

PALOS

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Weekly Commentary

Issue No. 11 | MARCH 14, 2022

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Rubellite Energy Inc. – The New Kids on the (Clearwater) Block

The Clearwater is located between 100 to 200 kilometres north of Edmonton in the heart of Alberta’s Western Canadian Sedimentary Basin (WCSB). Production in the Clearwater has grown from several hundred barrels of oil per day in 2017 to over 30,000 barrels by 2020.

Within the Clearwater “fairway” there are three core plays that include the Marten Hills play, Nipisi, and Jarvie. Operators in the area are comprised of both private and public companies. Spur Petroleum and Deltastream Energy dominate on the private side. Publicly listed Canadian companies include “larger cap” players like **Canadian Natural Resources (TSX/NYSE: CNQ)** with a \$90 billion market cap and **Cenovus Energy (TSX/NYSE: CVE)** with a \$41B billion cap. Other smaller cap players include **Tamarack Valley (TSX: TVE)**, with a \$2.3 billion cap, **Baytex Energy (TSX: BTE)** at \$3.4 billion, and **Headwater Exploration (TSX: HWX)** at \$1.5 billion.

What makes the Clearwater so attractive is a combination of economically advantageous factors: excellent geological characteristics like significant formation porosity, superior heavy oil viscosity, low water saturation, reservoirs that are close to the surface, and a low resource decline profile. These characteristics allow producers to use newer technologies like “multi-lateral” drilling techniques which are less costly and require a shorter time horizon from drilling to production. Clearwater wells are proving to be more productive than heavy oil peers operating in the basin.

Without getting overly technical, “multi-laterals” are basically a well design where companies will drill using a series of horizontal wellbores that are more tightly spaced than usual. The “laterals” can be up to several kilometres in length and spaced less than 100 meters apart. In general, horizontal wells are much more productive and less costly than vertical wells. Thus, the need to implement fracturing, thermal or steam-assisted techniques is mostly eliminated, offering significant cost savings.

Rubellite Energy Inc. (TSX: RBY) is a Calgary based company that is 100% focused on its Clearwater assets. The company was incorporated in Alberta on July 12, 2021, with the intention to acquire the Clearwater

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assets of **Perpetual Energy Inc. (TSX: PMT)** via a “special arrangement”. Subsequent to a special meeting of Perpetual shareholders held on August 31, 2021, Rubellite formally acquired the Clearwater assets for an aggregate consideration of \$65.6million. The acquisition included all of Perpetual’s land holdings, wells and infrastructure located in the Clearwater.

Management’s strategy is straightforward: the company is laser-focused on rapidly growing production, growing reserves through land purchases and drilling programs and creating exceptional and sustainable returns for shareholders. Robust cash flow is expected given the rapid paybacks and low risk/high return profile of the Clearwater. Management has pledged to follow a conservative approach to capital expenditures and the balance sheet.

RBV currently operates in three areas of the Clearwater. Ukalta, located an hour north of Edmonton, is 100% owned by RBV and is under active development, uses multi-laterals techniques and is testing additional methods designed to optimize recovery. Figure Lake, also 100% owned, commenced a drilling program in the second half of 2021 and so far results are promising. At Marten Hills, production began in July 2021 with two “eight-leg” multi-laterals. Four additional “eight-leg” drilling programs are scheduled in Q1/2022.

On March 10, Rubellite announced its intention to raise approximately \$25 million through a bought deal financing. The underwriting syndicate, led by Calgary based Peters & Co., agreed to purchase for distribution 4.8 million shares at a price of \$3.55 per share for proceeds to the company of \$17.04 million. The underwriters have the option to purchase an additional 15% to cover over allotments. As well, a number of officers, directors and employers of Rubellite disclosed their intention to purchase a minimum of 2.4 million shares at \$3.55 generating an additional \$8.5 million.

The Clearwater fairway is thought to have the “best economics” of any North American oil discovery in the last ten years and has been attracting an influx of participants since 2018. Getting more oil out of the ground at a lower cost than competing heavy oil peers is the main attraction. RBV has a market cap of \$158 million making it one of the smaller participants in the play. Further enhancing our views are management’s enshrined commitment to excellence in environmental protection, diversity, corporate governance, business conduct and workplace safety.

The **Palos Income Fund LP**, the **Palos Equity Income Fund** and the **Palos-Mitchell Alpha Fund** initiated an investment in Rubellite by participating in the recent private placement.

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Chart 1: Palos Domestic Funds versus Benchmarks (Total Returns) ¹	FundServ	NAVPS	YTD Returns
Palos Income Fund L.P.	PAL100	\$9.88	0.41%
Palos Equity Income Fund - RRSP	PAL101	\$7.24	-0.02%
Palos Merchant Fund L.P. (Dec 31, 2021) ²	PAL500	\$1.16	24.67%
Palos WP Growth Fund - RRSP	PAL213	\$17.68	-6.70%
Palos-Mitchell Alpha Fund ³	PAL300	\$9.74	-5.28%
S&P TSX Composite (Total Return with dividends reinvested)			1.57%
S&P 500 (Total Return with dividends reinvested)			-11.53%
S&P TSX Venture (Total Return with dividends reinvested)			-9.87%
Chart 2: Market Data ¹			Value
US Government 10-Year			1.99%
Canadian Government 10-Year			1.99%
Crude Oil Spot			US \$109.33
Gold Spot			US \$1,985.00
US Gov't10-Year/Moody BAA Corp. Spread			237 bps
USD/CAD Exchange Rate Spot			US \$0.7846

¹ Period ending March 11th, 2022. Data extracted from Bloomberg

² Fund is priced annually

³ Fund is priced weekly on Tuesdays

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