Surge Energy

Surge Energy Inc. Announces 2020 Budget

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CALGARY, Dec. 12, 2019 /CNW/ - Surge Energy Inc. ("Surge" or the "Company") (TSX: SGY) is pleased to announce its budget guidance for 2020 as approved by the Company's Board of Directors.



2020 BUDGET – DEFENSIVE AND SUSTAINABLE

Surge's disciplined 2020 capital expenditure budget reaffirms the Company's commitment to free cash flow generation and debt reduction.

Surge's Board of Directors has approved a defensive, sustainable budget for 2020 at US$56.50 WTI flat pricing (less than current strip), that:

1. Delivers production of 21,000 boepd (86 percent oil) in 2020, for total capital of $98.5 million;
2. Continues to pay down the Company's debt by more than $20 million;
3. Increases Surge's debt adjusted production per share by 3.1 percent[1] - cost effectively;
4. Improves Surge's all-in payout ratio to 86 percent[2];
5. Delivers the Company's dividend – using only 19.3 percent of 2020 adjusted funds flow[2];
6. Maximizes cash flow through a returns-focused, efficient, capital expenditure program;
7. Maintains operational flexibility to adjust to a changing commodity price environment; and
8. Provides disciplined capital allocation, with cash flow strategically allocated between capital projects, debt repayment, and the payment of Surge's dividend.

In summary, as a result of Surge's low 23 percent annual corporate decline, and by focusing drilling operations to the top tier production efficiencies associated with the Company's core Sparky play, Surge can deliver average production of 21,000 boepd in 2020 – spending $36.5 million less exploration and development capital than Surge's 2019 budget of $135 million.

On this basis, Surge is currently providing an attractive annual dividend yield of more than 9.5 percent, as well as a free cash flow yield of more than 6 percent, based on the Company's 2020 budget.

Details relating to the 2020 budget are set forth below.

OVERVIEW OF CURRENT BUSINESS ENVIRONMENT

Current pricing fundamentals for crude oil continue to improve. The forward one-year strip price for crude oil is currently over US$57 WTI per barrel. Spot oil prices are over US$59 WTI per barrel, and continue to show volatility in relation to various shorter-term events, including improving US/China trade talks, continued unrest in the Middle East (i.e. the Saudi oil installation bombing), OPEC production cuts, US and Canadian rig counts dropping, and the slowing of US shale oil production growth estimates.

On a macro scale, the long-term demand for crude oil continues to move upward. The IEA projects that world crude oil demand growth in Q3/19 was up 1.1 million barrels per day over the same period in 2018 (i.e. total crude oil demand is over 100 million barrels a day). Growth in world oil demand in 2020 is now projected to be up another 1.2 million barrels per day[3].

POSITIONING FOR SUCCESS IN 2019

In 2019, Surge anticipates spending approximately $15-16 million less than the Company's exploration and development capital budget guidance of $135 million, as management strategically chose to drill 21 percent less wells (12 wells), and to continue to pay down debt.

Despite drilling 21 percent fewer wells than budgeted, in 2019 Surge will still exit the year with production of approximately 21,000 boepd (85 percent oil).

Through a combination of primarily non-core asset sales and reduced capital spending, during the first nine months of 2019 Surge has reduced net debt[2] by $84 million, adding significant additional liquidity to the Company's credit facilities.

Furthermore, in the last three financial quarters Surge has:

1. Acquired 8.5 sections of highly prospective Crown land to the North of the Company's large, core area Sparky oil discovery at Betty Lake ("Betty Lake North") (with vertical Sparky well control and logs);
2. Leased 4 highly prospective sections of land at Betty Lake North (with vertical Sparky well control and logs);
3. Leased 2.75 sections of highly prospective Sparky land on an exciting new Sparky play, and acquired an additional section of Crown land on this play (which has vertical Sparky well control and well logs); and
4. Acquired 9.5 sections of highly prospective Slave Point acreage at the Company's large OOIP[4], waterflooded Nipisi light oil asset in the Greater Sawn core area; this acreage includes both Slave Point, and Clearwater rights.

