



# KAISEN Energy Corp.



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## KAISEN RELEASES ITS Q3 FINANCIAL RESULTS AND PROVIDES UPDATE ON A HIGHLY SUCCESSFUL SUMMER/FALL DRILLING SEASON DELIVERING 43% PRODUCTION GROWTH

It is startling how quickly the Christmas season approaches when it seems like only yesterday that our operators were knee deep in mud working to maintain production through an unusually wet spring break up. Now with a few short weeks remaining until we bid adieu to 2014, we look back with pride of accomplishment in observing how far Kaisen has come in these past 6-7 months. Of course none of this is possible without the support of our shareholders and for this we thank you for your support and your words of encouragement along the way.

We are confident in saying that Kaisen experienced its busiest and most successful quarter since inception with the execution of a significant development drilling and facility expansion program which generated production growth of 43%, averaging 1,104 boe per day for the three month period ending September 30, 2014 (or the "Quarter"). We were also successful in reducing operating costs by 33% over the same period which when coupled with continued strong commodity prices, resulted in an impressive 75% increase in our realized field netbacks (net of hedging) over the same period. These are solid results that reflect the tireless efforts and late night dedication put forth by our field operators in both Lone Rock and Edam. We tip our hats to you fellas!

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### OPERATIONS HIGHLIGHTS

In total, \$8.5 million was invested during the Quarter into drilling, completion and major facility projects, with another \$1.5 million forecast to project completion in the fourth quarter. 13 net heavy oil wells were drilled (four of which were completed subsequent to the Quarter end), a new salt water disposal ("SWD") facility was constructed at Edam, and numerous other construction projects were undertaken on several debottlenecking and operating cost reduction initiatives.



Kaisen's newly commissioned water facility (A5-29) at Edam was a key building block in nearly tripling our capacity up to 19,000 bbls of water per day

As we hoped it would, the summer/fall capital program has greatly enhanced the confidence factor of our properties, in particular the significant oil in place opportunity at Edam which may be further advanced through potential thermal recovery methods in the not-too-distant future as well as the developing potential of horizontal opportunities in both areas.

Production for the Quarter averaged 1,104 barrels of oil equivalent ("boe") per day, 43% higher than the 773 recorded in the prior quarter thanks to the success of our 13 well program with eight wells drilled at Lone Rock and five wells at Edam. At Quarter end, nine of these wells were on production adding approximately 530 bbls of oil per day for the full month of September for a total September average of 1,243 boe per day. With the remaining wells on stream and optimized in October, production adds from the 13 well program increased to approximately 800 bbls/d, for a total October average of 1,677 boe per day. Kaisen is

also pleased to report the discovery of a new Colony oil pool within the Lone Rock area, where we moved quickly to drill the first Colony well in September to prove commerciality and productivity. The Colony well was on stream early October with promising initial results. Costs for drilling, completing, and equipping these 13 wells averaged \$502,000 per well, which is in line with Company estimates of \$495,000 per well.

On the facilities front, the expansion of salt water disposal ("SWD") capacity at Edam was completed near the end of the Quarter and is forecast to nearly triple Kaisen's water handling capability. By the end of October, Edam SWD capacity demonstrated capability of up

to 19,000 bbls of water per day from past limitations of 7,000 bbls/d. This will provide the Company with ample water disposal capacity for future development in 2015 and beyond. Kaisen is nearly complete on the construction of several additional projects aimed at increasing Edam netbacks. These projects include the installation of water transfer pumps and flowlines on four existing wells to reduce fluid trucking expenses, along with the electrification and expansion of the Edam fuel gas network to reduce propane fuel costs. In aggregate, these projects are expected to reduce Edam operating costs by approximately \$850,000 per year or \$2.00 per bbl on a current run-rate of 1,000 bbls/d for the field.

Area	Current estimated field production (Sept)	Q3/14	Q2/14	Q1/14	Q4/13
Lone Rock (bbl)	850	529	291	421	534
Edam (bbl)	800	549	458	486	394
Other (boe)	-	26	24	35	35
<b>Total daily average</b>	<b>1,650</b>	<b>1,104</b>	<b>773</b>	<b>942</b>	<b>963</b>

98% of Kaisen's production for the Quarter was heavy oil from the Company's core operating areas at Lone Rock and Edam with the remaining production from the Company's non-operating interests in the Pembina area of Alberta. At Lone Rock, production increased by 81% averaging 529 boe per day (291 boe per day in the prior quarter), while at Edam, production increased by 20% to 549 boe per day (458 boe per day in the prior quarter). During the last weeks of November, we are currently estimating a field production rate of approximately 1,650 boe per day, reflecting the full benefit of our 13 well drilling program along with continued optimization of existing and new production volumes. Still to follow will be the results of the four well reactivation program currently underway.

