Freehold Royalties Ltd. Announces 2013 Second Quarter Results

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CALGARY, ALBERTA--(Marketwired - Aug 8, 2013) - Freehold Royalties Ltd. (Freehold) (TSX:FRU) announces second quarter results for the period ended June 30, 2013.

Results at a Glance

	Three Months Ended June 30			Six Months Ended June 30		
FINANCIAL ($000s, except as noted)	2013	2012	Change	2013	2012	Change
Gross revenue	44,109	36,163	22 %	84,746	80,529	5 %
Net income	14,292	7,862	82 %	24,785	20,922	18 %
Per share, basic and diluted ($)	0.21	0.12	75 %	0.37	0.33	12 %
Funds from operations (1)	30,115	20,522	47 %	53,932	46,135	17 %
Per share ($) (1)	0.45	0.31	45 %	0.81	0.72	13 %
Capital expenditures	3,313	6,598	-50 %	18,227	19,843	-8 %
Property and royalty acquisitions (2)	658	(99)	765 %	658	49,820	-99 %
Dividends declared	28,019	27,399	2 %	55,916	54,165	3 %
Per share ($) (3)	0.42	0.42	0 %	0.84	0.84	0 %
Long-term debt, period end (4)	55,000	23,000	139 %	55,000	23,000	139 %
Shares outstanding, period end (000s)	66,874	65,440	2 %	66,874	65,440	2 %
Average shares outstanding (000s) (5)	66,649	65,159	2 %	66,512	63,865	4 %
OPERATING						
Average daily production (boe/d) (6)	8,714	8,501	3 %	8,889	8,617	3 %
Average price realizations ($/boe) (6)	54.66	45.74	20 %	51.84	50.33	3 %
Operating netback ($/boe) (1) (6)	47.80	40.64	18 %	45.53	45.12	1 %

(1) See Additional GAAP Measures and Non-GAAP Financial Measures.
(2) Net of adjustments.
(3) Based on the number of shares issued and outstanding at each record date.
(4) Net debt as at June 30, 2013 was $50.6 million, down $4.9 million from $55.5 million at March 31, 2013.
(5) Weighted average number of shares outstanding during the period, basic.
(6) See Conversion of Natural Gas to Barrels of Oil Equivalent (boe).

August Dividend Announcement

The Board of Directors has declared the August dividend of $0.14 per share, which will be paid on September 16, 2013 to shareholders of record on August 31, 2013. This dividend is designated as an eligible dividend for Canadian income tax purposes. Including the September 16 payment, our 12-month trailing dividends total $1.68 per share.

2013 Second Quarter Highlights

- Average production for the second quarter rose 3%, and average price realizations climbed 20%, resulting in a 22% increase in gross revenue compared to the second quarter of 2012.
- Natural gas production accounted for 39% of boe production in the quarter but only 12% of gross revenue.
- Royalty production declined 4% (accounting for 71% of production), while working interest production increased 23% as a result of increased activity levels, particularly on our mineral title lands.

- Oil and NGL production declined 2% in the quarter, while natural gas production rose 9%. Both periods included positive prior period adjustments to royalty production, mainly due to our ongoing audit program. In the second quarter of 2013, positive prior period adjustments were 400 boe per day (100% natural gas), whereas in the second quarter last year, prior period adjustments were 500 boe per day (80% oil).
- Funds from operations totalled $30.1 million in the second quarter, up 47%, mainly due to higher realized prices.
- Net income of $14.3 million was 82% higher, mainly due to higher realized prices. Non-cash charges included in net income amounted to $15.9 million (Q2 2012 - $12.8 million).
- Dividends for the second quarter of 2013 totalled $0.42 per share, unchanged from the prior year.
- Average participation in our DRIP was 25% (Q2 2012 - 25%), allowing us to retain $6.9 million (Q2 2012 - $6.9 million) in dividend payments by issuing shares from treasury.
- Net capital expenditures on our working interest properties totalled $3.3 million, the majority of which was invested on our mineral title lands.
- In June 2013, we acquired seismic and a royalty interest on certain undeveloped land and a commitment from an operator to drill wells on these and other Freehold royalty lands in Alberta. The agreement calls for a maximum expenditure of $0.9 million and as at June 30, 2013, Freehold had spent $0.7 million.
- The current tax liability was reduced to $nil at June 30, 2013 from $23.1 million at December 31, 2012, as income taxes for the 2012 tax year were paid.
- At June 30, 2013, long-term debt was $55 million, and net debt was $50.6 million, down $4.9 million from March 31, 2013. Net debt at June 30, 2013 was 0.5 times trailing funds from operations and net debt obligations were approximately 14% of total capitalization.

