

Candax Energy Inc. (CAX-T, \$0.50)

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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
Target Price	\$1.15
Risk	SPECULATIVE

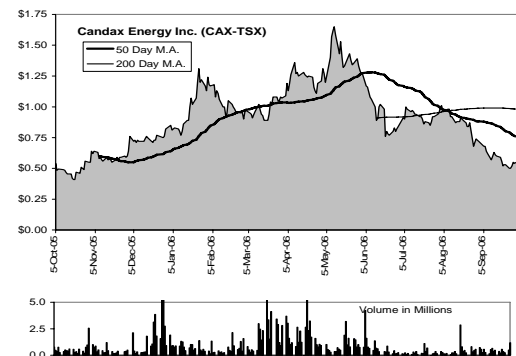
Current Price	\$0.50
Return (incl. dividend)	132%
52-Week High / Low	\$1.73 / \$0.39
Shares O/S	168.9M (basic) / 180.4M (F/D)
Market Capitalization	\$83.6 million
Enterprise Value	\$36.8 million
Daily Volume (3-mo. avg.)	589,000
Currency	C\$ unless noted
Company CEO	Michael Wood
Company Web Site	www.candax.com

Financial Forecast	2005	2006E	2007E	2007E/2006E
Liquids (bbl/d)	587	680	1,685	148%
Natural Gas (mmcf/d)	1.8	0.0	3.6	
Total (boe/d)	879	680	2,292	237%
% Liquids	67%	100%	74%	(26%)
Cash Flow (\$M)	5.3	10.9	35.1	222%
F/D CFPS	\$0.04	\$0.06	\$0.19	229%
F/D EPS	(\$0.03)	\$0.02	\$0.12	702%
Capital Expenditures (\$M)	45.5	25.0	35.0	40%
Net Debt (\$M)	(11.4)	(39.7)	(39.9)	0%
WTI (US\$/bbl)	\$56.54	\$67.50	\$65.00	(4%)
AECO (\$/GJ)	\$8.37	\$6.67	\$7.51	13%

Valuation Parameters	2005	2006E	2007E	2007E/2006E
Price/CFPS (multiple)	12.9	8.4	2.5	(70%)
Price/EPS (multiple)	(14.8)	32.9	4.1	(88%)
EV/boe/d		\$54,069	\$16,044	(70%)

Source: Candax Energy and Haywood Securities

Price Performance



Source: Bloomberg

El Bibane Oil Redevelopment – Finally?!?

It appears that the redevelopment of the offshore El Bibane field in Tunisia may finally begin

Candax announced that the drilling barge for Tunisia is expected to be mobilized soon. Support vessels and barges were mobilized to Zarzis, Tunisia, indicating that the jack-up drilling barge mobilization is not far behind. Once the drilling barge arrives in Tunisia, feet will be fitted to the jack-up legs, and a top drive unit attached to the drilling rig, with deployment to the offshore location to follow shortly thereafter.

No production from El Bibane before 2007

While drilling should begin at El Bibane prior to the end of November, production from the first well at EBB-4 is unlikely before the end of 2006. Full field redevelopment should result in full field production starting in late Q1/07. While we are estimating 1,000 bbl/d of production per well, there is potential for production of as much as 2,000 bbl/d per well.

Target and recommendation remain unchanged

Redevelopment of the El Bibane prospect provides Candax with increased cash flow in 2007. However, the upside in this story remains the deep potential from the Company's exploration prospects. The delayed evaluation of the Chaal-1 well leaves the upside potential of this prospect in limbo. We note that there will be no definitive determination of the potential of Chaal until H2/07.

Expectations – We expect that the share price of Candax will continue to languish, absent any near-term catalysts. However, commencement of the drilling at El Bibane could provide a small lift to the Company's share price later this year. We would also expect that at some point in the next 6 to 12 months, Candax will be able to close on one of the international production/development projects, but we have not factored this possibility into our valuation or production estimates.

Valuation – Our target price of \$1.15 includes the engineering value of 36 bcf proven plus probable net to Candax from Chaal, plus the Company's current assets. In the event that Chaal ultimately proves to be uneconomic, we still believe that our current valuation of Candax is supported by the Company's remaining assets and cash-flow prospects.