These smaller, core area top-up land acquisitions have added an internally estimated 71 net drilling locations[5] in Surge's Sparky core area, and an internally estimated 17 net locations[5] in the Greater Sawn core area, replacing more than 1.5 years of annual drilling inventory for Surge, at a low total cost of $5.4 million.

In Surge's core Sparky asset, the Company has now amassed a conventional, low cost, low risk, medium/light oil play that has:

a. > 900 million of net internally estimated OOIP;

b. Grown from 1,200 boepd four years ago, to more than 8,250 boepd (>90% oil) today;
c. An extensive 13-year drilling inventory[5];
d. Per well economics that deliver quick payouts and excellent rates of return at current strip prices;
e. Top tier production efficiencies of $9,565 per boepd (i.e. 115 boepd IP90 for a total cost of $1.1 mm); and
f. Excellent longer term waterflood results and profit to investment ratios (all at current strip prices).

Further, the Sparky core area has been "de-risked" geologically, operationally and financially over the last five years, as Surge has now drilled 121 out of 122 successful horizontal wells.

On this basis, the Sparky play provides a significant 'operational advantage' to the Company's management and Board when guiding and positioning the Company through the challenging business conditions present today. Surge's Sparky play has excellent production efficiencies and compelling economics - even in a low oil price environment.

2020 BUDGET – DEFENSIVE AND SUSTAINABLE

In 2020 Surge is budgeting to spend $98.5 million of exploration and development capital (including corporate overhead charges), which includes the drilling of 56 wells. The 2020 budget will primarily be focused in Surge's Sparky core area and will consist of returns-based development drilling. This focused drilling program increases Surge's oil and liquids weighting from 85 percent in 2019, to 87 percent exit 2020.

Using Surge's annual corporate decline of 23 percent, and a 2020 drilling and completion capital budget of $68 million, the drilling program will have robust production efficiencies of less than $15,000 boepd. These top tier efficiencies are being achieved from both Surge's high-quality drilling inventory, as well as the strong operational benefits of a large program utilizing pad drilling.

The table below provides a detailed list of the capital categories:

Capital Category	**2020e**
Drilling and Completions	$68.0 million
Facilities, Equipment, Pipelines, & Seismic	$23.5 million
Other (Land, Corporate)	$7.0 million
Total Exploration & Development Capital	**$98.5 million**

Production and Cost Guidance	**2020e**

Average Production	21,000 boepd (86% liquids)
Exit Production	21,000 boepd (87% liquids)
Net Operating Expenses[2]	$14.00 - $14.50 per boe
Transportation Expenses	$1.50 - $1.75 per boe
General & Administrative Expenses	$1.85 - $1.95 per boe

Financial & Pricing Guidance	**2020e**
Cash Flow from Operating Activities	$162.8 million
Asset Retirement Obligations	$6.0 million
Adjusted Funds Flow[2]	$168.8 million
Total Exploration & Development Capital	$98.5 million
Dividends	$32.6 million
Leasing expenditures	$10.8 million
WTI (US$/bbl)	$56.50
Edmonton Par Differential (US$/bbl)	($5.50)
WCS Differential (US$/bbl)	($15.50)
CAD/USD Exchange Rate	0.75
Natural Gas (AECO C$/GJ)	$1.50

OPERATIONAL HIGHLIGHTS

Successful Q4/19 Drilling Program

During the fourth quarter of 2019, the Company drilled 13 net successful wells, comprised of 12 Sparky wells and one Valhalla Montney well.

In the Sparky core area, Surge expects to add more than 1,500 boepd (>90% oil) from the 12 well program, at an estimated "all-in" capital cost of $13.5 million. Pad drilling continues to deliver significant cost savings, consistently driving the cost per pad well to less than budget estimates of $1.2 million per well.

At Valhalla, Surge drilled an exciting new light oil horizontal well into a large, conventional Montney (Turbidite) pool that sits below the Company's Doig pool. This Montney pool has large internally estimated OOIP of more than 40 million barrels, and a pay column of up to 17 meters thick. The new horizontal well is currently exceeding the Company's 300 bopd type curve by more than 85 percent, and has a number of follow-up drilling locations, as well as waterflood upside.

Environment, Social and Governance

In 2020 Surge will continue its commitment to being an industry leader in environmental, social, and governance matters.

