

# Deals from PwC

Drive your growth. Secure your future.

## US Oil & Gas Deals insights

First quarter 2019

### Executive summary

Oil and gas (O&G) deal activity started the year on a low note, the most anemic volume and value numbers in over a decade. Although we don't expect volumes or value to climb substantially this year, we do anticipate further consolidation, particularly in large and megadeals. Barring a spike in commodity prices, we expect lower deal values in 2019 compared to 2018, when an unprecedented number of corporate restructurings led to the supercharging of some asset values.



**“After finishing 2018 riding high, O&G deal-making hit record lows during the first quarter of 2019 due to uncertainty around sustaining higher commodity prices, the sector’s continued laser focus on capital discipline and the generation of positive free cash flow. Megadeals are expected to return in the next three quarters, but whether volumes and values approach 2018 levels will require much more robust deal making over the next nine months than we saw in the first three.”— Joe Dunleavy, US EU&M Deals**

#### 1Q19 value by the numbers

**\$19.18 B**

#### 1Q19 volume by the numbers

**27**

**71%**

**Decrease in deal value  
versus 4Q18**

**40%**

**Decrease in deal volume  
versus 4Q18**

Source: IHS Markit

#### Trends and highlights

- Total deal volumes and values were the lowest in years as investors remained focused on capital discipline, generating returns, and operating within existing cash flows.
- The upstream space, which typically generates the highest level of deal volume and value, sunk to record lows. Although capital remained available, most of the attractive deals seem to have been made already. Investors found few projects priced attractively, and/or which could also generate immediate positive cash flows.
- The only segment that remained somewhat active was midstream, where financial investors drove activity.
- We expect megadeals to return in the quarters to come, but achieving 2018 megadeal values will be a significant challenge for deal makers.

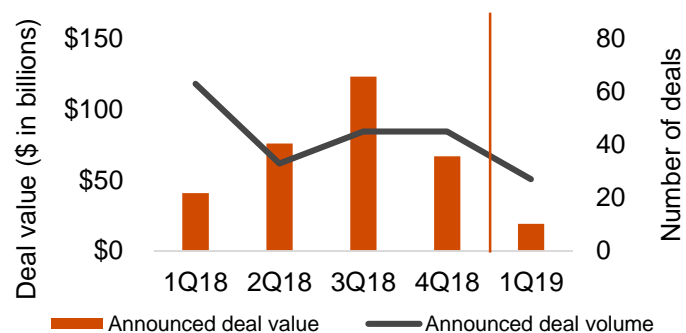
# Highlights of 2018 deal activity

## Deal value and volume overview

Deal volumes and values were significantly lower in the first quarter of 2019- lower than any quarter in the last decade. We do not expect a sustained recovery in the deal volumes in the next two quarters, and we expect total 2019 deal value to fall short of 2018.

Much of the deal activity in 2018 was driven by the wave of corporate restructurings in the midstream space. While we may see a few more restructuring transactions and a number of megadeal transactions in 2019, we don't expect to see the same level of activity as in 2018.

## Oil & Gas deal volume and value



Source: IHS Markit

## Megadeals (\$5B and over)

The softness in deal values and total deal volume was also evident in the mega deals space where no deal was announced with a value over \$5 billion. However, we expect megadeals to make a comeback in the near future. To an extent, the consolidation of smaller and mid-size players has already played out, but large companies in the US are now looking to refine their portfolios and boost investor returns.

