MEG Energy

MEG Energy reports fourth quarter and full-year 2016 results

MEG Energy positioned for growth through record-low per barrel annual operating costs, record-high annual production, and a strengthened balance sheet

All financial figures in Cdn$ unless otherwise noted

CALGARY, ALBERTA (February 9, 2017) – MEG Energy Corp. (TSX:MEG) today reported fourth quarter and full-year 2016 operating and financial results. Highlights include:

- Quarterly production volumes of 81,780 barrels per day (bpd) contributing to record annual production of 81,245 bpd;

- Record-low per barrel net operating costs for the full year of 2016 and record-low per barrel non-energy operating costs for the full year and the quarter;

- 2016 capital spending of $137 million, lower than previous guidance of $140 million announced in October 2016 and the original budget of $328 million, while still maintaining production guidance for the full year;

- Year-end cash and cash equivalents of $156 million.

- MEG is positioned to expand its eMSAGP technology, the first step in a series of high-return projects to boost production while lowering the company's cash costs and environmental footprint.

- Subsequent to the fourth quarter, MEG Energy announced the closing of a comprehensive refinancing which has contributed to a strengthened balance sheet, and will enable an increase in production and a reduction in costs per barrel.

MEG's fourth quarter 2016 production was 81,780 bpd, compared to 83,514 bpd for the fourth quarter of 2015. Full-year 2016 production was a record 81,245 bpd, meeting targets and reflecting the ongoing efficiency gains associated with MEG's patented eMSAGP reservoir technology.

MEG established record-low per barrel net operating costs and non-energy operating costs for the full year of 2016. Net operating costs were recorded at $8.24 per barrel in the fourth quarter of 2016 with net annual operating costs of $7.99 per barrel. At $4.99 per barrel, fourth quarter non-energy operating costs supported record-low annual non-energy operating costs of $5.62 per barrel, which were well below the bottom end of the company's 2016 revised guidance and 14% lower than in 2015. Lower operating costs on both a quarterly and annual basis are primarily due to efficiency gains and a continued focus on cost management.

On January 27, 2017, MEG announced the closing of its comprehensive refinancing plan, which was first announced on January 11, 2017, and comprised of four financing transactions including the raising of $518 million in equity. The transactions have contributed to a strengthened balance sheet, and will enable an increase in production and a reduction in costs per barrel.

"The last few months have been extremely important for MEG. We have extended the runway of our debt under favorable terms, retaining the covenant lite structure. The success of our equity raise opens the door for us to refocus on growth with a fully-funded capital program driven by our technological advances and capital efficiency gains," said Bill McCaffrey, President and Chief Executive Officer. "With the expansion of our eMSAGP technology to our Phase 2B wells, we expect to exit 2017 at 86,000 to 89,000 bpd, with further production increases through 2018 into 2019."

MEG's eMSAGP expansion and upcoming Phase 2B brownfield expansion will be the first of a series of high-return projects expected to increase production, decrease cash costs and further the sustainability of the company's balance sheet. "Over the next several years, we plan to grow our production to 210,000 bpd through the addition of more of these high return, short cycle 10,000 to 20,000 bpd brownfield projects," McCaffrey said.

MEG recorded adjusted funds flow of $40.0 million for the fourth quarter of 2016 compared to adjusted funds flow of $(44.1) million for the same period in 2015. Adjusted funds flow is directly correlated to the increase in U.S. crude oil benchmark pricing during the fourth quarter of 2016, which resulted in higher blend sales revenue. Adjusted funds flow was $(61.6) million for 2016 compared to adjusted funds flow of $49.5 million for 2015.

The company recorded a fourth quarter 2016 operating loss of $72 million compared to an operating loss of $140 million for the same period in 2015. The difference in operating earnings reflects the same factors impacting adjusted funds flow.

Capital Investment and Financial Liquidity

Total cash capital investment during the fourth quarter of 2016 was $63.1 million, as compared to $54.5 million for the same period in 2015. Total cash capital investment during 2016 totalled $137.2 million as compared to $257.2 million for 2015. Capital investment in 2016 was primarily directed towards sustaining capital activities.

At the end of the fourth quarter, MEG had $156 million of cash and cash equivalents on hand. This cash on hand, together with net proceeds from MEG's $518 million equity issuance completed subsequent to year end and 2017 funds flow, is expected to fund MEG's previously announced $590 million capital budget in 2017. MEG has entered into a series of hedges designed to protect its capital program against downward movements in crude oil prices. MEG's five-year covenant-lite US$1.4 billion credit facility remains undrawn.

"We believe that the production growth expected from the first two of a series of brownfield expansions will drive our debt to EBITDA metric into the 3x to 4x range, assuming a similar operating and price environment to what we are seeing currently," McCaffrey said. "In addition, the transactions give us the added flexibility to pursue additional deleveraging alternatives which would improve our debt metrics further."