Pursuant to the Company's 2020 budget, management has now increased Surge's target abandonment program to more than 150 wells, which is approximately three times the number of wells the Company plans to drill during the year.

OUTLOOK – RESILIENT ADJUSTED FUNDS FLOW BASE

Management's stated goal is to be the best positioned, top performing, light/medium gravity crude oil growth and dividend paying public company in its peer group in Canada.

Appointment of Senior Vice President, Geosciences

Surge is pleased to announce that Mr. Derek Christie has joined the Company as Senior Vice President, Geosciences effective November 18, 2019. Mr. Christie is a Senior Energy Executive and professional Geologist with over 28 years of wide-ranging experience across North American Basins in both conventional and unconventional reservoir exploration and development. Most recently, he was the Senior Vice President of Exploration & Corporate Development at a large Canadian oil

company.

"We are excited to have Derek join the Surge team. His extensive geoscience, operational, and strategic business experience will be a huge asset for the Company," said Surge President and CEO, Paul Colborne.

Consistent Production; Sustainable Dividend

In setting and approving the Company's 2020 budget, Surge's management team and Board were able to take advantage of:

1. Surge's high quality, large OOIP, low cost, conventional light and medium gravity crude oil asset base;
2. The Company's low annual corporate decline of 23 percent; and
3. The top tier production efficiencies, quick payouts, and excellent rates of return associated with Surge's Sparky core area.

As a result of these key operational strengths, in 2020 Surge anticipates:

- delivering average production of 21,000 boepd – spending $36.5 million less capital than Surge's 2019 capital budget of $135 million (with 2020 debt adjusted exit production per share increasing by 3.1 percent);
- continuing to pay down debt by more than $20 million;
- delivering an all-in payout ratio of 86 percent; and
- paying the Company's attractive dividend of $0.10 per share, per year – using only 19.3 percent of 2020 adjusted funds flow.

Consequently, Surge is currently providing an attractive annual dividend yield of more than 9.5 percent, as well as a free cash flow yield of more than 6 percent, based on the Company's 2020 budget.

Today the Company has over 2.5 billion barrels of internally estimated OOIP, a low 6.2 percent recovery factor to date, and a deep inventory of over 800 highly economic drilling locations[5] - providing a 13 year drilling inventory. Additionally, the Company has a low annual corporate decline, with over 60 percent of Surge's asset base under various stages of waterflood.

Based on the Company's forecast debt reduction of more than $20 million in 2020, and in conjunction with its semi-annual borrowing base review, Surge anticipates a renewal of its credit facilities at $425 million, comprised of a $300 million revolving line of credit, a $50 million operating line of credit, and an accordion of $75 million. This accordion feature allows Surge to increase the revolving credit facility portion from $300 million to $375 million, for total credit facilities of $425 million, upon exercise and unanimous syndicate approval. These credit facilities provide the Company ample liquidity to execute on its 2020 budget, and will significantly reduce stand-by fees. Surge anticipates closing its semi-annual borrowing base review on or before December 18th, 2019.

Surge's high quality, light and medium gravity, crude oil asset base provides an excellent platform for the Company to continue to grow its reserves, production base, and drilling inventory in its four core areas of Sparky, Valhalla, Greater Sawn, and Shaunavon through low risk development drilling, and waterfloods. Surge also applies growth capital to high quality, large OOIP, core area acquisitions where applicable. This is in accordance with management's disciplined Business Plan and Operating Strategy.

In light of the present business environment, Surge's primary focus in 2020 is on sustainability, balance sheet management, cost controls, and maintaining the Company's dividend.

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FORWARD LOOKING STATEMENTS:

This press release contains forward-looking statements. The use of any of the words "anticipate", "continue", "estimate", "expect", "may", "will", "project", "should", "believe" and similar expressions are intended to identify forward-looking statements. These statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements.