# 0 mega deals



## 1Q19 Largest deals

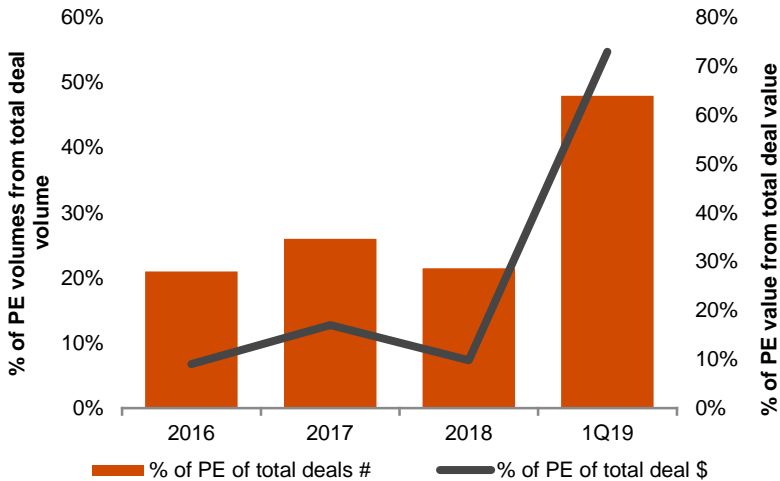
Announced date	Buyer	Seller	Deal value (\$b)	Sub-sector
01/31/2019	The Blackstone Group L.P.	Kelso & Company; Tallgrass KC, LLC; The Energy & Minerals Group	\$3,300.00	Midstream
01/07/2019	Elliott Management	QEP Resources Inc	\$2,070.00	Upstream
02/19/2019	The Blackstone Group L.P.	Targa Resources Corp.	\$1,600.00	Midstream
03/18/2019	Canada Pension Plan Investment Board	Williams Companies, Inc.	\$1,340.00	Midstream
03/11/2019	TPG Capital LP; Tailwater Capital, LLC	Goodnight Midstream, LLC	\$1,230.00	Midstream
03/22/2019	Tenaris S.A.	IPSCO Tubulars, Inc.; TMK, OAO	\$1,209.00	Midstream
03/14/2019	EQM Midstream Partners, LP	Morgan Stanley Infrastructure Partners	\$1,030.00	Midstream
01/08/2019	Stonepeak Infrastructure Partners LLC	Discovery Midstream Holdings II, LLC	\$1,000.00	Midstream

Source: IHS Markit

“After several quarters of sustained strength in megadeals, the first quarter of 2019 was soft. However, as the majority of the small and midsize dealmaking seems to be done, we expect megadeals will pick up, especially towards the year end, in keeping with its traditional seasonality.”  
 — Curt Karges, PwC Corporate Finance LLC

# 1Q19 deal themes

## Private equity deal volume and value



Source: IHS Markit

## Private equity highlights

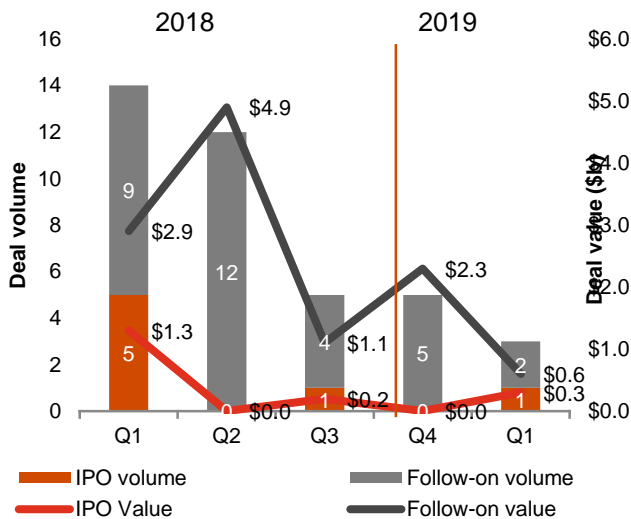
- Private equity (PE) firms were a major driver of activity in the first quarter of 2019, especially when it came to deals in the midstream space.
- Large PE and infrastructure funds looked to pick up cost advantageous acreage as public markets seem to have lost interest in the MLP space. This has resulted in favorable cost per mile pricing, attracting PE interest.
- Midstream activity in the quarter illustrates the spectrum of opportunities for financial investors weighing the risk and return tradeoff around commodity price, development, construction and other risks.

