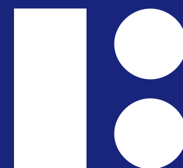


KAUPTHING

# Tanganyika Oil Company

**Buy**
(initiating coverage)
Price SEK 116.8
Target 210.0

## Join what looks set to be an amazing story

We are initiating coverage of Tanganyika with a Buy rating and a target price of SEK 210 per share. With outstanding earnings growth ahead, we see an exceptional buying opportunity.

**Continuously high oil prices expected.** We expect oil prices to remain high in an increasingly tight global market. After 2008, prices may ease along with increasing global production capacity, but risks are on the upside as producers struggle to keep up with demand.

**Outstanding earnings growth ahead.** We forecast that the Syrian fields will reach approximately 15,000bopd by the end of 4Q07, increasing to 59,000bopd in 2009. Future production looks set to be exceptionally profitable, and we forecast EPS of SEK 33 in 2009.

**Political and production delay risks.** Syria has a CCC credit rating and is accordingly a relatively risky country to invest in. Also, the company has been struggling with production delays lately. We have added a 5% Country Risk Premium and a 5% Country Specific Risk Premium to our discount rate in order to reflect these risks.

**Share price could reach SEK 290 by 2009.** Our analysis suggests that the share is trading at a P/E of 3.6x on 2009E earnings. We believe that the market could very well assess a seeing-is-believing P/E multiple of 9x 2009E EPS, indicating a share price of SEK 290 in two years. Consequently, we consider the current valuation extremely attractive and initiate coverage of Tanganyika Oil with a Buy rating and a target price of SEK 210, supported by our NAV of SEK 236.

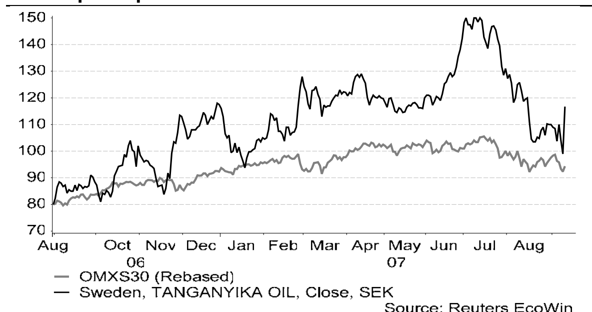
| | Sales (USDm) | EBITDA (USDm) | PTP (adj.) | EV/ sales | EPS (adj.) | EV/ EBITDA | P/E (adj.) | FCF yield (%) | Yield (%) |
|---|---|---|---|---|---|---|---|---|---|
| 2005 | 18 | 4 | 1 | n.m. | n.m. | n.m. | n.m. | n.m. | n.m. |
| 2006 | 33 | 33 | 19 | 22.33 | 0.4 | 22.3 | 42.9 | -1.4% | 0.0 |
| 2007E | 53 | 11 | -9 | 18.53 | -0.2 | 92.8 | n.m. | -10.0% | 0.0 |
| 2008E | 316 | 187 | 140 | 3.34 | 2.5 | 5.6 | 7.0 | -6.8% | 0.0 |
| 2009E | 583 | 382 | 277 | 1.60 | 4.9 | 2.4 | 3.6 | 12.2% | 11.2 |

**Share data**

| | |
|---|---|
| Market cap (SEKm) | 6,631 |
| Number of shares (m) | 56.8 |
| Bloomberg code | TYKSSDB SS |
| Reuter code | TYKSsdb.ST |
| Average volume | 649,693 |

| Performance | 1M | 3M | 12M |
|---|---|---|---|
| Abs. perf. (%) | -5 | -3 | 39 |
| Rel. to OMXS30 | -5 | 3 | 21 |

**Share price performance**




Source: Kaupthing estimates, company data. Share price as of Sep 11 2007.

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See important disclosures on last page of this report

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# Our investment case

Tanganyika Oil Company Ltd. is a Canadian oil and gas E&P company with interests in exploration and development properties in Syria. The operations in Syria consist of a 100% participating interest in the Oudeh block as well as the Tishrine and Sheik Mansour blocks located in the northeastern parts of the country.

Tanganyika Oil's shares are traded on the TSX Venture Exchange in Canada under the symbol "TYK" and on Stockholmsbörsen in Sweden under the symbol "TYKS". Currently, the market capitalization is approximately SEK 6bn with 56.8 million shares (fully diluted) outstanding. We initiate coverage of Tanganyika Oil with a Buy rating and a target price of SEK 210. The main arguments for our stance are:

- **Favourable oil market outlook**. We believe oil prices will remain high in an increasingly tight global market. After 2008, prices may ease along with increasing global production capacity, but risks are on the upside as producers struggle to keep up with demand.

- **Extensive growth ahead**. In total, we forecast that the Syrian fields will reach approximately 15,000bopd by the end of 4Q07, increasing to 59,000bopd in 209E. We estimate that Tanganyika's share of this will be 5,400bopd in 4Q07, increasing to 32,000bopd by 2009E. The profitability of this future production looks set to be exceptionally high and we forecast EPS of SEK 33 in 2009, increasing to SEK 52 in 2010E.

- **30% IRR**. Our net asset value approach suggests that future cash flows give an investor 30% annual return at current market cap. Our opinion is that an investor should demand an excess return, at least for the next couple of years when production delay risk is significant. However, we believe 20% return for the next five years and 15% thereafter gives an investor enough reward for risk taken.

- **The share price could reach SEK 290 by 2009**, or even up to SEK 500 in a "blue-skies" scenario. Our analysis suggests that the share is trading at a P/E of 3.6x on 2009E earnings. We believe that the market could very well assess a "seeing-is-believing" P/E multiple of 9x on 2009E earnings, indicating a share price of SEK 290 in two years' time. In a "blue-skies" scenario, we see potential upside to SEK 500.

- **No smoke without fire**. On 10 September, Dagens Industri reported that the state-owned Chinese oil company CNPC and another unnamed Chinese company had ongoing negotiations with Tanganyika in order to place a SEK 10bn bid for the entire Syrian operations. On the same day, Tanganyika denied being involved in any kind of discussions regarding selling the Syrian assets. However, with current valuation, Tanganyika is a clear takeover target and we would not be surprised to see an official bid for the company in the mid term.

- **Attractive valuation**. The stock is trading below our net asset value of SEK 236 and our target price of SEK 210 per share, suggesting 80% potential to current market valuation. Consequently, we consider the current risk/reward ratio extremely attractive.

# Valuation and recommendation

*Target price SEK 210*

We initiate coverage with a Buy rating and a target price of SEK 210 per share. Our target price is based on a NPV-adjusted (applying 20% WACC) P/E of 9x 2009E earnings. The WACC is derived on the following basis.

**WACC 2007-2012E**

| (USD) | |
|---|---|
| Risk free rate | 4.7% |
| Beta | 1.3 |
| ERP | 4.0% |
| CRP | 5.0% |
| CSRP | 5.0% |
| **WACC** | **20.0%** |
| | |
| Equity financing | 100.0% |
| Debt financing | 0.0% |

Note: ERP = Equity market Risk Premium, CRP = Country Risk Premium of Syria, CSRP = Company Specific Risk Premium

Source: Kaupthing estimates and company data

**WACC 2013-2029E**

| (USD) | |
|---|---|
| Risk free rate | 4.7% |
| Beta | 1.3 |
| ERP | 4.0% |
| CRP | 5.0% |
| CSRP | 0.0% |
| **WACC** | **15.0%** |
| | |
| Equity financing | 100.0% |
| Debt financing | 0.0% |

Source: Kaupthing estimates and company data

Note that we have applied a Country Risk Premium (CRP), assignable to Syria, of 5% and a Company Specific Risk Premium (CSRP) of 5% for the projected cash flows in 2007-2012. The CRP is based on Syria's CCC credit rating and will not change until the credit rating improves. However, the CSRP will decrease gradually as soon as we see signs of production reaching our targets.

*NAV of SEK 236*

We have also calculated a NAV for Tanganyika's operations of SEK 236 per share. The NAV is based on discounted expected cash flows from the Syrian oil fields, Oudeh and Tishrine, in 2007-2029. The production forecast is based on a probability weighted reserve calculation on the respective reserve level. Any potential production from the Sheikh Mansour/Sheikh Suliman block is not included.

**Net asset value summary**

| (USDm) | 3Q-4Q07E | 2008E | 2009E | 2010E | 2011E | 2012E | 2013E-2029E |
|---|---|---|---|---|---|---|---|
| Net income | -2 | 140 | 277 | 442 | 609 | 740 | 2,377 |
| EPS (USD) | 0.0 | 2.5 | 4.9 | 7.8 | 10.7 | 13.0 | 41.8 |
| EPS (SEK) | -0.2 | 16.5 | 32.6 | 52.2 | 71.8 | 87.3 | 280.4 |
| **Operating cash flow** | **11** | **187** | **382** | **597** | **794** | **947** | **4,264** |
| Net working capital change | 0 | -13 | -13 | -14 | -13 | -10 | 65 |
| Capital expenditures | -65 | -238 | -247 | -230 | -242 | -179 | -1,626 |
| **Free cash flow** | **-55** | **-64** | **122** | **353** | **540** | **758** | **2,703** |
| WACC | 20% | 20% | 20% | 20% | 20% | 20% | 15% |
| Discounted FCF | -54 | -55 | 87 | 211 | 268 | 314 | 1,117 |

| **NPV** | |
|---|---|
| 2007E-2012E | 771 |
| 2013E-2030E | 1,117 |
| **EV** | **1,888** |
| Net cash | 109 |
| **Value of shares** | **1,997** |
| - Per share (USD) | 35 |
| - Per share (SEK) | 236 |

Source: Kaupthing estimates and company data

We have estimated the net cash position based on reported cash and debt and then added approximately USD 70m equal to cash received from the sale of the Egyptian operations.

Our analysis suggests that the share is trading at a P/E of 3.6x on 2009E earnings. We believe that the market could very well assess a future P/E multiple of 9x on 2009E earnings, indicating a share price of SEK 290 in two years' time. This gives a potential return of approximately 150% in less than two years' time, based on the current share price level.

*Share price could reach SEK 290 by 2009*

## Sensitivity analysis

Tanganyika's earnings are highly sensitive to changes in oil prices and investors' required return. We have performed a NAV simulation by varying these variables.

