

THE A&D MARKET FOR INDEPENDENTS

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by

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Tonight we'll look at:

- **A brief summary of my background in A&D**
- **A history of Five States Energy Company**
- **The current A&D market for independents**
- **What to look for in sales packages**

Gary Stone

- **Petr Engr, Texas Tech University, 1978**
- **Consulting, energy banking, technical software, independent producers**
- **19+ years at Five States Energy**
- **Registered Professional Engineer, Member of the Petroleum Engineering Academy at Texas Tech, Board member for Texas Alliance of Energy Producers, past President of Texas Energy Council**

Five States Energy Company

- **Founded late 1984 by Jim Gibbs, past President of AAPG**
- **Formed small partnerships of private investment capital to buy annuity properties**
- **Targets were hard-rock, non-op, slow decline in Texas, Mid-Continent, and Rockies**
- **Due to changing market conditions, sold gas properties and low-volume oil in 2006-7**

Five States Energy Capital

- **Broadened our funds to allow for more risk**
- **Project focused, \$10-\$40 MM up to \$100 MM**
- **Direct purchase or equity co-investment**
- **Midstream assets (pipelines, gas plant, workover rigs) – equity or debt**
- **Mezzanine capital for development – help producers develop early-to-mid-stage projects that don't support bank debt**

Five States Energy Capital

- **Staff of three engineers for analysis, one for operations**
- **Prefer to partner with local companies on operated properties**
- **Review 200+ potential projects per year, perhaps 40% get to “light analysis”, 10% to “in depth analysis”**

The Current A&D Market

- **Are you buying or selling?**
- **If you're buying, do you plan to flip or hold and develop for the long haul?**

The Current A&D Market

- Let's focus on the < \$200 million market
- No one is selling for profit
- Sales are strategic
 - › *Large companies selling non-ops or large concentrations with "issues"*
 - › *At risk companies selling to pay down debt*
 - › *Bankruptcies or bank-directed sales*
- PDP vs other reserve categories and acreage

Strategic (Non-Forced) Sales Examples

- **Exit regions to concentrate elsewhere**
- **Sell large property groups with plugging liabilities, generally thru large brokers**
- **Sell smaller operated or non-op packages, generally by auction or thru smaller brokers**

Forced Sales Examples

- Not (yet) in bankruptcy, but close
 - › *Large companies selling non-core assets to reduce debt*
 - › *Smaller companies delay as long as possible*
 - › *“Sellable” properties (PDP) needed for cash flow*

Forced Sales Examples

- **Bank-forced sales**
 - › *“Kick the can” strategy – banks, regulators, companies, and the election*
 - › *Transferred to work-out divisions*
 - › *Foreclosure*
- **Bankruptcy**
 - › *Advantage of clean title, bid format*
 - › *Trustees can sometimes be difficult*

