ESA ENERGY SEARCH ASSOCIATES

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# 3 THINGS YOU MAY NOT KNOW....

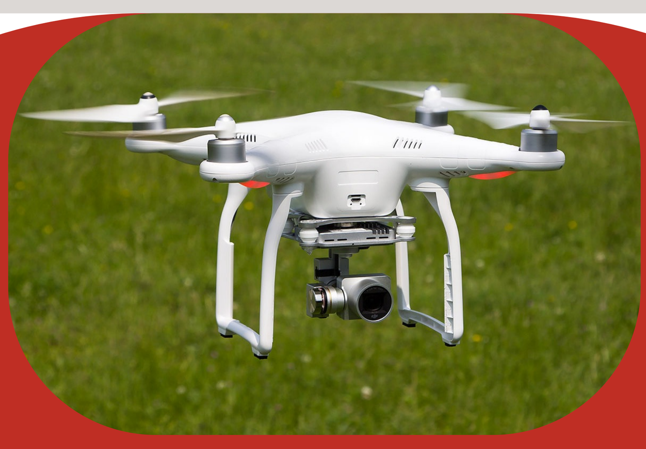
1. I played four years of Division I men's soccer at Vanderbilt.
2. I took my first ski lesson ever at a resort last year in the Italian Alps.
3. I am originally from Kansas City so will not entertain discussions on where to find the best BBQ.


**Brendan Matthews**
Managing Director at GRM Partners


Q&A

# Another New Age of an Old Industry

***E&P Capital Market Insights***



## Oilpatch Tech Futures!

**Did you know that drones are being developed to put out forest fires, replace cranes in construction, & identify Oilfield gas leaks (This article explains how one company is doing just that) ?!?**

**What might be next? Uploading measurements? Supporting remote VR observation capabilities?**

**If you have other interesting ideas to share, please reply to this email. We would love to hear your input.**

**With banks like BMO and others exiting the energy space, what effect will that have on the industry short / long term?**

The global economic timing uncertainty and geopolitical volatility that we experienced for the majority of last year allowed many to escape, but, make no mistake, capital access and availability are concerns keeps many up at night. The significant number of investors and capital providers looking to reduce (at a minimum) or exit (at the most extreme) the oil and gas sector continues to play out, and the expectation is that this impact will begin in earnest during the first half of 2021.

There are a number of social, political and fundamental reasons as to why energy has become a sector at siege, which will likely further divide an already widening gap amongst market winners and losers.

Expect investors and capital providers to respond with a flight to quality and preference for larger names in their portfolio. The effectiveness and security of the reserve-based loan instrument is quickly becoming obsolete, squeezing smaller operators into searching for alternatives sources of capital. Late last year, several operators expressed that 30% to 40% of their existing syndicate would exit if given the opportunity.

GRM Partners has been working with multiple sources of non-traditional capital to create a structured financing product that provides a readily available solution for operators assessing possible alternatives. This product is certainly competitive, and oftentimes favorable, to some of the other structured financing alternatives currently out in the market.

**Where will small startup operators get seed funding with Private Equity transitioning a lot of their fund dollars out of Oil & Gas? Will there be as many small startups in general?**

The business model for private equity sponsors has certainly been in transition but rest assured that there are pockets of capital available in this market. Despite the well-publicized exodus of capital dedicated to oil and gas, several traditional capital providers remain open for business with significant dry powder. However, these situations look drastically different than they have in years past. GRM Partners has spent considerable time with these differentiated, non-traditional sources of capital looking to deploy capital in this market. The most significant obstacle has been identifying management teams with the capabilities and mindset that reflect the current environment. These new investors are targeting a path to value through operational and cost efficiencies rather than through the drill bit.

The trend over the past few years from traditional capital providers has been larger capital commitments to a smaller number of management teams. Additionally, we have certainly seen these sponsors combine multiple management teams into one entity (i.e. SmashCo / JamCo companies). The market no longer supports where we were at the peak (an estimated 300 management teams), but that does not mean the opportunity for a new management team is non-existent.

**How will all the consolidations affect the industry short / long term?**

The consensus calls for consolidation have only increased as the industry evolves into the post-COVID world. However, the transactions themselves and rationale for pursuing them has dramatically shifted. The overarching sentiment is that consolidation is an absolute necessity to make the sector stronger.

These calls were answered during the second half of 2020 with more than $42 billion in M&A transactions. The predominant area of focus for these transactions is, unsurprisingly, the Permian, but there are the other key lessons learned from the investor response, market receptivity and performance of these transactions.

Size and scale are absolute necessities in order to establish, maintain relevance or differentiate oneself. The combined entity now creates a sustainable enterprise and paves the way for an increase in or maximization of operational synergies and efficiencies. Expect additional transactions to have a minimal to zero premium, merger-of-equal combinations with a cash flow neutral emphasis.

**Where will funds first be deployed when prices / market conditions improve?**

The simple answers here are "where you are able to make money" or "where you have the best rock". For a better part of the last decade, the focus for any kind of industry activity has started and ended in the Permian. The Permian will continue to generate its share of attention, but core areas in other producing regions will attract interest and capital as well.

A parallel conversation would identify where funds can be deployed at current commodity prices. Despite a recent rally on the front end of the curve for both oil and gas, the back end of each curve has remained consistent. The current focus for the Board of Directors as they define capital budgets and attempt to identify where the opportunities lie going forward averages approximately $50 / Bbl and $2.50 / MMBtu over the short-to-medium term.

A final conversation, though as much if not more vital, will test the discipline of operators and the message they have been preaching for a better part of the last two years. The incentive for growth is not there. The market has rewarded those companies who have focused on or looked to maintain capital discipline. Excess funds from an increase in commodity prices or improved market conditions would not be deployed through the drill bit, but rather concentrated toward continued debt reduction and returns to shareholders.

## New Product Spotlight:

## ESG Data Tool!!

Many of our professional Oil & Gas contacts have expressed interest in finding ESG data to compare to. We located an option for you.

Enverus has recently come out with a new product.

**CLICK HERE to learn more on their website**

**CLICK HERE to watch a 30 minute online presentation**

**Are conventional assets coming back into serious consideration? Why?**

The depth of the buyer universe for conventional and mature resource play assets reflects participation levels at the height of the market. In a year in which many transactions became negotiated processes by default due to interest from a limited number of parties, a recent marketing process for a diverse set of conventional assets received nearly fifty bids (I told you there were pockets of capital available out there!). These assets, quite simply, reflect how the playbook will change going forward.

Just as important of note, is that underlying valuation for these assets and where these transactions have recently cleared is essentially PDP number. The quality of the assets that are expected to come to market in 2021 combined with the clearing price for recent transactions is where there is an opportunity to seize and where we expect to see a lot of happy people three to five years from now.

**What do you think needs to happen in the market to get the energy industry back to a favorable spot for investors? For the public?**

The shale revolution represented a prosperous time for the industry, demonstrated the ingenuity of the people who dedicate their everyday lives and helped this country prosper, but it also led us to the state of the industry and where we all stand today. The industry is taking the time to reinvent itself, win back the trust of the investor community and attract capital, but it is a process that will take time. Fossil fuels are certainly not going away tomorrow, but the sustainability of the industry rests on how it positions itself as part of the solution going forward with the emerging technologies associated with energy transition.

The industry must also make more of a concerted effort to demonstrate how vital its existence is to the everyday things that the casual observer takes for granted.