

December 15, 2011

Hyperion Exploration Corp.¹ (HYX-V)

BUY

Last: \$0.73

Target: \$1.30

WHAT'S CHANGED

	NEW	OLD
Rating	NC	BUY
Target	NC	\$1.30
Production 2011E (boe/d) 6:1	NC	975
Production 2012E (boe/d) 6:1	NC	1,700
CFPS 2011E (f.d.d.)	NC	\$0.17
CFPS 2012E (f.d.d.)	NC	\$0.37

SHARE DATA

Shares o/s (mm, basic/f.d.)	54.2/71.4
52-week high/low	\$1.90/\$0.47
Market capitalization (mm)	\$40
Enterprise value (mm)	\$41
Net debt (mm) – Q3/11A	\$0.6
Dividend yield	Nil
Projected return	78%

FINANCIAL DATA

	2010A	2011E	2012E
Oil & NGLs (mb/d)	0.0	0.5	1.2
Natural Gas (mmcf/d)	0.4	2.7	2.9
Total (mboe/d) 6:1	0.1	1.0	1.7
Equivalent growth	nm	768%	74%
WTI (US\$/b)	79.51	91.50	85.00
HHUB (US\$/mmbtu)	4.38	4.15	4.50
FX rate (USD/CAD)	0.97	1.02	1.00
EPS (f.d.)	(\$0.22)	(\$0.07)	\$0.08
CFPS (f.d.d.)	(\$0.04)	\$0.17	\$0.37
Net Debt (mm)	(\$5.1)	\$12.7	\$21.1
Debt/CF	nm	1.5x	1.0x
P/CF		4.4x	1.9x
P/CF (d'adj'd)		6.3x	2.9x

Fiscal year ending December 31

HYX achieves its exit rate guidance in early December

Q4/11 operational update

Hyperion (HYX) announced a Q4 operational update this morning, highlighted by average production in the first two weeks of December exceeding management's exit rate guidance of 1,500 boe/d. That represents growth of 43% over Q3/11 and 172% over the 2010 exit rate, so the positive Cardium drilling results are translating into strong operational momentum and growth for the company. Another key item to note is that HYX's current oil weighting has increased to 69% from 42% in Q1/11, a critical shifting of the production base given the continuing (and growing) disparity between oil prices and gas prices. HYX recently tied-in 2 (2.0 net) Cardium oil wells in the Pembina region and plans to release IP30 data on these wells in January once the production is optimized. As a reminder the targeted 30-day type curve for the area is 275 boe/d so results on those wells could provide a positive catalyst to start 2012. In addition, drilling of the next Cardium well (50% WI) is planned for the Pembina region with a well expected to spud prior to year-end. HYX also remains in good shape financially with current net debt of less than \$10 million compared to an \$18 million bank line (which could be increased in the new year based on the strong recent drilling results). It is also important to note that HYX's exit production guidance has been achieved by spending less capital, as only 5 (4.6 net) wells of the 6 (5.2 net) wells planned for H2/11 have been drilled which speaks to the quality of the results and also contributes to the lower than expected net debt at year-end.

No changes to our estimates

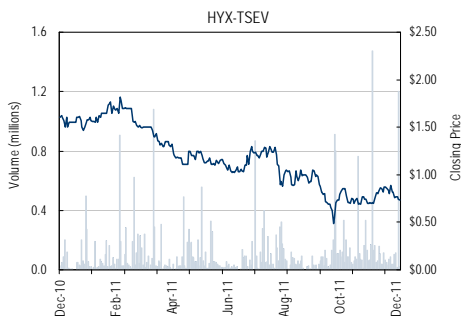
There are no changes to our estimates as production levels are ramping up as expected in Q4/11, with the added bonus of potentially lower net debt levels.

Attractive relative valuation

HYX is trading at 1.9x (2.9x debt adjusted) our 2012 estimate compared to the small cap peer group average of 3.4x (4.1x debt adjusted).

BUY Recommendation, \$1.30 target price

Overall we believe this was another good update from HYX. The company has consistently delivered upon its guidance throughout 2011, and that now includes a strong ramp-up in production in Q4/11 that should provide an increased cash flow base heading towards 2012. HYX's Cardium drilling results have exceeded type curve expectations which we believe has led to the strong year-end growth, and the company continues to have positive operational momentum as we move towards year-end and into 2012.





Q4/11 OPERATIONAL UPDATE

Positive Cardium drilling results translate into strong operational momentum

Hyperion (HYX) announced a Q4 operational update this morning, highlighted by average production in the first two weeks of December exceeding management's exit rate guidance of 1,500 boe/d. That represents growth of 43% over Q3/11 and 172% over the 2010 exit rate, so the positive Cardium drilling results are translating into strong operational momentum and growth for the company. Another key item to note is that HYX's current oil weighting has increased to 69% from 42% in Q1/11, a critical shifting of the production base given the continuing (and growing) disparity between oil prices and gas prices.

Additional Cardium results could provide early 2012 catalyst

HYX recently tied-in 2 (2.0 net) Cardium oil wells in the Pembina region. The company plans to release IP30 data on these wells in January once the production is optimized, and as a reminder the targeted 30-day type curve for the area is 275 boe/d so results on those wells could provide a positive catalyst to start 2012. In addition, drilling of the next Cardium well (50% WI) is planned for the Pembina region with a well expected to spud prior to year-end so the operational catalysts could continue in Q1/12.