More particularly, this press release contains statements concerning: Surge's budget for 2020, including Surge's anticipated dividend payout ratio, all-in payout ratio, production, capital expenditures, ability to pay down debt, cash flow, operational flexibility and capital allocation; anticipated 2020 exit rate production; predicted increases to Surge's oil and liquids weighting; Surge's declared focus and primary goals, and the ability of management to successfully implement such goals; reserves; management's expectations with respect to Surge's asset base; the quality and characteristics of Surge's assets; Surge's annual exploration and development capital expenditure program and budget; continued success of Surge's drilling and

waterflood programs; drilling inventory; corporate decline; anticipated 2020 realized crude oil prices and demand; commodity prices; availability of undrawn capacity with respect to Surge's credit facility; allocation of the Company's adjusted funds flow; and Surge's dividend policy and the expectations of management with respect to an increase to Surge's dividend.

Information respecting Surge's 2020 forecast operating netback and forecast cash flow from operating activities set forth in this press release may be considered to be future-oriented financial information or a financial outlook for the purposes of applicable Canadian securities laws. Financial outlook and future-oriented financial information and projected operational information contained in this press release are based on assumptions about future events based on management's assessment of the relevant information currently available that management considers to be reasonable in the circumstances. The future-oriented financial information and financial outlooks and projected operational information contained in this press release have been approved by management as of the date of this press release. Readers are cautioned that any such future-oriented financial information, financial outlooks and projected operational information contained herein should not be used for purposes other than those for which it is disclosed herein.

The forward-looking statements are based on certain key expectations and assumptions made by Surge; the performance of existing wells and success obtained in drilling new wells; anticipated expenses, cash flow and capital expenditures; the application of regulatory and royalty regimes; prevailing commodity prices and economic conditions; development and completion activities; the performance of new wells; the successful implementation of waterflood programs; the availability of and performance of facilities and pipelines; the geological characteristics of Surge's properties; the successful application of drilling, completion and seismic technology; the determination of decommissioning liabilities; prevailing weather conditions; exchange rates; licensing requirements; the impact of completed facilities on operating costs; the ability of Surge to continue to pay its dividend; the availability and costs of capital, labour and services; and the creditworthiness of industry partners.

Although Surge believes that the expectations and assumptions on which the forward-looking statements are based are reasonable, undue reliance should not be placed on the forward-looking statements because Surge can give no assurance that they will prove to be correct. Since forward-looking statements address future events and conditions, by their very nature they involve inherent risks and uncertainties. Actual results could differ materially from those currently anticipated due to a number of factors and risks. These include, but are not limited to, risks associated with the oil and gas industry in general (e.g., operational risks in development, exploration and production; delays or changes in plans with respect to exploration or development projects or capital expenditures; the uncertainty of reserve estimates; the uncertainty of estimates and projections relating to production, costs and expenses, and health, safety and environmental risks), commodity price and exchange rate fluctuations and constraint in the availability of services, adverse weather or break-up conditions, uncertainties resulting from potential delays or changes in plans with respect to exploration or development projects or capital expenditures or failure to obtain the continued support of the lenders under Surge's bank line. Certain of these risks are set out in more detail in Surge's Annual Information Form dated March 12, 2019 and in Surge's MD&A for the period endedSeptember 30, 2019, both of which have been filed on SEDAR and can be accessed at www.sedar.com.

The forward-looking statements contained in this press release are made as of the date hereof and Surge undertakes no obligation to update publicly or revise any forward-looking statements or information, whether as a result of new information, future events or otherwise, unless so required by applicable securities laws.

Reserves Data

Boe means barrel of oil equivalent on the basis of 1 boe to 6,000 cubic feet of natural gas. Boe may be misleading, particularly if used in isolation. A boe conversion ratio of 1 boe for 6,000 cubic feet of natural gas is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. Boe/d and boepd means barrel of oil equivalent per day. Original Oil in Place ("OOIP") is the equivalent to Discovered Petroleum Initially In Place ("DPIIP") for the purposes of this press release. DPIIP is defined as quantity of hydrocarbons that are estimated to be in place within a known accumulation. There is no certainty that it will be commercially viable to produce any portion of the resources. A recovery project cannot be defined for this volume of DPIIP at this time, and as such it cannot be further sub-categorized. Bbl means barrel of oil. NGLs means natural gas liquids.

Drilling Locations

This press release discloses drilling locations in two categories: (i) booked locations; and (ii) unbooked locations. Booked locations are proved locations and probable locations derived from an internal evaluation using standard practices as prescribed in the Canadian Oil and Gas Evaluations Handbook and account for drilling locations that have associated proved and/or probable reserves, as applicable.