“Midstream was the only segment that recorded solid M&A activity in the first quarter, as financial investors engaged both in pure M&A as well as backing up management teams in the form of equity commitments. However, some observers fear that overbuilding of infrastructure in some basins may diminish the appeal of the midstream segment in the next few quarters.”

— Rob McCeney, US Energy & Infrastructure Deals, PwC

## Equity highlights

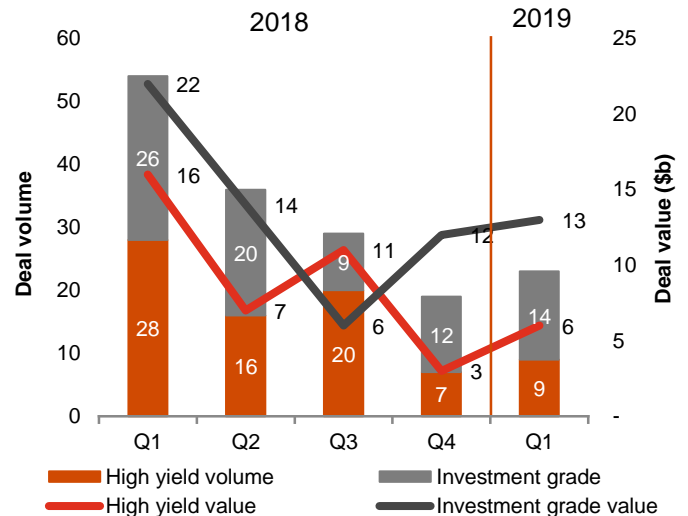
### IPO and follow-on offerings



Source: PwC U.S. IPO Watch and S&P LCD.