Royalty Drilling

Drilling on our royalty lands was down, and well licence activity was also down compared to last year. The reductions follow industry trends, where drilling was down 20% in the second quarter, largely due to additional snow accumulations and June rains.

To date in 2013, royalty drilling has focused primarily on recognized oil and liquids-rich natural gas trends within the Alberta and Williston basins, including the Lloydminster heavy oil area, the Mississippian subcrop and Bakken resource play in southeast Saskatchewan, and the Cardium light oil play in west central Alberta. About 80% of the equivalent net wells drilled in the first half of 2013 were oil, similar to last year. Both vertical and horizontal wells were drilled on our royalty lands, with horizontal drilling accounting for 60% of the activity, on par with last year.

Working Interest Activity

Capital investment in the second quarter of 2013 amounted to $3.3 million, bringing total capital expenditures for the year to date to $18.2 million. The majority of this activity centered on our mineral title lands. In the second quarter, we participated in the drilling of three (0.9 net) wells with a 100% success rate. In southeast Saskatchewan, we participated in the drilling of one (0.4 net) Bakken horizontal oil well. In Alberta, we drilled one (0.2 net) horizontal Viking oil well at Redwater and one (0.3 net) horizontal Glauconitic liquids-rich natural gas well at Willesden Green. This drilling activity had little effect on second quarter production but is expected to add to our production base as the wells are completed and tied in.

Guidance Update

The table below summarizes our key operating assumptions for 2013, updated to reflect actual results for the first half and our current expectations for the remainder of the year. The changes reflect the following factors:

- As a result of higher than anticipated production in the second quarter, we have increased our 2013 production forecast by 100 boe per day. On a boe basis, production volumes for 2013 are expected to be approximately 63% oil and natural gas liquids (NGL) and 37% natural gas, similar to our current product mix. We continue to maintain our royalty focus with royalty production accounting for 71% of forecasted 2013 production.

- We are increasing our capital budget for the year by $2.0 million as a result of additional drilling at Buck Lake, Alberta, and strong partner drilling in southeast Saskatchewan. Capital investment in the second half of 2013 is expected to total $13.8 million, with approximately 65% allocated to drilling and completions, primarily in southeast Saskatchewan and Alberta. This will add roughly 16 (6.0 net) wells.

- Operating expenses for the year are being increased by $0.30 per boe to reflect higher than expected costs in the first half of the year (including prior period adjustments and additional snow plowing charges) and the upcoming fall turnaround season.

- Average WTI and WCS oil prices were increased by $3.00 and $6.00 per barrel, respectively, while the average AECO natural gas price was reduced by $0.50 per Mcf.

- Under our current production and pricing assumptions (and excluding any potential acquisitions), we anticipate being able to reduce long-term debt to $44 million by the end of this year.

- Cash taxes payable in 2013 for the 2012 tax year are $1 million lower as our previous estimate was adjusted; as a result instalments for the 2013 tax year are also $1 million lower.

