

Candax Energy Inc. (CAX-T, \$1.07)

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Investment Brief – Candax Energy Inc. is a public junior international oil and gas company that is approximately one year old. Run by an internationally experienced management team, Candax is carrying out a strategy that uses all its business and technical expertise to develop and produce oil and gas assets in North Africa and the Middle East.

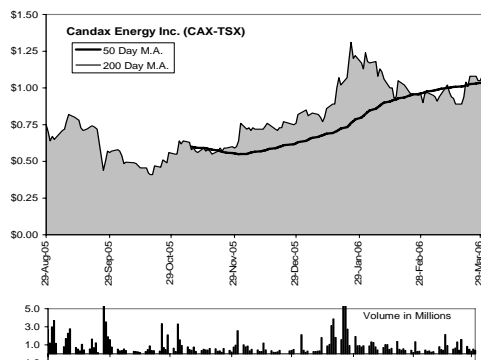
Rating **SECTOR OUTPERFORM**
(SPECULATIVE)
Target Price **\$1.25**

Current Price	\$1.07
Return (incl. dividend)	17%
52-Week High / Low	\$1.38 / \$0.39
Shares O/S	130.7M (basic) / 183.1M (F/D)
Market Capitalization	\$140 million
Enterprise Value	\$116 million
Daily Volume	893,000
Currency	C\$ unless noted
Company CEO	Michael Wood
Company Web Site	www.candax.com

Financial Forecast	2004	2005	2006E	'06/'05
Liquids (bbl/d)		881	1,350	53%
Natural Gas (mmcf/d)		2.8	2.3	(21%)
Total (boe/d)		1,354	1,725	27%
% Liquids		65%	78%	20%
Cash Flow (\$M)		5.3	23.2	336%
F/D CFPS		\$0.04	\$0.13	196%
F/D EPS		(\$0.03)	\$0.06	(272%)
Capital Expenditures (\$M)		45.5	25.0	
Net Debt (\$M)		(11.4)	(9.5)	(16%)
WTI (US\$/bbl)	\$41.46	\$56.54	\$60.00	6%
AECO (\$/GJ)	\$6.26	\$8.37	\$8.30	(1%)
Valuation Parameters				
Price/CFPS (multiple)		25.1	8.5	(66%)
Price/EPS (multiple)		(31.8)	18.5	(158%)
EV/boe/d		\$85,849	\$67,379	(22%)

Source: Candax Energy and Haywood Securities

Price Performance



Source: Bloomberg

2005 Year-end Results Announced

■ Candax ended 2005 with approximately \$25 million in cash

The Company is well funded for both its planned exploration projects and its redevelopment work. In addition to the \$25 million already in the bank, the Company could collect about \$50 million from the exercise of warrants due to expire on April 14, 2006, if the share price moves higher than \$1.20.

■ Q4 results down because of shut-in El Bibane production

Prior to the field being shut in during September of 2005 because of corrosion problems, El Bibane was producing 350 bbl/d of oil and 3.7 mmcf/d of natural gas. The redevelopment of the El Bibane field is expected to proceed shortly, as soon as the drilling barge has been safety certified.

■ Chaal well determines value of Company

The exploration well on the Chaal permit was spudded on February 5, 2006. A successful well could have as much as 844 bcf of associated reserves. However, the prospect could also contain non-economic quantities of gas.

Expectations – We expect that the redrilling of the El Bibane field could result in production that exceeds our forecasted numbers. We note that when the field first came onstream in 1998, it produced at rates of almost 5,000 bbl/d from one well. A successful well will likely also be a market catalyst for a higher share price.

Valuation – Our target price of \$1.25 is now slightly less than the risked exploration value of a successful Chaal well plus the Company's current assets. However, owing to the timing of the Chaal results, we leave our target price unchanged. An unsuccessful well at Chaal would see a \$0.50-per-share reduction in valuation and target price.

Catalysts – Our 2006 forecast is based on the successful redevelopment at El Bibane, with an expected oil production rate limited by the reservoir characteristics. Better than expected production results or exploration success would have a positive effect on our view of Candax.