## Debt highlights

### High yield & investment grade

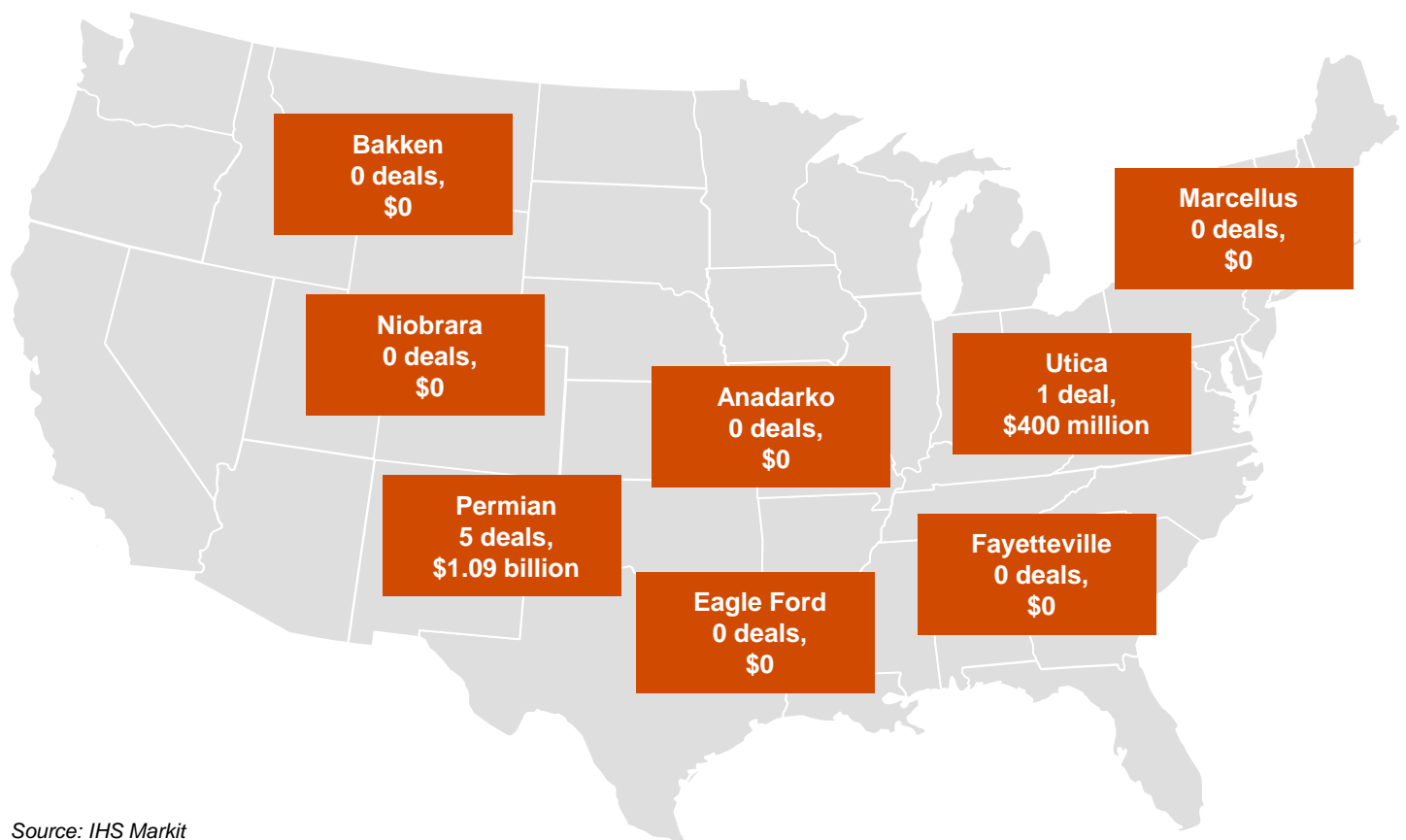


Source: PwC U.S. IPO Watch and S&P LCD.

## Highlights of 2018 deal activity, continued

After being a major driver of deal activity for several years, shale deals were mostly absent in the first quarter of 2019. The Permian was the only active basin with the exception of one Utica deal. The majority of the consolidation and new acreage acquisitions seem to have already materialized. Heavy investor scrutiny of a property's ability to generate immediate returns and positive cash flows as well as several quarters of strong acquisitions and divestitures left investors with few attractive options. Activity in the next quarter may remain subdued as companies look to integrate already acquired acreage. In the Permian, we might see a few large deals, but over the next few quarters, we believe the focus for most deal-makers going forward will be on combinations that promise greater drilling efficiency and leaner cost structures.

### 1Q19 upstream shale deals



Source: IHS Markit

“Consolidation in the Permian has already occurred, so the volume of deals going forward is likely to be lower than what we saw in the recent past. However, we are likely to see megadeals or large chunks of acreage being traded in what is now the most active basin in the US. In the meantime, in other basins, drilling efficiency and cost saving opportunities are likely to motivate deals.”

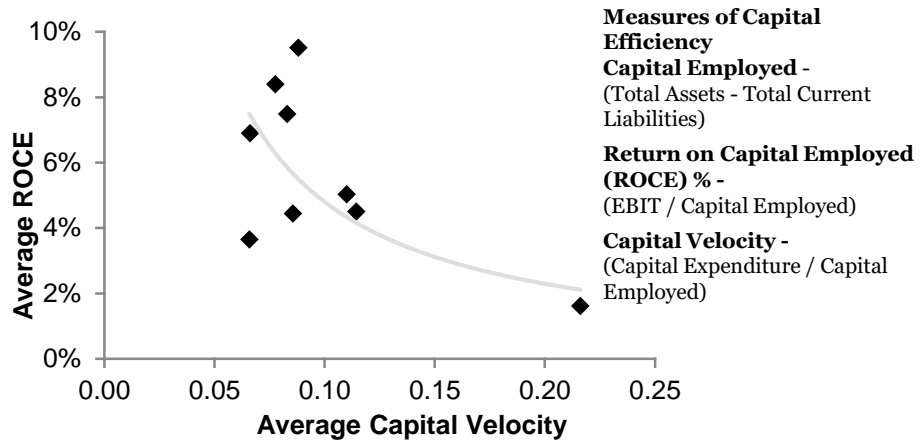
— Seenu Akunuri, US Oil & Gas Valuation Practice Leader, PwC

## Capital discipline and growing returns

Strong deal activity in 2018, announcements of new projects, and increased field productivity in the E&P space have bred a new level of competition among midstream third party players - all chasing the same customers to offer takeaway capacity.

