Surge Energy

CALGARY, Aug. 8, 2012 /CNW/ - Surge Energy Inc. ("Surge" or the "Company") (TSX: SGY) is pleased to announce its financial and operating results for the three and six month periods ended June 30, 2012.

FINANCIAL AND OPERATING SUMMARY:

($000s except per share amounts)

	Three Months Ended June 30,			**Six Months Ended June 30**		
	2012	2011	% change	**2012**	2011	% change
Financials highlights						
Oil and NGL sales	**45,610**	**25,172**	81%	**92,977**	**46,822**	99%
Natural gas sales	**3,308**	**4,637**	(29%)	**6,986**	**8,794**	(21%)
Other revenue	**9**	**(14)**	(164%)	**24**	**52**	(54%)
Total oil, natural gas, and NGL revenue	**48,927**	29,796	64%	**99,987**	55,668	80%
Funds from Operations[1]	**24,315**	**11,898**	104%	**48,322**	**21,670**	123%
Per share basic ($)	**0.34**	0.21	62%	**0.68**	0.39	74%
Per share diluted ($)	**0.34**	0.21	62%	**0.67**	0.38	76%
Net income (loss)	**13,273**	3,317	300%	**15,930**	2,815	466%
Per share basic ($)	**0.19**	0.06	217%	**0.23**	0.05	360%
Per share diluted ($)	**0.18**	0.06	200%	**0.22**	0.05	340%
Capital expenditures - petroleum & gas properties[2]	**27,707**	11,420	143%	**82,605**	47,317	75%
Capital expenditures - acquisitions & dispositions[2]	**9,347**	10,016	nm	**113,745**	19,119	495%
Total capital expenditures[2]	**37,054**	21,436	73%	**196,350**	66,436	196%
Net debt at end of period[3]	**171,692**	90,954	89%	**171,692**	90,954	89%
Operating highlights						
Production:						
Oil and NGL (bbls per day)	**6,568**	2,995	119%	**6,339**	3,042	108%
Natural gas (mcf per day)	**16,246**	12,334	32%	**16,822**	12,126	39%
Total (boe per day) (6:1)	**9,275**	5,051	84%	**9,142**	5,063	81%
Average realized price (excluding hedges):						
Oil and NGL ($per bbl)	**76.31**	92.36	(17%)	**80.59**	85.04	(5%)
Natural gas ($ per mcf)	**2.24**	4.13	(46%)	**2.28**	4.01	(43%)
Realized loss on financial contracts ($ per boe)	**(0.29)**	(2.58)	(89%)	**(0.61)**	(2.10)	(71%)
Netback (excluding hedges) ($ per boe)						
Oil, natural gas and NGL sales	**57.97**	64.83	(11%)	**60.09**	60.75	(1%)
Royalties			5%			27%

	(9.69)	(9.24)		**(10.94)**	(8.63)	
Operating expenses	**(10.63)**	(16.39)	(35%)	**(11.14)**	(16.56)	(33%)
Transportation expenses	**(2.59)**	(3.25)	(20%)	**(2.19)**	(2.90)	(24%)
Operating netback	**35.06**	35.95	(2%)	**35.82**	32.66	10%
G&A expenses	**(3.50)**	(5.44)	(36%)	**(3.56)**	(5.10)	(30%)
Interest expense	**(1.87)**	(1.75)	7%	**(1.81)**	(1.36)	33%
Corporate netback	**29.69**	28.76	3%	**30.45**	26.20	16%
Common shares (000s)						
Common shares outstanding, end of period	**71,065**	**56,102**	27%	**71,065**	**56,102**	27%
Weighted average basic shares outstanding	**71,058**	**56,098**	27%	**70,766**	**56,096**	26%
Stock option dilution (treasury method)	**1,080**	**1,188**	(9%)	**1,403**	**1,041**	35%
Weighted average diluted shares outstanding	**72,138**	**57,286**	26%	**72,169**	**57,137**	26%

[1] Management uses funds from operations (before changes in non-cash working capital) to analyze operating performance and leverage. Funds from operations as presented does not have any standardized meaning prescribed by IFRS and, therefore, may not be comparable with the calculation of similar measures for other entities.

[2] Please see capital expenditures note.

[3] The Company defines net debt as outstanding bank debt plus or minus working capital excluding the fair value of financial contracts.

ACHIEVMENTS AND HIGHLIGHTS

Surge has achieved excellent growth year to date in 2012, achieving record production and funds flow in the second quarter. The Company is well positioned with a strong balance sheet and risk management program, three core areas with an expanded oil drilling inventory of 570 gross (435 net) locations, internally estimated gross DPIIP[4] of 550 million barrels of oil and multiple waterflood opportunities and exploration initiatives.