Industry & Company Profile

Oil and Gas – Candax is a junior oil and gas exploration company focused on oil and natural gas exploration and production in North Africa and the Middle East.

Revisions, Date of Record

Rating – New, November 2, 2005
 Target – New, November 2, 2005
 Forecast – Revised production forecast, February 20, 2006

Risk Profile

Moderate
 Forecast Risk Moderate
 Financial Risk Moderate
 Valuation Risk Moderate
 Political Risk Low

Please see rating structure, important disclosures, risk profile parameters, disclaimers, and notes at the end of this report.

Candax Energy Ltd. (CAX-T)

Rating:	SECTOR OUTPERFORM (SPECULATIVE)		One-Year Target Price:	\$1.25
Current Price	\$1.07		Market Capitalization (\$M)	139.8
Current Shares Outstanding (million)	130.7	<u>Dilution</u>	Current Net Debt (est.) (\$M)	(23.6)
Fully Diluted Shares Outstanding (million)	183.1	40.1%	Enterprise Value (\$M)	116.2
Book Value (\$M)	64.5		EV / BV (multiple)	1.8

Production	2003	2004	2005	2006E	2005 / 2004	2006 / 2005
Liquids (bbl/d)			881	1,350		53%
Natural Gas (mmcf/d)			2.8	2.3		(21%)
Total (boe/d)			1,354	1,725		27%
Percent Liquids			65%	78%		20%
Percent Natural Gas			35%	22%		(38%)
Revenue (\$M)			12.9	33.6		161%
Cash Flow (\$M)			5.3	23.2		336%
CFPS Basic			\$0.06	\$0.18		178%
CFPS Fully Diluted			\$0.04	\$0.13		196%

CFPS Sensitivity		<u>\$/FD Share</u>	<u>% of CF</u>
	Oil (US\$1.00/bbl)	\$0.003	1%
	Gas (\$0.25/mcf)	\$0.001	0%
	100 bbl/d	\$0.004	2%
	1.0 mmcf/d	\$0.006	3%

Earnings (\$M)		(1.5)	10.6	(805%)
EPS Basic		(\$0.02)	\$0.08	(549%)
EPS Fully Diluted		(\$0.03)	\$0.06	(272%)
Capital Expenditures (\$M)		45.5	25.0	(45%)
Reinvestment Ratio		856%	108%	(87%)
Net Debt (\$M)		(11.4)	(9.5)	(16%)
Debt / Cash Flow - Trailing (years)		(2.1)	(0.4)	(81%)

Per BOE Analysis (\$/boe)				
Revenue		\$26.07	\$53.36	105%
Operating Expense		\$5.43	\$5.00	(8%)
Net Operating Revenue		\$20.64	\$43.02	108%
G&A		\$9.84	\$6.35	(35%)
Cash Flow		\$7.34	\$36.80	401%
DD&A		\$8.40	\$13.70	63%
Earnings		(\$5.16)	\$16.81	(426%)

Valuation Parameters				
Current Price / F/D CFPS (multiple)		25.1	8.5	(66%)
Debt-Adjusted CF Multiple		18.2	5.0	(73%)
Target Price / F/D CFPS (multiple)		29.3	9.9	(66%)
Current Price / F/D EPS (multiple)		(31.8)	18.5	(158%)
EV / boe/d		\$85,849	\$67,379	(22%)
Target EV / boe/d		\$112,253	\$89,162	(21%)

Price Assumptions						
Crude Oil WTI (US\$/bbl)	\$31.06	\$41.46	\$56.54	\$60.00	36%	6%
Company Average (C\$/bbl)			\$56.93	\$67.50		19%
AECO (C\$/GJ)	\$6.33	\$6.26	\$8.37	\$8.30	34%	(1%)
Company Average (C\$/GJ)			\$0.41	\$0.39		(5%)

Source: Haywood Securities

Investment Thesis

Candax Energy's management is a well-experienced, hands-on team that has founded, run, and sold private and public oil and gas companies. Combining the international expertise of senior management and its advisers with the technical skills of the remainder of the team, Candax should be able to deliver meaningful exploration-driven production growth with risked production potential that could more than double the Company's cash flow. We recommend the Company to investors for this exposure, and rank the overall risk profile as moderate. We are maintaining our rating of Candax Energy Inc. (CAX-T) at SECTOR OUTPERFORM (SPECULATIVE), and our 12-month target price of \$1.25 per share remains unchanged.