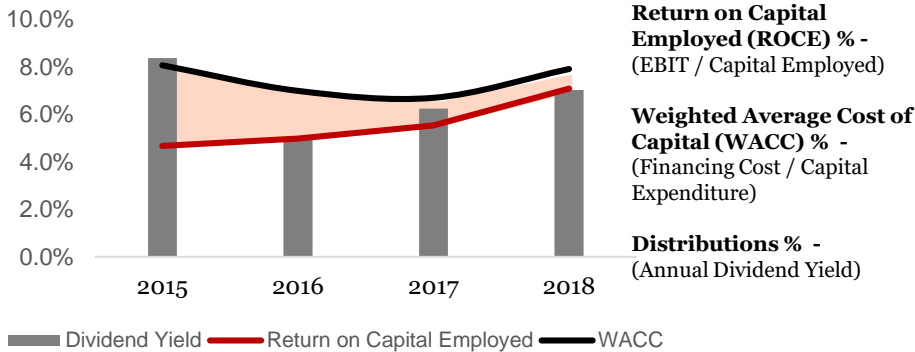
As capital deployment has accelerated, the market continues to be focused on pursuing profitable growth projects grounded in capital discipline.

Each competitor has opportunities to improve their return on capital employed in unique ways.



Source: Capital IQ, PwC analysis Sample size: top 10 U.S. midstream companies by enterprise value (EV)

## Sustainable distributions



Source: Capital IQ, PwC analysis Sample size: top 10 U.S. midstream companies by enterprise value (EV)

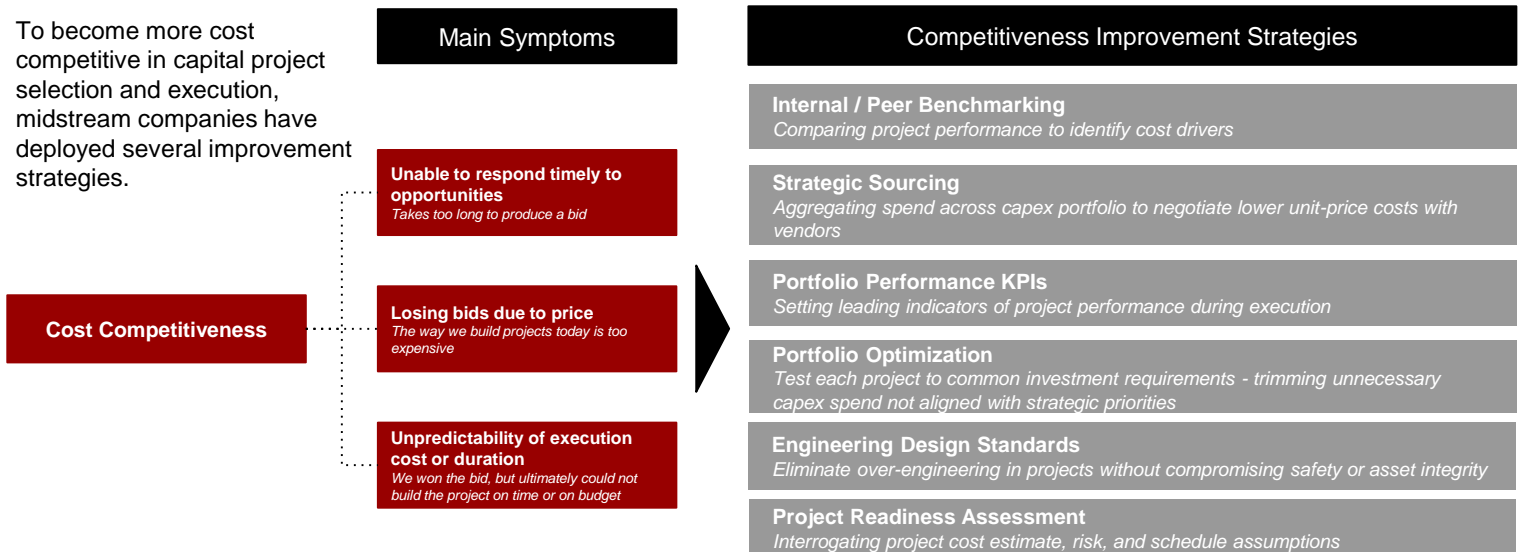
For private equity (PE) firms and retail investors alike, returns on investment in midstream assets and companies hinge on management's ability to maintain a balance between distributions and long-term capital investments.

