BULLETIN # 75 – SEPTEMBER 25 2011
WEEKLY WRAP

THE NEW REALITY—AND HOW I'M DEALING WITH IT
MARKET COMMENTS/DONY'S TECHNICAL ANALYSIS

Did anybody else have some left over market emotion hanging around them on the weekend? Spend any time thinking, geez, wish I would have sold that stock a few weeks ago, or not bought that stock this last week?

You weren't the only one. The junior oil sector was probably the single hardest hit on the TSX this week. All commodities got hit—copper dropped from $3.93-$3.31 this past week, and I'm sure everyone saw gold drop $100 Friday. The many investors who play the junior resource sector were looking at their favourite stories/stocks and wondering…how could…or…oh my…

And there could still be another 5-10% downside, which means I will continue looking for YIELD for my portfolio. Now that we are in a sideways to down market, yield stocks will hold up the best…and in the face of Operation Twist, which is keeping long term rates down, stocks that pay dividends should see "yield compression", meaning yields that were previously 8-12% go down to 6%. How does that happen? By having the stock price of the underlying issue go UP!

It's clear that a new level of fear has entered the market. The S&P 500 index has now bounced three times off of 1120, and now needs to hold that or expect another 5-10% drop. That may take months, or it may be a couple of days.

So stocks that I previously would have had a lot of patience for, now I don't—and those would be (as I have said several times) the junior more speculative companies in the portfolio. But even some of the my favourites are vulnerable to pullbacks here, and despite my love for companies like Coastal Energy, TAG Oil and others—I may let the chart tell me when to sell them as I find a compelling yield story (and I am onto one of the best I have ever seen…).

I'm going to keep raising cash. Of course, the fear is you're raising cash at the bottom. But the reality is I'm still in some great profit positions. And I can always buy them back—most of them are great growth stories, so I will.

I'll have some market comments at the bottom, but first a couple points on oil before I get into my stocks. The oil price chart has good support at $80 WTI/barrel and very strong support at $70. Donald Dony, who does a great job of chart reading atwww.technicalspeculator.com, says he expects oil to stay in the $75-$80 range, and that, for him, it would take a year-long bear market all the way through 2012 to see $70 oil. Senior oil stocks are already pricing that in so their correction is much closer to being complete than the juniors.

The current wave of negativity is almost unparalleled in my career; only the nuclear winter of junior mining stocks from 1997-2001 is close. Dony is expecting a bounce in stocks and oil in October, but I am taking that as a selling opportunity again for my juniors—and raise cash for my yield stocks.

Despite Dony's thoughts that the oil price is not going much lower, the junior stocks can still get sold. Most charts took their hit in June, and despite all the growing debt issues through late summer, they held up well until last week. Many gapped down, cutting through support, signalling a big change in investor opinion on them. Those stocks will have a hard time regaining upward momentum, and again, despite my love for them, may be able to be bought back at cheaper prices in the future. Donald Dony's regular commentary on select OGIB stocks is at the bottom of this as usual.

However, the only stocks I will consider buying for now are those that have yield, with Open Range Energy (ONR-TSX) and now GLNG ahead of CEU.

OPEN RANGE ENERGY – ONR:TSX

While I still have not been able to speak with Lyle Michaluk, the CFO who will be CEO of the new Poseidon Concepts water handling company, I did speak with one of the analysts who is very close to the company and does marketing with them to institutions.

My only question to him on the story was—what payout ratio does the company expect to have? That will decide the stock price. The way that works is…the higher the payout ratio, the riskier the stock is to the market, and the market will price in a higher yield…which means a lower stock price. The answer was 70% payout ratio, which to me implies an 11-12% yield—and in this market, maybe higher.

So that was (A LOT) higher than I expected. And this did come from an analyst, not management. The good news is that means management must own a lot of stock. But it will mean a lower share price than I expected for ONR.

A 12% yield on a $1.08 payout = $9/share. Multiply that by 0.882 to account for the current share structure gives a share price of $7.93. And in this market, I just might get to buy it there.

GOLAR LNG—GLNG:NASD

This moves up the food chain for me now. I'm not running out to buy stock right away, but I see LNG shipping as a fairly recession proof business right now—the cheaper natural gas gets around the world, the more demand there is for shipping. The tanker market is so tight that customers want 1-2 year contracts.