The Company has achieved operational efficiencies in each of its core areas, resulting in significant reductions in operating costs since inception. Surge continues to strive to become one of the lowest cost oil producers among its oil weighted peer group.

During the second quarter of 2012, Surge achieved a 100 percent success rate drilling six gross (5.37 net) wells. As a result of the Company's successful drilling results, combined with the Pradera Resources Inc. acquisition, Surge more than doubled funds from operations and increased production by 84 percent over the second quarter of 2011. Highlights for the quarter include:

- **Achieved record quarterly funds from operations of $24.3 million which increased 104 percent** from $11.9 million during the same period of 2011.

- **Funds from operations per share increased 62 percent** to $0.34 during the second quarter of 2012 from $0.21 during the same period of 2011.

- **Achieved record quarterly production of 9,275 boe per day which increased 84 percent,** from an average of 5,051 boe per day during the second quarter of 2011.

- **Increased production per basic share by 45 percent during the second quarter of 2012,** as compared to the second quarter of 2011.

- **Continued to make significant progress in becoming a low cost producer by reducing operating costs by 35 percent and transportation costs per boe by 20 percent** in the second quarter of 2012, as compared to the second quarter of 2011, with combined operating ($10.63 per boe) and transportation ($2.59 per boe) **costs decreasing by 33 per cent** from $19.64 per boe in the second quarter of 2011 to $13.22 per boe in the second quarter of 2012.

- **Increased Surge's operating netback by 10 percent** to $35.82 per boe for the first half of 2012 as compared to $32.66 in the first half of 2011, despite a five percent drop in realized oil & NGL prices and a 43 percent drop in realized natural gas prices.
- **Achieved a 100 percent success rate** drilling six gross (5.37 net) wellsin the second quarter of 2012. Only one of the six wells drilled in the second quarter were producing at quarter end, with the remainder to be brought on production during the third quarter of 2012.
- The continued success of Surge's 2012 drilling program drove the increase in **oil and natural gas liquids production weighting to 71 percent in the second quarter**.

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[4] "Discovered Resources" or "Discovered Petroleum Initially-In-Place" ("DPIIP"), are those quantities of petroleum estimated, as of a given date, to be contained in known accumulations prior to production. The recoverable portion of discovered petroleum initially-in-place includes production, reserves and contingent resources; the remainder is unrecoverable. "Contingent resources" are those quantities of petroleum estimated, as of a given date, to be potentially recoverable from known accumulations using established technology or technology under development, but which are not currently considered to be commercially recoverable due to one or more contingencies. Contingencies may include factors such as economic, legal, environmental, political, and regulatory matters, or a lack of markets. It is also appropriate to classify as Contingent Resources the estimated discovered recoverable quantities associated with a project in the early evaluation stage. There is no certainty that it will be commercially viable to produce any portion of the Contingent Resources. A recovery project cannot be defined for this volume of DPIIP at this time, and as such it cannot be further sub-categorized.

OPERATIONS OVERVIEW:

Nipisi/Gift (Slave Point/Gilwood), Western Alberta:

During the first quarter of 2012, Surge drilled its first two horizontal multi-frac wells into the Slave Point Formation (102/16-02-078-09W5 and 100/15-02-078-09W5) and completed its first two directional wells into the Gilwood Formation. The two Slave Point wells were completed early in the second quarter and have now been on production since April 2012. Both wells exceeded Surge's type curve expectations of best 30 day production average of 310 barrels per day of light oil. These two horizontal multi-frac wells in the Slave Point were re-entered to conduct sand/propant cleanouts and pump optimization during the third quarter. This unscheduled operation will impact the third quarter by approximately 100 barrels of oil per day. Surge believes modifications to the recent frac design should mitigate these problems going forward.

Surge drilled its third horizontal multi-frac well (102/10-10-078-09W5) into the Slave Point during the second quarter. This well was completed during the third quarter and is currently recovering load fluid.

Surge drilled its fourth and fifth horizontal multi-frac wells (100/12-02-078-09W5 & 102/03-02-078-09W5) in the Slave Point during the third quarter. The Company completed the 03-02 well and the 12-02 well will be completed imminently. Surge is currently drilling its sixth horizontal multi-frac well (102/13-11-078-09W5) at Nipisi. The drilling costs for Surge's most recent two horizontal multi-frac wells in the Slave Point have been executed at 20 percent less than the budgeted cost of $2.3 million per well. The largest part of the drilling cost reduction is due to the monobore well design.

Surge plans to drill a horizontal multi-frac Slave Point well on its recently acquired southern block at Nipisi during the fourth quarter of 2012. This well will offset a vertical Slave Point well that has recovered 31 thousand barrels of oil to date. The results from the well are expected to confirm the viability of the approximately 30 million barrels of DPIIP that Surge estimates to be in place on these lands.