Catalysts – Our 2007 forecast is based on 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	Revisions, Date of Record	Risk Profile	Moderate - High
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.	Rating – SECTOR OUTPERFORM from Under Review, June 21, 2006 Target – \$1.15 from Under Review, June 21, 2006 Forecast – Revised 2006 and 2007 production forecast, October 4, 2006	Forecast Risk Financial Risk Valuation Risk Political Risk	High Moderate Moderate Low

Please see rating structure, important disclosures, risk profile parameters, disclaimers, and notes on pages 7 to 10 of this report.

Candax Energy Inc. (CAX-T)

Rating: SECTOR OUTPERFORM	Risk: SPECULATIVE	One-Year Target Price:	\$1.15
Current Price	\$0.50	Market Capitalization (\$M)	83.6
Current Shares Outstanding (million)	168.9	<u>Dilution</u>	Current Net Debt (est.) (\$M)
Fully Diluted Shares Outstanding (million)	180.4	6.8%	<u>(46.8)</u>
Book Value (\$M)	105.5	Enterprise Value (\$M)	<u>36.8</u>
		EV / BV (times)	0.3

Production	2004	2005	2006E	2007E	2006E / 2005	2007E / 2006E
Liquids (bbl/d)		587	680	1,685	16%	148%
Natural Gas (mmcf/d)		1.8	0.0	3.6	(100%)	
Total (boe/d)		879	680	2,292	(23%)	237%
Percent Liquids		67%	100%	74%	50%	(26%)
Percent Natural Gas		33%	0%	26%	(100%)	
Revenue (\$M)		12.9	17.9	45.4	39%	154%
Cash Flow (\$M)		5.3	10.9	35.1	105%	222%
CFPS Basic		\$0.06	\$0.07	\$0.21	16%	180%
CFPS Fully Diluted		\$0.04	\$0.06	\$0.19	54%	229%
				<u>\$/FD Share</u>	<u>% of CF</u>	
CFPS Sensitivity	Oil (US\$1.00/bbl)			\$0.003	1%	
	Gas (\$0.25/mcf)			\$0.001	1%	
	100 bbl/d			\$0.004	2%	
	1.0 mmcf/d			\$0.006	3%	
Earnings (\$M)		(1.5)	2.8	21.7	(288%)	670%
EPS Basic		(\$0.02)	\$0.02	\$0.13	(207%)	564%
EPS Fully Diluted		(\$0.03)	\$0.02	\$0.12	(145%)	702%
Capital Expenditures (\$M)		45.5	25.0	35.0	(45%)	40%
Reinvestment Ratio		856%	229%	100%	(73%)	(56%)
Net Debt (\$M)		(11.4)	(39.7)	(39.9)	250%	0%
Debt / Cash Flow - Trailing (years)		(2.1)	(3.6)	(1.1)	70%	(69%)
Per BOE Analysis (\$/boe)						
Revenue		\$40.15	\$72.08	\$54.25	80%	(25%)
Operating/Transportation Expense		\$8.36	\$11.72	\$5.00	40%	(57%)
Net Operating Revenue		\$31.79	\$57.32	\$43.83	80%	(24%)
G&A		\$15.15	\$16.12	\$5.26	6%	(67%)
Cash Flow		\$11.30	\$41.00	\$41.98	263%	2%
DD&A		\$12.94	\$18.92	\$15.00	46%	(21%)
Earnings		(\$7.95)	\$7.01	\$25.99	(188%)	271%
Valuation Parameters						
Current Price / F/D CFPS (multiple)		12.9	8.4	2.5	(35%)	(70%)
Debt-Adjusted CF Multiple			3.8	1.4		(64%)
Target Price / F/D CFPS (multiple)		29.9	19.5	5.9	(35%)	(70%)
Current Price / F/D EPS (multiple)		(14.8)	32.9	4.1	(322%)	(88%)
EV / boe/d			\$54,069	\$16,044		(70%)
Target EV / boe/d			\$227,155	\$67,355		(70%)
Price Assumptions						
Crude Oil WTI (US\$/bbl)	\$41.46	\$56.54	\$67.50	\$65.00	19%	(4%)
Company Average (C\$/bbl)		\$56.93	\$71.61	\$72.89	26%	2%
AECO (C\$/GJ)	\$6.26	\$8.37	\$6.67	\$7.51	(20%)	13%
Company Average (C\$/GJ)		\$0.41	\$0.41	\$0.39	(1%)	(3%)

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 SECTOR OUTPERFORM rating of Candax Energy Inc. (CAX-T) and our 12-month target price of \$1.15 per share.

