

**Recommendation: Speculative Buy**  
**Target Price: C\$8.00**

**◆CGX Energy Inc. (OYL -TSXV)**  
**Upcoming 3D Seismic Program Could Act As**  
**A Catalyst For First Drilling Offshore Guyana**

Current Price	\$1.39	Target	\$8.00
52 Wk High	\$4.60	Proj. Return	476%
52 Wk Low	\$1.09	Basic Sh. (O/S)	122.9
NPV (1)	\$12.64	FD Sh. (O/S)	132.6
P/NPV	0.11x	Mngt. & Dir.	5.0
Working Cap. (MM)	\$38.4	- Pct. of basic	4%
D/CF	NA	Mkt. Cap. (MM)	\$170.8
DPS	NA	Float (MM)	\$163.8
Dividend Yield	NA	EV (MM)	\$132.3

(1) Risked NPV analysis based on the Eagle Shallow Fan and Eagle Deep West Prospects; assumes financing at \$1.50 per share to fund initial exploration well

Unless otherwise denoted, all figures shown in US\$

**Investment Thesis:**

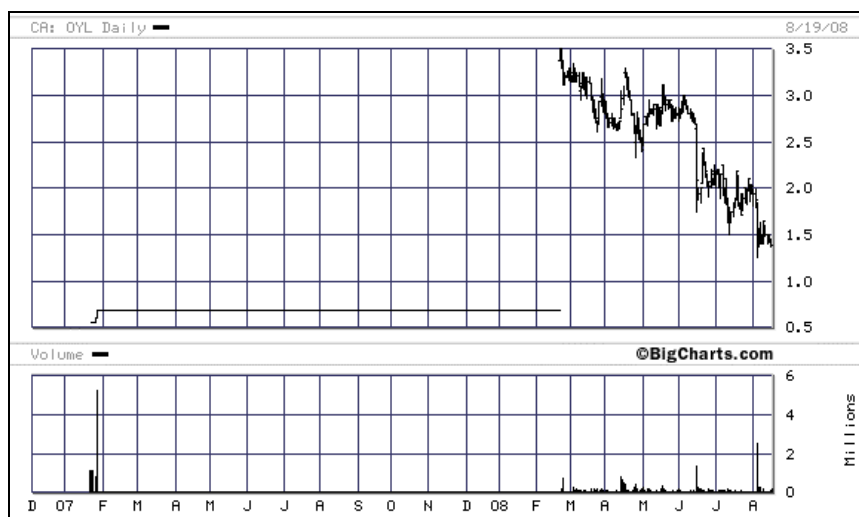
An investment in CGX offers investors exposure to billions of barrels of oil reserve potential with its interest in four exploration Licences, encompassing over nine million gross acres located largely offshore Guyana in South America. With the resolution of the Border dispute with Suriname, the region should re-open to exploration and business development activities.

**Highlights:**

- **Event**  
 With this report, we are transferring coverage of CGX Energy to David Beddis from Brent Watson. As a part of the due diligence process, we recently reviewed the Company's most recent presentation with management and are providing an operations update.
- **Impact**  
 With its high-impact exposure to huge potential reserves offshore Guyana and the equally high risk nature of the play, we believe that CGX should be held by investors as a part of a basket of junior international E&P companies. In our opinion, CGX offers an attractive risk reward profile as a successful discovery could provide material upside and value to shareholders. Our revised C\$8.00 target price (C\$10.00 previously) is based on a weighting of our risked evaluation of the Company's prospects under two scenarios. We reiterate our Speculative Buy rating.

**Company Description:**

CGX is a Canadian-based international oil and gas exploration company focused in Guyana, South America. CGX is listed in Canada on the TSX Venture exchange.



Source: BigCharts.com, August 19, 2008 (Charts C\$)

◆During the past twenty-four months, Cormark Securities Inc., either on its own or as a syndicate member, participated in the underwriting of securities for CGX Energy Inc.

Our disclosure statements are located at the end of this report.

**Details**

- We are transferring coverage of CGX Energy to David Beddis from Brent Watson. As a part of the due diligence process, we reviewed the Company's most recent presentation with management and are providing an operations update.
- In our opinion, CGX continues to offer investors the potential for material upside from its prospects in offshore Guyana. CGX's independent engineer, Gustavson Associates, has provided a P50 resource estimate of 2.7 billion barrels, which when risked, is the basis for our C\$8.00 target price; however, we note that the target is likely substantially higher if drilling is successful. With drilling in offshore Guyana still in early stages and given the high risk nature of the exploration drilling, we maintain our Speculative Buy rating. We believe that although CGX is a high risk holding, it also offers high reward and should be a part of investor's junior international portfolios.