**NAV simulation (SEK per share)**

| WACC 2008-2012 | Average brent oil price 2008-2012 | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | **46** | **50** | **54** | **58** | **62** | **66** | **70** | **74** | **78** | **82** | **86** |
| **10%** | 71 | 142 | 213 | 284 | 355 | 426 | 497 | 568 | 639 | 710 | 781 |
| **12%** | 60 | 123 | 186 | 249 | 311 | 374 | 437 | 500 | 563 | 626 | 689 |
| **14%** | 50 | 106 | 162 | 218 | 275 | 331 | 387 | 443 | 500 | 556 | 612 |
| **16%** | 42 | 92 | 143 | 193 | 244 | 294 | 345 | 395 | 446 | 496 | 547 |
| **18%** | 35 | 80 | 126 | 171 | 217 | 263 | 308 | 354 | 399 | 445 | 491 |
| **20%** | 29 | 70 | 111 | 153 | 194 | **236** | 277 | 318 | 360 | 401 | 442 |
| **22%** | 24 | 61 | 99 | 137 | 175 | 212 | 250 | 288 | 325 | 363 | 401 |
| **24%** | 19 | 54 | 88 | 123 | 157 | 192 | 226 | 261 | 295 | 330 | 364 |
| **26%** | 16 | 48 | 79 | 111 | 143 | 174 | 206 | 238 | 269 | 301 | 333 |
| **28%** | 13 | 42 | 71 | 100 | 130 | 159 | 188 | 217 | 247 | 276 | 305 |
| **30%** | 10 | 37 | 64 | 91 | 118 | 145 | 172 | 199 | 226 | 254 | 281 |
| **32%** | 8 | 33 | 58 | 83 | 108 | 133 | 158 | 184 | 209 | 234 | 259 |
| **34%** | 6 | 29 | 53 | 76 | 99 | 123 | 146 | 170 | 193 | 216 | 240 |

Source: Kaupthing estimates

We note that the market currently applies an extremely high risk premium (~18-34% WACC) to future cash flows for Tanganyika in combination with substantially lower oil prices (~USD 54–66pbo). Also interesting is that if current oil prices remain and the company delivers in line with our production forecast, we see a NAV in the range of SEK 395–500 per share in today's money.

*If current oil prices remain and if the company delivers, we see NAV of SEK 395-500*

# Earnings estimates

*We forecast EPS of SEK 33 in 2009, increasing to SEK 52 in 2010*

We expect oil prices to remain high in an increasingly tight global market. After 2008, prices may ease along with increasing global production capacity, but risks are on the upside as producers struggle to keep up with demand.

On the production level, we forecast that the Syrian fields will reach approximately 15,000bopd by the end of 4Q07, increasing to 59,000bopd in 2009E and 107,000bopd in 2011E. This future production looks set to be exceptionally profitable, and we forecast EPS of USD 4.9 (SEK 33) in 2009, increasing to USD 7.8 (SEK 52) in 2010.

**Interim breakdown**

| (USDm) | 1Q07 | 2Q07 | 3Q07E | 4Q07E | 2006 | 2007E | 2008E | 2009E | 2010E | 2011E |
|---|---|---|---|---|---|---|---|---|---|---|
| **Sales** | **7.5** | **10.1** | **11.2** | **24.5** | **32.8** | **53.3** | **315.7** | **583.0** | **861.3** | **1,114.0** |
| Production expenses | -2.3 | -5.6 | -6.6 | -11.1 | -15.3 | -25.5 | -105.7 | -176.5 | -237.5 | -290.6 |
| **Gross profit** | **5.2** | **4.5** | **4.6** | **13.5** | **17.5** | **27.8** | **210.0** | **406.6** | **623.7** | **823.4** |
| SG&A | -2.9 | -2.8 | -2.9 | -3.0 | -11.7 | -11.7 | -12.9 | -14.2 | -15.6 | -17.1 |
| Other income & costs - net | -1.7 | -1.9 | -1.0 | -0.8 | -3.3 | -5.5 | -10.0 | -10.3 | -11.0 | -11.8 |
| **EBITDA** | **0.6** | **-0.2** | **0.6** | **9.6** | **2.5** | **10.6** | **187.1** | **382.1** | **597.2** | **794.4** |
| Non-recurring items | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Depreciation and amortisation | -5.0 | -5.2 | -5.8 | -6.8 | -11.9 | -22.8 | -47.6 | -105.5 | -155.4 | -186.7 |
| **EBIT** | **-4.3** | **-5.5** | **-5.2** | **2.9** | **-9.4** | **-12.1** | **139.5** | **276.6** | **441.8** | **607.7** |
| Financial net | 0.6 | 0.5 | 0.2 | 0.0 | 1.2 | 1.3 | 0.0 | 0.0 | 0.4 | 0.9 |
| Exchange rate gains (losses) | 0.4 | 1.4 | 0.1 | 0.1 | 0.1 | 1.9 | 0.0 | 0.0 | 0.0 | 0.0 |
| **Pretax profit** | **-3.3** | **-3.6** | **-4.9** | **2.9** | **-8.2** | **-8.9** | **139.5** | **276.6** | **442.1** | **608.6** |
| Taxes | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| **Net income** | **-3.3** | **-3.6** | **-4.9** | **2.9** | **-8.2** | **-8.9** | **139.5** | **276.6** | **442.1** | **608.6** |
| **Adjusted results** | | | | | | | | | | |
| Items affecting comp. | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Operating result | -4.3 | -5.5 | -5.2 | 2.9 | -9.4 | -12.1 | 139.5 | 276.6 | 441.8 | 607.7 |
| Pretax result | -3.3 | -3.6 | -4.9 | 2.9 | -8.2 | -8.9 | 139.5 | 276.6 | 442.1 | 608.6 |
| Net income | -3.3 | -3.6 | -4.9 | 2.9 | -8.2 | -8.9 | 139.5 | 276.6 | 442.1 | 608.6 |
| **Margins** | | | | | | | | | | |
| Gross margin | 69.5% | 44.9% | 41.1% | 55.0% | 53.3% | 52.2% | 66.5% | 69.7% | 72.4% | 73.9% |
| EBIT margin | -57.8% | -54.1% | -46.4% | 11.7% | -28.8% | -22.7% | 44.2% | 47.4% | 51.3% | 54.6% |
| **Cost structure, % of sales** | | | | | | | | | | |
| Production expenses | 30.5% | 55.1% | 58.9% | 45.0% | 46.7% | 47.8% | 33.5% | 30.3% | 27.6% | 26.1% |
| SG&A | 39.1% | 28.1% | 26.2% | 12.3% | 35.7% | 22.0% | 4.1% | 2.4% | 1.8% | 1.5% |
| Other | 13.3% | 14.6% | 7.5% | 3.4% | 6.2% | 7.8% | 3.2% | 1.8% | 1.2% | 1.0% |
| **Growth** | | | | | | | | | | |
| Sales (yoy) | 2.9% | 35.0% | 5.6% | 229.8% | | 62.6% | 492.1% | 84.7% | 47.7% | 29.3% |
| Sales (qoq) | 1.0% | 34.3% | 10.5% | 120.0% | | n.a. | n.a. | n.a. | n.a. | n.a. |
| Operating result (yoy) | n.m | -10.7% | 18.0% | n.m | | 28.4% | n.m. | 98.2% | 59.7% | 37.6% |
| Pretax result (yoy) | n.m | -14.3% | 19.5% | n.m | | 8.5% | n.m. | 98.2% | 59.9% | 37.7% |
| **Earnings per share** | | | | | | | | | | |
| Tax (%) | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% |
| EPS (USD) | -0.06 | -0.06 | -0.09 | 0.05 | -0.16 | -0.16 | 2.46 | 4.87 | 7.78 | 10.72 |
| EPS (SEK) | -0.4 | -0.4 | -0.6 | 0.3 | -1.1 | -1.1 | 16.5 | 32.6 | 52.2 | 71.8 |
| No of shares, diluted | 56.6 | 56.7 | 56.8 | 56.8 | 51.9 | 56.7 | 56.8 | 56.8 | 56.8 | 56.8 |

Source: Kaupthing estimates and company data

### Kaupthing estimates vs. consensus

Comparing our estimates with consensus, we see that large deviations appear on the earnings level for 2008 and 2009. We believe this is mainly because we are more aggressive on cost recovery for the company.

**Kaupthing vs. consensus estimates**

| USDm | 2007E | 2008E | 2009E |
|---|---|---|---|
| **Sales** | | | |
| Kaupthing | 53 | 316 | 583 |
| Consensus | 58 | 304 | 667 |
| - Diff to consensus | -8% | 4% | -13% |
| **EBIT** | | | |
| Kaupthing | -12 | 140 | 277 |
| Consensus | -11 | 95 | 188 |
| - Diff to consensus | 6% | 47% | 47% |
| **Net income** | | | |
| Kaupthing | -9 | 140 | 277 |
| Consensus | -12 | 89 | 172 |
| - Diff to consensus | -26% | 57% | 61% |
| Consensus min | -18 | 26 | 45 |
| Consensus max | -6 | 140 | 277 |
| **EPS (USD)** | | | |
| Kaupthing | -0.2 | 2.5 | 4.9 |
| Consensus | -0.2 | 1.4 | 3.0 |
| - Diff to consensus | -27% | 73% | 61% |
| Consensus min | -0.3 | 0.5 | 0.8 |
| Consensus max | -0.1 | 2.5 | 4.9 |
| Nr of estimates | 5 | 5 | 3 |

Source: Kaupthing estimates and JCF

## Risks to our case

*Key risks relate to lower oil prices and production delays*

Since Tanganyika keeps its expected oil production unhedged, the main risk factor we see to our investment case and estimates is related to lower oil prices and production delays.

- **Lower oil prices**. Lowering our oil price forecast by 10% on a straight line basis would have a negative impact of 25% on NAV.
- **Production delays**. The company has been struggling with production delays lately and further delays cannot be ruled out, which could place the company in need of further cash. In our model, postponing all production by one year would lower NAV by 14%.
- **Political risk**. Syria has a CCC credit rating and is accordingly a relatively risky country to invest in. If credit ratings were to deteriorate, this could add an additional 5% CRP to our discount rate and impact NAV negatively by 22%.

# Oil market

## Summary

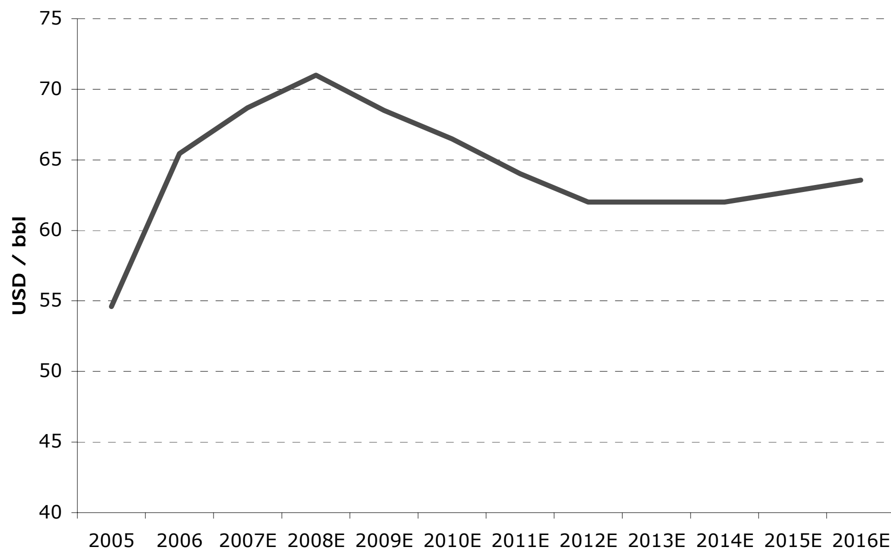
*Continuously high oil prices expected*

We expect oil prices to stay above USD 70/bbl through 2008, as global markets are tight and may become even tighter this autumn, with stronger-than-expected demand growth and project delays adding to OPEC production cuts. Non-OPEC production continues to disappoint.