In recent years, ROCE has lagged distributions for many midstream companies, focusing management's attention on the quality of their capital project portfolio.

Selecting the right projects and executing them well is thus paramount to sustainable distribution growth.

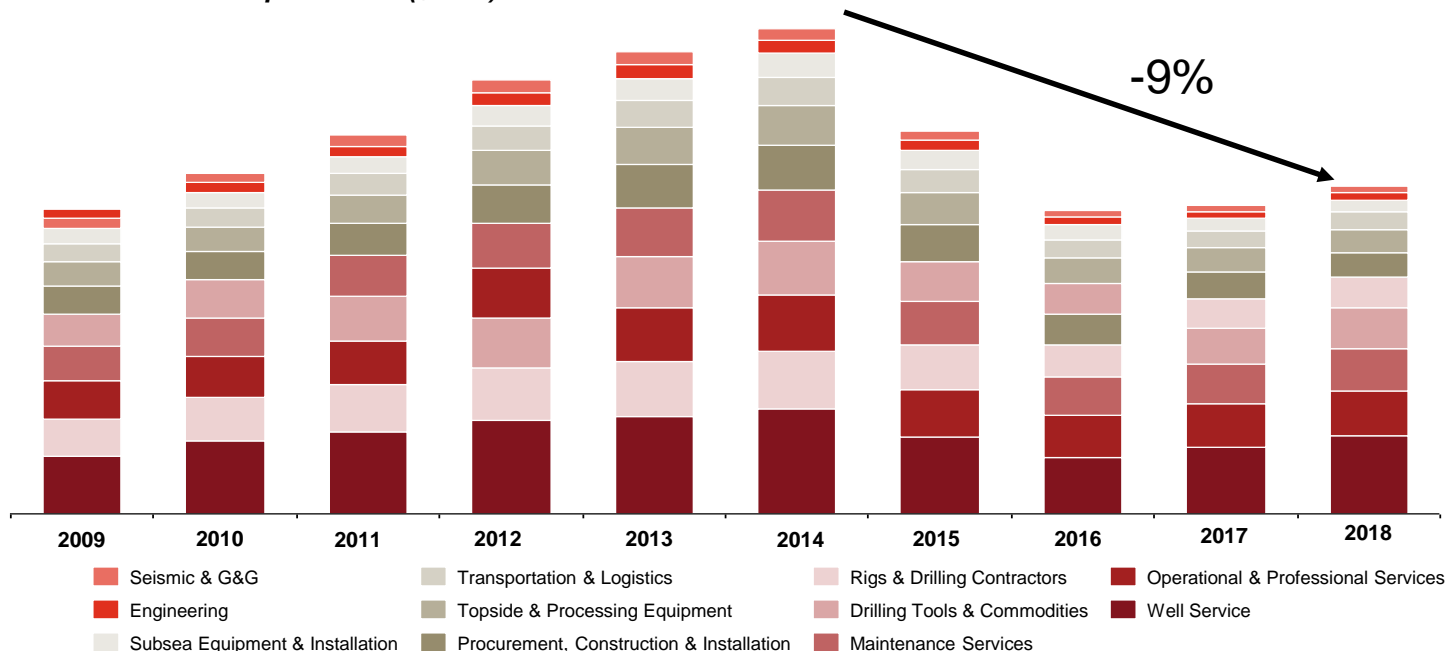
**“Disciplined capital allocation, strong project execution and portfolio management drive higher ROCE, resulting in sustainable cash flows. In turn, predictable distributions attract investors and lower the cost of capital.”**  
 — Tony Caletka, Energy Capital Projects Leader, PwC

To become more cost competitive in capital project selection and execution, midstream companies have deployed several improvement strategies.