Surge continues to make progress on the Nipisi Slave Point waterflood. The Company anticipates submitting a waterflood application during the third quarter of 2012 with the first injection during the first half of 2013, pending regulatory approvals. Based on successful waterflood implementation, Surge anticipates that it will ultimately recover up to 20 percent of the 85 million barrels of DPIIP.

Surge has a total of five horizontal multi-frac wells (100 percent working interest) budgeted at Nipisi for the second half of 2012, for a total of eight gross (eight net) wells budgeted for the year. Surge is on track to meet its targeted all-in costs of $4.3 million per well. As at December 31, 2011, Surge had 38 gross (38 net) horizontal multi-frac Slave Point wells remaining in inventory, of which 24 gross (24 net) wells were unbooked.

Sounding Lake and Silver Lake (Cretaceous Sands), South East Alberta:

Surge drilled four gross (four net) horizontal wells in South East Alberta during the second quarter, one of which was multi-frac'd, for a total of eight gross (eight net) wells drilled this year. All four second quarter wells were all on production during the third quarter. The wells drilled in the first quarter and brought on production during the second quarter have performed to the Company's type curve expectations. The Company continues to make strategic acquisitions in specific play fairways to add to its land position and drilling inventory in this area.

The Company initiated a waterflood expansion at Silver Lake, which included two new water injection wells, one well conversion and facility expansion to handle an additional 12,000 barrels of water per day. The expansion project was completed by the end of July and will impact third quarter production due to the shut-in by approximately 100 barrels of oil per day.

Surge plans to drill another eight gross (eight net) horizontal wells in South East Alberta during the second half of 2012 for a total of 16 gross (16 net) for the year. As at December 31, 2011, Surge had 76 gross (76 net) horizontal wells (mix of horizontal wells and horizontal multi-frac wells) remaining in inventory, of which 73 gross (73 net) wells were unbooked.

Valhalla South (Doig), Western Alberta:

Surge drilled and completed the Company's 11th horizontal multi-frac well (100/05-31-074-08W6; 44 percent working interest) during the second quarter in the northern part of the light oil pool at Valhalla South. The well has been producing for 75 days and its best 30 day average production rate was 1,570 boe per day (1,260 barrels of oil and NGLs per day). The 05-31 well results have outperformed the Company's expectations for reservoir quality in the area and confirmed the extension of the pool to the north.

During the second quarter, Surge also purchased an additional 3.75 gross (3.75 net) section of land at Wembley, just one township south of Valhalla South. Surge internally estimates 18 million barrels of gross DPIIP in the Doig Formation and sees potential for an additional six gross (six net) horizontal multi-frac well locations. This estimate is based on data from existing vertical wells and a producing horizontal multi-frac oil well adjacent to Surge's new land. The Company plans to drill its first horizontal multi-frac well at Wembley in 2013.

During the third quarter, Surge completed an unscheduled facility upgrade at Valhalla South, which will impact third quarter production by approximately 125 boe per day.

Surge plans to drill two gross (1.25 net) additional horizontal multi-frac well at Valhalla South during the second half of 2012, for a total of five gross (3.13 net) wells budgeted for the year. As at December 31, 2011, Surge had 32 gross (23.9 net) horizontal multi-frac wells remaining in inventory, of which 19 gross (14.3 net) wells were unbooked.

Williston Basin (Spearfish), Manitoba and North Dakota:

At Waskada, Surge has a total of 21 gross (21 net) horizontal multi-frac Spearfish oil wells producing to the Company's recently constructed battery. All 21 wells were drilled, completed and on production prior to the second quarter of 2012.

As a result of this new battery, operating costs at Waskada have decreased by 45 percent to $12.00 per barrel, which is in line with the Company's original budget expectations. Surge also recently entered into a clean oil delivery and pipeline agreement with a nearby operator, which will result in further savings on transportation costs and increase delivery reliability.

Surge continues to make progress on the Waskada Unit 15 waterflood pilot. The Company submitted the Waskada Unit 15 waterflood progress report/amendment during the second quarter of 2012. The third party waterflood study is now complete and the results are encouraging. The results from the report have prompted Surge to move up the implementation to the second half of 2012 instead of the first quarter in 2013.

During the third quarter, Surge successfully drilled a step out, earning, horizontal multi-frac Spearfish well (102/09-06-002-26W1; 100 percent working interest) on lands north west of where it has drilled all of its previous wells at Waskada. The results from this well have confirmed the presence of oil resource in the area that is in addition to the existing resource already identified at Waskada. The well will be completed and production tested in during the third quarter.

In North Dakota, Surge participated in the drilling and completion of seven gross (2.5 net) non-operated horizontal multi-frac wells with two of its working interest partners during the first quarter. Production from these wells also commenced during the second quarter and on average, the wells performed above the Company's best month average production well type curve of 125 barrels of oil per day.