After 2008, prices are expected to soften as OPEC and non-OPEC production capacity increases, improving the global supply/demand balance. For non-OPEC members, increased production from FSU and Brazil and growth in non-conventional oil and NGL outweigh project delays and declines in mature areas. A gradual easing of the refinery situation is supporting the downward trend. However, there is a risk that supply growth might not materialise in line with expectations, resulting in tight supply and sustained high oil prices beyond 2008.

In the long term, a tightening demand/supply balance and increasing OPEC market power is expected to gradually increase prices. By 2015, we expect non-OPEC production to be past its peak. OPEC is expected to continue to adjust capacity expansion according to the projected call-on-OPEC, but large investments are required to enable production capacity to keep up with demand. OPEC will gain more market power and be able to target increasingly higher prices.

**Oil price assumptions (Brent)**




Source: Kaupthing estimates

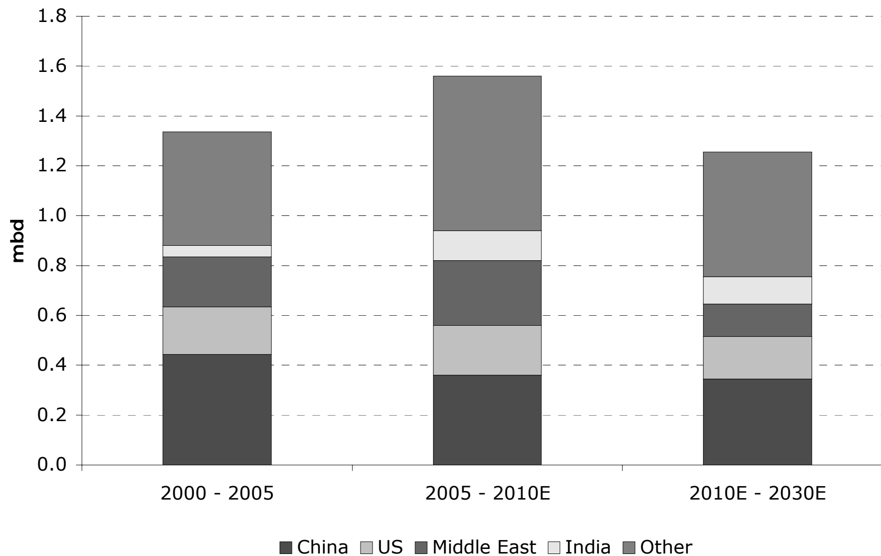
## Demand

Oil demand is expected to be strong and to continue to grow steadily. The growth will be particularly strong in the near term, due to high economic growth globally. For the next five years, we expect average annual demand growth of 1.7mbd. China, the United States and the Middle East are the major contributors to the increase in oil consumption, accounting for more than two thirds of the growth. Oil demand in China has grown by almost 40% since 2003, and we expect this strong growth to continue.

Domestic production covers almost 50% of oil consumption in China this year, but with strong demand growth and virtually flat production outlook, imports look set to increase by 45% over the next four years.

The transportation sector is the main driver of demand growth globally, accounting for over half of the increase.

**Annual demand growth 2000-2030E**




Source: Kaupthing estimates and IEA

## Unconventional supply

Alternative supply, such as biofuels and oil sands, will increase rapidly – but from a small share. Biofuels are expected to show strong growth over the next years, backed by political support, but growth is limited by availability of land and water and by competition with food production.

Alternative energy supply, such as solar and wind power, is growing strongly, but will remain a minor share of total energy use. The IEA predicts use of renewables other than biomass to expand fivefold by 2030, growing to 1.7% of world primary energy demand. However, growth in renewables will generally not replace oil, as an increasing share of oil is used in the transportation sector.

Canada has an enormous resource base, and Canadian oil sands producers expect to be delivering around 3 million b/d of synthetic crude by 2015, up from about 1.2 million b/d by the end of this year. The rapid expansion has led to cost overruns and delays, and performance beyond 2015 is uncertain. Just getting to the target figure will be challenging enough, as a number of factors could slow the effort in spite of high oil prices.

The development of heavy oil projects in Venezuela beyond the 0.6mbd produced in 2006 is expected to be significantly delayed after the nationalisation of oil resources, where Conoco and ExxonMobil chose to abandon their projects.

Gas-to-liquids and Coal-to-liquids (GTL/CTL) were expected to show strong growth, but gas price increases and significant cost overruns have dampened the optimism. New projects seem to be on hold until experience can be drawn from existing projects.

## Conventional supply

We expect the largest non-OPEC production increases to come from the FSU, followed by Latin America. Towards 2010, production in North America, Africa and Asia should grow somewhat, before starting to decline. After this period, we believe that supply increases from growth regions will not be able to offset the decline in mature areas, and we expect non-OPEC production to peak.

Supply is difficult to estimate, and there is a risk that production targets will not be met. Rates of decline could be steeper than expected or capacity additions could be smaller due to shortages of skilled personnel and equipment, regulatory delays, cost inflation and geopolitics. If supply does not keep up with demand growth, markets will remain tight and prices will remain at high levels.

Non-crude liquids will add significant amounts to global production growth. Rising natural gas production, particularly in the Middle East, will increase natural gas liquids (NGL) and condensate output. We expect OPEC NGLs to grow 2mbd over the next five years.

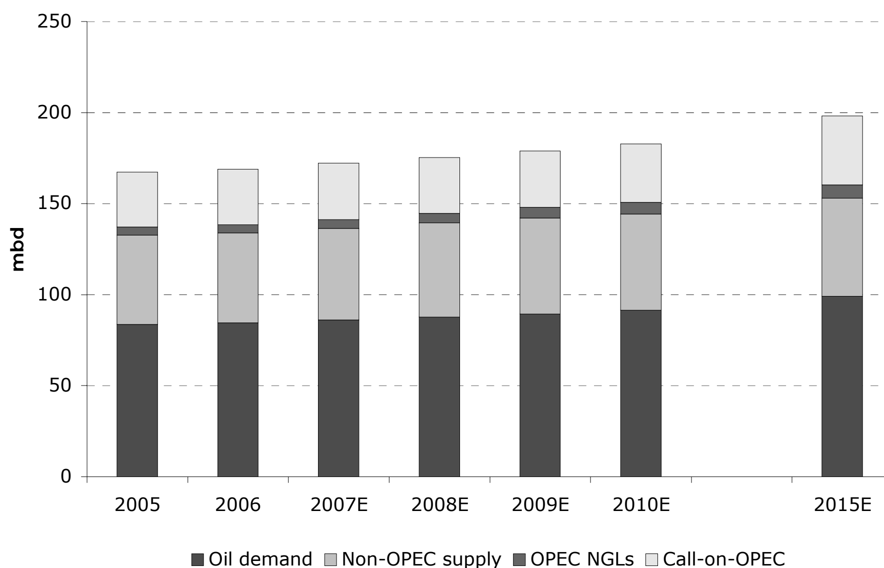
OPEC is expected to continue to adjust production and capacity expansion according to the expected call-on-OPEC. For the next five years, increased demand will be at least 3mbd and probably more, considering that non-OPEC production continues to disappoint.

All OPEC countries except Qatar and Indonesia are expected to increase production capacity in the long term, with the largest capacity increases in Saudi Arabia, Iraq and Iran – the countries with the largest conventional oil resources.

Increasing tightness in the global oil market after 2015 will put upward pressure on crude oil prices. With non-OPEC production in decline, and limits to growth in unconventional production, OPEC's market power will increase over time and it will be able to target an increasingly high oil price.

However, large investments are needed to increase production capacity. The IEA has estimated that cumulative global investment in the oil sector will amount to about USD 164bn per year towards 2030 to meet the growing oil demand. If industry investment falls behind the level required to meet future demand, a crisis is threatening. Any distortion of the market equilibrium may lead to booming crude prices. Several factors could cause under-investment. Governments' policy could be to keep resources for future generations. The political, security or infrastructure situation may prevent investment, as may lack of capital and/or the know-how to develop projects, and restriction of access for foreign investments due to national sovereignty (as has been seen recently). Fiscal and/or contractual terms can reduce the profitability of projects, or the escalating costs may delay investment decisions.

**Global balance to 2015E**




Source: Kaupthing estimates and IEA

## Risk factors

There is significant uncertainty regarding many of the key variables to the forecasts, such as the resource base, production growth, economic growth, environmental policies, and geopolitical development. However, risks are definitely on the upside. With the current strong global economic growth, supply may have difficulties keeping up with demand. Large investments are needed to increase production capacity: What will happen if these investments do not take place? Any distortion of the market equilibrium may lead to increased crude prices.

## Refinery capacity

The tight refinery situation in the US has contributed to the oil price increases this year. Significant expansion of global refining capacity over the next few years has been announced, but escalating engineering and construction costs may slow refinery growth. Higher investment costs render some refinery projects less likely. As a result, the refinery market may remain relatively tight, especially as product demand shows robust growth. Additional capacity is needed as increasing amounts of sour, heavy crude are produced, and mid-distillates are increasingly in demand.

# Oil production and revenues

## Oil production

*Probability weighted reserves of 744mbo*

The production forecast presented below is based on probability-weighted reserves on the three levels, 1P, 2P and 3P. The first level, 1P, is weighted with 90% probability, 2P with 50% and 3P with 10%, which results in weighted gross reserves of 465mbo, which should be put in relation to unweighted 1P+2P reserves of 744mbo.

