



## 2 Small-Cap, High-Growth Plays in the Patch

### Description

The current crisis in Iraq is fueling further speculation over the direction of oil prices, resulting in renewed interest among energy investors for lower-risk jurisdictions. This has seen Canada's energy patch become particularly attractive for investors, as it holds the world's third-largest oil reserves and is a low-risk jurisdiction with a stable political and economic climate.

The **S&P/TSX Composite Index** (^OSPTX) already closed at a new high on Wednesday, buoyed by solid gains among energy and gold mining stocks. It is expected that these gains will continue as the price of crude appreciates, the gold price rises, and investors making a bet on black gold seek out safe jurisdictions in which to invest.

While energy majors like **Suncor** (TSX: SU)(NYSE: SU) are well positioned to benefit from this crisis, with analysts expecting its full-year 2014 earnings to surge 42%, it is small-cap, growth-oriented players that offer the most potential upside for investors.

However, this does come at a greater risk, because these companies do not possess the same degree of financial resources as the integrated energy majors, leaving them at a disadvantage in a capital-intensive industry.

Let's take a closer look at two small-cap players in the patch offering considerable potential upside.

### This company aims for growth through accretive acquisitions

It was only earlier this year that Canadian intermediate oil producer **Long Run Exploration** (TSX: LRE) successfully transitioned to a dividend-plus-growth operational model. This is focused on rewarding investors through a regular monthly dividend while growing the company's core assets and ultimately its share price through a range of accretive acquisitions.

Since then, Long Run has entered into an agreement to acquire **Crocotta Energy** (TSX: CTA) for \$357 million, adding almost 33 million barrels of oil reserves and additional daily production of 7,500 barrels of crude, weighted to 30% oil. This acquisition, along with an earlier one in April 2014, has seen Long Run revise its full-year 2014 guidance upward, with forecast oil production up 22% compared to

its original 2014 guidance, to 32,100 barrels daily.

As a result, funds flow from operations has increased by 16% to \$320 million, and the annual dividend increased by 2.6% to \$0.4125 per share.

These figures indicate that the company is well positioned to continue growing oil and gas production, funds flow from operations, and its bottom line, allowing it to further reward investors over the long term.

### **This relative newcomer to the patch continues to surge ahead**

Another small-cap operator in the patch with solid growth prospects is **Surge Energy** ([TSX: SGY](#)), which recently closed the acquisition of **Longview Oil** (TSX: LNV) for around \$430 million. This transaction has boosted Surge's oil reserves by a massive 51%, or by almost 38 million barrels, and increased its daily production by 66%, or 5,700 barrels, both of which have a weighting of 80% light and medium oil. This leaves Surge well-positioned to take advantage of higher crude prices.

Thus, the company has revised its 2014 guidance with average daily production forecast to increase by 29% compared to its earlier 2014 guidance, which will see funds flow from operations jump a healthy 34% to \$326 million. This has allowed Surge to also announce a dividend increase, with its annual dividend boosted by 11% to \$0.60 per share, or \$0.05 monthly. This means that Surge has a very tasty yield of 8.6%, one of the highest in the patch.

Clearly, such strong production growth will continue to see revenue and cash flow grow. When combined with higher oil prices, these companies will see stronger bottom lines and higher dividend payments, pushing share prices higher. This will see patient, risk-tolerant investors further rewarded as both companies continue to execute their growth strategies.

### **CATEGORY**

1. Investing

### **TICKERS GLOBAL**

1. TSX:SGY (Surge Energy Inc.)
2. TSX:SU (Suncor Energy Inc.)

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