## Capital expenditure in the oilfield segment plunged 9% over the past 5 years

Oilfield Services Expenditures (\$ in B)

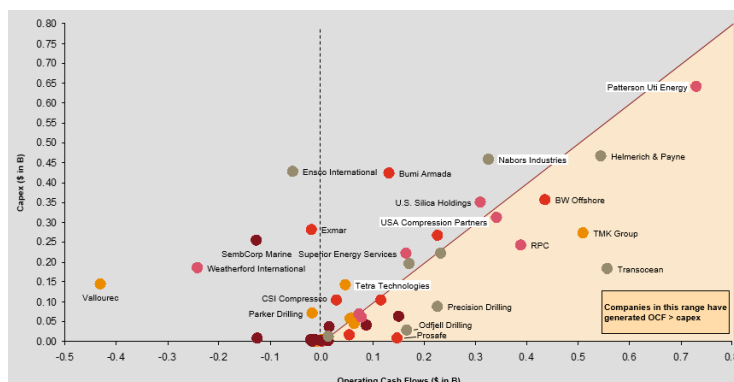


Source: Rystad, Strategy & | PwC Analysis

### Not all oilfield companies are made the same

- Over the past three years, upstream spending on oilfield services has dropped by approximately 9% as upstream companies tightened their belts. Although this is a significant reduction in spending, oil and gas production did not follow a similar trajectory. Activity has returned to the oil patch, with oilfield services companies absorbing much of the spending reductions, impacting their top and bottom lines negatively.
- Similar to their upstream peers, oilfield players are well aware of the investors' mandate to operate within their existing cash flows. However, our analysis indicates that many oilfield companies have not stayed within their cash flow means. Two factors contribute to whether a company stays with cash flows:
  - Their segment, and
  - Their scale
- Well Services, Drilling Tools and Commodities, and Rigs and Drilling contractors have largely reduced capex in line with their cash flows.
- Operational and professional services companies continue to invest in capex beyond cash flows, financing primarily through debt.
- Procurement, construction & installation companies experienced volatile cash flows, but in total their leverage increased.

### Oilfield services cash flow vs. capex



Source: CapitalIQ, Pitchbook, Strategy & | PwC Analysis

**“In a world of living within existing cash flows, size matters. We expect companies with strong balance sheets to look for opportunities to further enhance their size and scope. Such companies will be in a position to upgrade their fleets ‘on the cheap’. Also, technology continues to enable efficiency and effectiveness. We expect to continue seeing technology deals in 2019, albeit smaller.”**

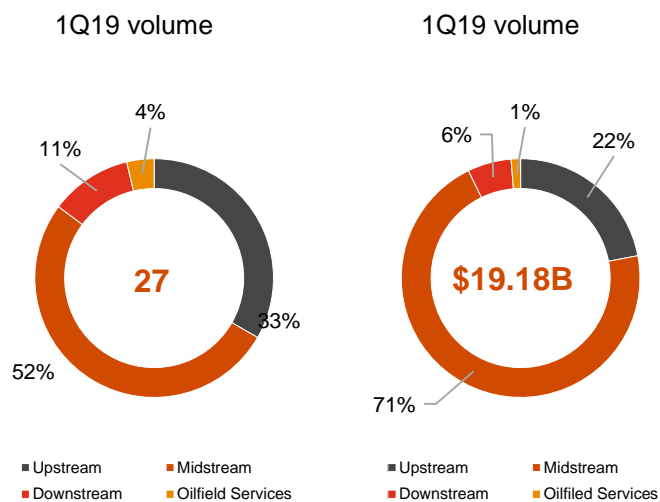
**— Mile Milisavljevic, Deals Strategy Energy, Oil and Gas Leader, PwC**

