

Candax Energy Inc.¹ (CAX-T, \$0.71)

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

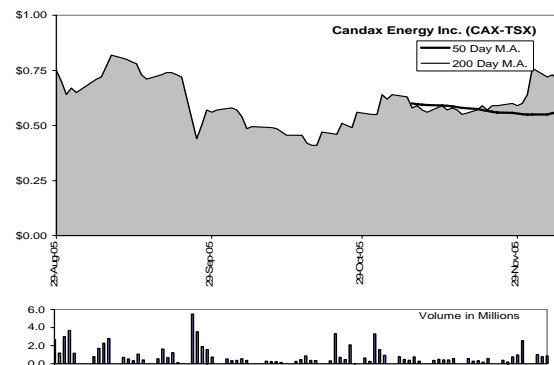
Rating	SECTOR OUTPERFORM
	(SPECULATIVE)
Target Price	\$1.25

Current Price	\$0.71
Return (incl. dividend)	76%
52-Week High / Low	\$0.93 / \$0.39
Shares O/S	130.7M (basic) / 183.1M (F/D)
Market Capitalization	\$95.4 million
Enterprise Value	\$79.9 million
Daily Volume	N/A
Currency	C\$ unless noted
Company CEO	Michael Wood
Company Web Site	www.candax.com

Financial Forecast	2004	2005E	2006E	'06/'05
Liquids (bbl/d)		583	1,900	226%
Natural Gas (mmcf/d)		1.8	4.4	149%
Total (boe/d)		875	2,629	200%
% Liquids		67%	72%	9%
Cash Flow (\$M)		7.0	33.7	382%
F/D CFPS		\$0.06	\$0.18	226%
F/D EPS		(\$0.01)	\$0.09	(1346%)
Capital Expenditures (\$M)		50.7	25.0	
Net Debt (\$M)		(17.5)	(26.3)	50%
WTI (US\$/bbl)		\$57.00	\$60.00	5%
AECO (\$/GJ)		\$7.58	\$8.30	9%
Valuation Parameters				
Price/CFPS (multiple)		12.9	4.0	(69%)
Price/EPS (multiple)		(97.8)	7.8	(108%)
EV/boe/d		\$91,314	\$30,389	(67%)

Source: Candax Energy and Haywood Securities

Price Performance



Source: Bloomberg

Mitsubishi Farm-in Final Agreement, Chaal-1 to Spud Mid-January

Agreement with Mitsubishi Corporation signed

Candax's previously announced farm-out of a 20% interest in the Chaal Permit to Mitsubishi Corporation has now been officially signed. Mitsubishi Corporation is paying a maximum of US\$8.0 million to earn a 20% interest in the Permit, covering almost 300,000 acres in Tunisia. Candax retains a 60% interest in the Chaal Permit and is the operator.

Chaal-1 spud date estimated for mid-January 2006

Candax is the operator of this 4,500-metre well which is twinning a gas discovery drilled in 1963. With a rig already under contract for Chaal-1, the CTF-06 rig will move to the well site of Chaal-1 as soon as it completes its current operations in southern Tunisia.

Chaal-1 targeting previously tested gas accumulation

The Chaal-1 well is planned to twin a well drilled in 1963 which tested gas at maximum rates of approximately 3.0 mmcf/d. The discovery well identified 150 metres of hydrocarbon column.

Success means an immediate second well

Candax has the rig for one well, plus an option for a second well. Should Chaal-1 discover gas, Candax intends to drill a second well to delineate the size of the gas pool. Current reserves evaluation gives the pool a total of 60 bcf of proven plus probable reserves. However, the potential size of the pool could be 200 bcf to as much as 800+ bcf.

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.

Valuation – Our target price of \$1.25 represents our estimate of the Company's risked current net asset value as well as the \$0.25-per-share impact of one successful exploration prospect on its Chaal Permit in Tunisia. However, we note that based on 2006 production and fully diluted CFPS, the target price represents a 6.8x multiple, well within the range of international junior companies that trade at as much as 10x fully diluted CFPS.