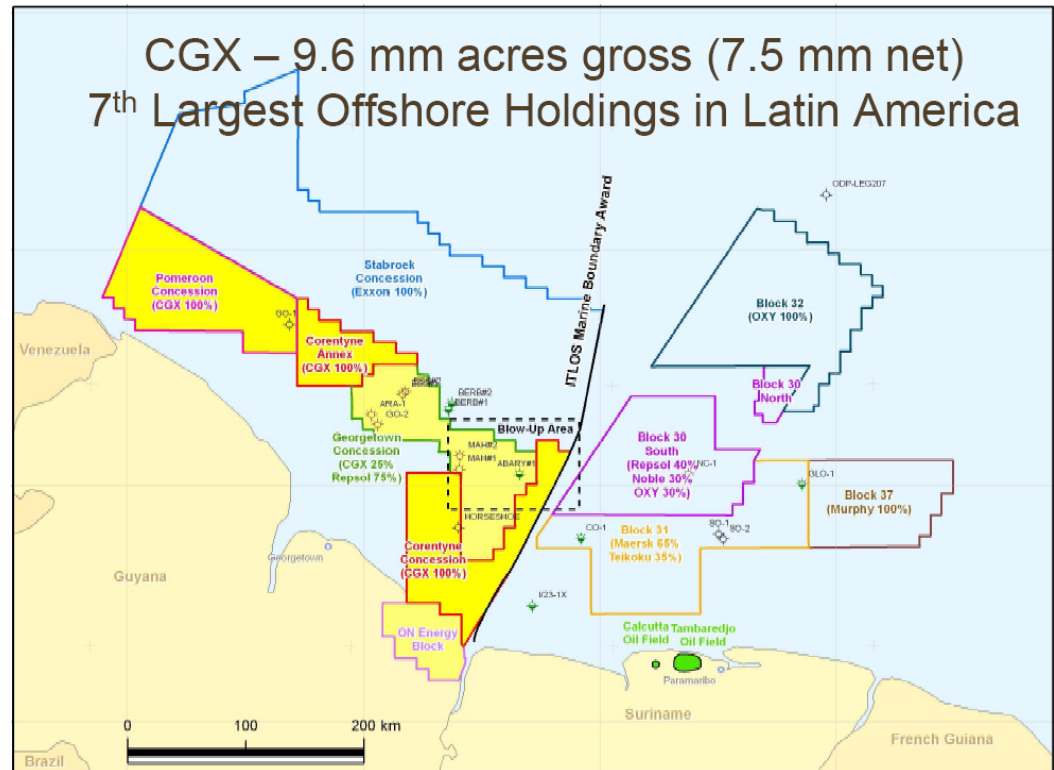
Operations Update:

- CGX has access to 9.5 million (7.2 million net) acres over four blocks in the under explored region of offshore Guyana. The Company's focus has been on its Corentyne block where it currently holds a 100% working interest. Thus far, the Company has identified several leads on the block and plans to shoot a 500 km<sup>2</sup> 3D seismic program this fall to further help define its prospects. At this stage, the first prospect is likely to be a Cretaceous-aged structural target at a depth of ~18,000 feet with secondary potential in Tertiary Turbidites, which it has labelled Eagle Deep West and Eagle Shallow, respectively. Combined, these two prospects have a third party P50 resource best estimate of 1.4 billion barrels, giving CGX exposure to huge reserve potential on its block.
- Adjacent to the Corentyne block, CGX holds a 25% working interest in the Georgetown concession, with Repsol holding the other 75%. The Companies remain at earlier stages of evaluating the Georgetown concession, and it is likely that some seismic will be shot on the block before a drilling decision is made. Though Georgetown could offer some interesting prospects, the rate of activity is controlled by Repsol (who is the operator) and as a result we expect CGX's near- and mid- term focus to remain on the Corentyne concession.
- In addition, the Company holds 100% working interest in the Pomeroun and Corentyne Anex concessions, which at this stage are not likely to see much activity as the Company focuses on drilling its first well on the Corentyne block.

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**Figure 1 CGX Landholdings Offshore Guyana**



Source: CGX Energy Inc.

