

# Growth Stocks Weekly

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**Performance:** Year ended April 1996 116.9%; 1997 28.1%; 1998 36.4%; 1999 39.4%; 2000 180.9%; 2001 -50.5%; 2002 18.7%; 2003 28.8%; 2004 166.7%

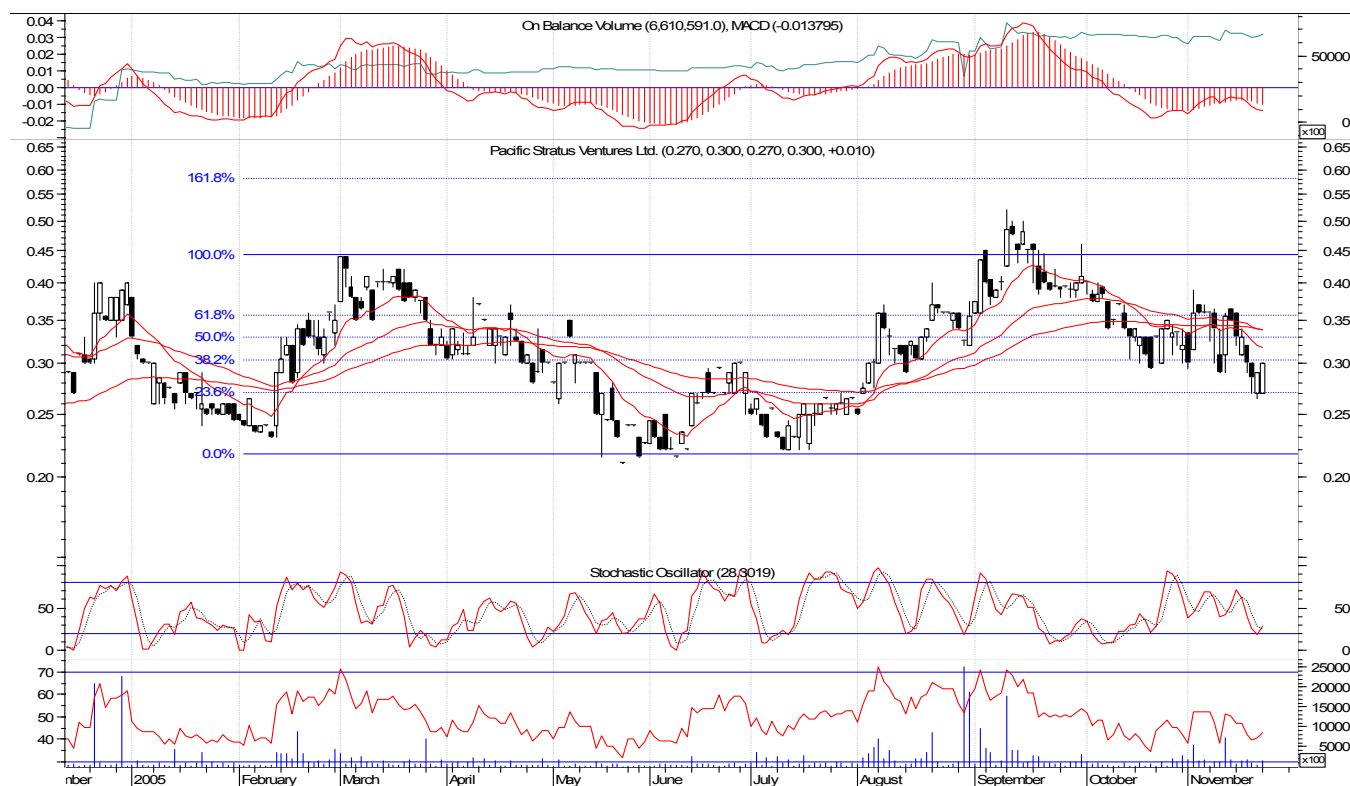
## Junior Gold and Natural Resource Sector Report

November 20, 2005

### Early-Stage Oil & Gas Development Opportunity (Colombian Exposure)

#### UPDATE REPORT

#### PACIFIC STRATUS ENERGY (PVL-TSX Venture Exchange)



Daily chart, High C\$0.52, Low C\$0.21, Last Trade C\$0.29

#### Commentary

Much has happened since our initial report issued October 2004. With \$17 million in the bank, completion of their Gran Columbia acquisition and an expanded management team, it is becoming clear that this company is fast-tracking to become a serious oil & gas player in South America. After more than a year of due-diligence, several fundings, and key acquisitions, Pacific Stratus is at the start of a growth curve that will be led by drilling success, production, cash-flow and increasingly higher-profile deals.