Q4/05 and 2005 Results Summary

Candax began operation in 2005, after its acquisition of the Tunisian operations of Centurion Energy International Inc. (CUX-T). The Company has been reworking its acquired onshore Tunisian assets and is in the process of redeveloping its offshore El Bibane field. The Company is also currently drilling its first exploration well on the Chaal permit in Tunisia, through a joint-venture agreement with Mitsubishi Corporation.

Q4/05 and 2005 Annual Results Summary

	Q4	Q3		Annual
	2005	2005	Q4 vs. Q3	2005
Production				
Liquids (bbl/d)	468	809	(42%)	881
Gas (mmcf/d)	0.0	2.6	(100%)	2.8
Total (boe/d)	468	1,242	(62%)	1,354
Sales Price				
Liquids Price (\$/bbl)	\$66.12	\$67.26	(2%)	\$56.93
Gas (\$/mcf)	\$0.43	\$0.43	(1%)	\$0.43
Equivalent (\$/boe)	\$31.65	\$34.92	(9%)	\$26.07
Financials				
Cash Flow (\$M)	(1.1)	5.4	(120%)	5.3
F/D CFPS	(\$0.01)	\$0.04	(125%)	\$0.04
Earnings (\$M)	(4.3)	3.0	(244%)	(1.5)
F/D EPS	(\$0.05)	\$0.04	(233%)	(\$0.03)
Net Debt (\$M)	(11.4)	(15.5)	(27%)	(11.4)
Trailing D/CF (multiple)	2.6	(0.7)	(465%)	(2.1)
Capex (\$M)	1.1	0.4	145%	45.5

Source: Candax Energy and Haywood Securities

2005 Reserves Summary

As previously reported, Candax showed slight reserves growth in 2005, mostly as a result of its rework of existing assets. Candax's reserves are evaluated by Ryder Scott Petroleum Consultants, with the exception of the Chaal Permit, which is evaluated by Glendower International Limited.

Candax Reserves at Year-end 2005

At December 31, 2005	Liquids (mmbbl)	Natural Gas (bcf)	Total (mmboe)
Proven	2.4	9.8	4.0
Probable	3.1	51.6	11.7
Proven + Probable	5.4	61.4	15.7

Source: Candax Energy and Haywood Securities

Based on a 2005 exit rate of 700 boe/d, Candax has a reserve-life index (RLI) of 15.6 years proven and 61.3 years proven plus probable. The theoretical RLI, assuming the restart of the El Bibane field at 1,500 boe/d net to Candax, is 5.0 years proven and 19.5 years proven plus probable.

Candax Reserves Additions in 2005

At December 31, 2005	Liquids (mmbbl)	Natural Gas (bcf)	Total (mmboe)
Proven	0.7	4.0	1.4
Probable	0.7	(3.6)	0.1
Proven + Probable	1.3	0.4	1.4

Source: Candax Energy and Haywood Securities

We note that the new reserves are primarily proven and probable oil. The main impact has been the redevelopment of the El Bibane oilfield. Also significant, but to a lesser degree, are the new reserves from the reactivated Al Manzah oil field, currently producing at approximately 250 bbl/d.

Corporate Update

The deep gas exploration well at Chaal 1 was spudded on February 4, 2006. About one week ago, the well passed approximately 3,200 metres depth. Intermediate casing is currently being run in and will be cemented in place. Drilling progress is roughly on time, as the well was originally expected to take about 50 days to drill the total depth to 4,500 metres. Up to an additional 30 days of testing time are expected to be required to fully evaluate the potential of the productive horizon.

We anticipate news on the well in the next few days and expect that it will come out just before the warrants expire in mid-April. If the well results are good, the Company's share price could be propelled above the \$1.20 exercise price of the warrants. However, testing will take as much as 30 days, so full news

on the well is not likely until late April. Full exercise of these warrants would bring in just under \$50 million.

