

June 1, 2010

Orca Exploration (ORC CN)

Last: C\$4.90

BUY

Target: C\$7.40

WHAT'S CHANGED

	NEW	OLD
Rating	nc	BUY
Target	C\$7.40	C\$6.90
Production 2010E (boe/d) 6:1	nc	5,817
Production 2011E (boe/d) 6:1	nc	6,229
CFPS 2010E (f.d.)	nc	\$0.53
CFPS 2011E (f.d.)	nc	\$0.81

SHARE DATA

Shares o/s (mm, basic/f.d.)	29.5/32.1
52-week high/low	C\$5.43/C\$3.00
Market capitalization (mm)	\$154
Enterprise value (mm)	\$128
Net debt (mm) – 2009A	(\$16.8)
Dividend yield	n/a
Projected return	51%

FINANCIAL DATA

	2009A	2010E	2011E
Oil & NGLs (mb/d)	0.0	0.0	0.0
Natural Gas (mmcf/d)	28.5	34.9	37.4
Total (mboe/d) 6:1	4.8	5.8	6.2
Equivalent growth	20%	22%	7%
Brent (US\$/b)	62.04	79.00	84.00
UK Gas (US\$/mmbtu)	4.16	5.75	6.00
FX rate (USD/CAD)	0.88	0.99	0.95
EPS (f.d.)	\$0.11	\$0.23	\$0.39
CFPS (f.d.)	\$0.43	\$0.53	\$0.81
Net Debt (mm)	(\$16.8)	(\$29.1)	(\$6.3)
Debt/CF	nm	nm	nm
P/CF	11.5x	9.4x	6.1x
P/CF (d'adj'd)	18.7x	13.9x	9.3x

*(In US\$ unless otherwise stated)

Orca adds exploration/appraisal assets to its portfolio

Increasing target price and reiterating our BUY recommendation

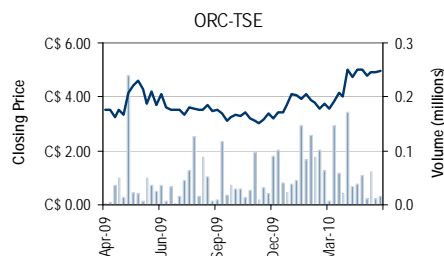
We are increasing our target price to C\$7.40/sh from C\$6.90/sh as Orca earns 15% interest in the Elsa-2 appraisal well and 15% interest in 11 of Petroceltic's existing Adriatic permits in Italy. With an expected return of 51% we are reiterating our BUY recommendation.

Signing of the farm-in agreement

Orca Exploration signed an agreement with Petroceltic International to farm in on PCI's B.R268.RG Permit offshore Italy (PCI 55% WI). The farm-in commits Orca to fund 30% of the Elsa-2 appraisal well up to a maximum of US\$11.5 mm to earn a 15% WI in the permit and also pay 15% of the back costs up to a maximum of US\$0.5 mm. The agreement is subject to regulatory approvals. PCI plans to appraise the Elsa discovery well by drilling and testing the Elsa-2 well. An environmental impact assessment for the Elsa-2 well was submitted to the Italian Ministry for the Environment in August 2009 and is expected to be approved in Q2/10. Appraisal drilling on the Elsa field, which tested 15 degree API oil in the Elsa-1 well and holds 80-170 mmb potential, is expected to commence in September 2010. Further, Orca also has the right to a 15% participating interest in 11 of PCI's existing Adriatic permits.

Changes to our target price

We are updating our EMV to reflect the farm-in and incorporate the Elsa field potential as well as other Italian permits. The Elsa-2 appraisal well is targeting 33 mmboe of gross resources and is included in our target price calculation. We increase our 12 month price target to C\$7.40/sh and with a 51% return maintain our BUY recommendation. Orca continues its active review of new high impact oil opportunities and we expect Orca to have more farm-in activities in the near future. The farm-in agreement positively impacts our valuation as Orca is executing its acquisition plans that allow the company to add more exciting exploration prospects to its stable production and development portfolio. Orca is also balancing its risk by picking the lower risk exploration/appraisal in proven hydrocarbon basin with significant upside.





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Further, Orca also has the right to a 15% participating interest in 11 of PCI's existing Adriatic permits. These include d505BR, d500BR, d499BR, d498BR, d497BR, d496BR, d495BR, d494BR, d493BR, d492BR and d507BR-EL.

CHANGES TO OUR TARGET PRICE

We are updating our EMV to reflect the farm-in and incorporate the Elsa field potential as well as other Italian permits. The Elsa-2 appraisal well is targeting 33 mmb of gross resources and is included in our target price calculation. We value Elsa field's C90 resources at C\$0.68/sh and its C50 potential at C\$0.80/sh. We also include 3 of the 11 Adriatic permits and value d505BR/ d497BR and d493BR at C\$1.06/sh and C\$0.14/sh respectively.