Key Operating Assumptions (1)

		Guidance Dated		
2013 Annual Average		August 8, 2013	May 15, 2013	Mar. 7, 2013
Daily production	boe/d	8,800	8,700	8,500
WTI oil price	US$/bbl	96.00	93.00	95.00
Western Canada Select (WCS)	Cdn$/bbl	75.00	69.00	71.00
AECO natural gas price	Cdn$/Mcf	3.00	3.50	3.10
Exchange rate	Cdn$/US$	0.98	0.98	1.00
Operating costs	$/boe	5.30	5.00	5.00
General and administrative costs (2)	$/boe	2.60	2.60	2.60
Capital expenditures	$ millions	32	30	30
Dividends paid in shares (DRIP) (3)	$ millions	28	28	28
Long-term debt at year end	$ millions	44	44	48
Cash taxes payable in 2013 for 2012 tax year (4)	$ millions	22	23	23
Cash taxes payable for 2013 tax year (instalments) (4)	$ millions	24	25	25
Weighted average shares outstanding	millions	67	67	67

(1) A sensitivity analysis of the potential impact of key variables on funds from operations per share is provided on page 5 of our 2012 Annual MD&A.

(2) Excludes share based and other compensation.

(3) Assumes an average 25% participation rate in Freehold's dividend reinvestment plan, which is subject to change at the participants' discretion.

(4) Corporate tax estimates will vary depending on commodity prices and other factors.

Recognizing the cyclical nature of the oil and gas industry, we continue to closely monitor commodity prices and industry trends for signs of deteriorating market conditions. We caution that it is inherently difficult to predict activity levels on our royalty lands since we have no operational control. As well, significant changes (positive or negative) in commodity prices (including Canadian oil price differentials), foreign exchange rates, or production rates may result in adjustments to the dividend rate.

Despite commodity price volatility, we have been able to maintain a steady monthly dividend rate of $0.14 ($1.68 annually) per share since January 2010. Based on our current guidance and commodity price assumptions, and assuming there are no significant changes in the current business environment, we expect to maintain the current monthly dividend rate through 2013, subject to the Board's quarterly review and approval.

Availability on SEDAR

Freehold's 2013 second quarter interim unaudited financial statements and accompanying Management's

Discussion and Analysis (MD&A) are being filed today with Canadian securities regulators and will be available at www.sedar.com and on our website.

Forward-looking Statements

This news release offers our assessment of Freehold's future plans and operations as at August 8, 2013, and contains forward-looking statements that we believe allow readers to better understand our business and prospects. These forward-looking statements include our expectations for the following:

- our outlook for commodity prices, including light/heavy oil price differentials;
- changing economic conditions;
- industry drilling, development, and licensing activity on our royalty lands;
- development of working interest properties;
- participation in the DRIP and our use of cash preserved through the DRIP;
- estimated capital budget and expenditures and the timing thereof;
- estimated operating expenses;
- long-term debt at year end;
- average production and contribution from royalty lands;
- key operating assumptions;
- amounts and rates of income taxes and timing of payment thereof; and
- maintaining our monthly dividend rate through 2013 and our dividend policy.

By their nature, forward-looking statements are subject to numerous risks and uncertainties, some of which are beyond our control, including the impact of general economic conditions, industry conditions, volatility of commodity prices, currency fluctuations, imprecision of reserve estimates, royalties, environmental risks, taxation, regulation, changes in tax or other legislation, competition from other industry participants, the lack of availability of qualified personnel or management, stock market volatility, and our ability to access sufficient capital from internal and external sources. Risks are described in more detail in our Annual Information Form.

With respect to forward-looking statements contained in this news release, we have made assumptions regarding, among other things, future oil and gas prices, future capital expenditure levels, future production levels, future exchange rates, future tax rates, future participation rates in the DRIP and use of cash retained through the DRIP, future legislation, the cost of developing and producing our assets, our ability and the ability of our lessees to obtain equipment in a timely manner to carry out development activities, our ability to market our oil and natural gas successfully to current and new customers, our expectation for the consumption of crude oil and natural gas, our expectation for industry drilling levels, our ability to obtain financing on acceptable terms, and our ability to add production and reserves through development and acquisition activities. The key operating assumptions with respect to the forward-looking statements referred to above are detailed in the body of this news release.