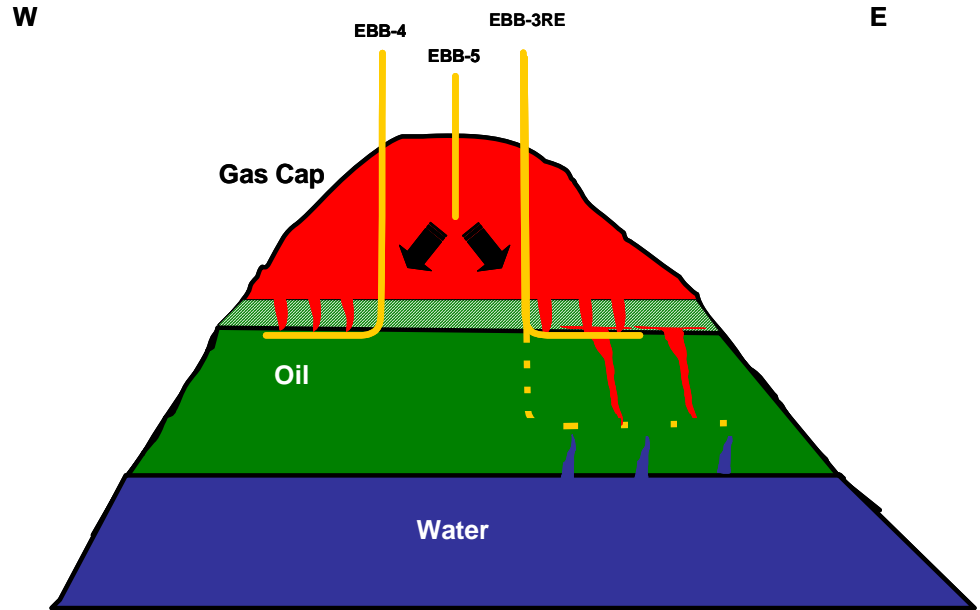
As previously reported, the exploration well at Chaal is a joint venture between Candax and Mitsubishi. They are drilling a twin of a well, ABK1, that in 1963 tested gas and condensate from a 150-metre hydrocarbon section on the Permit. The ABK1 well tested natural gas and varying amounts of natural gas liquids at rates up to 3.0 mmcf/d, and condensate volumes that ranged from 25 bbl/mmcf to 80 bbl/mmcf over an extended test period. This well was followed by a second, which found a similar hydrocarbon column but was left untested. It is believed that the Company that drilled the wells was looking for oil and gave up the block after the two wells proved unsuccessful.

Candax is drilling the twin of the ABK1 discovery well to confirm the old production-test results, including flow rates and condensate ratios. Gross reserves of approximately 60 bcf have been assigned to the structure identified by the ABK1 and ABK2 wells. However, the full structure could be 200 bcf to 500 bcf in size, with potential for as much as 844 bcf of reserves.

Candax has refined the parameters for a successful well. The well is being drilled to evaluate the productivity of the Lower Nara Formation. Flow rates of less than 5.0 mmcf/d would cause the technical team to go back and re-evaluate the prospect. However, a flow rate from the well of more than 5.0 mmcf/d would be deemed successful and would move Candax ahead with field development and the drilling of a second well. The original plans were to drill the second well immediately after the first. However, Candax has deferred drilling the second well to later 2006, in the September/October time frame. The postponement would give the technical team time to fully evaluate the test results from Chaal-1 before picking a second drilling location. However, we note that Candax has a guaranteed option for the rig to drill a second well this year, and the time slot is approximately set.

As we noted one month ago, the continued delays to the final stages of fabrication and safety certification of the El Bibane drilling barge appear to be nearly over. We understand sea trials of the barge should take place shortly, which could see mobilization of the drilling barge to Tunisia in early to mid-April. With approximately 10 days required to travel from the shipyard across the Mediterranean, Candax could be on location by the end of April and could start drilling by late April/early May.