Operational and Financial Highlights

The following table summarizes selected operational and financial information of the Corporation for the periods noted. All dollar amounts are stated in Canadian dollars ($ or C$) unless otherwise noted.

	Year ended December 31	2016	2015

($ millions, except as indicated)	2016	2015	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Bitumen production - bbls/d	**81,245**	80,025	**81,780**	83,404	83,127	76,640	83,514	82,768	71,376	82,398
Bitumen realization - $/bbl	**27.79**	30.63	**36.17**	30.98	30.93	11.43	23.17	31.03	44.54	25.82
Net operating costs - $/bbl[1]	**7.99**	9.39	**8.24**	7.76	7.43	8.53	8.52	9.10	9.43	10.49
Non-energy operating costs - $/bbl	**5.62**	6.54	**4.99**	5.32	5.81	6.45	5.66	5.98	7.01	7.57
Cash operating netback - $/bbl[2]	**13.13**	15.72	**21.73**	16.74	16.09	(3.71)	9.05	16.41	29.64	9.83
Adjusted funds flow[3]	**(62)**	49	**40**	23	7	(131)	(44)	24	99	(30)
Per share, diluted[3]	**(0.27)**	0.22	**0.18**	0.10	0.03	(0.58)	(0.20)	0.11	0.44	(0.13)
Operating loss[3]	**(455)**	(374)	**(72)**	(88)	(98)	(197)	(140)	(87)	(23)	(124)
Per share, diluted[3]	**(2.01)**	(1.67)	**(0.32)**	(0.39)	(0.43)	(0.88)	(0.62)	(0.39)	(0.10)	(0.56)
Revenue[4]	**1,866**	1,926	**566**	497	513	290	445	460	555	467
Net earnings (loss)[5]	**(429)**	(1,170)	**(305)**	(109)	(146)	131	(297)	(428)	63	(508)
Per share, basic	**(1.90)**	(5.21)	**(1.34)**	(0.48)	(0.65)	0.58	(1.32)	(1.90)	0.28	(2.27)
Per share, diluted	**(1.90)**	(5.21)	**(1.34)**	(0.48)	(0.65)	0.58	(1.32)	(1.90)	0.28	(2.27)
Total cash capital investment[6]	**137**	257	**63**	19	20	35	54	32	90	80
Cash and cash equivalents	**156**	408	**156**	103	153	125	408	351	438	471
Long-term debt[7]	**5,053**	5,190	**5,053**	4,910	4,871	4,859	5,190	5,024	4,678	4,759

(1) Net operating costs include energy and non-energy operating costs, reduced by power revenue.

(2) Cash operating netback is calculated by deducting the related diluent expense, transportation, operating expenses, royalties and realized commodity risk management gains (losses) from proprietary blend revenues and power revenues, on a per barrel of bitumen sales volume basis.

(3) Adjusted funds flow, Operating earnings (loss) and the related per share amounts do not have standardized meanings prescribed by IFRS and therefore may not be comparable to similar measures used by other companies. For the three months and years ended December 31, 2016 and December 31, 2015, the non-GAAP measure of adjusted funds flow is reconciled to net cash provided by (used in) operating activities and the non-GAAP measure of operating loss is reconciled to net loss in accordance with IFRS under the heading "NON-GAAP MEASURES" and discussed further in the "ADVISORY" section.

(4) The total of Petroleum revenue, net of royalties and Other revenue as presented on the Interim Consolidated Statement of Earnings (Loss) and Comprehensive Income (Loss).

(5) Includes a net unrealized foreign exchange loss of $119.6 million and a net unrealized foreign exchange gain of $148.2 million on the Corporation's U.S. dollar denominated debt and U.S. dollar denominated cash and cash equivalents for the three months and year ended December 31, 2016, respectively. The net losses for the three months and year ended December 31, 2015 include net unrealized foreign exchange losses of $159.0 million and $785.3 million, respectively.

(6) Defined as total capital investment excluding dispositions, capitalized interest, capitalized cash-settled stock-based compensation and non-cash items.

