

PALOS

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Weekly Commentary

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ARC Resources Announces its 5-Year Plan

ARC Resources (ARX:TSX) is a Calgary-based oil and natural gas exploration company with operations in Western Canada. With its operations concentrated in the Montney play, ARC has become Canada's largest producer of condensates (natural gas liquids) and the third largest producer of natural gas. Condensates are frequently used as a diluent that is combined with heavy crude (bitumen) which is the grade that's commonly mined from Canada's massive oil sands reserves. Adding diluent enables heavier grades of crude to be transported by pipeline.

The Montney formation, which straddles the borders of Northeastern BC and Northwestern Alberta, has massive potential. Using horizontal drilling and hydraulic fracturing techniques (fracking), it's estimated that over 400 trillion cubic feet of natural gas, 15 million barrels of natural gas liquids (NGLs), and one billion barrels of oil could be recovered. This equates to well over a hundred years of Canada's consumption. Over the last decade, ARC has transformed from an average production of 110 thousand barrels of energy produced per day (Mboe/d) to 350 Mboe/d in 2023. In 2014, ARC began a program to concentrate operations in Montney.

Today, the company owns more than 1,600 Montney sections, over 5,000 drilling locations, and vast owned-and-operated infrastructure that can transport over 1.5 billion cubic feet per day (Bcf/d). Infrastructure ownership is driving efficiency and this gives ARC a competitive advantage. In terms of cost "avoidance", the annual "savings" equate to roughly \$300 million. ARC is currently the largest producer in the Montney.

On June 22, ARC hosted an investor day to update investors and to also unveil the company's 5-year strategic plan. With a very strong balance sheet, management is committed to bolstering shareholder returns through dividends and share buybacks. The current quarterly dividend of \$0.17 (4.2% yield) has increased by 180% from pre-Covid levels and buybacks have reduced the number of shares outstanding by 16% over the past two years. Management describes the company as a "balance sheet first" organization and by exercising strong capital discipline, ARC's debt complex has received an investment-grade rating.

There are potential catalysts on the horizon. As we move towards the commissioning of LNG Canada's export facility on the BC coast, ARC has secured confirmed supply agreements which should kick in by the 2024-25. In addition to supplying LNG Canada with an estimated 150 billion cubic feet of LNG per day (MMcf/d), agreements with BC's Cedar LNG (200 MMcf/d) and U.S. Gulf Coast operator Cheniere Energy LNG (140 MMcf/d) are confirmed. Further, access to markets in Malin, CA and the U.S. Midwest offer exposure to international pricing which historically has been

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significantly higher than domestic pricing. LNG Canada will target Asian markets where LNG trades at several multiples higher than Canadian LNG.

As part of the 5-year plan, ARC confirmed that it will develop the Attachie play (Phases I and II) which is in BC. Attachie Phase I is a high-quality asset with an estimated average production of 40,000 barrels of oil per day (boe/d), 90 MMcf/d of gas processing capacity and 25,000 boe/d in liquids processing capacity. The plant will be electrified and a water recycling facility will be built to minimize the consumption of fresh water. ARC strives to be a global leader in ESG and has one of the lowest emissions profiles amongst peers in Canada.

ARC is recognized for its capital discipline and its ability to execute. The company's asset base includes eight different locations in the world-class Montney which implies multiple decades of reserves at hand. An established, high-quality infrastructure optimizes access to multiple markets and hence, better pricing. Management has clearly telegraphed a commitment to maximizing shareholder returns. With an exemplary track of execution and a reputation as a premium operator in the Canadian exploration and production space, ARC Resources "checks all the boxes" and stands to remain a premium producer for many decades to come. The Palos Equity Income Fund, the Palos Income Fund LP and the Palos-Mitchell Alpha Fund are currently invested in ARC Resources.

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Chart 1: Palos Domestic Funds versus Benchmarks (Total Returns) ¹	FundServ	NAVPS	YTD Returns
Palos Income Fund L.P.	PAL100	\$8.06	0.04%
Palos Equity Income Fund - RRSP	PAL101	\$6.47	-0.21%
Palos WP Growth Fund - RRSP	PAL213	\$11.05	-11.32%
Palos-Mitchell Alpha Fund ³	PAL300	\$9.58	18.29%
S&P TSX Composite (Total Return with dividends reinvested)			1.76%
S&P 500 (Total Return with dividends reinvested)			14.18%
S&P TSX Venture (Total Return with dividends reinvested)			5.08%
Chart 2: Market Data ¹			Value
US Government 10-Year			3.73%
Canadian Government 10-Year			3.36%
Crude Oil Spot			US \$69.16
Gold Spot			US \$1,919.10
US Gov't10-Year/Moody BAA Corp. Spread			195 bps
USD/CAD Exchange Rate Spot			US \$0.7586

¹ Period ending June 23rd, 2023. Data extracted from Bloomberg

² Fund is priced annually

³ Fund is priced weekly on Tuesdays

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