Exhibit 1: Risked Exploration Value

Country	Property/Prospect	Gross Resource (mmboe)	Working Int. (%)	Costs (%)	Well Costs (US\$ mm)	Overall COS (%)	Value/BOE (US\$)	Net Risked Resources (mmboe)	Risked NAV (US\$ mm)	US\$/sh (FD)	C\$/sh (FD)	Unrisked NAV (C\$/sh)
Producing Assets												
Tanzania	SS Main (Proved Producing)	50.1	100%	100%		100%	\$ 3.46	50.1	173.65	5.40	5.35	5.35
								50.1	173.65		5.35	
Risked Upside												
Tanzania	SS Main (Proved Non Prod.)	14.0	100%	100%	4.00	80%	3.46	11.2	38.10	1.19	1.17	1.50
Tanzania	SS Main (Probables)	17.6	100%	100%	5.00	80%	3.46	14.0	47.65	1.48	1.47	1.87
Tanzania	SS West	90.9	100%	100%	5.00	30%	1.71	27.3	43.01	1.34	1.32	4.77
Tanzania	SS Main (Possibles, Contract ext)	56.4	100%	100%	5.00	50%	1.71	28.2	45.64	1.42	1.41	2.97
Tanzania	SS North	28.3	100%	100%	5.00	60%	1.71	17.0	26.92	0.84	0.83	1.48
Italy	Elsa-2	33.0	15%	30%	15.00	40%	\$ 12.47	2.0	22.00	0.68	0.68	1.94
Italy	Elsa (C50 upside)	56.0	15%	30%	55.00	25%	\$ 18.26	2.1	25.97	0.81	0.80	4.82
Italy	Adriatic - Sangiovese (d505BR/d497BR)	180.0	15%	15%	50.00	10%	\$ 15.21	2.7	34.33	1.07	1.06	12.91
Italy	Adriatic - Pampanuto (d493BR)	50.0	15%	15%	50.00	10%	\$ 15.21	0.8	4.66	0.15	0.14	3.59
								105.2	288.28		8.88	
Gross Resources Total		576.3						155.3	461.92	14.37	14.23	41.20
Fully Diluted Shares Outstanding (mm)		32.15										
USD:CAD Exchange Rate		0.99										
Notes												
Estimates of Reserves and Resources are provided by third party engineering firms, management and GMP securities												
Overall COS = Chance of success after taking all risks into consideration including geological risk, political risk, etc												
Value/BOE is calculated from a field model in the specific fiscal regime of the host country after government take, all capex and costs have been removed, and the time value of money is applied												
Risked NAV is equivalent to Expected Monetary Value (EMV). Risked NAV = (Reward * C.o.S.) - [Capital at Risk * (1-C.o.S.)]												
Fully diluted shares outstanding = shares at period end + options + all dilutive securities												
Cost % = the difference (if any) in costs paid versus working interest. Of relevance when farm-outs or farm-ins occur												

Source: Orca Explortion, GMP Estimates

The bulk of Orca's value is very robust and is based on its long life producing Songo Songo gas field, Tanzania. Our core NAV of C\$5.23/sh consists of the proved producing reserves currently supplying the gas market in Dar es Salaam. This more than underpins the current stock price of C\$4.90/sh. In addition, we believe there is substantial additional upside from Songo Songo North and West.

Exhibit 2: Net Asset Value

Net Asset Value Breakdown				
	MMBOE	US\$/BOE	US\$MM	C\$/sh
Production Assets	50.1	3.46	173.65	5.35
Cash/(Net Debt)			16.84	0.53
Other items incl G&A			(20.69)	(0.65)
Core NAV	50.1	3.39	169.80	5.23
<i>Price to NAV (%)</i>				<i>0.94</i>
Option Proceeds			10.55	0.33
Risked Upside	105.2	2.74	288.28	9.06
Risked NAV	155.3	3.02	468.63	14.73
<i>Price to Risked NAV (%)</i>				<i>33%</i>
			Current Stock Prices	C\$ 4.90
			Unrisked	C\$ 46.75
Notes				
Reserves evaluated by McDaniel and Associates Ltd. as of December 31st, 2008.				
Long term Brent flat price is US\$84.00 and UK Gas price is US\$10.00/mmBtu.				
All asset values are NPV10 After Tax and in USD unless noted.				
Two years of G&A are deducted to ensure 'going concern' costs are captured.				

Source: Orca Exploration, GMP Estimates

Exhibit 3: Target Price

<u>Target Price Calculation</u>	
Orca Exploration Group	C\$/sh
Production Assets	5.35
Cash/(Net Debt)	0.53
Undeveloped Assets	-
<u>Other Items incl G&A</u>	<u>(0.65)</u>
Core NAV	5.23
Risked Upside - Included from EMV Sheet	
SS Main (Proved Non Prod.)	1.17
Elsa-2	0.68
<u>Option Proceeds</u>	<u>0.33</u>
Sum of Parts	7.41
TARGET PRICE	7.40
Share Price	4.9
Expected Return	51.2%
USD:CAD Exchange Rate	0.99
<u>Notes:</u>	
Target set off the Proved Reserves for SongoSongo (producing and non-prod)	

Source: Orca Exploration, GMP Estimates

We increase our 12 month price target to C\$7.40/sh and with a 51% return maintain our BUY recommendation. Orca continues its active review of new high impact oil opportunities and we expect Orca to have more farm-in activities in the near future. The farm-in agreement positively impacts our valuation as Orca is executing its acquisition plans that allow the company to add more exciting exploration prospects to its stable production and development portfolio. Orca is also balancing its risk by picking the lower risk exploration/appraisal in proven hydrocarbon basin with significant upside.



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FOCUS BUY. Small cap stocks (defined as stocks with less than \$500 million market capitalization) in this category have a total return potential (including dividends payable) of greater than 25% and large cap stocks a greater than 20% total return potential, as well as superior qualitative and timing characteristics.

BUY. These stocks will have 15% or greater (small cap) or 10% or greater (large cap) total return potential.

SPECULATIVE BUY. These stocks will have a 30% or greater total potential return and they will have a speculative component which could be material to the return expectations.

HOLD. Small cap stocks ranked Hold will have a total return potential of 0% to 15%; large cap stocks ranked Hold will have a total return potential of 0 to 10%; and stocks that have a speculative component which could be material to the return expectations ranked HOLD will have a total return potential of 0% to 30%.

REDUCE. Companies ranked Reduce have a negative potential total return.

FOCUS REDUCE. Companies ranked Focus Reduce have a significant negative potential total return and materially compromised qualitative and timing characteristics.

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