Revisions to Estimates

Candax provided an update to activities in Tunisia on October 3, 2006. The Company issued a press release as well as gave a presentation at the Canadian Oil Patch Investor's Conference (COPIC) in Toronto. Redevelopment of the El Bibane field is further delayed from our previous estimates, but the mobilization of the offshore drilling barge appears to be in sight. As a result, we are revising our estimates as shown below. However, we note that there appears to be a better degree of certainty in our revision as the drilling barge is expected to mobilize to Tunisia shortly, perhaps as soon as next week.

Revision of 2006 and 2007 Estimates

	2006E				2007E			
	Revised	Previous	Change	%	Revised	Previous	Change	%
Production								
Liquids (bbl/d)	680	1,000	(320)	(32%)	1,685	2,200	(515)	(23%)
Gas (mmcf/d)	0.0	0.5	(0.5)	(100%)	3.6	4.5	(0.9)	(19%)
Total (boe/d)	680	1,083	(403)	(37%)	2,292	2,950	(658)	(22%)
Sales Price								
Liquids Price (\$/bbl)	\$71.61	\$72.79	(\$1.18)	(2%)	\$72.89	\$72.10	\$0.79	1%
Gas (\$/GJ)	\$0.41	\$0.40	\$0.01	3%	\$0.39	\$0.41	(\$0.02)	(4%)
Equivalent (\$/boe)	\$72.08	\$68.15	\$3.94	6%	\$54.25	\$54.43	(\$0.17)	(0%)
Financials								
Cash Flow (\$M)	\$10.9	\$19.4	(\$8.5)	(44%)	\$35.1	\$45.6	(\$10.5)	(23%)
F/D CFPS	\$0.06	\$0.10	(\$0.05)	(44%)	\$0.19	\$0.25	(\$0.06)	(23%)
Earnings (\$M)	\$2.8	\$8.9	(\$6.0)	(68%)	\$21.7	\$28.6	(\$6.8)	(24%)
F/D EPS	\$0.02	\$0.05	(\$0.03)	(69%)	\$0.12	\$0.16	(\$0.04)	(24%)
Net Debt (\$M)	(\$39.7)	(\$52.7)	\$13.0	(25%)	(\$39.9)	(\$63.3)	\$23.4	(37%)
Trailing D/CF (multiple)	(3.6)	(2.7)	(0.9)	34%	(1.1)	(1.4)	0.3	(18%)
Capital Expenditures (\$M)	\$25.0	\$25.0	\$0.0	0%	\$35.0	\$35.0	\$0.0	0%

Source: Haywood Securities

Corporate Update

In conjunction with the Company's presentation at the Toronto COPIC Conference, Candax indicated that the main drilling barge for the redevelopment of the El Bibane field offshore Tunisia should be mobilized shortly. Management confirmed that the majority of the necessary barge work has been completed in the shipyard in Montenegro. Candax has also mobilized support barges to the seaport of Zarzis in Tunisia which would subsequently be mobilized to the El Bibane offshore drilling location. Once the main drilling barge is mobilized to Zarzis, feet must be attached to the legs of the barge—a non-critical operation that should only take a few days, as it does not require a shipyard or dry-dock to make the attachment. Assuming that the drilling barge is mobilized to Zarzis by mid-October, it should be ready to drill before the end of November.

While we have heard this before (several times!), it would appear that on this occasion it may be true. It is our understanding that the drilling barge jack-up legs are now working—their modification was previously the primary reason for the delay in mobilizing the jack-up barge. On arrival in Zarzis, Tunisia, the top-drive unit will be fitted to the drilling rig and deployed to the location.

Candax intends to drill a total of three wells at El Bibane. The first well at El Bibane (EBB-4) is a new horizontal drilling location on the northwest flank of the El Bibane structure. This well is intended to be brought onstream as soon as possible after drilling and completion, before drilling the remaining two wells. The second well at EBB-3RE is a redrill of the original production well. Recall that this well's horizontal section is being redrilled closer to the estimated location of the current gas-oil contact within the reservoir. The final well at EBB-5 is a vertical well to be drilled as a natural gas injection well.

Included in the field redevelopment is the installation of onshore gas compression and separation facilities. The El Bibane field natural gas production is primarily processed in an onshore gas-fired electrical generation facility. However the facility is capable of burning only approximately 6.0 mmcf/d. With the field redevelopment, the two new horizontal wells are expected to produce 20 mmcf/d or more. As a result, Candax will reinject gas into the EL Bibane reservoir. The reinjection will allow Candax to produce the El Bibane oil at optimal production rates without being constrained by gas consumption.