## FINANCIAL UPDATE

	Three Months Ended September 30, 2014 <i>(unaudited)</i>	Three Months Ended June 30, 2014 <i>(unaudited)</i>	Three Months Ended March 31, 2014 <i>(unaudited)</i>	Nine Months Ended September 30, 2014 <i>(unaudited)</i>
<b>Financial results</b>				
Petroleum and natural gas sales	\$7,593,071	\$5,480,037	\$5,782,300	\$18,855,409
Realized hedging losses	\$335,140	\$687,913	\$403,764	\$1,426,818
Funds flow from operations <sup>(1)</sup>	\$2,510,180	\$746,809	\$727,675	\$3,984,663
Per share – basic <sup>(1)</sup>	\$0.20	\$0.06	\$0.06	\$0.33
Per share – diluted <sup>(1)</sup>	\$0.16	\$0.06	\$0.06	\$0.27
Net earnings / (loss)	\$1,617,717	(\$104,200)	(\$1,853,544)	(\$340,029)
Per share – basic	\$0.13	(\$0.01)	(\$0.16)	(\$0.03)
Per share – diluted	\$0.11	(\$0.01)	(\$0.16)	(\$0.03)
Expenditures on oil & gas properties	\$8,486,501	\$1,535,661	\$2,460,367	\$12,482,530
Net debt	\$3,619,743	\$5,282,236	\$4,358,738	\$3,619,743
<b>Common shares</b>				
Outstanding – basic	15,420,029	11,911,922	11,895,122	15,420,029
Outstanding – diluted	18,649,028	14,735,921	14,719,113	18,649,028
Weighted average– basic	12,865,212	11,911,922	11,895,122	12,233,177
Weighted average– diluted	15,390,767	14,735,921	11,895,122	14,758,732
<b>Operating Netbacks</b>				
Sales price	\$74.76	\$77.86	\$68.37	\$73.48
Royalties	(\$19.14)	(\$18.84)	(\$16.42)	(\$18.16)
Operating expenses	(\$19.48)	(\$29.09)	(\$24.73)	(\$23.85)
Transportation expenses	(\$2.09)	(\$2.62)	(\$2.19)	(\$2.27)
Netbacks (before hedging)	\$34.05	\$27.31	\$25.03	\$29.20
Realized loss on hedging contracts	(\$3.30)	(\$9.77)	(\$4.70)	(\$5.56)
<b>Netbacks (after hedging)</b>	<b>\$30.75</b>	<b>\$17.54</b>	<b>\$20.33</b>	<b>\$23.64</b>

<sup>(1)</sup> The reader is referred to the section - "Non-IFRS Measurements".

<sup>(2)</sup> The reader is referred to the section - "Oil, Natural Gas Liquids and Natural Gas Conversions to Boe's".

Significant production growth coupled with continued strength in realized heavy oil prices during the Quarter account for the nearly 40% increase in revenues over the prior quarter. Operating netbacks for the Quarter (after hedging) averaged \$30.75 per boe (\$23.64 per boe year to date), 75% higher than the \$17.54 per boe recorded in the prior quarter, generating field level profits (after hedging) of \$3,123,383, 153% higher than the \$1,234,478 recorded in the prior quarter.

In direct correlation to the strong realized market prices, the Company's risk management contracts (hedging contracts) generated a realized loss of \$3.30 per boe during the Quarter (\$5.56 per boe year to date) producing an average realized heavy oil price (net of hedging) of \$71.46 (\$67.92 year to date). The Company's hedging contracts were initiated in February and expire at the end of December 2014.

We continue to pinch pennies on the G&A front which for the Quarter delivered costs in line with expectations, averaging \$4.88 per boe as compared to \$6.73 in the prior quarter. And from a debt leverage perspective, our net working capital deficit declined over the prior quarter by \$1.6 million ending at \$3.6 million thanks to the proceeds from our \$7.9 million September equity offering along with strong cash flows from August and September production. Our current debt level demonstrates the strength of our balance sheet with only 33% drawn on our current \$11.1 million lending base representing a very low 0.4x debt to funds flow ratio (annualizing third quarter funds flow). In other words, we have the capacity to fully eliminate our current debt from cash flow (assuming no further capital investment) in less than five months, admittedly a conservative estimate considering the rate of funds flow growth anticipated in the fourth quarter.