**Probability-weighted reserves**

| | Oudeh | Tishrine | **Total** |
|---|---|---|---|
| **Assessed probabilities** | | | |
| 1P | 90% | 90% | |
| 2P | 50% | 50% | |
| 3P | 10% | 10% | |
| **1P + 2P Reserves** | | | |
| **Heavy Oil** | | | |
| Gross (Total field) | 344 | 400 | **744** |
| Net (Company share) | 200 | 201 | **401** |
| **Natural Gas Liquids** | | | |
| Gross (Total field) | 199 | 0 | **199** |
| Net (Company share) | 119 | 0 | **119** |
| **3P Reserves** | | | |
| **Heavy Oil** | | | |
| Gross (Total field) | 136 | 119 | **255** |
| Net (Company share) | 74 | 93 | **168** |
| **Natural Gas Liquids** | | | |
| Gross (Total field) | 0 | 0 | **0** |
| Net (Company share) | 1 | 0 | **1** |
| **Probability weighted** | | | |
| **Heavy Oil** | | | |
| Gross (Total field) | 222 | 243 | **465** |
| Net (Company share) | 127 | 125 | **252** |
| **Natural Gas Liquids** | | | |
| Gross (Total field) | 159 | 0 | **159** |
| Net (Company share) | 92 | 0 | **92** |

Source: Kaupthing estimates and company data

In order for the company to reach designated production targets, it is absolutely essential to get access to drilling equipment and relevant personal expertise. Management has stated end-FY07 production goals for Syria at 23– 26,000bopd (gross field) and 10-12,000bopd (company share). (A detailed description of how the company share is derived as a function of oil field production can be found in the Appendix to this report.) However, due to issues relating to rig logistics, water handling and electricity, we believe the expected production ramp-up will be delayed. We forecast year-end production to reach 15,000bopd (gross field) and 5,000bopd (company share).

At the end of 2Q07, the company had four drilling rigs, one work-over (maintenance) rig and two steam generators in operation in Syria. In 3Q07, based on company guidance, we expect six drilling rigs, three work-over rigs and six steam generators to be in operation. Working at maximum efficiency, one drilling rig is able to drill five wells per quarter in Oudeh and seven wells per quarter in Tishrine. However, the rigs are unlikely to work at 100% utilisation on a continuous basis (maintenance, time slack between wells, etc). For 2Q07, the drilling utilisation was only 60% due to the problems mentioned above. We believe that the problems recorded in 2Q07 will continue to have a hampering effect also in 3Q07 and hence we expect the drilling utilisation to remain at 60% for this quarter. For the period going forward, we expect utilisation to improve to a stable 80%.

Based on discussions with management, we expect the company to increase the total number of drilling rigs to eight on average for 2008, divided equally between Oudeh and Tishrine. These rigs will, assuming 80% utilisation, be able to drill 65 wells per year in Oudeh and 97 wells in Tishrine.

After wells have been drilled, steam generators will be applied to boost production. This process is divided into three steps; steaming, soaking and production (described in more detail in the Appendix). One cycle is approximately 110 days, of which production is 90 days, soaking two days and steaming 20 days. After that, the well has to go through a new cycle.

We are assuming that, on average, eight steam generators will be available to the company in 2008, and that an additional six generators will be added each year until 2012-2013E, when production is expected to be at maximum level.

In total, we forecast that the Syrian fields will reach approximately 15,000bopd by 4Q07, increasing to 59,000bopd in 2009E. The company share will accordingly be 5,400bopd for 4Q07E, increasing to 32,000bopd by 2009E.

**Oil production breakdown (pro forma, excl. Egypt)**

| | 1Q07 | 2Q07 | 3Q07E | 4Q07E | 2007E | 2008E | 2009E | 2010E | 2011E | 2012E |
|---|---|---|---|---|---|---|---|---|---|---|
| **Oudeh** | | | | | | | | | | |
| Nr of drilling rigs in operation | 1 | 2 | 3 | 3 | 2 | 4 | 4 | 4 | 5 | 5 |
| Drilling days (per well) | 18 | 18 | 18 | 18 | 18 | 18 | 18 | 18 | 18 | 18 |
| - Utilisation factor | 90% | 60% | 60% | 80% | 73% | 80% | 80% | 80% | 80% | 80% |
| Nr of wells drilled | 4 | 6 | 9 | 12 | 31 | 65 | 65 | 65 | 81 | 81 |
| Nr of producing wells (BoP) | 25 | 29 | 35 | 44 | 25 | 56 | 121 | 186 | 251 | 332 |
| Nr of producing wells (EoP) | 29 | 35 | 44 | 56 | 56 | 121 | 186 | 251 | 332 | 413 |
| Average nr of wells | 27 | 32 | 40 | 50 | 41 | 89 | 154 | 219 | 292 | 373 |
| Average volume per well (bopd) | 93 | 76 | 80 | 105 | 83 | 154 | 145 | 140 | 137 | 133 |
| **Gross field production (kbo)** | **226** | **222** | **291** | **482** | **1,221** | **4,973** | **8,107** | **11,200** | **14,526** | **18,086** |
| - bopd | 2,509 | 2,440 | 3,160 | 5,241 | 3,344 | 13,626 | 22,211 | 30,684 | 39,797 | 49,550 |
| ICOP after BCP and royalty (kbo) | 127 | 124 | 184 | 353 | 787 | 4,085 | 6,840 | 9,559 | 12,481 | 15,608 |
| - bopd | 1,408 | 1,362 | 2,001 | 3,832 | 2,157 | 11,191 | 18,740 | 26,189 | 34,195 | 42,761 |
| Profit oil (bopd) | 422 | 408 | 600 | 1,150 | 647 | 3,357 | 5,622 | 7,857 | 10,259 | 12,828 |
| Cost oil (bopd) | 985 | 953 | 1,401 | 2,682 | 1,510 | 7,834 | 13,118 | 18,332 | 23,937 | 29,932 |
| Company share of profit oil (bopd) | 127 | 123 | 180 | 345 | 194 | 1,007 | 1,687 | 2,357 | 3,078 | 3,848 |
| Company share of cost oil (bopd) | 973 | 944 | 1,401 | 2,682 | 1,504 | 7,834 | 13,118 | 18,332 | 23,937 | 29,932 |
| **Total company production (bopd)** | **1,100** | **1,067** | **1,581** | **3,027** | **1,699** | **8,841** | **14,805** | **20,689** | **27,014** | **33,781** |
| **Tishrine-Sheikh Mansour** | | | | | | | | | | |
| Nr of drilling rigs in operation | 2 | 2 | 3 | 3 | 3 | 4 | 4 | 4 | 3 | 0 |
| Drilling days (per well) | 11 | 12 | 12 | 12 | 12 | 12 | 12 | 12 | 12 | 12 |
| - Utilisation factor | 25% | 40% | 60% | 80% | 51% | 80% | 80% | 80% | 80% | 80% |
| Nr of wells drilled | 4 | 6 | 14 | 18 | 42 | 97 | 97 | 97 | 73 | 0 |
| Nr of producing wells (BoP) | 134 | 138 | 144 | 158 | 134 | 176 | 273 | 370 | 467 | 540 |
| Nr of producing wells (EoP) | 138 | 144 | 158 | 176 | 176 | 273 | 370 | 467 | 540 | 540 |
| Average nr of wells | 136 | 141 | 151 | 167 | 155 | 225 | 322 | 419 | 504 | 540 |
| Average volume per well (bopd) | 45 | 48 | 48 | 60 | 49 | 95 | 115 | 125 | 133 | 147 |
| **Gross field production (kbo)** | **547** | **621** | **667** | **923** | **2,759** | **7,816** | **13,466** | **19,049** | **24,488** | **29,011** |
| - bopd | 6,083 | 6,826 | 7,248 | 10,034 | 7,558 | 21,415 | 36,893 | 52,188 | 67,090 | 79,481 |
| ICOP after BCP and royalty (kbo) | 1 | 71 | 117 | 347 | 536 | 5,055 | 10,088 | 15,057 | 19,897 | 23,931 |
| - bopd | 9 | 782 | 1,271 | 3,772 | 1,468 | 13,849 | 27,637 | 41,252 | 54,512 | 65,564 |
| Profit oil (bopd) | 4 | 407 | 661 | 1,961 | 763 | 7,202 | 14,371 | 21,451 | 28,346 | 34,093 |
| Cost oil (bopd) | 985 | 953 | 1,401 | 2,682 | 705 | 6,648 | 13,266 | 19,801 | 26,166 | 31,471 |
| Company share of profit oil (bopd) | 1 | 122 | 198 | 588 | 229 | 2,160 | 4,311 | 6,435 | 8,504 | 10,228 |
| Company share of cost oil (bopd) | 123 | 374 | 610 | 1,811 | 734 | 6,648 | 13,266 | 19,801 | 26,166 | 31,471 |
| **Total company production (bopd)** | **124** | **496** | **809** | **2,399** | **963** | **8,808** | **17,577** | **26,237** | **34,670** | **41,699** |
| **TOTAL** | | | | | | | | | | |
| Gross fields production (kbo) | 773 | 843 | 958 | 1,405 | 3,979 | 12,790 | 21,573 | 30,248 | 39,014 | 47,096 |
| - bopd | 8,592 | 9,266 | 10,408 | 15,275 | 10,902 | 35,041 | 59,105 | 82,872 | 106,887 | 129,031 |
| **Company production (bopd)** | **1,224** | **1,563** | **2,389** | **5,426** | **2,661** | **17,649** | **32,382** | **46,926** | **61,684** | **75,480** |

Source: Kaupthing estimates and company data

## Revenues

The oil price received for produced oil in the Oudeh and Tishrine fields is derived by a formula, based on a number of factors such as API (expresses the specific gravity of petroleum) and the price of Syrian heavy crude in general. Tanganyika does not disclose the formula, but management has guided that the quality of produced oil will improve going forward and, accordingly, the discount to Brent price will decrease from current levels of USD 24pbo to USD 14pbo in 2010.

As we expect continuously high prices and production will start to boost in 2008, we see significant sales increases going forward, with some stability reached from 2012 and forward.