The timing looks to be perfect - their recent \$14.4 million financing priced at \$0.25 becomes free-trading on November 21, 2005, offering near-term liquidity around the current \$0.27-0.30 support area. Toronto-based Sprott Securities and Haywood Securities participated in this last financing. Sprott in particular is recognized as one of Canada's mining powerhouses and "smart money". It's important for a Canadian-listed company receive strong sponsorship out of Toronto in order to attract serious institutional interest, and we suspect that once news starts to flow we will see such market leadership develop.

There is much fertile ground in long-neglected Colombia and Ecuador, with better royalties and government programs available to well-capitalized applicants seeking to take advantage of under-developed assets. Significant economic reforms are well established (see my recent published report on Colombia which follows this update). Opportunities exist for experienced and locally conversant fast-movers to step into low-risk exploration and production fields.

### **Strong Sponsorship**

We took great pains in our initial report to point out the value of the strong relationship Pacific Stratus enjoys with Endeavour Mining Capital group. Probably best known for the incredible success of Wheaton River (since bought out by Goldcorp (G-TSX)) and Northern Orion (NNO-TSX), and its company-building abilities within the mining sector, Endeavour is a mining finance house that continues to prosper from a winning combination of talent and timely ventures.

Endeavour shifted its focus to include energy back in 2004, and set out to acquire the necessary talent and resources to execute several well-thought-out strategies in that sector. We had already [profiled](#) and enjoyed success with early stage oil & gas-focused Bankers Petroleum (BNK-TSX) starting back at about \$0.40 (subsequently over \$2 this last year). More recently Endeavour floated UrAsia Energy (UUU-TSXv), raising over half-a-billion dollars and creating the world's 3<sup>rd</sup> largest uranium producer out-of-the-gate.

Similarly, Pacific Stratus is a story about access to capital and the implementation of North American technology and engineering methods. There are discovered but undeveloped oil & gas fields around the world that can quickly increase production given technical know-how and cash. South America and Colombia in particular is overlooked. Exceptional opportunities are available to well connected and funded operators.

Technical management is a key ingredient. Pacific Stratus' team includes South American nationals who have each spent 20-plus years in the oil and gas business and senior management who have created much wealth for investors in their earlier ventures – in fact, one of their other companies, Bolivar Gold Corp. (BGC-TSX), is the subject of a US\$330 million cash buyout offer from South African mining giant Gold Fields Ltd. as we go to press.

### **Operations**

Pacific Stratus operates in a niche market: exploring for and developing production in known fields where technical risk is low, but target reserves are high – but not high enough to attract competition from major oil companies.

Pacific Stratus has assembled four very low-risk properties in Colombia, totaling half a million acres. The targets to be drilled are surrounded by production, in proven oil and gas basins with established successful oil wells. Their holdings include "work-overs", old wells requiring new technology to re-establish or improve production. These interests were acquired a year ago when the price of oil was significantly lower.

As these wells are brought into production, Pacific Stratus will convert the oil & gas resource surrounding their properties - independently estimated to be at over 43 million barrels - into a more valuable "reserve" status, allowing them to include them on their balance sheet. That allows the company to raise debt and equity for progressively larger acquisitions.

On November 10, 2005 Pacific Stratus announced encouraging initial drilling results from Don Pedro-1, located in the Doima Block in the Upper Magdalena Basin of Colombia. The total measured depth of the well was 3,555 feet, reaching all four main targeted reservoirs. The well has shown excellent pressurized gas (1200 PSI), with casing head pressure (CHP) equal to 450-500 PSI, and oil-bearing deep reservoirs, all of which lead the company to believe that what has been encountered is one of a series of prospective structures along the gas-producing Monserrate - Montañuelo trend in the Doima Block. The company has a net land position of 325,000 acres in the highly prospective Doima Block.

### **Current Market Capitalization**

126.1 million Shares outstanding, Market cap = \$36.5 million

180.8 million fully diluted shares outstanding, Market cap (FD) = \$52.4 million

Cash (Sept 05) = CAD\$17 million

### **Technicals**

Price has effectively traded in a relatively narrow base-building range between \$0.22 and \$0.45. The last rally saw an attempt at a break out, with a new high reached near the low-\$0.50 area. A pattern of higher lows and higher highs seems well-established, hinting at a coming breakout that will likely see new support form and hold in the \$0.45 area. Timing seems particularly good right now for new positions or to add to earlier purchases given the fundamentals and news-flow are aligning with price trading on an important support area in the \$0.27-\$0.30 range. This also coincides with the release of restricted shares from their last financing at \$0.25, providing some opportunity to buyers to take advantage of any pending sellers looking for liquidity. It should be noted that there has been some shorting in anticipation of the free-trading date, and so it may now be a non-event. A move through \$0.36 would suggest a run to test the \$0.55 area for a potential breakout.