Catalysts – Our 2006 forecast is based on the successful work at El Bibane, with an expected oil production rate limited by gas consumption at the Company's Société d'Electricité El Bibane (SEEB) electrical power-generation facility. Better than expected production results or exploration success would have a positive effect on our view of Candax.

Industry & Company Profile	Revisions, Date of Record	Risk Profile	Moderate
Oil and Gas – Candax is a junior oil and gas exploration company focused on oil and natural gas in North Africa and the Middle East.	Rating – New, November 2, 2005 Target – New, November 2, 2005 Forecast – New, November 2, 2005	Forecast Risk Financial Risk Valuation Risk Political Risk	Moderate Moderate Moderate Low

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

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

Mitsubishi Agreement Signed

Candax confirmed that it has signed the final agreement with Mitsubishi Corporation for the farm-out in the Chaal Permit. The arrangement, as originally defined by the late October Heads of Agreement, has Mitsubishi farming in for a 20% interest on the Chaal Permit in Tunisia. Candax will retain a 60% interest in the Permit and act as the licence operator, with Mitsubishi committing to spend a maximum of US\$8.0 million to drill the Chaal-1 well. Mitsubishi has an option to acquire a further 5% interest in the Permit prior to the drilling of a second well on Chaal subject to certain unspecified conditions.

Chaal-1 is expected to spud mid-January. The CTF-06 rig is already under contract to drill Chaal-1, and Candax has an option to drill a second well. The rig will move into position as soon as it completes its current operations in southern Tunisia. The rig release date is not yet firm, but it is expected that the well will spud near the middle of January. Candax and Mitsubishi are drilling a twin of a well drilled in 1963 that tested gas and condensate from a 150-metre hydrocarbon section on the Permit. The well is being drilled to properly evaluate the production potential of the hydrocarbon column. The size of the prize could range from 60 bcf to as much as 844 bcf of possible reserves over a prospect which extends across as much as 300 square kilometres. Total drilling time should be 35 days to 40 days.

Elsewhere in Tunisia, Candax's plans are underway to redevelop the El Bibane field starting early in 2006. Plans are proceeding to drill the second horizontal producer as well as re-drilling the current producer and a third well to be used for gas reinjection. In addition, jackets will be constructed for all three offshore wells, and a new compressor and gas line will be used to reinject gas not consumed by the SEEB power plant.

Valuation

Candax's share price saw a significant drop when the announcement was made that efforts to restart the El Bibane field were unsuccessful. The Company's share price dropped almost 40%, reducing its market capitalization by \$36 million as investors reacted to this news. However, we note that as the Company approaches two significant drilling events in Tunisia, the share price has recovered somewhat.

While the shut-in of the El Bibane field has temporarily reduced the Company's cash flow, we do not believe it has affected the reserves base. In the Company's engineering report, the engineers estimate that the El Bibane #3 well, with artificial lift installed, will be capable of recovering an additional 0.7 million barrels of oil over the next five or more years. Note that the well already produced approximately 3.1 million barrels to December 31, 2004.

Therefore, after discussing the issue with management and reviewing the engineering and geology of the El Bibane field, we conclude that the value of the Company remains intact.

In the following table, we summarize a series of calculations that reflect the estimated net asset value for the Company. We note that the last reserves report was done on December 31, 2004, at a time when prices were much lower than at present, and reserves reports were compiled using future price curves not representative of the current view. We have included the original reserves report data, which have been adjusted for Candax's revised Chaal Permit interest of 60%, and two price scenarios using our current price outlook (2005 US\$57/bbl, 2006 US\$ 60/bbl, and 2007 US\$ 55/bbl), plus a long-term price as noted. As well, we have included Candax's comparative calculation of NAV using its price outlook, also adjusted for the revised working interest in the Chaal Permit.