**Revenue breakdown (pro forma, excl. Egypt)**

| | 1Q07 | 2Q07 | 3Q07E | 4Q07E | 2007E | 2008E | 2009E | 2010E | 2011E | 2012E |
|---|---|---|---|---|---|---|---|---|---|---|
| **Oudeh** | | | | | | | | | | |
| Average nr of wells | 27 | 32 | 40 | 50 | 41 | 89 | 154 | 219 | 292 | 373 |
| Average volume per well (bopd) | 93 | 76 | 80 | 105 | 83 | 154 | 145 | 140 | 137 | 133 |
| Field gross production (bopd) | 2,509 | 2,440 | 3,160 | 5,241 | 3,344 | 13,626 | 22,211 | 30,684 | 39,797 | 49,550 |
| **Company production (bopd)** | **1,099** | **1,067** | **1,581** | **3,027** | **1,699** | **8,841** | **14,805** | **20,689** | **27,014** | **33,781** |
| Realised price (USD per bo) | 36.4 | 46.8 | 52.0 | 52.0 | 46.8 | 51.0 | 51.5 | 52.5 | 50.0 | 48.0 |
| - Discount to Brent oil (USD per bo) | -25.4 | -23.0 | -21.0 | -21.0 | -22.6 | -20.0 | -17.0 | -14.0 | -14.0 | -14.0 |
| **Oil sales (USDm)** | **3.6** | **4.5** | **7.6** | **14.5** | **30.2** | **164.6** | **278.3** | **396.5** | **493.0** | **591.8** |
| **Tishrine-Sheikh Mansour** | | | | | | | | | | |
| Average nr of wells | 136 | 141 | 151 | 167 | 155 | 225 | 322 | 419 | 504 | 540 |
| Average volume per well (bopd) | 45 | 48 | 48 | 60 | 49 | 95 | 115 | 125 | 133 | 147 |
| Field gross production (bopd) | 6,083 | 6,826 | 7,248 | 10,034 | 7,558 | 21,415 | 36,893 | 52,188 | 67,090 | 79,481 |
| **Company production (bopd)** | **124** | **496** | **809** | **2,399** | **963** | **8,808** | **17,577** | **26,237** | **34,670** | **41,699** |
| Realised price (USD per bo) | 35.3 | 41.0 | 45.6 | 45.6 | 41.9 | 47.0 | 47.5 | 48.5 | 49.0 | 47.0 |
| - Discount to Brent oil (USD per bo) | -26.5 | -28.8 | -27.4 | -27.4 | -27.5 | -24.0 | -21.0 | -18.0 | -15.0 | -15.0 |
| **Oil sales (USDm)** | **0.4** | **1.9** | **3.4** | **10.1** | **15.7** | **151.1** | **304.7** | **464.5** | **620.1** | **715.3** |
| **TOTAL** | | | | | | | | | | |
| Fields gross production (bopd) | 8,592 | 9,266 | 10,408 | 15,275 | 10,902 | 35,041 | 59,105 | 82,872 | 106,887 | 129,031 |
| **Company production** | **1,223** | **1,563** | **2,389** | **5,426** | **2,661** | **17,649** | **32,382** | **46,926** | **61,684** | **75,480** |
| Realised price (USD per bo) | 36.3 | 44.9 | 49.8 | 49.2 | 47.2 | 49.0 | 49.3 | 50.3 | 49.4 | 47.4 |
| - Discount to Brent oil (USD per bo) | -25.5 | -24.9 | -23.2 | -23.8 | -22.2 | -22.0 | -19.2 | -16.2 | -14.6 | -14.6 |
| **Oil sales (USDm)** | **4.0** | **6.4** | **11.0** | **24.5** | **45.9** | **315.7** | **583.0** | **860.9** | **1,113.1** | **1,307.2** |

Source: Kaupthing estimates and company data

# Operating costs

*All production assignable costs are recovered eventually*

Tanganyika is able to recover all costs, except for SG&A, assignable to production and maintenance of the Syrian fields. This is realised through income from SPC's (the Syrian partner) share of the cost oil. If there is not enough income from cost oil to recover all production assignable costs, the costs that are not covered are accumulated and will be recovered through future cost oil income. Further details about cost recovery can be found in the Appendix.

Even though production costs are recovered eventually, these will have a significant impact on earnings, especially for 2007 and 2008. A significant part of the production costs for the next couple of years is assignable to well drilling. Management has guided that every well in the Oudeh and Tishrine fields has an initial cost of USD 1.2m and USD 0.8m respectively. The higher cost for Oudeh is mainly due to the fact that the reservoirs are on deeper levels, on average, in relation to the Tishrine reservoirs.

Other costs include direct production expenses and maintenance costs, and we find it reasonable to believe that these costs will be subject to economies of scale going forward. For the latest four quarters, these costs have varied in the interval of USD 8–10pbo for the Syrian operations, and management has guided that the costs should come down to around USD 5pbo. We have a more aggressive view of cost increases and have assumed that these costs will gradually decrease to USD 7pbo.

# Appendix

## Company overview

Tanganyika Oil Company Ltd. is a Canadian oil and gas exploration and production company with interests in exploration and development properties in Syria. The key operations in Syria consist of a 100% participating interest in the Oudeh block as well as the Tishrine and Sheik Mansour blocks located in the northeastern parts of the country.

Tanganyika Oil's shares are traded on the TSX Venture Exchange in Canada under the symbol "TYK" and on Stockholmsbörsen in Sweden under the symbol "TYKS". Currently, the market capitalization is approximately SEK 6bn with 56.8 million shares (fully diluted) outstanding.

## Reserves

As of 31 December 2006, Tanganyika reported proven and probable gross field reserves (including the Sheikh Mansour/Sheikh Suliman blocks) of 768 mbo.

**Reserves**

| (Mbo) | Oudeh | Tishrine | Sheikh Mansour / Sheikh Suliman | **Total** |
|---|---|---|---|---|
| Location | Syria | Syria | Syria | |
| **1P Reserves** | | | | |
| **Heavy Oil** | | | | |
| Gross (Total field) | 91 | 77 | 2 | **170** |
| Net (Company share) | 49 | 37 | 2 | **88** |
| **Natural Gas Liquids** | | | | |
| Gross (Total field) | 149 | 0 | 0 | **149** |
| Net (Company share) | 81 | 0 | 0 | **81** |
| **2P Reserves** | | | | |
| **Heavy Oil** | | | | |
| Gross (Total field) | 253 | 324 | 21 | **598** |
| Net (Company share) | 151 | 164 | 13 | **328** |
| **Natural Gas Liquids** | | | | |
| Gross (Total field) | 50 | 0 | 0 | **50** |
| Net (Company share) | 38 | 0 | 0 | **38** |
| **1P + 2P Reserves** | | | | |
| **Heavy Oil** | | | | |
| Gross (Total field) | 344 | 400 | 24 | **768** |
| Net (Company share) | 200 | 201 | 15 | **416** |
| **Natural Gas Liquids** | | | | |
| Gross (Total field) | 199 | 0 | 0 | **199** |
| Net (Company share) | 119 | 0 | 0 | **119** |
| **3P Reserves** | | | | |
| **Heavy Oil** | | | | |
| Gross (Total field) | 136 | 119 | 16 | **270** |
| Net (Company share) | 74 | 93 | 12 | **180** |
| **Natural Gas Liquids** | | | | |
| Gross (Total field) | 0 | 0 | 0 | **0** |
| Net (Company share) | 1 | 0 | 0 | **1** |
| **1P + 2P + 3P Reserves** | | | | |
| **Heavy Oil** | | | | |
| Gross (Total field) | 479 | 520 | 39 | **1,038** |
| Net (Company share) | 274 | 294 | 27 | **596** |
| **Natural Gas Liquids** | | | | |
| Gross (Total field) | 199 | 0 | 0 | **199** |
| Net (Company share) | 120 | 0 | 0 | **120** |

Source: Company data

## Operations

### Map of operations

Source: Reproduced with permission from Taganyika

### Infrastructure

A 57km pipeline from the Oudeh field transports the oil to the main pipeline, which gathers all of the Syrian heavy oil for shipping onward to the Homs refinery. From there, the oil is piped to the Tartus export terminal on the Mediterranean coast approximately 725 kilometres from the Oudeh oil station.

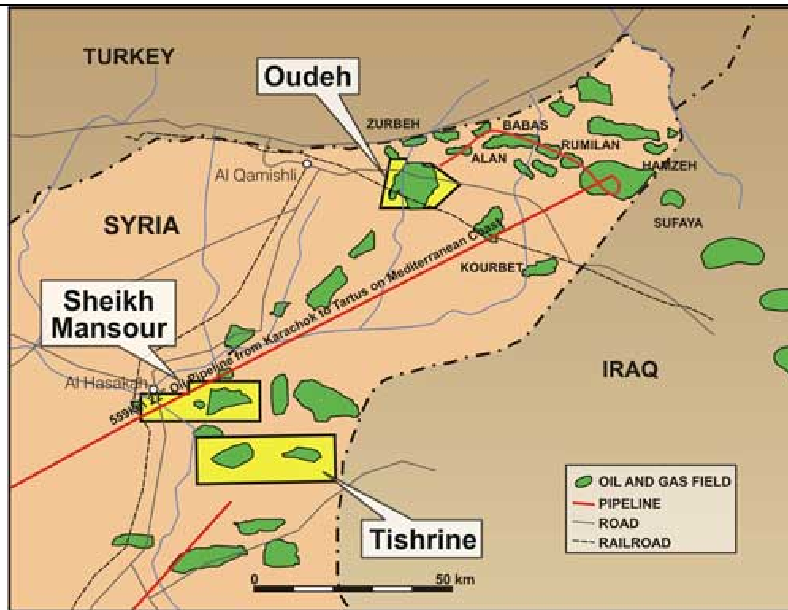
According to Tanganyika, the main pipeline has an estimated capacity of approximately 300,000bopd. The latest estimate is that the pipeline has spare capacity of 100-130,000bopd which is available for future development and expansion.

### Oudeh block

- Status: Development and production
- Participation interest: 100%
- Subsidiary: Dublin International Petroleum (Syria) Limited
- Partner: SPC (the "Syrian Petroleum Company" owned by the Syrian state)

The Oudeh block, which is located in the northeastern part of Syria and encompasses approximately 192 square kilometres, was acquired by Tanganyika in 2003. The contract (Contract for Development and Production) has a duration of 20 years with a provision for a five-year extension. The purpose of the contract is to increase oil recovery and crude oil production at the fields by applying enhanced oil recovery techniques. In 2Q07, Tanganyika's share of production from the Oudeh block reached 1,100bopd.

**Syria field map**




Source: Reproduced with permission from Taganyika

**Tishrine/Sheikh Mansour**

- Status: Development and production
- Participation interest: 100%
- Subsidiary: Dublin International Petroleum (Syria) Limited
- Partner: SPC

The Tishrine field, discovered in 1974, is located in the oil producing region of Jbisseh in the eastern parts of Syria, 120km southwest of the existing Oudeh field and 8km south of the Sheik Mansour field. Tishrine's gross production started exceeding the base crude production levels in the middle of 2006, and Tanganyika's share of production averaged approximately 500bopd in 2Q07.

## Production sharing agreements

### Oudeh

In May 2003, a Contract for Development and Production of Petroleum was signed between the Government of the Syrian Arab Republic, SPC and Oudeh PSA. The contract was approved by the Syrian Government in July the same year and has a duration of 20 years with a provision for a five-year extension.

The contract governs, among other things, the terms of the cost recovery formula and provides for certain obligations of Tanganyika Oil. Tanganyika Oil has an interest in all incremental production above the base crude production levels from wells in existence at the time the development contract was signed. The base crude production level declines at a rate of 5% per year calculated on a monthly basis. The table below shows a schedule of base crude production levels for the Oudeh block for 2006-2012E.