The new FSRU business is a $250 million ship that replaces a $2 billion land based LNG terminal. The current 27.5 cent per quarter dividend is supported by the cash flow from the Indonesian FSRU expected to become operational in Q1 2012.

STOCKS THAT WERE HIT HARD THIS WEEK

DeeThree (DTX-TSX)is late on news of drilling results. They have only announced one well, a good one, and we know the second one won't be that good. But the anonymous JV partner in the SW corner of their lands has drilled two wells, and likely completed (read: fracked) them. The northern JV partner, (again anonymous) is set to spud their first well late this week.

I still see strong growth in production here in the near term. However, the lack of IP rates means I won't be buying any more stock. The first few drill results on the Canadian side of the play have been spotty; there are no official results on the American side.\

Interestingly, **Primary Petroleum (PIE-TSXv)**has one of the best stock charts in my portfolio right now. Primary has a large land position in the Alberta Bakken in Montana.

TAG Oil (TAO-TSX)has several coming catalysts, but it's unclear if it will be enough for this great trading stock. Sometime next month they should announce that all the (very) successful summer drilling is tied in—taking production to a flush 6000 bopd, and likely a base rate of 4500 bopd (Flush production is the first part of an unconventional well that has such a high flow rate BEFORE the steep decline ends, and what is called the "long tail" of production declines begins). But that is priced in. The other will be another program in the Taranaki Basin, being as Apache will be spending the money on the Whangai shale.

Again, TAG's biggest catalyst will likely be an announcement by New Zealand Energy (NZ-TSX) of drilling and completing their Ranui-1 well in the Whangai shale this fall. Keep your fingers crossed on that one…that would be a big catalyst.

GASFRAC (GFS-TSX)needs to put together some strong quarterly financials. Q3 will be weak, as they said on the Q2 conference call that the rigs only got to work in August, and one rig is still in customs at the US border. To meet revenue projections it needs to add more rigs—which could mean an equity raise early in 2012. However, their balance sheet is in great shape (had they used debt in the February 2011 raise this stock would be $4 right now) and can grow by tapping their debt line now.

Should oil prices go much below $80, GasFrac's higher cost fracks could become more of an issue.

BORDER PETROLEUM (BOR-TSX)has been quiet as a mouse as they wait for government approval on the mineral title to their Loon Lake First Nations deal. The Canflame acquisition which hosts another anonymous asset has also been quiet. In one of the releases announcing this deal they said there was (aside from 220 bopd oil) a test well on this still-anonymous asset. No test results have been released on this well. The stock traded well despite no news until this last week, but a junior oil stock THAT QUIET just can't hold up in a market meltdown.

TORQUAY OIL (TOC.A-TSX)is in the same boat as DeeThree and Border. They have issued no drill results for a long time (sadly, no successful drill results for a really long time), and again, the unproven potential of a large Bakken land package is not enough to hold up the stock in a market like this.

MARKET COMMENTS

I'll keep this brief. One thing I am fairly certain of is that the new reality of the Euro – whatever that may be – will be kinder for investors than the current dithering we're experiencing. It's the waiting that is killing the markets. I've even read some reasoned articles explaining how a Greek default would not be such a big deal and we could get on with life.

Would there be contagion, where the markets shun the other PIIGS hard and fast causing all them to default? Nobody really knows. Remember that when you're reading the newspaper or the web and you're listening to a guru whose degrees have more letters than his last name. Nobody really knows. There are so many competing views and we've never been here before. But it is the waiting that is the problem right now.

Of course, one of the real problems is deciding how much of a haircut, or loss, the lenders to these PIIGS countries should take. The rest of the amount owing gets socialized, i.e., the taxpayers pay for it. I see that over the last few months that number has gone from zero to 10% to 20% and now I'm seeing 50% in the media sometimes.

I'm not saying 50% is a fair number but whenever I see half-half compromise I think we're close to a deal.

On one hand, why should the people pay anything? Everybody knew these countries were way past their EU debt guidelines, that wasn't hidden (to the best of my knowledge) and being as banks/lenders do much better research than equity issuers, I would suggest the lenders knew exactly what they were lending into and so why should anyone else pay for their incompetence? I can relate to the Greek protesters. THEY would potentially be better off with a default and no huge debt overhang for the next 10 years.