What's Being Sold

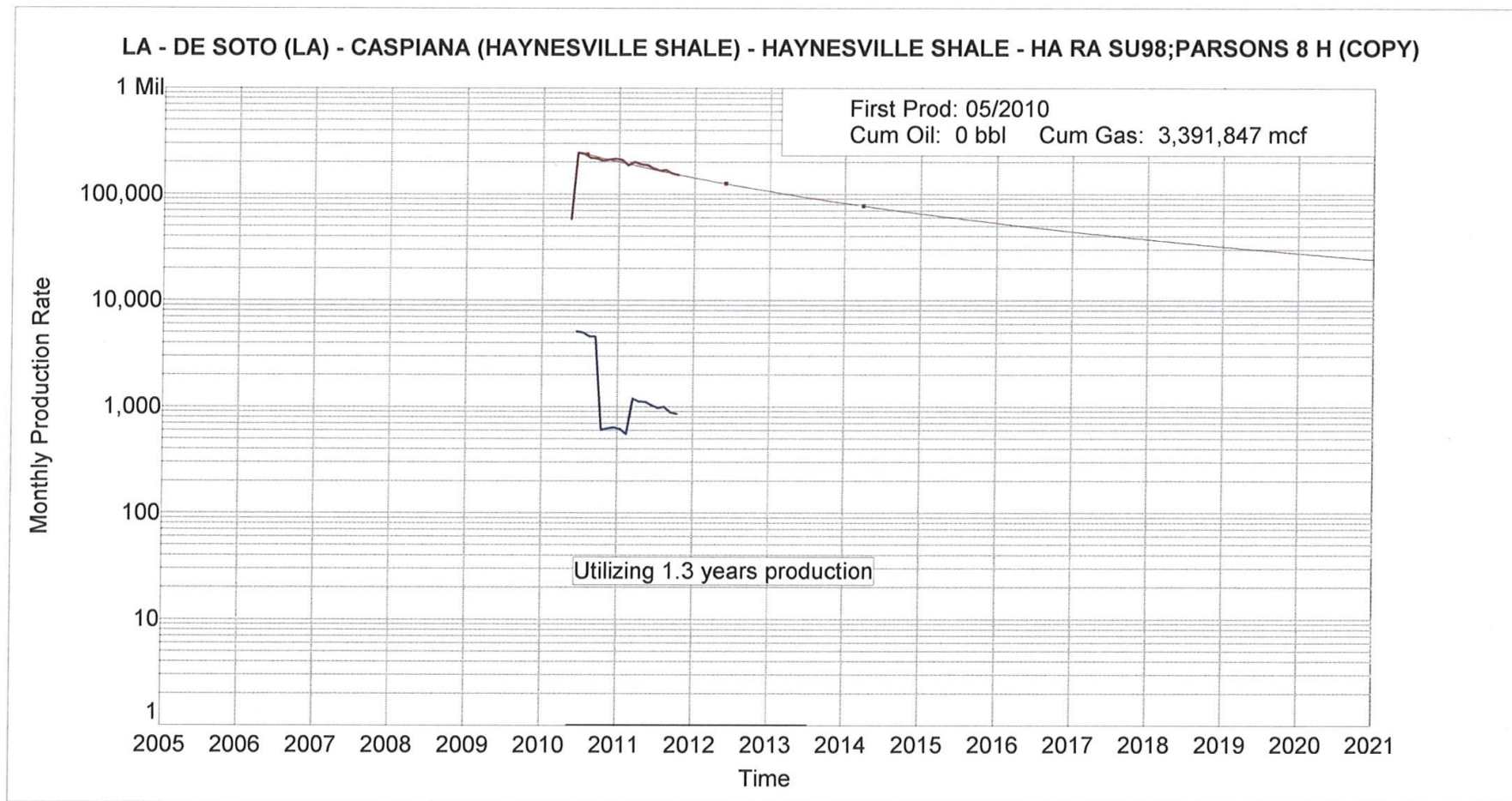
- PDP everywhere
- PDNP & PUDs
 - › *Value being given by buyers only for well-proven and economic reserves*
 - › *Risked by region*
- Acreage
 - › *Only in economic basins (Eagle Ford, Delaware, SCOOP/STACK, Utica)*