(7) On December 8, 2016, Fitch Ratings ("Fitch") assigned the Corporation a first-time Long-Term Issuer Default Rating of B, and assigned a rating of BB to the Corporation's covenant-lite revolving credit facility and term loan and a rating of B to the Corporation's Senior Unsecured Notes. On January 12, 2017, Fitch assigned a BB rating to the Corporation's new second lien secured notes (see the "Capital Resources" section of the MD&A contained in MEG's Fourth Quarter 2016 Report to Shareholders). Fitch's rating outlook is negative. On January 12, 2017, Standard & Poor's Ratings Services ("S&P") assigned a BB+ rating to the Corporation's new second lien secured notes. On January 12, 2017, Moody's Investors Service ("Moody's") upgraded the Corporation's Corporate Family Rating to B3 from Caa2, the Probability of Default Rating to B3-PD from Caa2-PD and the Corporation's Senior Unsecured Notes rating to Caa2 from Caa3. Moody's Speculative Grade Liquidity Rating was raised to SGL-1 from SGL-2. Moody's also assigned a rating of Ba3 to the Corporation's covenant-lite revolving credit facility and refinanced term loan and a rating of Caa1 to the new second lien secured notes. Moody's rating outlook was changed to stable from negative.

ADVISORY

Basis of Presentation

MEG prepares its financial statements in accordance with International Financial Reporting Standards ("IFRS") and presents financial results in Canadian dollars ($ or C$), which is the corporation's functional currency.

Non-GAAP Measures

Certain financial measures in this document including: net marketing activity, funds flow, adjusted funds flow, operating loss and operating cash flow are non-GAAP measures. These terms are not defined by IFRS and, therefore, may not be comparable to similar measures provided by other companies. These non-GAAP financial measures should not be considered in isolation or as an alternative for measures of performance prepared in accordance with IFRS.

Funds Flow and Adjusted Funds Flow

Prior to the fourth quarter of 2016, the Corporation reported cash flow from (used in) operations as a non-GAAP measure. Beginning in the fourth quarter of 2016, the Corporation changed the label of this non-GAAP measure to “funds flow” and “adjusted funds flow”. The Corporation believes that this labelling and presentation better distinguishes these measures from the IFRS measurement “net cash provided by (used in) operating activities”.

Funds flow and adjusted funds flow, previously referred to as cash flow from (used in) operations, are non-GAAP measures utilized by the Corporation to analyze operating performance and liquidity. Funds flow excludes the net change in non-cash operating working capital while the IFRS measurement “net cash provided by (used in) operating activities” includes these items. Adjusted funds flow excludes the net change in non-cash operating working capital, net change in other liabilities, contract cancellation expense and decommissioning expenditures while the IFRS measurement "net cash provided by (used in) operating activities" includes these items. Funds flow and adjusted funds flow are not intended to represent net cash provided by (used in) operating activities calculated in accordance with IFRS. Funds flow and adjusted funds flow are reconciled to net cash provided by (used in) operating activities in the table below.

	Three months ended December 31		**Year ended December 31**	
($000)	**2016**	**2015**	**2016**	**2015**
Net cash provided by (used in) operating activities	**$ 82,621**	$ 12,515	**$ (94,074)**	$ 112,158
Net change in non-cash operating working capital items	**(43,636)**	(76,388)	**25,061**	(77,991)
Funds flow	**38,985**	(63,873)	**(69,013)**	34,167
Adjustments:				
Net change in other liabilities	**787**	541	**6,116**	541
Contract cancellation expense	**-**	18,759	**-**	12,879
Decommissioning expenditures	**195**	443	**1,290**	1,873
Adjusted funds flow	**$ 39,967**	$ (44,130)	**$ (61,607)**	$ 49,460

Operating Loss

Operating loss is a non-GAAP measure which the Corporation uses as a performance measure to provide comparability of financial performance between periods by excluding non-operating items. Operating loss is defined as net loss as reported, excluding unrealized foreign exchange gains and losses, unrealized gains and losses on derivative financial instruments, impairment charges, gains and losses on disposition of assets, unrealized gains and losses on risk management, debt extinguishment expense, contract cancellation expense, onerous contracts, insurance proceeds and the respective deferred tax impact on these adjustments. Operating loss is reconciled to "Net loss", the nearest IFRS measure, in the table below.

	Three months ended December 31		Year ended December 31	
($000)	**2016**	**2015**	**2016**	**2015**
Net loss	**$ (304,758)**	$ (297,275)	**(428,726)**	$(1,169,671)
Adjustments:				
Unrealized net loss (gain) on foreign exchange[(1)]	**119,610**	159,009	**(148,153)**	785,310
Unrealized loss (gain) on derivative financial instruments[(2)]	**(7,146)**	(15,890)	**(12,508)**	(13,289)
Impairment charge	**80,072**	-	**80,072**	-
Gain on disposition of assets[(3)]	**-**	(68,192)	**-**	(68,192)
Unrealized loss on risk management[(4)]	**42,049**	-	**30,313**	-
Debt extinguishment expense[(5)]	**28,845**	-	**28,845**	-
Contract cancellation expense	**-**	18,759	**-**	12,879
Onerous contracts[(6)]	**16,383**	58,719	**47,866**	58,719
Insurance proceeds[(7)]	**(4,391)**	-	**(4,391)**	-
Deferred tax expense (recovery) relating to these adjustments	**(42,653)**	4,636	**(48,416)**	19,870
Operating loss	**$ (71,989)**	$ (140,234)	**(455,098)**	$ (374,374)

(1) Unrealized net foreign exchange gains and losses result from the translation of U.S. dollar denominated long-term debt and cash and cash equivalents using period-end exchange rates.

