



## Cimarex Energy

### Relative Value

Cimarex (XEC) ranks relatively high within the peer group in context of facing the current commodity downturn. Its strong financial profile creates a solid platform; its sub 1x net leverage level (0.6x at end of Q3 14) is the lowest amongst our peer group and liquidity is solid at \$1.6 billion including \$564 million of cash and undrawn revolver of \$1.0 billion. The favorable financial position is attributable to conservative management, which over the years has focused on maintaining a strong balance sheet. During the Q3 call, management reiterated its focus on the balance sheet pointing out this would be one of the major factors in determining the FY 15 capex program. Besides a solid financial profile, XEC's asset quality and strong operational momentum are both unparalleled. In its core Permian play (~55% of FY 14E Permian capex budget), XEC has successfully drilled longer laterals with upsized fracs providing solid upside to well returns. In a recent update, XEC noted that its traditional Wolfcamp well (i.e. Culberson County, Wolfcamp D well) with a 10K foot lateral would provide an impressive 89% before tax return at a price deck \$60/3.50. The returns on a normal 5K foot lateral are also highly competitive at 45% before tax (@\$60/3.50) clearly explaining XEC's investment opportunities. Wells results in its other core Permian zone –the 2nd and 3rd Bone Spring – continue to yield solid results with 30-day average IPs rates (New Mexico wells drilled in FY 14) improving 47% YoY. 2014 also saw XEC's renewed interest in Cana where returns improved on applying upsized fracs; the new frac designs allowed XEC to expand its addressable Cana acreage. Cana opportunities were widened further with possible Meramec prospects – where the company has drilled seven wells with the encouraging results from inception – 30-day IP rate was 9.4 Mmcf/d. Driven by the positive developments in Mid-Continent (24% of FY 14 Capex), XEC plans to increase capex in this play for FY 15. The quality Permian and Cana assets has allowed XEC to build a strong operating momentum; the company has raised production guidance from 13% growth at the start of year to 25% YoY now, and all this is happened with capex of \$2 billion, which implies modest cash burn of ~\$350 million (majority funded by asset sales, net of acquisitions). Moving ahead, the positive momentum will play a crucial role in limiting cash burn given the bleak commodity outlook; we see the company moving down towards a run-rate capex of \$1.5 billion while maintaining 10-12% annual production growth. Despite a largely unhedged profile, the company still be able to limit cash burn through FY 16 to under \$700 million, and we expect net leverage to be less than 1.5x at FYE 16.