On the other hand, people always get the government they deserve, just as management always gets the labour they deserve. So the people said give me more, and the government did, and here we are. So maybe 50-50 split isn't such a bad idea. Whatever the number is Europe, let's get on with it.

The other thing I'm thinking about is how the Internet and mobile communications have turned the world upside down so fast—in just 20 years. The masses really do have a lot more political and economic power than ever before, and nobody – neither the old elites nor the newly empowered masses – knows how to deal with that responsibly.

Just a couple other quick things to wrap this up: One is, I truly doubt we are going to see a repeat of the 2008 collapse. But sadly, I think we are not likely to see a 2009 style rebound either. The governments will not allow another Lehman-style financial default where the back end liquidity—bank-to-bank—gets frozen. Bank to bank interest rates still aren't anywhere near what they got to in 2008. Neither governments nor central bankers are going to allow that to happen again…but that brings up its own issues.

And private sector balance sheets are much better. Asset values are already way down. US existing home sales are at a 5 month high and building permits are at an eight month high. The S&P 500 is trading at 11x earnings, which is very low.

DONALD DONY'S COMMENTS

On stocks I may consider buying still (and while this list is getting shorter, for the short term, I'm hoping to have my new yield pick ready within a week—it's also a growth stock that I think can more than double in the next 9-12 months!)

OPEN RANGE--ONR: Primary trend is up. Likely a price top is forming. 1st support is at $8.50. Outlook is weakening. Expected to pullback to $7.00-$7.50 main support level. Recommendation: Continue to hold. Expect a short term decline.

GOLAR--GLNG: Primary trend is up. 1st support is $27.50-$30.00. Outlook is deteriorating. The gap today is a negative change in investor's attitudes. Recommendation: Continue holding for now. Keep stops at $28. Be prepared to sell.

CDN ENERGY SERVICES--CEU: Primary trend is up. Currently consolidating. On 1st key support level of $10.50. Outlook is deteriorating. The gap down in today's trading suggests and change in investors thinking. Recommendation. Keep stops at $10.00. Be prepared to sell.

While I love these companies—CEN, TAO and IAE all have discovered significant new production they are bringing onstream in the near term—I am not considering adding to any of them at this time.

COASTAL ENERGY--CEN: Primary is changing. Gap in today's trading is negative. Outlook is deteriorating. On 1st support level. Recommendation: Sell. Take your profits.

TAG OIL--TAO: Primary trend is flat. Broken 1st support level. Outlook is deteriorating. Gap today signals a new downward trend. Recommendation: Try to sell close to $7.00. Failed breakout. $5.80 is main support—buy at bottom of that range

ITHACA ENERGY--IAE: Primary trend is down. Outlook if for a continuation of the down movement. Recommendation: Stay on the sidelines.

WAVEFRONT--WEE: Primary trend is down. Breaking 1st support line. --Recommendation: Stay on the sidelines.

GASFRAC--GFS: Primary trend is down. Gap in today's trading is negative. Did not break through the resistance line of $8.50-$8.60 which is the buy level. recommendation: Hold or wait on the sidelines. Wait until the end of the month. Watch the $7.00 support level.

Lastly, many subscribers profited from a great run in Xcite Energy (XEL-TSXv), a North Sea explorer that is developing the Bentley heavy oil field. It was one of my biggest winners.

The stock has been holding in OK recently, trading at $2 on very light volume. While I am not a buyer in this kind of market, I am watching the stock, as their neighbour in the North Sea, Nautical Petroleum (NPE-AIM, the London Stock Exchange junior board) rallied by almost 8% on talk of a positive update early next week on tests of its Kraken prospect, off the coast of the Shetland Islands.

They’re completing their first horizontal appraisal well on their Kraken field (2km away from Bentley). They flowed 300 boe from their vertical appraisal well last year just prior to Xcite's horizontal well drill. The Kraken heavy oil has very similar characteristics to Bentley. IF NPE hits big (news expected in a couple weeks), that will cause me to watch Xcite a little more closely. But I won't be buying stock as they need to convey to the market how they are going to finance.

After several North Sea assets were just bought by Apache, a successful well could turn investors back into North Sea oil stocks, depending on the market.

TOMORROW IS THE BIG DAY – OUR SUBSCRIBER SUMMIT. LOOKING FORWARD TO MEETING MANY OF YOU! West coast locals should come to dinner at 630 pm at Joey's on Burrard at Hastings even if you can't make the presentations.