El Bibane Field Schematic Cross Section



Source: Candax Energy

First to be drilled will be the new well at EBB-4. This is a new horizontal well on the northwest flank of the field, being drilled to access new reserves. Once the well is completed, it will be immediately placed on production—possibly around the end of May or early June. Then the recompletion of EBB-3 would be undertaken, and finally, the gas injection well at EBB-5 would be drilled. Note that as a result of the proximity of the horizontal wells to the gas cap, the gas injection well is required. However, it is believed that it will allow Candax to access as much as an additional 1.0 million barrels of liquids contained in the natural gas.

As we highlighted in our previous reports, owing to the close proximity of the new horizontal wells to the gas cap of El Bibane, much more gas will be produced at El Bibane than from the previous well. Therefore, full field production is contingent on the drilling of the gas injection well at EBB-5, as well as on the completion of the required surface facilities, as gas consumption at the SEEB power plant is limited to approximately 6.5 mmcf/d. The full field redevelopment is expected to cost Candax approximately US\$22 million for its 74% interest. The Company is fully funded for this expenditure.

Valuation

In the following table, we summarize a series of calculations that reflect the estimated net asset value for the Company. We note that the reserves report was done effective December 31, 2005, and the new reserves report reflects a material increase in reserves and reserves value. The increased reserves and value mainly reflect the incremental reserves attributable to the redevelopment of the El Bibane oil field. However, the upside in the Company's value still remains with a larger gas reserve at Chaal than is currently accounted for in the latest reserves report, which has given the prospect gross proven plus probable reserves of 60bcf.

Net Asset Value

Estimated Net Asset Value (summary)	Dec 31, 2005, Reserves		Dec 31, 2004, Reserves	
	Net Reserves	NPV10%	Net Reserves	NPV10%
	Dec 31, 2005 (Mboe)	Value (C\$M)	Dec 31, 2004 (Mboe)	Value (C\$M)
Proven Reserves	4.0	45.3	3.0	25.1
Proven Plus Probable Reserves	11.7	79.9	11.6	29.5
Total Reserves	15.7	125.2	14.6	54.6
Cash in Bank		21.0		21.0
		146.2		75.6
Shares Outstanding (millions)				
Basic		130.7		130.7
Fully Diluted		183.1		183.1
Net Asset Value per Share				
Basic		1.12		0.58
Fully Diluted		1.12		0.73
41.3 Million Warrants @ \$1.20/Share = \$49.6M				
11.2 Million Options @ \$0.80/Share = \$9.0M				

Source: Candax Energy and Haywood Securities

In our previous calculation of target price for Candax, we included an additional \$0.25 per share for upside from exploration. We note that our value for potential upside from Chaal to Candax equated to only 120 bcf gross reserves for the Chaal feature. As the drilling of Chaal-1 is nearing total depth, and well results are approximately one month away, we leave our target price unchanged.

Our target price represents our estimation of the net asset value of the current assets in the Company. Using \$1.12 per basic share from existing reserves and an incremental \$0.25 per share for undetermined exploration upside potential on the Chaal Permit, there is an upward bias to our existing 12- to 18-month target price of \$1.25. We note, however, that over the next six weeks, exploration drilling on the Chaal Permit will result in share-price volatility—of

which investors should be mindful along with the likely short-term buying or selling opportunities presented.

Should the Chaal well come up dry, the short-term potential of the prospect would likely be eliminated, and our value and target price for Candax would see a decrease of \$0.50 per share.

For comparative purposes, we are including a table of international oil and gas producers. While it is not based on cash flow, we note that our target price for Candax derived from a multiple of cash flow is in line with companies of a similar type in the current market.

