

ORCA EXPLORATION GROUP INC.

ORC.B-TSX V: \$4.40 — BUY

TARGET PRICE: \$6.25; PROJECTED RETURN: 42%

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Orca Completes \$19 Million Rights Offering

EVENT – Completion of Financing

Orca issued 4,955,687 Class B shares at a price of \$3.90 per share for total gross proceeds of \$19.3 million.

HIGHLIGHTS – Proceeds to Fund Exploration Drilling

Exploration in Tanzania and Italy: The primary use of proceeds will be to fund the drilling of the **Songo Songo West (SSW)** exploration prospect in latter half of 2011. Independent engineering firm McDaniel & Associates Consultants Ltd. assigned an unrisksed recoverable resource estimate of 551.6 bcf to the prospect. Success could more than double Orca’s 2P reserves of 490.2 bcf. In addition, a portion of the proceeds has been allocated to the drilling of the **Elsa-2 appraisal well** in Italy. Orca will fund 30% of the well to earn a 15% working interest in the permit. Management’s internal median estimate is that the field could contain approximately 450 million barrels of original oil in place. Drilling was originally scheduled for Q4/10, but has been delayed by a proposal by the Italian Minister of Environment to prohibit drilling within 5 miles of the coastline. Drilling will commence once the legislative issues concerning offshore drilling have been resolved.

VALUATION – Minor Change

With the dilution of the equity financing, our core NAV decreases from \$10.50/fd share to \$9.55/fd share and our risked NAV decreases from \$13.21/fd share to \$12.29/fd share.

RECOMMENDATION – BUY on Exploration Potential

Post financing, we estimate that Orca has positive working capital of \$44 million. Combined with cash flow generated from its Songo Songo natural gas field in Tanzania, Orca has ample capital to fund the SSW exploration well and the Elsa-2 appraisal well. We maintain our **BUY** recommendation on the B shares and we have lowered our target price from \$6.60 to \$6.25, equivalent to a 0.5x multiple of our new risked NAV.

VALUATION CATALYST – Commencement of Exploration Drilling

- Spud of the SSW exploration well.
- Spud of the Elsa-2 appraisal well.
- Announcement of a new oil exploration project.

Financial Metrics (C\$)

Shares O/S (mm)*:	34.4	Mkt. Cap (\$ mm):	\$151.6
FD Shares (mm):	37.2	W.Capital (\$ mm)**:	\$44.0
Price:	\$4.40	Ent.Value (\$ mm):	\$107.6
52-Wk High:	\$5.43	52-Wk Low:	\$3.00

* 32.7 million Class B shares and 1.75 million Class A shares.

**Estimated working capital in C\$ as at October 12, 2010

FY December 31 2008A 2009A 2010E 2011E

Production

Liquids (bbl/d)	-	-	-	-
Gas (mmcf/d)	23.7	28.5	35.0	35.5
Boe/d (6:1)	3,945	4,756	5,830	5,925

Financials (US\$)

Cash Flow (US\$m)	\$9.8	\$12.7	\$18.9	\$25.1
CFPS (FD)	\$0.33	\$0.43	\$0.60	\$0.70
EV/DACF	14.6x	11.4x	6.1x	5.1x
D/CF	na	na	na	na

2010 Quarters

	Q1A	Q2E	Q3E	Q4E
Liquids (bbl/d)	-	-	-	-
Gas (mmcf/d)	34.9	33.0	35.0	37.0
Boe/d (6:1)	5,817	5,500	5,833	6,167
CFPS (FD) US\$	\$0.14	\$0.16	\$0.16	\$0.13

Target Valuation Parameter

0.5x Risked NAV; 7.4x 2011 EV/DACF



Courtesy of BigCharts.com

Key Risks

Expansion of the processing and transportation infrastructure projects will require Songas Limited and EWURA to reach an agreement on terms. Any delays in an agreement could impact Orca’s ability to achieve our forecasts

Corporate Profile

Orca Exploration Group Inc. (www.orcaexploration.com) is an international oil and gas exploration and production company that produces and markets natural gas in Tanzania.