Net Asset Value

Estimated Net Asset Value (Summary)	Net Reserves Dec 31, 2004 (Mboe)	Commodity-Price Scenarios			
		Dec 31/04	US\$50/bbl	US\$45/bbl	Candax
		NPV10% Value (C\$M)	NPV10% Value (C\$M)	NPV10% Value (C\$M)	NPV10% Value (C\$M)
Tunisian Assets (Centurion acquisition - Ryder Scott Report)*	5.1	38.3	84.9	78.3	55.0
Chaal Permit (Glendower International Limited Report)	6.0	11.3	33.0	30.4	29.6
Cash in Bank	0.0	25.0	25.0	25.0	25.0
	11.1	\$74.6	\$142.9	\$133.7	\$109.6
Shares Outstanding					
Basic	130.7				
Fully Diluted	183.2				
Net Asset Value per Share					
Basic		\$0.57	\$1.09	\$1.02	\$0.84
Fully Diluted		\$0.73	\$1.10	\$1.05	\$0.92
41.3 Million Warrants @ \$1.20/Share = \$49.6M					
11.2 Million Options @ \$0.80/Share = \$9.0M					

* Note that the Centurion assets were evaluated in US\$ and converted at our current exchange rate of \$0.83.

Source: Candax Energy and Haywood Securities

Based on the above summary, estimates of net asset value range from \$0.84 to \$1.09 per basic share. We note that under the current commodity-price scenario, the assumptions used generate little difference in NAV, owing to the impact of high prices used over the next three years.

However, we note the potential for upside to this evaluation based on the size of the Chaal Permit and future exploration potential. In our view, unexplored risked upside potential on the Chaal Permit should have a value equivalent to the reserves value assigned to the known discovery on the block (the ABK wells). This value represents approximately \$30 million or \$0.25 per basic share. Should the possible reserves, up to 844 bcf, associated with the ABK wells be found to be real, the impact on Candax could result in a doubling of the Company's asset value—significantly higher than our risked reserves assumption.

Our target price represents our estimation of the net asset value of the current assets in the Company. Using \$1.00 per basic share from existing reserves and an incremental \$0.25 per share for undetermined exploration upside potential on the Chaal Permit, we establish a 12- to 18-month target price of \$1.25. We note, however, that exploration drilling on the Chaal Permit, as well as other potential opportunities, will result in share-price volatility—of which investors should be mindful along with the likely short-term buying or selling opportunities presented.

For comparative purposes, we are including a table of international oil and gas producers. While 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> ¹ CAX-T	<u>PanOcean</u> ^{1,2,4,6} POC.SV.B-T (US\$ except share & target price)	<u>TransGlobe</u> ¹ TGL-T US\$ except share & target price)
Production (2006 estimate)			
Oil and NGL (bbl/d)	1,900	15,001	4,950
Natural Gas (mmcf/d)	4.4	0.0	7.6
Total (boe/d)	2,629	15,001	6,217
Share Price (Dec 7/05)	\$0.71	\$27.64	\$6.40
2006 F/D CFPS	\$0.18	\$5.97	\$0.85
Current P/CF Multiple (times)	4.0	3.8	6.3
Target Price	\$1.25	\$50.00	\$9.00
Target P/CF Multiple (times)	6.8	7.0	8.8
Current Shares Outstanding (millions)	130.7	24.7	58.0
F/D Shares Outstanding (millions)	183.1	26.8	60.9
2006 Cash Flow (\$M)	34	152	52
2006 Capital Expenditures (\$M)	25	112	45
2006 Net Debt (\$M)	(26)	(7)	1
Enterprise Value (\$M)	80	547	288
Current EV / boe/d	\$30,389	\$36,441	\$46,269
Target EV / boe/d	\$52,130	\$80,995	\$82,716

Source: Company data and Haywood Securities

Candax Energy Ltd. (CAX-T)

Rating:	SECTOR OUTPERFORM (SPECULATIVE)		One-Year Target Price:	\$1.25
Current Price	\$0.73		Market Capitalization (\$M)	95.4
Current Shares Outstanding (millions)	130.7	<u>Dilution</u>	Current Net Debt (est) (\$M)	<u>(15.5)</u>
Fully Diluted Shares Outstanding (millions)	183.1	40.1%	Enterprise Value (\$M)	<u>79.9</u>
Book Value (\$M)	66.4		EV / BV (multiple)	1.2