Valuation Comparison Table

	<u>Candax</u> CAX-T	<u>Oilexco</u> OIL-T (based on 2007 estimates US\$ except share & target price)	<u>PanOcean</u> POC.SV.B-T (US\$ except share & target price)	<u>TransGlobe</u> TGL-T (US\$ except share & target price)
Production (2006 estimate)				
Oil and NGL (bbl/d)	1,350	26,997	13,083	4,500
Natural Gas (mmcf/d)	2.3	0.0	0.0	7.6
Total (boe/d)	1,725	26,998	13,083	5,767
Share Price (Mar 28/06)	\$1.07	\$4.70	\$37.38	\$6.20
2006 F/D CFPS	\$0.13	\$2.02	\$5.32	\$0.77
Current P/CF Multiple (times)	8.5	2.0	6.1	7.0
Target Price	\$1.25	\$8.00	\$54.00	\$8.50
Target P/CF Multiple (times)	9.9	3.5	8.8	9.6
Current Shares Outstanding (millions)	130.7	195.0	24.7	58.5
F/D Shares Outstanding (millions)	183.1	212.7	26.8	61.4
2006 Cash Flow (\$M)	23	426	137	47
2006 Capital Expenditures (\$M)	25	200	163	45
2006 Net Debt (\$M)	(10)	(138)	3	(12)
Enterprise Value (\$M)	116	686	740	301
Current EV / boe/d	\$67,379	\$25,413	\$56,579	\$52,121
Target EV / boe/d	\$89,162	\$46,964	\$99,954	\$84,546

Source: Company data and Haywood Securities

Rating Structure

SECTOR OUTPERFORM – Haywood’s top rating category. The analyst believes that the security will outperform its sector. Furthermore, the shares are forecast to provide attractive returns measured against alternative investments when considering risk profiles. The rating carries a minimum total return threshold of 15% for equities and 12% for trusts. The rating applies to companies that have tangible underlying assets that give a measure of support to the market valuation. The rating category considers both the absolute and relative values in assigning the highest rating on the security.

SECTOR OUTPERFORM (SPECULATIVE) – Investment for risk accounts only. The security has strong upside although its risk profile leaves the potential for significant downside. Return expectations should generally exceed those of SECTOR OUTPERFORM to allow for the additional risk. Companies in this rating category carry greater financial and/or execution risk without tangible assets for underlying support.

SECTOR PERFORM – The analyst believes that the security will trade with tight correlation to its underlying sector. Furthermore, the target price (together with any anticipated distributions) is at or above the market price, and forecast risk-adjusted returns are attractive relative to alternative investments.

SECTOR UNDERPERFORM – Investors are advised to sell the security or hold alternative securities within the sector. Stocks in this category are expected to underperform relative to their sector. The category also represents stocks with unattractive forecast returns relative to alternative investments.

TENDER – The analyst is recommending that investors tender to a specific offering for the company’s stock.

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Risk Profile Parameters – Oil and Gas Sector

Forecast Risk: *High* – Haywood forecasts are below guidance. The Company has a history of missing targets and/or Haywood expects guidance to be lowered. Limited hedging increases commodity risk beyond peers. To raise expectations requires higher commodity prices or production that is ahead of guidance. *Moderate* – Haywood forecasts are generally in line with guidance. The Company has a history of meeting or exceeding guidance. Forecasts are consistent with current commodity pricing and production guidance. Hedging practices are in line with peers. *Low* – Haywood forecasts exceed guidance. The Company has a history of meeting or exceeding guidance. Forecasts allow for modestly lower commodity pricing or production levels. Commodity hedging lowers volatility relative to peers.

Financial Risk: *High* – The capital expenditure program in the current year or the next year of the forecast is not fully funded but requires additional debt and/or equity financing. This categorization does not necessarily predict whether the additional funds will be raised. *Moderate* – The capital expenditure program in the current year or the next year is fully funded with cash flow and limited debt. *Low* – The capital expenditure program in the current year or the next year is fully funded with cash flow and no new debt.

Political Risk: *High* – Properties are located in an area with limited petroleum industry activity or infrastructure. An environment unfriendly to the industry makes obtaining permits to drill or produce hydrocarbons challenging. Significant government or local opposition exists. *Moderate* – Properties are located in an area with minimal petroleum industry activity or infrastructure. An environment friendly to the industry makes obtaining permits relatively straightforward. All levels of government are considered indifferent to hydrocarbon activity. *Low* – Properties are located in an area with established petroleum exploration and development activity. Oil and gas Production Sharing Agreements or Exploration Permits are in hand. Government at all levels supports the sector.

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