**Oudeh base crude production**

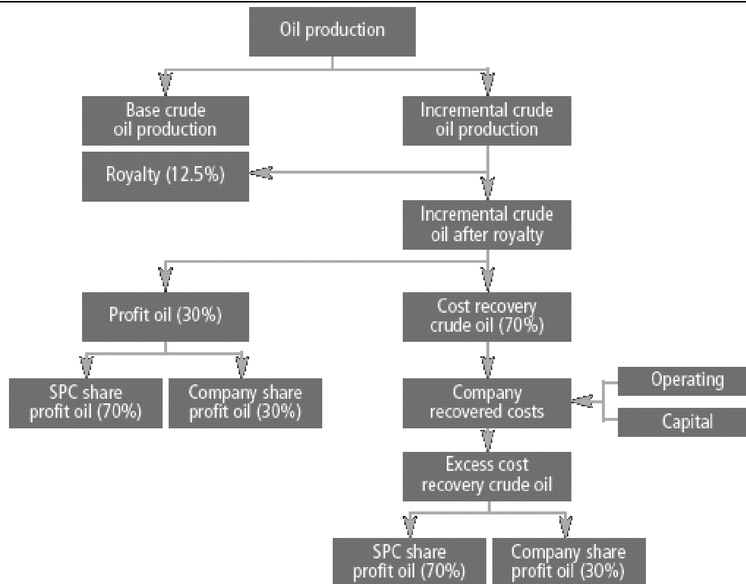
| | 2006 | 2007E | 2008E | 2009E | 2010E | 2011E | 2012E |
|---|---|---|---|---|---|---|---|
| BOPD | 916 | 880 | 836 | 794 | 754 | 717 | 681 |

Source: Kaupthing estimates and company data

After subtraction of the base crude production, a royalty of 12.5% is subtracted and submitted to the Syrian government. 30% of the shareable crude oil production from

the block is designated as profit oil and is split among SPC (70%) and Tanganyika Oil (30%). Up to 70% of the remaining crude oil production is available as cost oil to Tanganyika Oil to recover exploration, development and operating costs. To the extent that these costs exceed the proceeds from the sale of cost oil in any quarter, the excess can be carried forward into following quarters. If the costs are less than the proceeds of the cost oil, the excess proceeds are split between SPC (70%) and Tanganyika Oil (30%). All taxes are the responsibility of SPC from its share of profit and excess cost oil.

**Oudeh production sharing agreement**




Source: Reproduced with permission from Taganyika

### Tishrine-Sheikh Mansour

In November 2004, a Contract for Development and Production of Petroleum was signed between the Government of the Syrian Arab Republic, SPC and Tishrine-Shaikh Mansour PSA. The contract was approved by the Syrian Government in February the following year and has duration of 20 years with a provision for a five-year extension.

The contract governs, among other things, the terms of the cost recovery formula and provides for certain obligations of Tanganyika Oil. Tanganyika Oil has an interest in all incremental production above the base crude production levels from wells in existence at the time the development contract was signed. The base crude production level declines at a rate of 5% per year calculated on a monthly basis. The table below shows a schedule of base crude production levels for the Oudeh block for 2006-2012E.

**Tishrine-Sheikh Mansour base crude production**

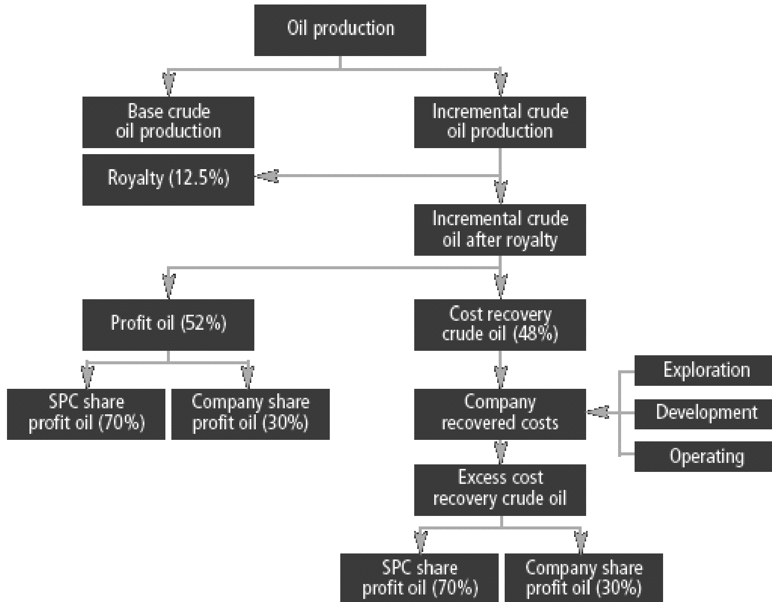
| | 2006 | 2007E | 2008E | 2009E | 2010E | 2011E | 2012E |
|---|---|---|---|---|---|---|---|
| BOPD | 6,175 | 5,881 | 5,587 | 5,308 | 5,042 | 4,790 | 4,551 |

Source: Kaupthing estimates and company data

After subtraction of the base crude production, a royalty of 12.5% is subtracted and submitted to the Syrian government. 52% of the shareable crude oil production from the block is designated as profit oil and is split among SPC (70%) and Tanganyika Oil (30%). Analogous to the methodology of the Oudeh block, up to 48% of the remaining crude oil production is available as cost oil to Tanganyika Oil to recover exploration, development and operating costs. To the extent that these costs exceed the proceeds from the sale of cost oil in any quarter, the excess can be carried forward

into following quarters. If the costs are less than the proceeds of the cost oil, the excess proceeds are split between SPC (70%) and Tanganyika Oil (30%). All taxes are the responsibility of SPC from its share of profit and excess cost oil.

**Tishrine-Sheikh Mansour production sharing agreement**

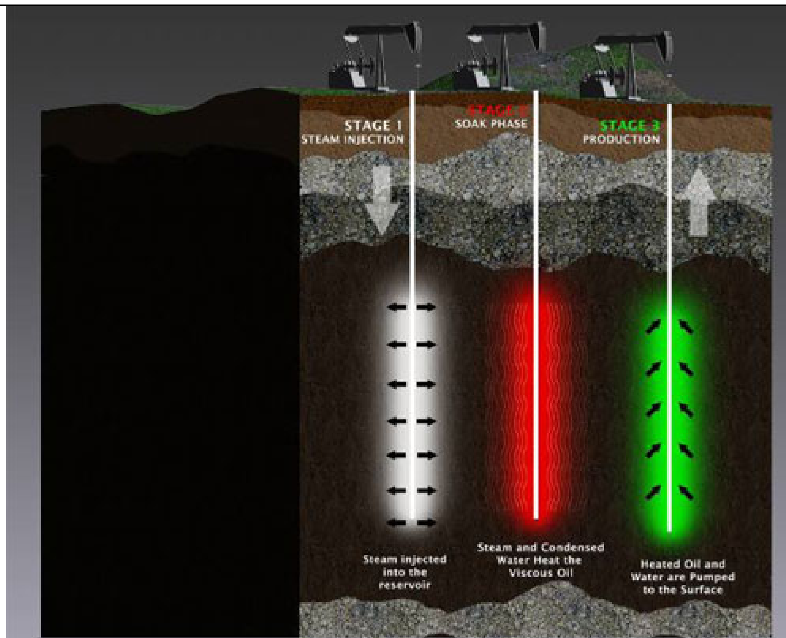



Source: Reproduced with permission from Taganyika

## Enhanced oil recovery

Enhanced oil recovery (EOR) through steam stimulation involves a three-stage cyclical process: 1) Steam injection, 2) Soak period, and 3) Production period. According to the company, the model for the program suggests scheduled cycle times for injection, soak and production phases will be approximately 20 days, 2 days and 30-90 days respectively for a total cycle time of approximately 110 days.

**Enhanced oil recovery cycle**




Source: Reproduced with permission from Taganyika

The EOR steam pilots in Syria began during 3Q06 and the results from the tests have been encouraging. On average, the EOR tests have resulted in approximately 2.5x higher production over cold.

## Management

**President and CEO, Director: Gary Guidry**

Mr Guidry has been a director of Tanganyika Oil since 5 May 2005. Prior to Tanganyika Oil, he was President and CEO of Calpine Natural Gas (CNG) Trust. He has an extensive background in international petroleum development and project execution, operating in diverse environments.

**Executive Vice President and General Manager - Egypt: Mamdouh Nagati**

Mr. Nagati joined Tanganyika Oil in 1992. Prior to Tanganyika Oil, he worked for several major oil companies in Egypt and Dubai. As of 10 July 2007, he held 91,300 shares in Tanganyika Oil.

**General Manager – Syria: Gonzalo Ruiz**

Prior to Tanganyika Oil Company Ltd. Mr. Ruiz was President of a highly successful petroleum consultancy working throughout the heavy oil regions of South America. He has over 30 years of international technical and commercial experience in the oil and gas industry. As of 10 July 2007, he held 70,000 shares in Tanganyika Oil.

**CFO: Ian Gibbs**

Mr. Gibbs was Chief Financial Officer of Valkyries Petroleum Corp. prior to its takeover by Lundin Petroleum AB in 2006. He has been a director of Fortress Minerals Corp. since June 2005 and Chief Financial Officer of Canmex Minerals Corp. since October 2006.

## Board of Directors

**Chairman and Director: Lukas H. Lundin**

Mr. Lundin has been a director of Tanganyika Oil since 20 October 1994. He is also Chairman of Tanganyika Corporation, Denison Mines Corp., Red Back Mining Inc., Tenke Mining Corp. and Canadian Gold Hunter Corp. He is director and/or senior officer of Canmex Minerals Corporation, Lundin Petroleum AB, Vostok Nafta Investments Ltd., Pearl Exploration and Production Ltd. and Atacama Minerals Corp. As of 10 July 2007, he held 258,083 shares in Tanganyika Oil.

Mr. Lundin was born in Stockholm (Sweden) in 1958, educated in Geneva (Switzerland) and graduated in 1981 from the New Mexico Institute of Mining and Technology (engineering). Since then, he has, among other things, headed International Petroleum Corporation's international operations, been President of International Musto Exploration as well as a senior director of Lundin Oil AB.

**President and CEO, Director: Gary Guidry**

Mr. Guidry has been a director of Tanganyika Oil since 5 May 2005. He is also President, CEO and a director of Pearl Exploration and Production Ltd. As of 10 July 2007, he held 160,000 shares in Tanganyika Oil.

Mr. Guidry is an Alberta-registered Professional Engineer, a petroleum engineer by training. He was most recently President and CEO of Calpine Natural Gas Trust and has previously held executive positions including President of AEC International and senior management positions for CanOxy/Nexen, Benton Oil and Gas and Occidental Petroleum.

**Directors:**

**John H. Craig**

Mr. Craig has been a director of Tanganyika Oil since 5 September 2003. His other current board duties include: Tanganyika Corporation, Consolidated HCI Holdings Corporation, Denison Mines Corp., Tenke Mining Corp, Canadian Gold Hunter Corp

and Atacama Minerals Corp. As of 10 July 2007, he held 10,000 shares in Tanganyika Oil.