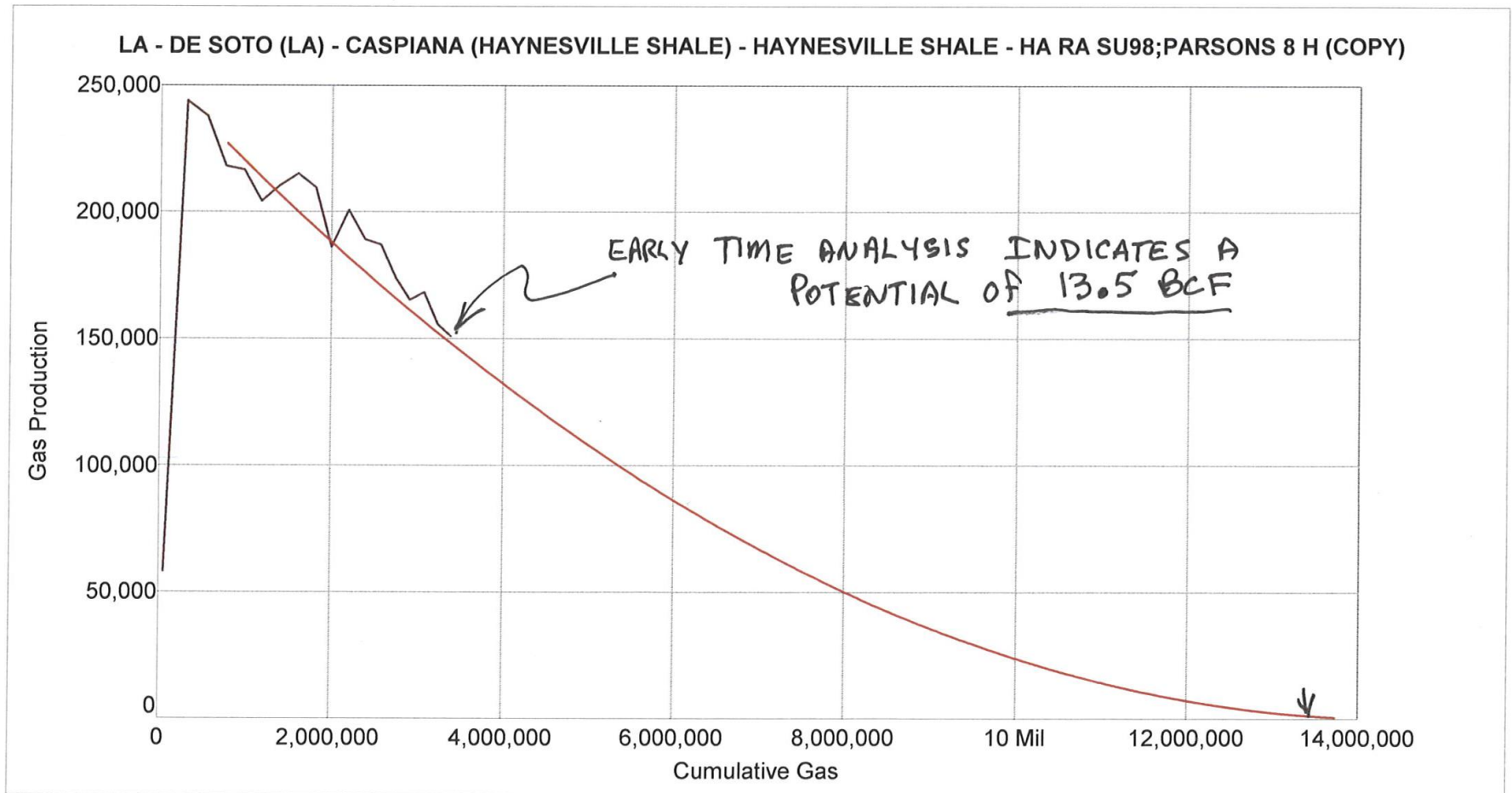
What to Look for in Sales Packages

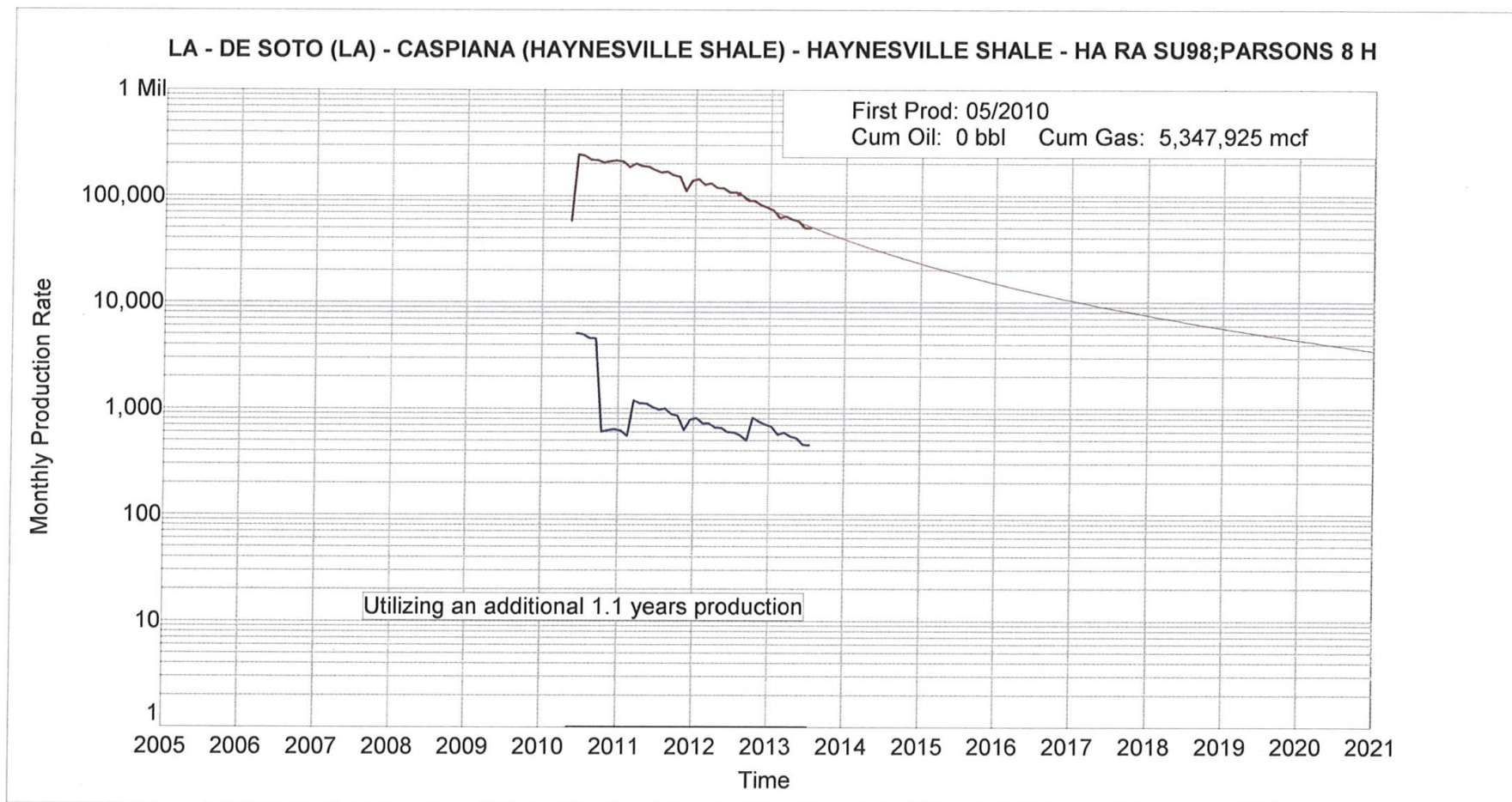
- **Brian's Laws**
 - › *Believe no one.*
 - › *Doubt everything.*
 - › *Demand proof.*
- **Be careful of the consultant, and remember that brokers are working for the seller.**
- **Never trust published type curves or data from public companies; investment banks may or may not be better (check hedging).**