You are cautioned that the assumptions used in the preparation of such information, although considered reasonable at the time of preparation, may prove to be imprecise and, as such, undue reliance should not be placed on forward-looking statements. Our actual results, performance, or achievement could differ materially from those expressed in, or implied by, these forward-looking statements. We can give no assurance that any of the events anticipated will transpire or occur, or if any of them do, what benefits we will derive from them. The forward-looking information contained in this document is expressly qualified by this cautionary statement. Our policy for updating forward-looking statements is to update our key operating assumptions quarterly and, except as required by law, we do not undertake to update any other forward-looking statements.

You are further cautioned that the preparation of financial statements in accordance with IFRS requires management to make certain judgments and estimates that affect the reported amounts of assets, liabilities, revenues, and expenses. These estimates may change, having either a positive or negative effect on net income, as further information becomes available and as the economic environment changes.

Conversion of Natural Gas To Barrels of Oil Equivalent (BOE)

To provide a single unit of production for analytical purposes, natural gas production and reserves volumes are converted mathematically to equivalent barrels of oil (boe). We use the industry-accepted standard conversion of six thousand cubic feet of natural gas to one barrel of oil (6 Mcf = 1 bbl). The 6:1 boe ratio is based on an energy equivalency conversion method primarily applicable at the burner tip. It does not represent a value equivalency at the wellhead and is not based on either energy content or current prices. While the boe ratio is useful for comparative measures and observing trends, it does not accurately reflect individual product values and might be misleading, particularly if used in isolation. As well, given that the value ratio, based on the current price of crude oil to natural gas, is significantly different from the 6:1 energy equivalency ratio, using a 6:1 conversion ratio may be misleading as an indication of value.

Additional GAAP Measures

This news release contains the term "funds from operations", which does not have a standardized meaning prescribed by GAAP and therefore may not be comparable with the calculations of similar measures for other entities. Funds from operations, as presented, is not intended to represent operating cash flow or operating profits for the period nor should it be viewed as an alternative to net income or other measures of financial performance calculated in accordance with GAAP. We consider funds from operations to be a key measure of operating performance as it demonstrates Freehold's ability to generate the necessary funds to fund capital expenditures, sustain dividends, and repay debt. We believe that such a measure provides a useful assessment of Freehold's operations on a continuing basis by eliminating certain non-cash charges. It is also used by research analysts to value and compare oil and gas companies, and it is frequently included in their published research when providing investment recommendations. Funds from operations per share is calculated based on the weighted average number of shares outstanding consistent with the calculation of net income per share.

Non-GAAP Financial Measures

Within this news release, references are made to terms commonly used as key performance indicators in the oil and natural gas industry. We believe that operating income, operating netback, and net debt to funds from operations are useful supplemental measures for management and investors to analyze operating performance, financial leverage, and liquidity, and we use these terms to facilitate the understanding and comparability of our results of operations and financial position. However, these terms do not have any standardized meanings prescribed by GAAP and therefore may not be comparable with the calculations of similar measures for other entities.

Operating income, which is calculated as gross revenue less royalties and operating expenses, represents the cash margin for product sold. Operating netback, which is calculated as average unit sales price less royalties and operating expenses, represents the cash margin for product sold, calculated on a per boe basis. Net debt to funds from operations is calculated as net debt (total debt less working capital) as a proportion of funds from operations for the previous twelve months. In addition, we refer to various per boe figures, such as revenues and costs, also considered non-GAAP measures, which provide meaningful information on our operational performance. We derive per boe figures by dividing the relevant revenue or cost figure by the total volume of oil and natural gas production during the period, with natural gas converted to equivalent barrels of oil as described above.

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