Production	2005E	2006E	2006/2005
Liquids (bbl/d)	583	1,900	226%
Natural Gas (mmcf/d)	1.8	4.4	149%
Total (boe/d)	875	2,629	200%
Percent Liquids	67%	72%	9%
Percent Natural Gas	33%	28%	(17%)
Revenue (\$M)	13.1	47.5	261%
Cash Flow (\$M)	7.0	33.7	382%
CFPS Basic	\$0.10	\$0.26	150%
CFPS Fully Diluted	\$0.06	\$0.18	226%

CFPS Sensitivity		\$/FD Share	% of CF
Oil (US\$1.00/bbl)		\$0.004	1%
Gas (\$0.25/mcf)		\$0.002	1%
100 bbl/d		\$0.004	2%
1.0 mmcf/d		\$0.006	2%

Earnings (\$M)	(0.5)	17.0	(3497%)
EPS Basic	\$0.01	\$0.13	1495%
EPS Fully Diluted	(\$0.01)	\$0.09	(1346%)
Capital Expenditures (\$M)	50.7	25.0	(51%)
Reinvestment Ratio	724%	74%	(90%)
Net Debt (\$M)	(17.5)	(26.3)	50%
Debt / Cash Flow - Trailing (years)	(2.5)	(0.8)	(69%)

Per BOE Analysis (\$/boe)			
Revenue	\$41.17	\$49.51	20%
Operating Expense	\$8.88	\$5.00	(44%)
Net Operating Revenue	\$31.76	\$39.56	25%
G&A	\$9.39	\$4.17	(56%)
Cash Flow	\$21.23	\$35.16	66%
DD&A	\$13.07	\$13.34	2%
Earnings	(\$2.33)	\$17.76	(861%)

Valuation Parameters			
Current Price / F/D CFPS (multiple)	12.9	4.0	(69%)
Debt-Adjusted CF Multiple	10.7	2.3	(78%)
Target Price / F/D CFPS (multiple)	22.1	6.8	(69%)
Current Price / F/D EPS (multiple)	(97.8)	7.8	(108%)
EV / boe/d	\$91,314	\$30,389	(67%)
Target EV / boe/d	\$166,635	\$52,130	(69%)

Price Assumptions						
Crude Oil WTI (US\$/bbl)	\$31.06	\$41.46	\$57.00	\$60.00	37%	5%
Company Average (C\$/bbl)			\$54.89	\$67.50		23%
AECO (C\$/GJ)	\$6.33	\$6.26	\$7.58	\$8.30	21%	9%
Company Average (C\$/GJ)			\$0.41	\$0.42		1%

Source: 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. **RESEARCH COMMENT** – An analyst comment about an issuer event that does not include a rating. **COVERAGE DROPPED** – Haywood Securities will no longer cover the issuer. Haywood will provide notice to clients whenever coverage of an issuer is discontinued. The termination of coverage will not occur unless clients have been provided with advice relating to positions they may still hold, such as a recommendation to sell their securities.

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.

Valuation Risk: High – The current valuation is at the high end of historic levels and/or at a premium to peers. The valuation reflects continued production growth and/or continuing strong commodity prices or further appreciation. Where applicable, the market capitalization exceeds the NAV by more than 30%. **Moderate** – The current valuation is within historic ranges and generally consistent with peers. The valuation reflects reasonable production growth and/or commodity price appreciation. Where applicable, the market capitalization exceeds the NAV by 15% to 30%. **Low** – The current valuation is at the low end of historic ranges and/or at a discount to peer valuations. The valuation reflects limited production growth and/or no commodity price appreciation. Where applicable, the market capitalization exceeds the NAV by less than 15% or falls below the capitalization.

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This report has been approved by HSUK for the purposes of section 21 of the UK’s Financial Services and Markets Act 2000. If you wish to contact HSUK please email Bonnie Chang at bchang@haywood.com.

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- (b) in the event of a dispute, access to the UK’s Financial Ombudsman Service;
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