(2) Unrealized gains and losses on derivative financial instruments result from the interest rate floor on the Corporation's long-term debt and interest rate swaps entered into to effectively fix a portion of its variable rate long-term debt.

(3) A gain related to the sale of a non-core undeveloped oil sands asset in the fourth quarter of 2015.

(4) Unrealized gains or losses on commodity risk management contracts represent the change in the mark-to-market position of the unsettled commodity risk management contracts during the period.

(5) At December 31, 2016, the Corporation recognized $28.8 million of debt extinguishment expense associated with the planned redemption of the 6.5% Senior Unsecured Notes on March 15, 2017, under the comprehensive refinancing plan completed on January 27, 2017.

(6) During 2016, onerous contracts expenses were recognized primarily due to changes in estimated future cash flows related to the onerous office lease provision.

(7) Includes insurance proceeds related to the small fire that occurred during the first quarter of 2016, which caused damage to the Sulphur Recovery Unit at the Corporation's Christina Lake facility.

Forward-Looking Information

This document may contain forward-looking information including but not limited to: expectations of future production, revenues, expenses, cash flow, operating costs, steam-oil ratios, pricing differentials, reliability, profitability and capital investments; estimates of reserves and resources; the anticipated reductions in operating costs as a result of optimization and scalability of certain operations; and the anticipated sources of funding for operations and capital investments. Such forward-looking information is based on management's expectations and assumptions regarding future growth, results of operations, production, future capital and other expenditures, plans for and results of drilling activity, environmental matters, business prospects and opportunities.

By its nature, such forward-looking information involves significant known and unknown risks and uncertainties, which could cause actual results to differ materially from those anticipated. These risks include, but are not limited to: risks associated with the oil and gas industry, for example, the securing of adequate supplies and access to markets and transportation infrastructure; the availability of capacity on the electricity transmission grid; the uncertainty of reserve and resource estimates; the uncertainty of estimates and projections relating to production, costs and revenues; health, safety and environmental risks; risks of legislative and regulatory changes to, amongst other things, tax, land use, royalty and environmental laws; assumptions regarding and the volatility of commodity prices, interest rates and foreign exchange rates, and, risks and uncertainties related to commodity price, interest rate and foreign exchange rate swap contracts and/or derivative financial instruments that MEG may enter into from time to time to manage its risk related to such prices and rates; risks and uncertainties associated with securing and maintaining the necessary regulatory approvals and financing to proceed with MEG's future phases and the expansion and/or operation of MEG's projects; risks and uncertainties related to the timing of completion, commissioning, and start-up, of MEG's future phases, expansions and projects; and the operational risks and delays in the development, exploration, production, and the capacities and performance associated with MEG's projects.

Although MEG believes that the assumptions used in such forward-looking information are reasonable, there can be no assurance that such assumptions will be correct. Accordingly, readers are cautioned that the actual results achieved may vary from the forward-looking information provided herein and that the variations may be material. Readers are also cautioned that the foregoing list of assumptions, risks and factors is not exhaustive.

Further information regarding the assumptions and risks inherent in the making of forward-looking statements can be found in MEG's most recently filed Annual Information Form ("AIF"), along with MEG's other public disclosure documents. Copies of the AIF and MEG's other public disclosure documents are available through the SEDAR website which is available at www.sedar.com.

The forward-looking information included in this document is expressly qualified in its entirety by the foregoing cautionary statements. Unless otherwise stated, the forward-looking information included in this document is made as of the date of this document and MEG assumes no obligation to update or revise any forward-looking information to reflect new events or circumstances, except as required by law.

A full version of MEG's Fourth Quarter 2016 Report to Shareholders, including unaudited financial statements, is available at www.megenergy.com/investors and at www.sedar.com.

A conference call will be held to review the financial results at 8:30 a.m. Mountain Time (10:30 a.m. Eastern Time) on Thursday, February 9, 2017. The U.S./Canada toll-free conference call number is 1 866-225-0198. The international/local conference call number is 416-340-2218.

MEG Energy Corp. is focused on sustainable in situ oil sands development and production in the southern Athabasca oil sands region of Alberta, Canada. MEG is actively developing enhanced oil recovery projects that utilize SAGD extraction methods. MEG's common shares are listed on the Toronto Stock Exchange under the symbol "MEG."

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