There was no additional news on the Chaal natural gas prospect. Candax and its partners are continuing a technical review of the appraisal and development drilling options available for the Chaal prospect.

Given the time required to investigate and assess the options, then book a drilling date with a rig contractor, we believe it will be H2/07 before Candax returns to the Chaal prospect. While management has given no further indication of the timing of Chaal except as noted above, previous presentations by Candax had indicated that a new rig may be brought into the country to drill at both Chaal and the Company's potential high-impact deep-gas prospect at Ezzaouia. Drilling the deep Triassic prospect at Ezzaouia requires reaching an

agreement with the Tunisian government about a change in the cost-sharing of the well. Should reaching an agreement drive the timing of a new rig for Chaal, we estimate that a further Chaal evaluation well could be delayed until the middle or possibly second half of 2007.

Valuation

Should the Chaal well ultimately prove to be uneconomic, the potential of the prospect would be eliminated, and our value and target price for Candax would decrease marginally. However, until such a possibility is definitely established, now pushed out to 2007, we are maintaining our target price and recommendation. Also, should a prospect size of more than 120 bcf be proven at Chaal, it would cause us to review our target price with a positive view. We also note that while the market is looking for the Chaal prospect as a catalyst to value Candax, our assumption of cash flow in 2007 from the Company's current assets supports our target price.

The redevelopment of El Bibane should soon be underway. Our current production estimates for 2007 include only 1,000 bbl/d from each of the two redeveloped El Bibane wells. Should the production prove to be more in line with management's estimates of as much as 2,000 bbl/d per well, our cash flow per share for 2007 would increase to as much as \$0.35 per fully diluted share. Once El Bibane is placed onstream later this year, a conservative cash-flow multiple could see us with a higher target price.

Valuation Comparison Table

	<u>Candax</u> CAX-T	<u>Oilexco</u> OIL-T (US\$ except Share & Target Price)	<u>TransGlobe</u> TGL-T (US\$ except Share & Target Price)
Production (2007 estimate)			
Oil and NGL (bbl/d)	1,685	30,487	4,450
Natural Gas (mmcf/d)	3.6	0.0	9.0
Total (boe/d)	2,292	30,490	5,950
Share Price (Oct 3, 2006)	\$0.50	\$6.20	\$5.16
2007 F/D CFPS	\$0.19	\$2.45	\$0.93
Current P/CF Multiple (times)	2.5	2.3	5.0
Target Price	\$1.15	\$12.00	\$8.50
Target P/CF Multiple (times)	5.9	4.4	8.2
Current Shares Outstanding (millions)	168.9	195.5	58.7
F/D Shares Outstanding (millions)	180.4	217.0	61.8
2007 Cash Flow (\$M)	35.1	530.5	56.9
2007 Capital Expenditures (\$M)	35.0	250.0	55.0
2007 Net Debt (\$M)	(39.9)	(174.8)	(5.5)
Enterprise Value (\$M)	36.8	1133.1	269.3
Current EV / boe/d	\$16,044	\$37,165	\$45,259
Target EV / boe/d	\$67,355	\$63,377	\$73,783

Source: Company data and Haywood Securities

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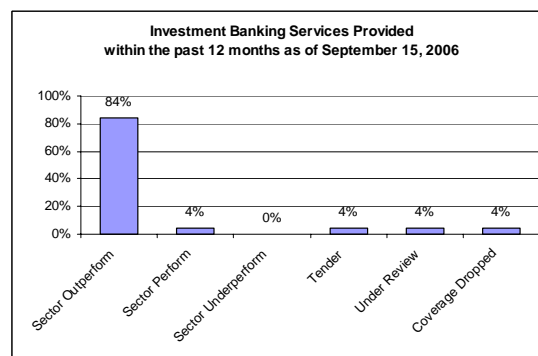
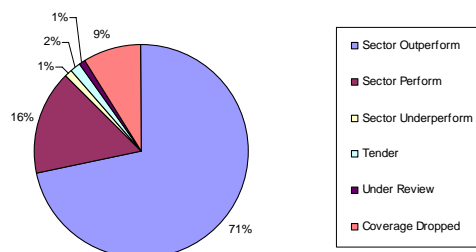
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