## Sub-sector trends and outlook

### Announced deal volume and value by sub-sector

- In the upstream segment, several quarters of consolidation have played themselves out. Today, there seems to be no clear value proposition, resulting in softness in upstream deal making activity during the first quarter of 2019. We expect that trend to continue as companies remain laser focused on capital efficiency, generating returns for investors, and operating within existing cash flows.
- In the midstream segment PE and financial investors remained active due to the attractive cost per mile of deals; while upstream and downstream companies looked to add midstream assets and vertically integrate parts of the value chain.
- The oilfield services segment continues to see limited deal activity as excess capacity and focus on cash flow push investors to the sidelines.
- The downstream segment also saw dismal levels of deal making in the first quarter of 2019. However, going forward we expect to see more deals in the downstream as segment, as the US continues to build export capacity and terminals become more important.

### Sub-sector deals by volume and value



### US Oil & Gas outlook for 2019

The first quarter's results suggest a quiet year ahead, but that's only on the surface.

Bigger changes are underway in the sector as a whole, as the industry shifts away from the pursuit of growth at all costs it had followed for nearly a decade to a new kind of model. This new model focuses less on what you might achieve 'some day' and more on the profitability and positive cash flow of your business right now.

In short, investors have plenty of dry powder, but only for companies with good prospects for cost leadership.

**"We've seen very little activity in the OFS sector in the last two quarters. Living within cash flow will likely push companies to consider further scale acquisitions, investments in technology, or asset rationalizations."**

**— Mile Milisavljevic, Deals Strategy  
Energy, Oil and Gas Leader, PwC**

# About PwC deals

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Smart deal makers are perceptive enough to see value others have missed, flexible enough to adjust for the unexpected, aggressive enough to win favorable terms in a competitive environment, and circumspect enough to envision the challenges they will face from the moment the contract is signed. But in a business environment where information can quickly overwhelm, the smartest deal makers look to experienced advisors to help them fashion a deal that works.

PwC's Deals group can advise power and utility companies and private equity firms on key M&A decisions, from identifying acquisition or divestiture candidates and performing detailed buy-side diligence, to developing strategies for capturing post-deal profits and exiting a deal through a sale, carve-out, or IPO. With more than 20,000 deals professionals worldwide, we can deploy seasoned teams that combine deep power and utility industry skills with local market knowledge virtually anywhere and everywhere your company operates or executes transactions.

Although every deal is unique, most will benefit from the broad experience we bring to delivering strategic M&A advice, due diligence, transaction structuring, M&A tax, merger integration, valuation, and post-deal services.

In short, we offer integrated solutions, tailored to your particular deal situation and designed to help you extract peak value within your risk profile. Whether your focus is deploying capital through an acquisition or joint venture, raising capital through an IPO or private placement, or harvesting an investment through the divestiture process, we can help.

For more information about PwC's Energy practice, visit: [www.pwc.com/energy](http://www.pwc.com/energy).

## About the data

The information presented in this report is an analysis of deals in the oil and gas industry where the target company, the target ultimate parent company, the acquiring company, or the acquiring ultimate parent company was located in the United States of America. Deal information was sourced from IHS Markit, PwC U.S. IPO Watch, ECM and DCM Analytics, and S&P LCD Comps, and includes deals for the following industries: Upstream/E&P, Midstream, Downstream, Oilfield Equipment & Services, Integrated/Diversified. The deal types covered in the analysis include: acquisitions, joint ventures, mergers, swaps, debt and equity offerings.

This analysis includes all individual deals with value exceeding \$50 million. Deals with undisclosed values are omitted from this analysis. The time horizon for the analysis covers data through March 31, 2019.

Percentages and values are rounded to the nearest whole number which may result in minor differences when summing totals.