Upcoming Events/Potential Catalysts:

- The Company's 500 km<sup>2</sup> 3D seismic program to be shot over the Corentyne field is expected to begin in early September. The Company has contracted Furgio-GeoTeam to complete the program, which is expected to take four weeks and will be shot using the 'R/V GeoPacific' vessel. This \$13 million program will add to the 2D seismic already covering the field and ultimately aid in identifying the first prospect to be drilled, which could come as early as late 2009. The shoot will go forward whether the Company has a partner or not, as CGX has enough capital to fully fund the program on its own. In addition, if a JV partner in the play has yet to be identified, initial interpretation of the seismic could provide more data to attract potential partners.
- With exploration in the waters offshore Guyana and Suriname still in early stages, we believe that any increased activity by industry majors present in the area (such as Noble, Repsol, Exxon, Murphy and Teikoku) would be positive and support the potential in the area given large inventory of opportunities and resulting competition for capital in these larger companies.
- The search for a JV partner in the Corentyne block is ongoing. With the exploration well having the potential to cost in the order of \$100 million, CGX is looking to farm down its interest with the farm-in partner paying a promote on the initial well for a working interest in the field. We believe that the announcement of a partner would be positive as it would provide more certainty to drilling, especially if funding (partial or full) of the first well is a part of the agreement.

Financial Flexibility:

- As at March 31, 2008, CGX had positive working capital of \$36.6 million including \$38.0 million in cash. As mentioned, this will allow the Company to move forward with the planned \$13 million

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3D seismic program with or without a JV partner for the project. However, in its current financial position, CGX would be unable to fund 100% of the well costs, which could be in excess of \$100 million. As a result, we believe that a successful farm-out becomes a necessary event for the first exploration well to be drilled, as the 3D seismic alone is not likely enough for CGX to raise the money necessary to drill the well 100%. That said, completion of the 3D seismic could be a very important part of securing a drilling partner for the prospect.

Valuation:

- We are updating our valuation to include two scenarios under which the first exploration well will be drilled. In the first scenario, CGX funds the entire well 100% and in the second scenario we assume a farm-out of the prospect in which the farmee pays 100% of the well costs to earn 50% in the Corentyne concession. We then apply a weighting to each scenario to reflect the likelihood of that scenario playing out, in our opinion. We describe each scenario in more detail below.
- Our first scenario is based on a risked probability of success on the Company's initial targets at Eagle Shallow and Eagle Deep West assuming CGX undergoes the project alone at 100%. Our NPV10 values are based on those provided in the Gustavson Associates report, while our probability of success is half that of what is attributed by Gustavson. We have then also assumed an equity issue at \$1.50 per share to reflect the potential dilution should the Company need to raise the additional capital to drill the well. Based on an estimated well cost of \$121 million and a net cash position of \$25 million after completion of the seismic, this would imply a shortfall of \$96 million resulting in an additional 64 million shares issued. We then apply an additional 60% capital and timing risk factor, which is done in an attempt to take into account current market conditions and risk that CGX would not be able to source the capital needed to drill the well alone. The result is a risked NPV estimate of \$5.05 per share.
- Figure 2 shows our calculation of the risked NPV for the Eagle Shallow/Deep prospects under the 100% CGX scenario.

Figure 2 Eagle Shallow Fan / Eagle Deep West Risked NPV Estimate – Scenario 1							
	P50 Recoverable MMBbls	Unrisked			Cormark Risk Factor	Risked	
		Capital \$MM	10% NPV	NPV \$/Bbl		Recoverable MMBbls	10% NPV
Eagle Shallow + Deep West	1,404	3,336	23,641	16.84	2.4%	33	556
Eagle Shallow	545	2,167	8,522	15.64	9.5%	52	813
Eagle Deep West	859	1,116	14,248	16.59	7.5%	65	1,072
No Discovery	-	121	(104)		80.6%	-	(84)
<b>Two Prospects</b>					<b>100%</b>	<b>150</b>	<b>2,357</b>
Wishbone Shallow	439						
Eagle Deep East	904						
<b>Four Prospects</b>	<b>2,747</b>						
Risked NPV	2,357						
Capital/Timing Risk factor	60%						
Risked NPV (incl. Capital Risk)	943						
Add'n'l equity assumed (\$MM)	96						
Equity raised at (\$/sh)	1.50						
Additional shares issued (MM)	64.0						
Pro-forma basic s/o (MM)	186.9						
<b>NPV per share</b>	<b>\$5.05</b>						

Source: Cormark Securities Inc., Gustavson Associates

- Our second scenario explores a case in which CGX successfully farms out a portion of its interest to be carried on the exploration well. Under our assumptions, CGX would have the farmee pay 100% of the exploration well costs for a 50% go forward interest in the Corentyne concession, therefore no additional funds would be required to drill the well. We note that we are showing this for representative purposes only and the terms of our farm-out assumptions may

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differ from the actual terms of any farm-out. We then lowered the capital and timing risk factor to 10% as a pay 100% for 50% deal with a partner significantly lowers that risk, in our view. Under these assumptions, the risked NPV estimate increases to \$8.94/share.