<b>Quarterly Netbacks</b> <i>(\$ per boe)</i>	<b>Q3/14</b> Sept 30, 2014 <i>(unaudited)</i>	<b>Q2/14</b> June 30, 2014 <i>(unaudited)</i>	<b>Q1/14</b> Mar 31, 2014 <i>(unaudited)</i>	<b>Q4/13</b> Dec 31, 2013 <i>(unaudited)</i>
Sales price	<b>74.76</b>	77.86	68.37	54.27
Royalties	<b>(19.14)</b>	(18.84)	(16.42)	(13.86)
Operating expenses	<b>(19.48)</b>	(29.09)	(24.73)	(17.95)
Transportation expenses	<b>(2.09)</b>	(2.62)	(2.19)	(2.02)
<b>Operating Netbacks</b>	<b>34.05</b>	27.31	25.03	20.44
Realized loss on hedging	<b>(3.30)</b>	(9.77)	(4.70)	-
<b>Netbacks (after hedging)</b>	<b>30.75</b>	17.54	20.33	20.44
G&A	<b>(4.88)</b>	(6.73)	(11.23)	(4.99)
Cash interest costs	<b>(0.33)</b>	(0.65)	(0.35)	(0.17)
Current taxes	-	-	-	(3.85)
<b>Corporate Netback (before taxes)</b>	<b>25.54</b>	10.16	8.75	11.43

Subsequent to the Quarter end on October 24, 2014, Kaisen was successful in divesting it's non-core non-operated Alberta assets with production in the Pembina area of approximately 25 bbl/d of production heavily weighted to natural gas. Proceeds before selling costs of \$950,000 will be redirected towards our core area development.

For further details on our third quarter financial results, please refer to the accompanying unaudited financial statements and management discussion and analysis.

## OUTLOOK FOR REMAINDER OF 2014 AND EARLY 2015

As a follow on to the exceptional results of this third quarter of 2014, much time and effort has been invested into the continued refinement of our budget for the balance of 2014 and our plans for 2015. In our previous quarter end outlook we positioned ourselves to execute a 17 well program for a total cost of \$15.4 million with a 2014 exit range between 1,500 and 1,800 boe per day. Kaisen is nimble and capable of quick adaptation to ever changing market conditions. This is a luxury we aim to exploit to the fullest through continuous strategy development. For the balance of 2014, we are keenly aware of the pricing volatility that commenced in October which will negatively impact realized commodity prices for November and December production months and into 2015. In light of this unpredictable volatility and the duration for which it may last, we have reviewed our remaining capital program for 2014 and have made the proactive decision to cease with any further drilling for the balance of the year and instead will focus our efforts during the balance of the year towards optimizing our existing production and completing four additional well reactivations which were kicked off in late November. To some this may seem reactionary to what we hope will be a short volatility cycle, however when reviewing our results to date on the 13 wells drilled in the current quarter coupled with results from the four well reactivations soon to be completed, we are confident that we will deliver a production at exit safely within the guidance previously forecasted for the end of the year. Furthermore, we will deliver these results on a program that is approximately 25% or \$3.5 million cheaper than planned. This outcome will leave Kaisen with an enviably strong balance sheet (forecasted to be less than 20% leveraged) and strong production/funds flow setting the stage for maximum optionality in 2015. As for 2015, we are currently developing a comprehensive drilling program tentatively scheduled to kick-off in January where we hope to see continued production growth through the first quarter. However, no program is cast in stone and although we will ensure full readiness for this planned program, we will also remain flexible to make further adjustments in response to market conditions and opportunities that may evolve.

The key message in our outlook for the balance of 2014 and into 2015 is that we have optionality. Optionality to utilize our balance sheet strength and strong funds flow to accelerate production growth, or to defensively sustain production and endure any possible prolonged market challenges that may evolve. However, it is our view that current commodity price volatility will stabilize as we enter into 2015 and with a bullish longer term view on North American heavy oil demand, coupled with continued debottlenecking of transport capacity on both rail and pipeline, prices will eventually stabilize and strengthen, particularly for heavy oil. We are happy with the position we are in at this point in the year and we look forward to continued operational successes as we approach 2015, always being mindful and attentive to the eventual opportunity to delivery liquidity to shareholders as and when the opportunity arises.

From our families to yours, we wish you all the best over the holiday season, Merry Christmas and a Happy New Year!

### KAISEN EXECUTIVE MANAGEMENT TEAM:

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President & CEO

*Jeff Holmgren*  
Senior VP & CFO

*Chris McGinnis*  
VP Operations & Engineering

*Andy Kramchynski*  
VP Geology