that tubing out, and are getting ready to start that production logging program over the next few weeks.

***Chen Lin***

Great. Thank you. Just a curiosity, is the Equinor paying for this? Or now it's a 50/50 with Equinor?

***Sean Guest***

No, we would be sharing the cost 50/50 with Equinor.

***Chen Lin***

Thank you. The next well you're drilling at Devepinar, right? So what's the maximum depths you're planning to go, how deep do you plan to?

***Sean Guest***

Yeah. Chen, it's a good question because Inanli we were pushing that well down towards 5,000 metres because we wanted to really look to the full extent of how deep does this overpressured gas go. With Inanli, we saw that the gas goes down to the total depths and down to 4,900 metres.

But as we were talking about, what we do know is that porosity decreases with depth and the better-quality rock is in the shallower formations.

And what I mean by that is we're still talking from that interval of approximately 3,000 metres to 5,000 metres. But we expect the better rocks in the shallower part in the 3,000- to 3,500-metre range rather than down at 4,500 metres. So Inanli proved that the gas goes all the way down. We're not sure we need to be doing that anymore because our focus is now on demonstrating commerciality.

Drilling very deep down to 5,000 metres is expensive. And I would rather see our capital allocated towards actually the testing and demonstrating that we can achieve commercial flow, rather than trying to prove up volumes that likely wouldn't be developed until 2040 or 2050. The deeper stuff we expect to be later-life development. The shallower stuff would likely have better reservoir quality and would be the first things that you would develop.

So when we look at Devepinar and the future drilling, while we've maintained a well design that is capable of pushing that deep, we're not sure in the end that we will drill that full way.

***Chen Lin***

Okay. Thank you. Back to the Inanli, so my understanding on the prior questions was you do some testing at the bottom first. The first real production test will be started at the end of April, have I heard correctly?

***Sean Guest***

That's correct. That's our current timing now is about the end of April. We need to get this pressure data from what we call a DFIT analysis to look at the maximum pressure in the well because it then determines what type of pressure equipment we need at the surface. And so that's one of the key drivers there.

***Chen Lin***

And then you will—assuming in May you will start testing; if it goes well then you will have extended testing maybe three to four weeks. Is that correct?

***Sean Guest***

That's correct. So you could be looking at on a positive result each test could be taking three weeks or even more, depending on how we view the produced data. So it could extend for quite a lengthy time, but again, in our view that would be very good news.

***Chen Lin***

Yes. Okay. Great. Thank you, Sean.

***Sean Guest***

Thanks, Chen.

***Operator***

Thank you. Your next question is from Colin Smith from Panmure Gordon. Please go ahead.

***Colin Smith, Analyst, Panmure Gordon***

Thanks very much. Hi, Sean. Hi, everybody there. Just apropos of your point about the sort of success of the vertical drilling that you've had so far, are you expecting that the sort of last appraisal well in the program will also be a vertical well? Or would you consider drilling horizontally at this stage, bearing in mind your major comments about having identified the shallower rock as really the main target?

***Sean Guest***

Yes. Thanks, Colin. Good afternoon. It is a good question because we've been working with our partner to really determine what we'd like out of that third well. And I think there's a recognition that getting to a horizontal well here will be quite important. It really is one of the challenges we're having is the timing of information that we're getting which is coming from production and further drilling, and then being ready to be able to say, well, I can go to a horizontal well for that third well.

So at this point, we think it is much more likely that it will be a vertical well; however, the location could be selected to the point that it sets you up to then be able to do a horizontal well, whether from that same

pad or from another pad nearby that then goes towards that well. In your first horizontals, it is preferable that you have what we call a heel and a toe well; in other words, that you have a vertical well near both ends of the horizontal, as it helps guide you through that drilling.

So we would like to get to a horizontal in that third one, but I think it will be challenged, given the timing of the production data that we're going to get.

***Colin Smith***

Okay. Thank you.

***Operator***

Thank you. Ladies and gentlemen, as a reminder should you have any questions, please press \*, 1.

And your next question comes from Garrett Ursu from Cormark. Please go ahead.

***Garrett Ursu, Analyst, Cormark Securities***

Hey, guys. Just curious with some of the more—or the extra work on Yamalik and stuff like that, I'm just hoping to get a sense of capital spending for Q1 and Q2? As well as part of your ... some of your shallow stuff what you're spending there, what you're doing there, and what we could expect for the kind of first-half spending?

***Sean Guest***

Yeah. There is a rough ... in our corporate presentation we do include a timeline kind of a breakdown of the capital expenditures by quarter there. So it's I think as you've got there, as we get into Q1 now, Devepinar we're paying our working interest share of 31 percent, so that is going to start ... we are going to start spending money during that period. And then that will continue as we look for the third well and as we continue on testing of Devepinar and that.

In our shallow activities, the current plan right now is quite limited. So even looking out over the year, we're currently spending on the order of, I think, it's about 1 million to 2 million.

***Steve Bjornson***

Yeah. So across, Q1 is going to be about 5 million. If everything's on time, about 5 million and then you'd get anywhere from 10 million to 13 million in Q2. Often we've been delayed on moving equipment and getting things done. But I think that's kind of Canadian dollars.

But if you want to look at the summary for the program in US dollars and Canadian dollars that we reflect in all of our disclosure, and it lays out where and when the timing of the wells.

***Garrett Ursu***

Okay. Okay. Thanks. And just to be clear, I guess, when you're testing some of these wells, the production won't be recorded, I guess, in barrels, and the cash flow will go against CapEx? Or how will that be kind of accounted for go forward?

***Steve Bjornson***

Yeah. Yeah. Well, what's happening is when you end up in this extended test period, Garrett, the well doesn't really move into production until it's really on production at that point in time. So when we're doing extensive work downhole, that's basically still part of the capital.

Any test production obviously has to be matched up with the capital so that kind of it gets capitalized, if you kind of follow me.

***Garrett Ursu***

Yup.

***Steve Bjornson***

So that's likely going to happen with every well at this stage.

***Garrett Ursu***

And that's included in the capital spending estimates kind of a net number?

***Steve Bjornson***

Yeah. It's a net number. But there's—the rates—the net cash flow on the well is not going to be that significant to change. I mean, if we get a better production it will help us.

***Garrett Ursu***

Okay. Okay. Thank you.

***Steve Bjornson***

But the capital numbers that we put in there are probably the more conservative numbers.

***Garrett Ursu***

Okay. Thanks.

***Operator***

Thank you. At this time, we have no further questions. You may proceed.

***Sean Guest***

We may proceed. No further questions

***Operator***

No further questions.

***Sean Guest***

Okay. So I'd like to thank everyone for joining us here today. And again, as we've emphasized, please feel free to reach out and contact us if you do have any further questions.

***Operator***

Ladies and gentlemen, this concludes today's call. We thank you for participating, and ask that you please disconnect your lines.