**Website:** <http://www.pacificstratus.com/s/Home.asp>

## APPENDIX

### *Colombia – Attractive for Oil & Gas Exploration & Development*

Colombia is a country of significant natural resources, endowed with substantial oil reserves along with major deposits of gold, silver, emeralds, platinum and coal. It has also been ravaged by a decades-long violent conflict, involving guerrilla insurgencies, drug cartels and gross violations of human rights. Needless to say, this has deterred investors and tourists alike.

What may be less known is that the economy has been gradually and relentlessly transformed since 1999 in the aftermath of the country's worst economic crisis in 30 years. The result is real economic growth of 4% per year, unemployment down to 12% from over 20%, the public deficit down to a low 1.3% of GDP, inflation down to 5.5% - the lowest level in decades, a steep decline in the poverty rate, a strengthening peso and recovering banking sector. Recently, the IMF commended the Colombian government's pursuit of sound policies and structural reforms, and the resulting lowered country risk premium. Violence has been dropping significantly due in large part to the "get tough" attitude of the current president.

When President Alvaro Uribe came to power in May 2002, he was the first candidate ever to win a first-round political victory. He continues to enjoy high approval ratings. A Harvard and Oxford-educated lawyer and staunch Roman Catholic, he is considered hard-line and right-leaning, a workaholic and a disciplined scholar. He is a survivor, having been elected mayor of Medellin in 1982 and governor of Antioquia 1995-97. His father was a wealthy landowner, killed when FARC rebels tried to kidnap him. Mr. Uribe himself has survived a handful of assassination attempts.

Mr. Uribe has had much success in stemming the murder and kidnappings, simultaneously engaging in formal peace talks with far-right warlords, seeking international mediation, courting U.S. military and financial assistance, boosting the military and police presence, and launching major offensives against the various violent elements.

The U.S., a key market for Colombian cocaine, has increasingly bankrolled the fight against the drug cartels in particular, with billions of dollars, equipment, manpower and expertise. Colombia is the third-largest recipient of U.S. foreign aid, after Israel and Egypt, dispensed through the world's largest U.S. Embassy (at least until the new Iraq one is built).

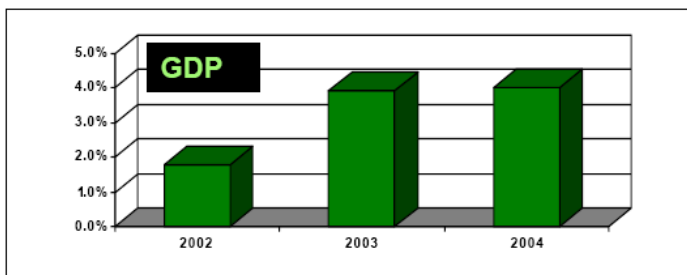
Colombia is proof that having vast natural resources does not necessarily determine how wealthy that country is. In fact, it is often those very same natural resources that motivate the theft and larceny that ultimately impoverish a country's institutions and culture. With a renewed emphasis on property rights, transparency, personal security and freedom, Colombia is attracting significant new foreign investment capital.

One of Colombia's largest relatively untapped assets is hydrocarbons (oil and gas). Colombia produced over 800K boe/d at its peak, but currently produces only about 550K boe/d. Meanwhile, domestic consumption has grown from under 200K boe/d to nearly 400K boe/d. If Colombia does not start to grow production they will soon become an importing nation, along with the associated negative balance of payments pressures. For this reason extensive fiscal changes were made that encourage exploration in the country.

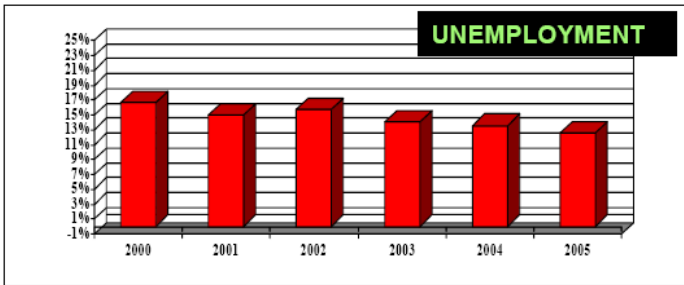
The country is vastly under-explored relative to the U.S. and Canada and yet has extensive infrastructure in place. Discoveries can be brought on line quickly. The producing basins are connected to refineries and ports by an ample oil and gas pipeline system. Colombia has enacted new legislation to encourage drilling in the country. With success in limiting terrorism, the upside for companies in the country is significant. The key for companies considering doing business in Colombia is to have the expertise and local relationships in place. There are relatively few foreign operators, and so there exists much opportunity for those able to bring expertise and technology to the table. The national oil company Ecopetrol usually retains the right to back in for a 30% interest.