Unbooked locations are internal estimates based on prospective acreage and assumptions as to the number of wells that can be drilled per section based on industry practice and internal review. Unbooked locations do not have attributed reserves or resources. Unbooked locations have been identified by Surge's internal certified Engineers and Geologists (who are also Qualified Reserve Evaluators) as an estimation of our multi-year drilling activities based on evaluation of applicable geologic, seismic, engineering, production and reserves information. There is no certainty that the Company will drill all unbooked drilling locations and if drilled there is no certainty that such locations will result in additional oil and gas reserves, resources or production. The drilling locations on which the Company actually drills wells will ultimately depend upon the availability of

capital, regulatory approvals, seasonal restrictions, oil and natural gas prices, costs, actual drilling results, additional reservoir information that is obtained and other factors. While certain of the unbooked drilling locations have been de-risked by drilling existing wells in relative close proximity to such unbooked drilling locations, the majority of other unbooked drilling locations are farther away from existing wells where management has less information about the characteristics of the reservoir and therefore there is more uncertainty whether wells will be drilled in such locations and if drilled there is more uncertainty that such wells will result in additional oil and gas reserves, resources or production.

Assuming a Jan 1, 2020 reference date, the company will have over >800 gross (>800 net) drilling locations identified herein, of these >400 gross (>400 net) are unbooked locations. Of the 388 net booked locations identified herein 297 net are Proved locations and 91 net are Probable locations based on Sproule's 2018YE reserves. The Company's Sparky core area has 136 net booked locations, of which 100 net are Proved locations and 36 net are Probable locations based on 2018YE reserves. The Company's Greater Sawn area has 79 net booked locations, of which 58 net are Proved locations and 21 net are Probable locations based on 2018YE reserves.

Surge type curves were constructed using a representative, factual and balanced analog data set, as ofAug 31, 2019. All locations were risked appropriately, and EUR's were measured against OOIP estimates to ensure a reasonable recovery factor was being achieved based on the respective spacing assumption. Other assumptions, such as capital, operating expenses, wellhead offsets, land encumbrances, working interests and NGL yields were all reviewed and accounted for on a well by well basis by Surge's Qualifies Reserve Evaluators. All type curves fully comply with Part 5.8 of the Companion Policy 51 – 101CP.

Non-GAAP Financial Measures

Certain secondary financial measures in this press release – namely, "adjusted funds flow", "all-in payout ratio", "net operating expenses" and "net debt" are not prescribed by GAAP. These non-GAAP financial measures are included because management uses the information to analyze business performance, cash flow generated from the business, leverage and liquidity, resulting from the Company's principal business activities and it may be useful to investors on the same basis. None of these measures are used to enhance the Company's reported financial performance or position. The non-GAAP measures do not have a standardized meaning prescribed by IFRS and therefore are unlikely to be comparable to similar measures presented by other issuers. They are common in the reports of other companies but may differ by definition and application. All non-GAAP financial measures used in this document are defined below:

Adjusted Funds Flow

The Company adjusts cash flow from operating activities in calculating adjusted funds flow for changes in non-cash working capital, decommissioning expenditures, transaction and other costs, and cash settled stock-based compensation plans, particularly cash used to settle withholding obligations on stock-based compensation arrangements that are settled in shares. Management believes the timing of collection, payment or incurrence of these items involves a high degree of discretion and as such may not be useful for evaluating Surge's cash flows.

Changes in non-cash working capital are a result of the timing of cash flows related to items such as accounts receivable and accounts payable, which management believes reduces comparability between periods. Management views decommissioning expenditures predominately as a discretionary allocation of capital, with flexibility to determine the size and timing of decommissioning programs to achieve greater capital efficiencies and as such, costs may vary between periods. Transaction and other costs represent expenditures associated with acquisitions, which management believes do not reflect the ongoing cash flows of the business, and as such reduces comparability. Subsequent to the third quarter of 2018, all of the Company's stock-based compensation plans are equity classified as the Company has the intention of settling all awards with shares. Cash settled stock-based compensation currently represents the statutory tax withholdings required on stock-based compensation awards and is a discretionary allocation of capital. The Company has the option to either require the holder to sell shares earned in the stock-based compensation plan to satisfy tax withholdings, or the Company can issue less shares to the individual and remit a cash payment to satisfy tax withholding requirements. Each of these expenditures, due to their nature, are not considered principal business activities and vary between periods, which management believes reduces comparability.