Multiple Share Structure

Two-share structure: 1.75 million Class A shares are outstanding with 20 votes each, and 34.5 million Class B single-voting shares. The Chairman & CEO of Orca holds 99.5% of the Class A shares.

Orca Exploration Group Inc.
ORC.B

Share Data and Market Value		Price and Target			
Basic Shares (mm)	34.4	Close C\$:		\$4.40	
Diluted Sh. (Treasury)	35.7	52-Week High C\$:		\$5.43	
Fully Diluted (mm)	37.2	52-Week Low C\$:		\$3.00	
Market Cap. (C\$ mm)	151.6	Target Price C\$:		\$6.25	
Enterprise Value (C\$ mm)	107.6	Potential Return:		42.0%	
Net Debt (W.C.) (C\$ mm)	(44.0)	Risky NAV		0.5x	
Production		2008A	2009A	2010E	2011E
Oil & Liquids	bbl/d	-	-	-	-
Natural Gas	mmcf/d	23.7	28.5	35.0	35.5
Boe/d	6:1	3,945	4,756	5,830	5,925
Production Growth	%	(33%)	21%	23%	2%
Percentage Natural Gas	%	100%	100%	100%	100%
Production/Million Shares		114.5	161.8	190.4	172.0
Cash Flow & Earnings (US\$)		2008A	2009A	2010E	2011E
Cash Flow	\$ mm	9.8	12.7	18.9	25.1
Cash Flow/Share	\$/share	0.33	0.43	0.62	0.73
Cash Flow/FD Share	\$/share	0.31	0.41	0.58	0.70
CF Per Share Growth	%	9%	30%	43%	19%
\$/Barrel of Oil Equivalent (US\$)		2008A	2009A	2010E	2011E
Revenue	\$/boe/d	24.12	21.59	23.19	21.02
Operating Costs	\$/boe/d	1.03	1.62	1.64	1.50
G&A	\$/boe/d	8.52	5.96	5.16	5.55
Cash Flow	\$/boe/d	6.77	7.30	8.87	11.60
Valuation Metrics (C\$)		2008A	2009A	2010E	2011E
FD Cash Flow Multiple		13.3x	10.2x	7.4x	6.3x
EV/DACF Multiple		14.6x	11.4x	6.1x	5.1x
EV/Production	C\$/boe/d	27.3	22.6	18.5	18.2
EV/boe reserves	C\$/boe	1.31	1.32		
Commodity Price		2008A	2009A	2010E	2011E
Industrial	US \$/mcf	\$11.97	\$8.36	\$8.50	\$8.75
Power	US \$/mcf	\$2.37	\$2.40	\$2.40	\$2.40
Exchange Rate	US \$ per C\$	1.06	1.14	0.98	1.00
Capex and Capital Structure		2008A	2009A	2010E	2011E
Capex/Cash Flow	%	390%	42%	103%	140%
Weighted Average Basic	mm	34.5	29.4	30.6	34.5
Dilutive Shares	mm	31.0	31.0	32.3	36.0
Market Cap	C\$ mm	151.6	129.4	134.7	151.6
Enterprise Value	C\$ mm	143.2	114.5	99.8	127.3
Year-end Net Debt (WC)	C\$ mm	(8.4)	(14.8)	(34.9)	(24.3)
Net Debt/Cash Flow		na	na	na	na
Net Asset Value Estimate		Reserve Estimate		12/31/2007	
	(C\$ thous ands)	Proven	79%	(mboe)	
Reserves (P + P)*	341,040	Probable	21%	64,150	
Net Debt (W. Capital)	44,000	P+P		81,700	
Other Assets	-	Reserve Life Index			
Other Liabilities	-	Production			
Net Asset Value	297,041		2010	2011	
NAV/Share	\$9.90	Proven	30.1	29.7	
NAV/FD Share	\$9.55	P+P	38.4	37.8	
Risky Exploration (C\$)	\$84,180				
Risky NAV/share (C\$)	\$11.07				
Risky NAV/FD share (C\$)	\$12.29				

Figure 1. Fundamentals & Key Ratios

Source: Company reports, Mackie Research Capital

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