**William A. Rand**

Mr. Rand has been a director of Tanganyika Oil since 19 October 1994. His other current board duties include Canadian Gold Hunter Corp., Dome Ventures Corporation, Denison Mines Corp., Lexacal Investment Corp., Tanganyika Corporation, Lundin Petroleum AB, Pender Financial Group Corporation, Tenke Mining Corp. and Vostok Nafta Investment Ltd. As of 10 July 2007, he held 15,000 shares in Tanganyika Oil.

**Keith C. Hill**

Mr. Hill has been a director of Tanganyika Oil since 18 December 2002. His other current board positions include Ausam Energy Corporation, Pearl Exploration and Production, Canmex Minerals Corporation and Bayou Bend Petroleum Ltd. As of 10 July 2007, he held no shares in Tanganyika Oil.

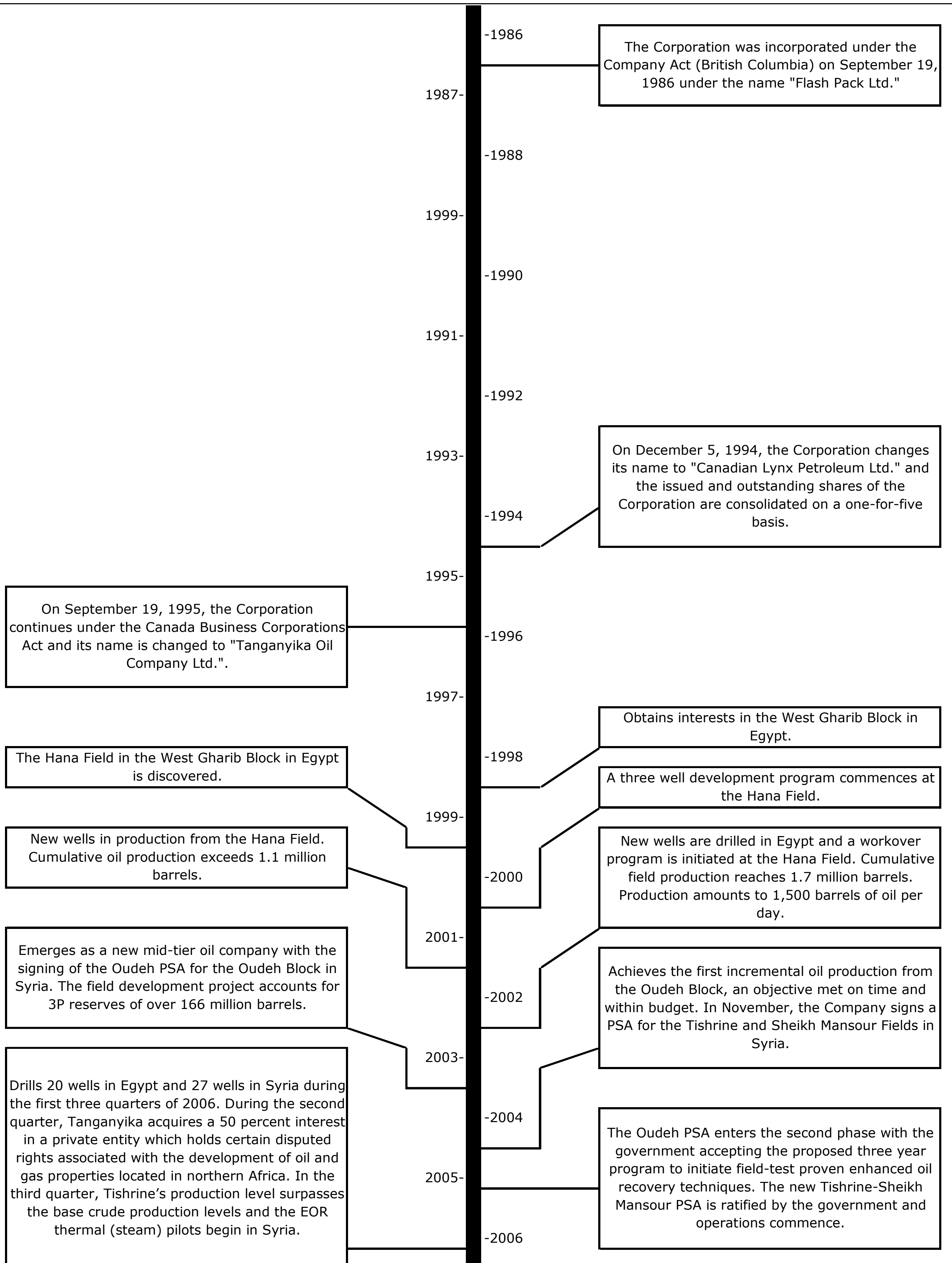
**Bryan A. Benitz**

Mr. Benitz has been a director of Tanganyika Oil since 20 November 1996. He is also a director of MagIndustries Corp., Monroe Minerals Inc., Scandinavian Gold Limited and Island Oil and Gas PLC. As of 10 July 2007, he held 70,000 shares in Tanganyika Oil.

**Håkan Ehrenblad**

Mr. Ehrenblad has been a director of Tanganyika Oil since 3 May 2006. He is also a director of the board of Tethys Oil AB.

## Company history




Source: Company data

## Forecast P&L, cash flow - Tanganyika Oil Company (USDm)

| Profit and loss | 2002 | 2003 | 2004 | 2005 | 2006 | 2007E | 2008E | 2009E |
|---|---|---|---|---|---|---|---|---|
| Total sales | 0 | 0 | 0 | 18 | 33 | 53 | 316 | 583 |
| Total expenses | 0 | 0 | -5 | -14 | 0 | -43 | -129 | -201 |
| **EBITDA** | **0** | **0** | **-5** | **4** | **33** | **11** | **187** | **382** |
| Depreciation | 0 | 0 | 0 | -5 | -12 | -23 | -48 | -106 |
| Amortisation | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Impairment charges, gw. | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Other items / EBIT adj. | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| **EBIT** | **0** | **0** | **-5** | **-1** | **21** | **-12** | **140** | **277** |
| Net financial items | 0 | 0 | 0 | 1 | -2 | 3 | 0 | 0 |
| Share of res. of ass. companies | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| **PTP** | **0** | **0** | **-5** | **1** | **19** | **-9** | **140** | **277** |
| Tax | 0 | 0 | 0 | -1 | 0 | 0 | 0 | 0 |
| Profit after taxes | 0 | 0 | -5 | 0 | 19 | -9 | 140 | 277 |
| EO items not in EBIT | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Net income before min. int. | 0 | 0 | -5 | 0 | 19 | -9 | 140 | 277 |
| **Net profit, reported** | **0** | **0** | **-5** | **0** | **19** | **-9** | **140** | **277** |
| **Adjusted profit and loss** | | | | | | | | |
| Analyst adjustments | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| EBIT (adj.) | 0 | 0 | -5 | -1 | 21 | -12 | 140 | 277 |
| PTP (adj.) | 0 | 0 | -5 | 1 | 19 | -9 | 140 | 277 |
| Net profit (adj.) | 0 | 0 | -5 | 0 | 19 | -9 | 140 | 277 |
| Impairment charges, gw. | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |

## Balance sheet - Tanganyika Oil Company (USDm)

| Assets | 2002 | 2003 | 2004 | 2005 | 2006 | 2007E | 2008E | 2009E |
|---|---|---|---|---|---|---|---|---|
| Goodwill | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Other intangibles | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Tangible assets | 0 | 0 | 0 | 40 | 105 | 194 | 384 | 526 |
| Fixed assets, other | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Shares, associated companies | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| **Total fixed assets** | **0** | **0** | **0** | **40** | **105** | **194** | **384** | **526** |
| Inventory | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Accounts receivable | 0 | 0 | 0 | 8 | 25 | 41 | 242 | 447 |
| Other current ass. and tax | 0 | 0 | 0 | 18 | 7 | 12 | 70 | 129 |
| Cash and equivalents | 0 | 0 | 17 | 17 | 94 | -5 | -71 | 49 |
| **Total current assets** | **0** | **0** | **17** | **43** | **126** | **48** | **241** | **625** |
| **Total assets** | **0** | **0** | **17** | **83** | **232** | **242** | **625** | **1,150** |
| **Equity and debt** | | | | | | | | |
| Shareholders equity | 0 | 0 | 0 | 70 | 201 | 192 | 332 | 608 |
| Minority interest | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| **Total equity** | **0** | **0** | **0** | **70** | **201** | **192** | **332** | **608** |
| Deferred tax debt | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Pension provisions | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Other provisions and l-t liab. | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Convertible debt | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Long-term int.-bearing debt | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| **Total long-term liab.** | **0** | **0** | **0** | **0** | **0** | **0** | **0** | **0** |
| Accounts payable | 0 | 0 | 0 | 12 | 30 | 50 | 294 | 542 |
| Other current liab. and tax | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Short-term int.-bearing debt | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| **Total current liab.** | **0** | **0** | **0** | **12** | **30** | **50** | **294** | **542** |
| **Total liab. and equity** | **0** | **0** | **0** | **83** | **232** | **242** | **625** | **1,150** |
| | | | | | | | | |
| Interest-bearing debt | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Net debt (- =assets) | 0 | 0 | -17 | -17 | -94 | 5 | 71 | -49 |
| Operating capital | 0 | 0 | 0 | 54 | 107 | 197 | 403 | 559 |

Source: Kaupthing estimates, company data

## Cash flow - Tanganyika Oil Company (USDm)

| Cash flow statement | 2002 | 2003 | 2004 | 2005 | 2006 | 2007E | 2008E | 2009E |
|---|---|---|---|---|---|---|---|---|
| Operating profit | 0 | 0 | -5 | -1 | 21 | -12 | 140 | 277 |
| Provisions | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Total depr. and writedowns | 0 | 0 | 0 | 5 | 12 | 23 | 48 | 106 |
| Chg. working capital | 0 | 0 | 0 | -14 | 12 | -1 | -15 | -16 |
| Other non-cash items | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Net financial items | 0 | 0 | 0 | 1 | -2 | 3 | 0 | 0 |
| Income taxes paid | 0 | 0 | 0 | -1 | 0 | 0 | 0 | 0 |
| Operating cash flow | 0 | 0 | -5 | -8 | 43 | 13 | 172 | 367 |
| Capex | 0 | 0 | 0 | -30 | -55 | -111 | -238 | -247 |
| FCF from operations | 0 | 0 | -5 | -38 | -12 | -98 | -67 | 120 |
| Fin. inv. and acquisitions | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Share issue/repurchase | 0.0 | 0.0 | 0.0 | 0.0 | 77.1 | 0.0 | 0.0 | 0.0 |
| Dividend paid | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Other items | 0.0 | 0.0 | 21.4 | 38.3 | 12.0 | 0.0 | 0.0 | 0.0 |
| Change in net debt | 0 | 0 | 17 | 0 | 77 | -98 | -67 | 120 |