The following table reconciles forecast cash flow from operating activities to adjusted funds flow

($000s)	**2020e**
Petroleum and natural gas revenue	**$388,962**
Processing and other income	**$4,600**
Royalties	**-$55,933**
Operating expenses	**-$114,106**
Transportation expenses	**-$11,529**
Loss on financial contracts	**-$2,561**
Operating netback	**$209,433**
G&A expense	**-$14,400**
Interest expense	**-$26,239**
Adjusted Funds Flow	**$168,794**

Changes in non-cash working capital	**$0**
Abandonments	**-$6,000**
Cashflow from Operating Activities	**$162,794**

All-in Payout Ratio

All-in payout ratio is calculated using the sum of total exploration and development capital, plus dividends paid, divided by adjusted funds flow, less lease obligations and asset retirement obligations. This capital management measure is used by management to analyze allocated capital in comparison to the cash being generated by the principal business activities. This measure is provided to allow readers to quantify the amount of adjusted funds flow that is being used to either: i) pay dividends; and ii) deployed into the Company's development and exploration program. A ratio of less than 100% indicates that a portion of the adjusted funds flow is being retained by the Company and can be used to fund items such as asset abandonment, repayment of debt, fund acquisitions or the costs related thereto, withholding tax obligations on stock-based compensation, or other items.

Net Debt

There is no comparable measure in accordance with IFRS for net debt. Net debt is calculated as bank debt plus the liability component of the convertible debentures plus or minus working capital, however, excluding the fair value of financial contracts and other long term liabilities. This metric is used by management to analyze the level of debt in the Company including the impact of working capital, which varies with timing of settlement of these balances. Net debt reduction includes $11 million in lease obligation repayments, it is calculated as follows:

($000s)	**2020e**
Cashflow from Operating Activities	**$162,794**
Less:	
Lease expenditures	**-$10,800**
Total Exploration & Development Capital	**-$98,500**
Dividends	**-$32,600**
Total Estimated Net Debt Reduction	**$20,894**

Net Operating Expenses

Net operating expenses are determined by deducting processing and other revenue primarily generated by processing third party volumes at processing facilities where the Company has an ownership interest. It is common in the industry to earn third party processing revenue on facilities where the entity has a working interest in the infrastructure asset. Under IFRS this source of funds is required to be reported as revenue. However, the Company's principal business is not that of a midstream entity whose activities are dedicated to earning processing and other infrastructure payments. Where the Company has excess capacity at one of its facilities, it will look to process third party volumes as a means to reduce the cost of operating/owning the facility. As such, third party processing revenue is netted against operating costs.

Additional Metrics

This press release contains additional metrics commonly used in the oil and natural gas industry. These terms have been calculated by Management and do not have a standardized meaning. Management uses these oil and gas metrics to further analyze the performance of the Company over time and to compare the results of the Company with others in the industry.

Additional information relating to non-GAAP and capital management measures can be found in the Company's most recent management's discussion and analysis MD&A, which may be accessed through the SEDAR website (www.sedar.com).

Neither the TSX nor its Regulation Services Provider (as that term is defined in the policies of the TSX) accepts responsibility for the adequacy or accuracy of this release.

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1 Debt-adjusted shares are calculated using exit shares of 326.2 million for 2019 and 2020 respectively, adjusted by the reduction in exit net debt, divided by a $1.00 share price for 2019 and the 2020 budget.

2 This is a non-GAAP financial measure which is defined in the Non-GAAP Financial Measures section of this document.

3 Source: IEA (2019), "Oil Market Report - November 2019", IEA, Parishttps://www.iea.org/reports/oil-market-report-november-2019.
4 See Reserves Data in the Forward-Looking Statement section of this document for further details.
5 See Drilling Locations Section in the Forward-Looking Statement section of this document for further details.

SOURCE Surge Energy Inc.

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