HYX remains in good shape financially

HYX also remains in good shape financially with current net debt of less than \$10 million compared to an \$18 million bank line (which could be increased in the new year based on the strong recent drilling results). It is also important to note that HYX's exit production guidance has been achieved by spending less capital than originally budgeted, as only 5 (4.6 net) wells of the 6 (5.2 net) wells planned for H2/11 have been drilled which speaks to the quality of the results and also contributes to the lower than expected net debt at year-end.

NO CHANGES TO OUR ESTIMATES

No changes to our estimates

There are no changes to our estimates as HYX's Q4/11 operational update was generally in line with our expectations (with one potential exception being net debt which could be below our forecasts). For 2011 we continue to forecast average production of 975 boe/d and this results in forecasted CFPS (f.d.d.) of \$0.17 and year-end net debt of \$12.7 million or 1.5x cash flow. For 2012, we continue to forecast average production of 1,700 boe/d and this results in forecast CFPS (f.d.d.) of \$0.37 and year-end net debt of \$21.8 million or 1.0x cash flow.

SEGMENTED TARGET VALUATION APPROACH

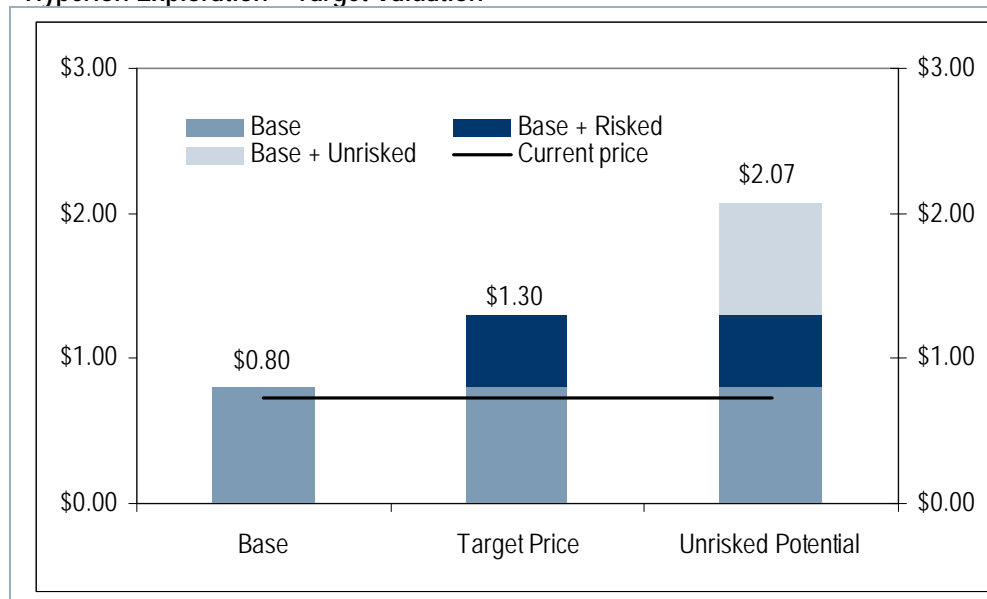
We continue to use a segmented valuation approach to derive our target price to encompass HYX's base cash flow and its Cardium oil resource opportunity. We utilize a conservative base cash flow component plus risked upside potential from the company's Cardium exposure.

The base cash flow component is unchanged at \$0.80/share and is based on a 3.1x debt adjusted cash flow multiple valuation. This is below the small cap group average (excluding resource valuations) of 4.3x given the company's earlier stages of operations, but we could see HYX meriting an improved valuation over time as development progresses on its resource-focused opportunity base.

We then estimate the company's unrisks Cardium potential to be \$1.27/share, and apply an unchanged 40% risk factor to drive an incremental \$0.50/share in value. Together this drives an unchanged \$1.30 target price, and on a combined basis this implies a 4.3x debt adjusted target multiple which is conservative compared to the peer group average of 5.6x.

One of the key highlights for HYX remains its attractive valuation relative to the peer group, particularly given its Cardium light oil focus. HYX is trading at 1.9x (2.9x debt adjusted) our 2012 estimate compared to the small cap peer group average of 3.4x (4.1x debt adjusted), a sizeable discount that we believe creates a good buying opportunity at current levels.

Hyperion Exploration – Target Valuation



Source: Company reports, GMP estimates

RECOMMENDATION

Overall we believe this was another good update from HYX. The company has consistently delivered upon its guidance throughout 2011, and that now includes a strong ramp-up in production in Q4/11 that should provide an increased cash flow base heading towards 2012. HYX's Cardium drilling results have exceeded type curve expectations which we believe has led to the strong year-end growth, and the company continues to have positive operational momentum as we move towards year-end and into 2012. **We reiterate our BUY recommendation and \$1.30 target price, which indicates potential upside of 78% from current levels.**



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⁶ multiple-voting

⁷ The analyst who prepared this report has viewed the material operations of this issuer.

⁸ The analyst who prepared this research report owns this issuer's securities.

⁹ limited voting

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BUY. These stocks will have 15% or greater (small cap) or 10% or greater (large cap) total return potential.

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REDUCE. Companies ranked Reduce have a negative potential total return.

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