## Key figures - Tanganyika Oil Company

| Valuation | 2002 | 2003 | 2004 | 2005 | 2006 | 2007E | 2008E | 2009E |
|---|---|---|---|---|---|---|---|---|
| Market cap | n.m. | n.m. | n.m. | n.m. | 826 | 983 | 983 | 983 |
| Enterprise value | n.m. | n.m. | n.m. | n.m. | 732 | 988 | 1,055 | 935 |
| P/E | n.m. | n.m. | n.m. | n.m. | 43.2 | n.m. | 7.0 | 3.6 |
| P/E (adj.) | n.m. | n.m. | n.m. | n.m. | 42.9 | n.m. | 7.0 | 3.6 |
| P/E (adj. excl. gw.) | n.m. | n.m. | n.m. | n.m. | 42.9 | n.m. | 7.0 | 3.6 |
| P/CE | n.m. | n.m. | n.m. | n.m. | 26.7 | 70.9 | 5.3 | 2.6 |
| P/S | n.m. | n.m. | n.m. | n.m. | 25.4 | 18.4 | 3.1 | 1.7 |
| P/BV | n.m. | n.m. | n.m. | n.m. | 4.1 | 5.1 | 3.0 | 1.6 |
| Yield (%) | n.m. | n.m. | n.m. | n.m. | 0.0 | 0.0 | 0.0 | 11.2 |
| EV/EBITDA (adj.) | n.m. | n.m. | n.m. | n.m. | 22.3 | 92.8 | 5.6 | 2.4 |
| EV/EBIT (adj.) | n.m. | n.m. | n.m. | n.m. | 35.1 | n.m. | 7.6 | 3.4 |
| EV/S | n.m. | n.m. | n.m. | n.m. | 22.33 | 18.53 | 3.34 | 1.60 |
| **Data per share** | | | | | | | | |
| Adjusted EPS (also gw.) | n.m. | n.m. | n.m. | n.m. | 0.4 | -0.2 | 2.5 | 4.9 |
| EPS (adj. excl. gw.) | n.m. | n.m. | n.m. | n.m. | 0.4 | -0.2 | 2.5 | 4.9 |
| CEPS | n.m. | n.m. | n.m. | n.m. | 0.6 | 0.2 | 3.3 | 6.7 |
| Dividend per share | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 1.9 |
| BV per share | n.m. | n.m. | n.m. | n.m. | 4.2 | 3.4 | 5.8 | 10.7 |
| Net debt per share | n.m. | n.m. | n.m. | n.m. | -2.0 | 0.1 | 1.3 | -0.9 |
| FCF per share | n.m. | n.m. | n.m. | n.m. | -0.3 | -1.7 | -1.2 | 2.1 |
| **Growth (%)** | | | | | | | | |
| Sales growth | n.m. | n.m. | n.m. | n.m. | 82.5 | 62.6 | 492.1 | 84.7 |
| Net profit growth | n.m. | n.m. | n.m. | n.m. | 4,074.9 | n.m. | n.m. | 98.2 |
| Equity growth | n.m. | n.m. | n.m. | n.m. | 185.2 | -4.4 | 72.6 | 83.4 |
| Dividend growth | n.m. | n.m. | n.m. | n.m. | n.m. | n.m. | n.m. | n.m. |
| **Margins and profitability (%)** | | | | | | | | |
| Gross margin | n.m. | n.m. | n.m. | 24.2 | 100.0 | 20.0 | 59.3 | 65.5 |
| EBIT margin (adj.) | n.m. | n.m. | n.m. | -2.8 | 63.6 | -22.7 | 44.2 | 47.4 |
| Net profit margin (adj.) | n.m. | n.m. | n.m. | 2.6 | 58.7 | -16.7 | 44.2 | 47.4 |
| Return on equity, RoE | n.m. | n.m. | n.m. | 1.3 | 14.2 | -4.5 | 53.3 | 58.9 |
| ROCE | n.m. | n.m. | n.m. | 2.8 | 14.3 | -4.5 | 53.3 | 58.9 |
| **Capital structure** | | | | | | | | |
| Debt/equity ratio | n.m. | n.m. | n.m. | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Capital employed | 0 | 0 | 0 | 70 | 201 | 192 | 332 | 608 |
| Net debt/equity | n.m. | n.m. | n.m. | -0.24 | -0.47 | 0.02 | 0.21 | -0.08 |
| Net debt (- =assets) | 0 | 0 | -17 | -17 | -94 | 5 | 71 | -49 |
| Asset turnover | n.m. | n.m. | 0.0 | 0.2 | 0.1 | 0.2 | 0.5 | 0.5 |
| Equity ratio (%) | 0.0 | 0.0 | 0.0 | 85.0 | 86.8 | 79.5 | 53.0 | 52.9 |
| **Cash flow** | | | | | | | | |
| Capex/sales (%) | n.m. | n.m. | n.m. | 167.0 | 167.7 | 208.3 | 75.5 | 42.3 |
| Capex/depr. (%) | n.m. | n.m. | n.m. | 618.3 | 460.7 | 488.0 | 501.1 | 233.6 |
| Working capital | 0 | 0 | 0 | 14 | 2 | 3 | 18 | 34 |

Source: Kaupthing estimates, company data

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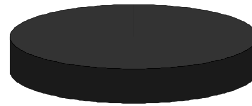
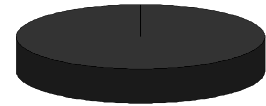
## Company data - Tanganyika Oil Company

| Owners | % of capital |
|---|---|
| Straumur-Burdaras | 8.3 |
| Zebra Holdings | 8.0 |
| Ellegrove Capital | 4.5 |
| Abalone Capital | 1.9 |
| Lukas Lundin | 0.5 |
| Gary Guidry | 0.3 |
| Mamdou Nagati | 0.2 |
| Others | 76.3 |

| Geogr. areas | % of sales |
|---|---|
| Syria | 100.0 |

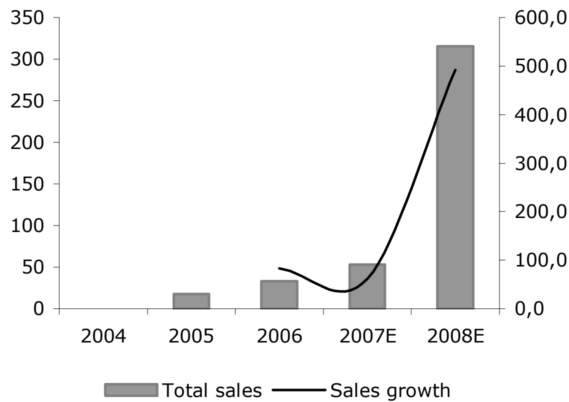



| Business areas | % of sales |
|---|---|
| Oil exploration and production | 100.0 |

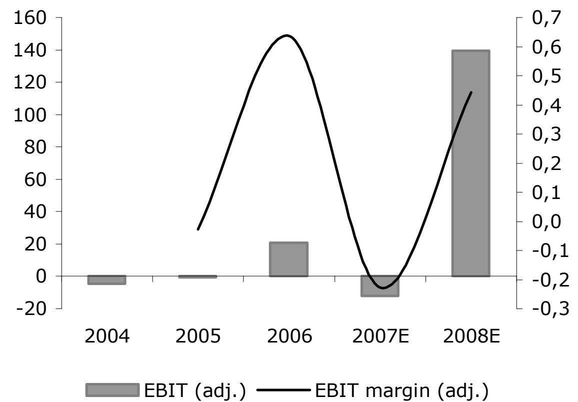



| Management | |
|---|---|
| Chairman | Lukas H. Lundin |
| CEO | Gary S. Guidry |
| CFO | Ian Gibbs |
| IR | Robert Eriksson |

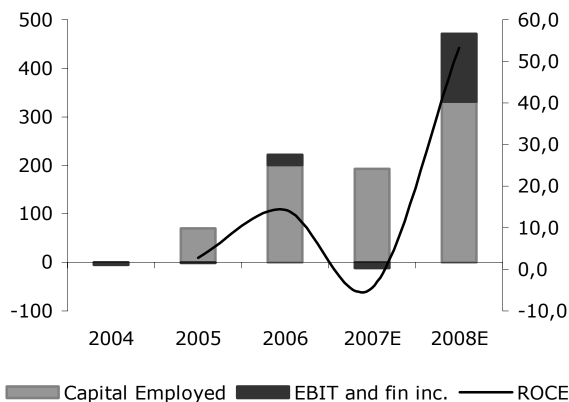
### Sales and growth



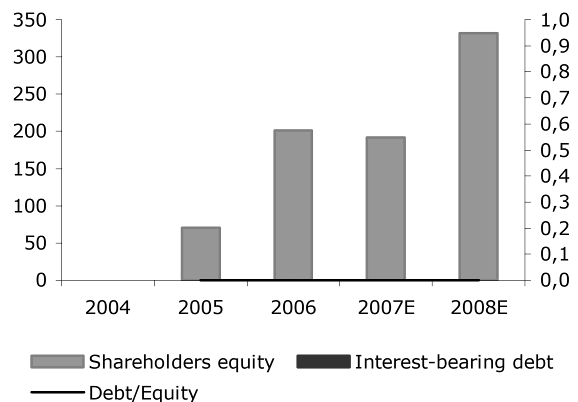

### Operating profit and margin




### Return on capital employed




### Gearing




Source: Kaupthing estimates, company data

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# IMPORTANT DISCLOSURES

**Company covered: Tanganyika Oil Company** (Hereafter referred to as "This Company")

Planned frequency for updates of report about this Company: 3-4 times per year
Shares held by the analyst(s) and/or close associate in this Company: 0
Other material interest (if any): None
This report has not been presented to the Company before publication.
* Below refers to recommendations set in Kaupthing's recommendation structure before 22 January 2007. See definitions below
Kaupthing's recommendation history for during the last 12 months: 12 Sep 2007 Buy (initiation of coverage)

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(Note: Before 22 January 2007, we used a four-stage recommendation structure where Buy indicated expected return of greater than +15%; Accumulate: greater than +5% and less than or equal to +15%; Reduce, greater than -10% and less than or equal to +5%; and Sell, less than -10%.)

**Current recommendations of the Research Department:** (refers to recommendations published prior to this report)

| Kaupthing | Percent | SRO Equivalent | Percent |
|---|---|---|---|
| Buy | 51% | Buy | 51% |
| Neutral | 40% | Hold | 40% |
| Reduce | 8% | Sell | 8% |
| Total | 100% | Total | 100% |

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