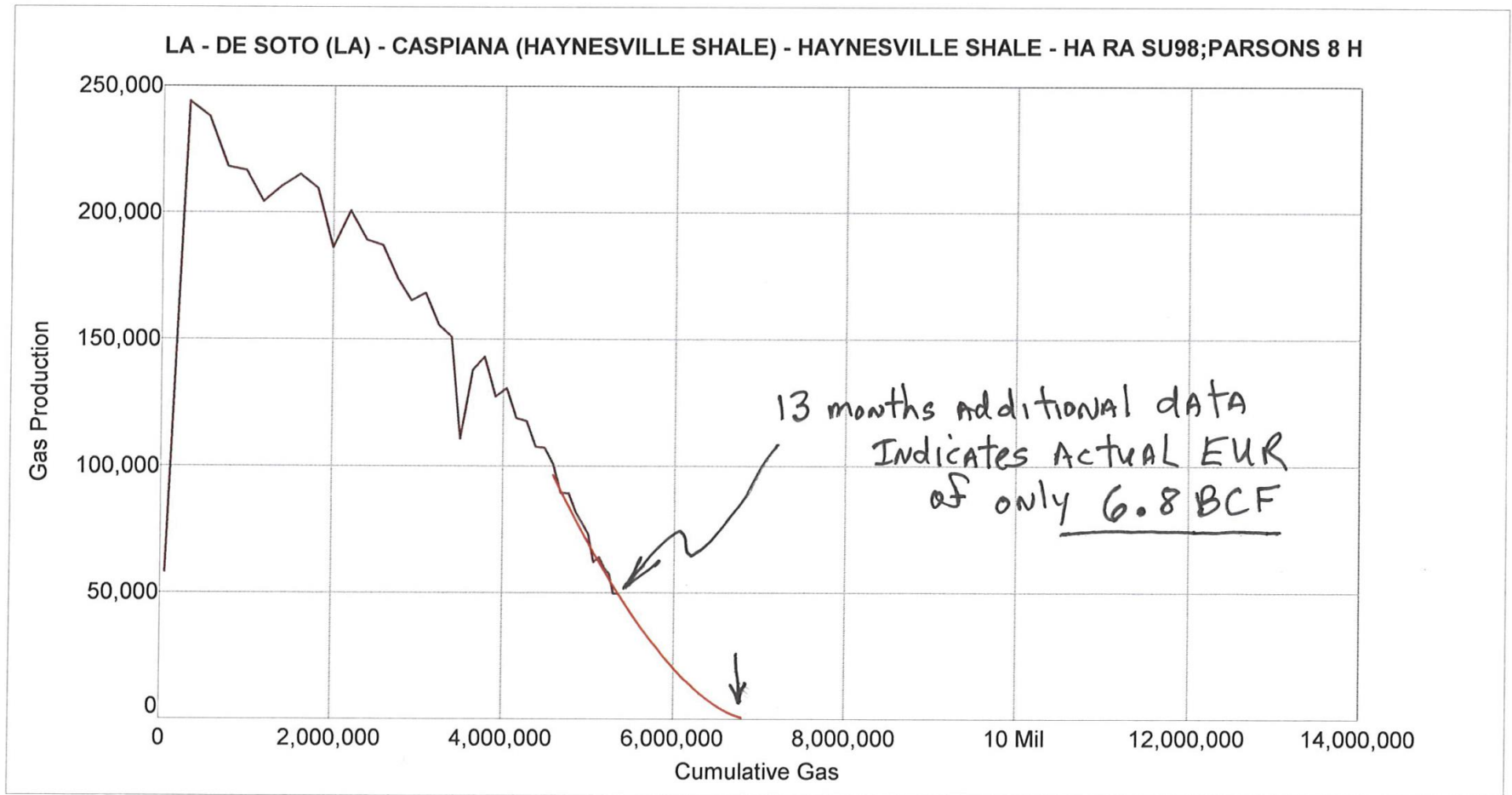
Sales Packages (*“They’re lying.”*)

- Reserves
 - › *PDP exaggerated in curves, response – use Rate v Cuml Prod plus Rate v Time*
 - › *PDNP, PUD non-existent or “thin”*
- Operating costs, prices, differentials
 - › *Costs scrubbed of recurring items*
 - › *Differentials minimized*
- Plugging and environmental concerns









THANK YOU !

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