- Figure 3 shows our calculation of the risked NPV for the Eagle Shallow/Deep prospects assuming the farm-out scenario described above.

<b>Figure 3 Eagle Shallow Fan / Eagle Deep West Risked NPV Estimate</b>							
	P50 Recoverable MMBbls	Unrisked			Risked		
		Capital \$MM	10% NPV	NPV \$/Bbl	Cormark Risk Factor	Recoverable MMBbls	10% NPV
Eagle Shallow + Deep West	702	1,668	11,821	16.84	2.4%	16	278
Eagle Shallow	273	1,084	4,261	15.64	9.5%	26	407
Eagle Deep West	430	558	7,124	16.59	7.5%	32	536
No Discovery	-	-	-	-	80.6%	-	-
<b>Two Prospects</b>					<b>100%</b>	<b>75</b>	<b>1,221</b>
Wishbone Shallow	439						
Eagle Deep East	904						
<b>Four Prospects</b>	<b>2,045</b>						
Risked NPV	1,221						
Capital/Timing Risk factor	10%						
Risked NPV (incl. Capital Risk)	1,099						
Add'n'l equity assumed (\$MM)	-						
Equity raised at (\$/sh)	0.00						
Additional shares issued (MM)	-						
Pro-forma basic s/o (MM)	122.9						
<b>NPV per share</b>	<b>\$8.94</b>						

Source: Cormark Securities Inc., Gustavson Associates

- Given the scenarios described above, and CGX's current financial position, we believe the most likely case is that CGX continues to pursue some sort of farm-out agreement at Corentyne. As a result, we are applying a 75% weighting to our farm-out valuation of \$8.94/share and a 25% weighting to the 100% CGX case of \$5.05/share, which results in a weighted risked NPV estimate of \$7.97. This is the basis for our revised C\$8.00/share target price. We maintain our Speculative Buy rating, as we believe CGX continues to be a high risk holding while offering the potential for material upside with exploration success. We continue to believe that CGX should be a part of investor's junior international portfolios.

Conclusion:

- We believe that CGX offers investors the opportunity for material upside from high exploration risk drilling targeting material reserves offshore Guyana. With upcoming catalysts, including the 3D seismic program, which is expected to commence in early September, and subsequent interpretation likely leading to selection of the first location we believe the stock has the opportunity to gain some positive momentum. In addition, the potential for an announcement of a JV partner over the coming months would be positive to the story and provide more certainty and visibility to the first exploration well. As such, we believe that CGX should be a part of any junior international portfolio, offering the potential for material upside from exploration success.

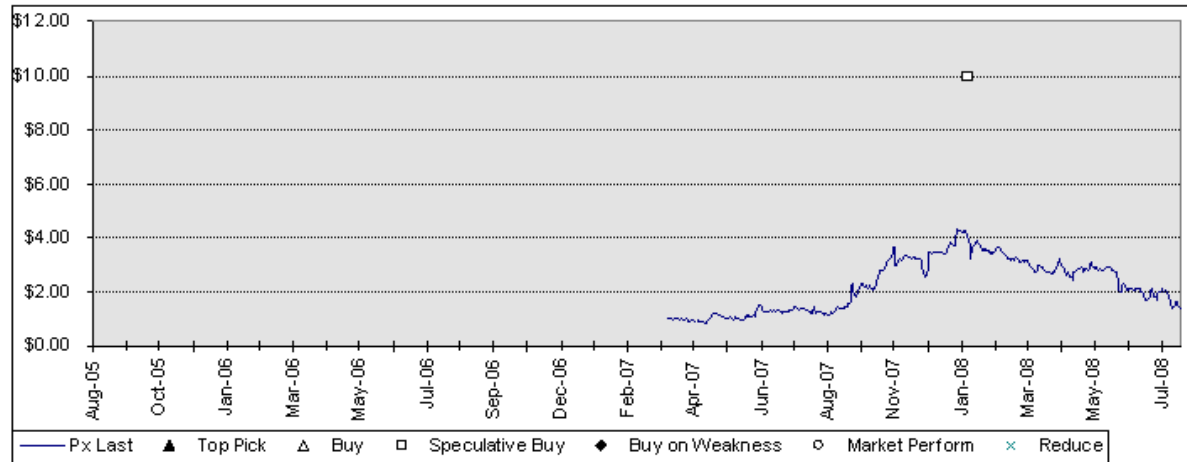
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**CGX Energy Inc.**

Source: Cormark Securities Inc.



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Recommendation / Target Chg

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Date	C\$
16-Jan-08	10.00 (B-S)

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Updated July 2008

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<b>Reduce</b>	expected to underperform its peer group

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