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Saguaro Resources won't be a junior producer for long

By Dale Lunan May 24, 2017, 2:34 p.m.

Saguaro Resources CEO Stacy Knull. Image: Joey Podlubny/JWN

As far as first impressions are concerned, Saguaro Resources is considered a privately held, emerging producer, initially capitalized in late 2012 with annualized average production that has grown from 117 boe/day that year (just two months) to a bit under 7,100 boe/day last year.

But those are first impressions. Dig a little deeper, and you'll find an "emerging" producer that is now, in early 2017, a growing intermediate with production averaging more than 12,000 boe/day, 160 sections of 100 per cent working interest land in the liquids-rich fairway of the Montney in northeastern B.C. and enough de-risked drilling locations to reach 140,000 boe/day within the next 10 years.

According to Stacy Knull, Saguaro's president and chief executive officer, the company is fortunate in that it derives a large portion of its revenues—more than 40 per cent in the third quarter of 2016—from high-value condensate. Most of the rest is propane and butane, and dry gas and crude oil make up only seven per cent of its revenue stream.

"Condensate has been less volatile than oil—the lowest it ever fell to was about $38, and right now it's around $70, so we've always been able to generate good shareholder returns, and we've always been cautious with our capital program," Knull says. "We can stop and start pretty easily."

Saguaro acquired most of its B.C. Montney real estate in 2013, when Crown sales were deep in the tank, Knull says. This gave the company a running start on making money from modest drilling programs those first couple of years.

“We bought most of our land at around $1,100/acre as opposed to as much as $5,000/acre for some of the other acquisitions in the area,” he says. “We have an opportunity to really grow shareholder value over a long period of time.”

Serious drilling began in 2014, with a 13-well program that was part of a $187-million capital program that also saw the development of a 35 mmcf/d compression/dehydration facility. The company has since expanded the facility to 60 mmcf/day and procured the equipment to expand to 100 mmcf/day.

Drilling slowed a bit in 2015 as commodity prices cratered, and the company drilled only six wells, but activity picked up again in 2016 with 12 more wells drilled. Going forward, Saguaro’s development plan is predicated on a six-bcf type curve characterized by 2,000-metre laterals on relatively shallow (1,400–1,900-metre) wells.

Because the wells are shallow and because Saguaro is constantly tweaking its completions program, drilling and completion costs have fallen steadily in the last couple years, from about $7.2 million per well prior to the start of the full development program in 2015 to a budgeted $4.8 million per well for the 28 wells contemplated in the 2017 capital plan. That should take production by the end of this year to around 16,000 boe/day, and because much of this year’s drilling will take place late in the year, production by the end of 2018 could surge to around 26,000 boe/day, Knull says.

The 2017 capital program will likely be funded from additional borrowing facilities the company is hoping to nail down. In the past, Knull says, Saguaro’s been “fairly allergic” to debt, but now with reserves climbing steadily, he feels its appropriate to gradually boost its reserves-based borrowing.

“Our reserves grew from about 108 million boe at the end of 2015 to 235 million boe in September last year and to about 270 million boe by the end of 2016,” he says. “That underpins our value, which underpins our ability to take on a little bit more debt and still stay below a two times debt-to-cash-flow ratio.”

Saguaro is currently running its production through any of three third-party processing facilities, where it has contracted firm service of 40 mmcf/day and where “substantial” interruptible capacity is also available. But it’s also contemplating building its own full processing facility and is eyeing participation in various third-party infrastructure initiatives.

“We really have no concerns on infrastructure—we’re not thinking five or 10 years out, we’re thinking 40 years out,” Knull says. “We’re not big enough to drive the [TransCanada] Mainline to Ontario or the Spectra system all the way down to the west coast, but where we are at, we have access to possibly as many as five midstream plants, so we have a lot of flexibility.”

Saguaro’s full development plan contemplates running one rig for most of this year to drill 28 wells, but ramping activity steadily higher starting in 2018, when two rigs and more than 35 wells are planned, continuing in 2019 with three rigs and more than 50 wells and 2020 before levelling off in 2021, when five rigs will be used to drill more than 80 wells per year. By then, production should be around 75,000 boe/d and well on its way to more than 125,000 boe/d by 2025.