Colombia has put in a very attractive new fiscal regime that several Canadian companies are taking advantage of. The one caveat is that while Colombia's government has had success in restraining terrorism, if a new government is elected in 2006 and changes policy (unlikely, but this is South America!) this could be negative for the oil industry. However, historically no existing contracts have ever been modified. Getting access to drilling rigs in Colombia is fairly difficult at this time.

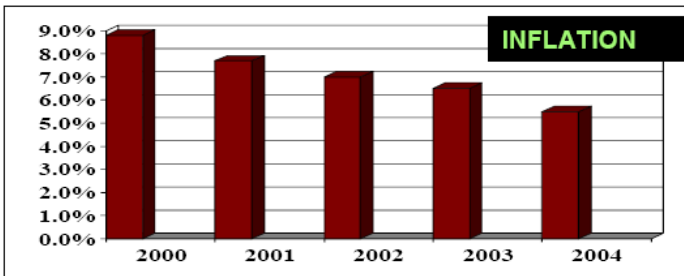
#### ◆ **Gross Domestic Product (GDP) Growing**



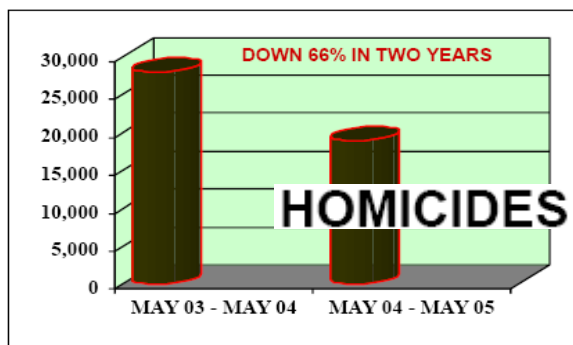
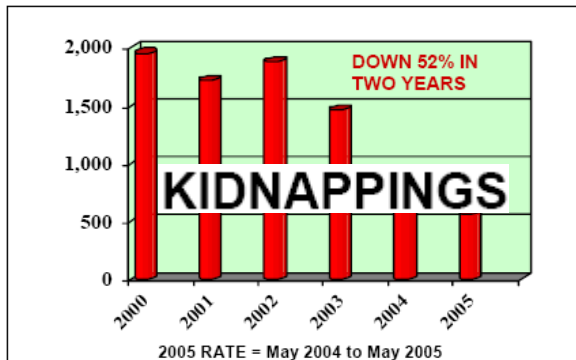
- ◆ Unemployment still high but dropping



- ◆ Inflation below 6%, the lowest in 30 years and among the lowest in Latin America



- ◆ International Debt Rating (S&P) increased from negative to stable in 2003
- ◆ The Colombian stock market rose 120% in \$US terms in 2004 –the highest in the world
- ◆ Military personnel increased from 273,000 to 370,000 in 2 years
- ◆ U.S. assistance now approximately \$US600 million per year
- ◆ Most assaults on the military now reduced to land mines versus previous direct attacks by groups of 30 to 100 guerillas



## Summary

Colombia offers many attractions to foreign investors:

- Located at the midway point between North and South America.
- The only country in South America with Atlantic and Caribbean coasts.
- Easy access to North American, European, Asian and Latin American markets.
- One of the most stable economies in Latin America.
- Steady economic growth, above the Latin American average.
- Growth rate of 4.10% in 2004.
- Declining inflation over the past few years, reaching 5.5% in 2004.
- Declining foreign debt.
- Uninterrupted democracy except for a four-year period in the 1950s.
- The workforce is considered the best in the Andean Community and is among the most qualified in Latin America for managerial, operational and technical positions.
- The adult literacy rate in Colombia is one of the highest in Latin America.
- The workforce is competitive in terms of labor costs, with services salaries and hourly manufacturing wages highly competitive compared to other developing and developed countries.
- Human capital development in Colombia, particularly at the professional level, does not discriminate against women.
- Working shifts are between 6 a.m. and 10 p.m. for a regular 48-hour work week, reducing overtime and extra night time pay for companies needing to employ workers for two shifts.
- Companies can reduce labor costs by hiring apprentices under service contracts, and there are reduced compensation levels for dismissal without just cause.
- There is a defined export platform and privileged access to world markets through various trade agreements and tariff preferences.
- 10 Duty Free Zones offering a number of tax and procedural incentives, as well as foreign exchange benefits.
- 5 Special Economic Export Zones offering a special regime for new export-oriented businesses.
- Incentives for large exporters
- Special import - export systems.
- Colombia has the third largest population in Latin America (45 million inhabitants), after Brazil and Mexico.
- Modern communications infrastructure.
- Increasing investment in transport infrastructure.
- Over 400 multinational companies are doing business in Colombia, successfully growing their businesses and expressing confidence in the country's potential.

## ***Richard Reinhard's Growth Stocks Weekly***

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