In North Dakota, Surge submitted permit applications for an additional nine gross (100 percent working interest and operated) horizontal multi-frac Spearfish wells. Surge has signed a drilling rig contract with two other operators to move in a drilling rig that is suitable and specifically designed to drill shallower pad wells in the Spearfish. Utilizing this rig should result in reduced drill costs and operational efficiencies. Surge plans to begin drilling its 100 percent working interest and operated wells from a five well pad during the third quarter of 2012.

The Company currently has five gross (five net) operated and five gross (two net) non-operated horizontal multi-frac Spearfish wells budgeted for the remainder of the year in North Dakota. As at December 31, 2011, Surge had 334 gross (212.6 net) horizontal multi-frac Spearfish wells remaining in inventory, of which 297 gross (186.2 net) wells were unbooked.

Windfall (Bluesky), Western Alberta:

The Energy Resources Conservation Board (ERCB) has approved the waterflood pilot at Windfall. The original horizontal multi-frac well (9-9-59-15W5, 100 percent working interest) has now been converted for water injection, the water source application has been submitted and all major equipment for the injection facility has been ordered. Surge expects to commence injection during the third quarter, pending all regulatory approvals.

As at December 31, 2011, Surge had 38 gross (38 net) horizontal multi-frac Bluesky wells remaining in inventory, of which 31 gross (31 net) wells were unbooked.

For more information about Surge Energy Inc., please see the Company's corporate presentation available on its website at www.surgeenergy.ca.

OUTLOOK - POSITIONED FOR CONTINUED LIGHT OIL GROWTH

In just 30 months, management has positioned Surge with a strong balance sheet and risk management program, assembled more than 570 gross (435 net) oil drilling locations, made significant progress in reducing its cost structure and increasing netbacks and gained exposure to an internally estimated DPIIP of more than 550 gross million barrels of oil, with multiple waterflood opportunities and exploration initiatives.

With the achievement of record production and funds flow in the second quarter, Surge forecasts continued growth organically by drilling in each of its core areas, the implementation of waterflood and continuing to make accretive acquisitions that fit its business plan. Surge is committed to delivering top quartile corporate performance and creating value for shareholders by growing reserves, cash flow and production on a per share basis.

As previously discussed, the unscheduled well servicing and facility upgrades at Nipisi, Silver Lake and Valhalla South during the third quarter will impact production by approximately 350 boe per day. Even with impact to third quarter production rates, Surge is positioned to meet its 2012 average production rate of 9,750 boe per day (72 percent oil and NGLs), and its 2012 exit production rate of 11,000 boe per day (77 percent oil and NGLs).

Surge is an oil focused oil and gas company with operations throughout Alberta, Manitoba and North Dakota. Surge's common shares trade on the Toronto Stock Exchange under the symbol SGY. At quarter end, the Company had 71.1 million basic and 78.0 million fully diluted common shares outstanding.

FINANCIAL STATEMENTS AND MANAGEMENT'S DISCUSSION AND ANALYSIS:

Surge has filed with Canadian securities regulatory authorities its unaudited financial statements for the three and six month periods ended June 30, 2012 and the accompanying Management's Discussion and Analysis ("MD&A"). These filings are available for review at www.sedar.com or www.surgeenergy.ca.

FORWARD-LOOKING STATEMENTS:

This press release contains forward-looking statements. More particularly, this press release contains statements concerning anticipated: (i) capital expenditures for 2012, (ii) exploration, development, drilling, construction and acquisition activities, (iii) average and exit oil & natural gas production during 2012, (iv) operating and transportation costs, (v) primary and secondary recovery potentials and implementation thereof, (vi) regulatory applications and the expected success thereof, and (vii) realization of anticipated benefits of acquisitions.

The forward-looking statements are based on certain key expectations and assumptions made by Surge, including expectations and assumptions concerning the performance of existing wells and success obtained in drilling new wells, anticipated expenses, cash flow and capital expenditures and the application of regulatory and royalty regimes.

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 uncertainties resulting from potential delays or changes in plans with respect to exploration or development projects or capital expenditures. Certain of these risks are set out in more detail in Surge's Annual Information Form which has 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.

Note: 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 means barrel of oil equivalent per day.

In this press release: (i) mcf means thousand cubic feet; (ii) mcf/d means thousand cubic feet per day (iii) mmcf means million cubic feet; (iv) mmcf/d means million cubic feet per day; (v) bbls means barrels; (vi) mbbls means thousand barrels; (vii) mmbbls means million barrels; (viii) bbls/d means barrels per day; (ix) bcf means billion cubic feet; * mboe means thousand barrels of oil equivalent; and (xi) mmboe means million barrels of oil equivalent.

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