

# VALUE FOCUS ENERGY



## Third Quarter 2015

### Exploration & Production Overview

As the 4th quarter begins, uncertainty is rife within the Exploration and Production (E&P) industry. Over 12 months into a declining oil price environment, barrel prices have experienced levels not seen since the financial crisis. The changing economics and marketplace have presented a challenging operating environment and E&P companies need to address their production levels, leverage levels and appetite for more (or less) reserve assets. Let's first explore what has led us to the current situation: oil demand, supply, and price.

[www.mercercapital.com](http://www.mercercapital.com)

<b>World Oil Demand</b>	1	<b>Midstream Operations</b>	19
<b>World Oil Price</b>	5	<b>Alternative Energy</b>	21
<b>M&amp;A Transaction Activity</b>	9	<b>Historical Valuations</b>	23
<b>Market Valuations and Transaction Activity</b>	10	<b>Stock Performance</b>	25
<b>Guideline Public Company Valuation Multiples</b>	10	<b>Rig Count</b>	26
		<b>U.S. Oil and Gas Resources</b>	28
<b>Appendices:</b>		<b>About Mercer Capital</b>	30
<b>Commodity Prices</b>	11	<b>Erickson Partners Merges with Mercer Capital</b>	31
<b>Selected Public Company Information</b>			
Exploration & Production	12	<b>Special Supplement: Fairness Opinions and Down Markets</b>	
Oil Field Services and Equipment	15		

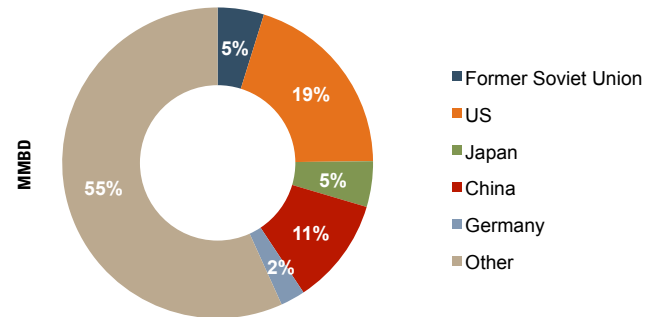
# World Oil Demand

Crude Oil & Natural Gas

92 mboe/d

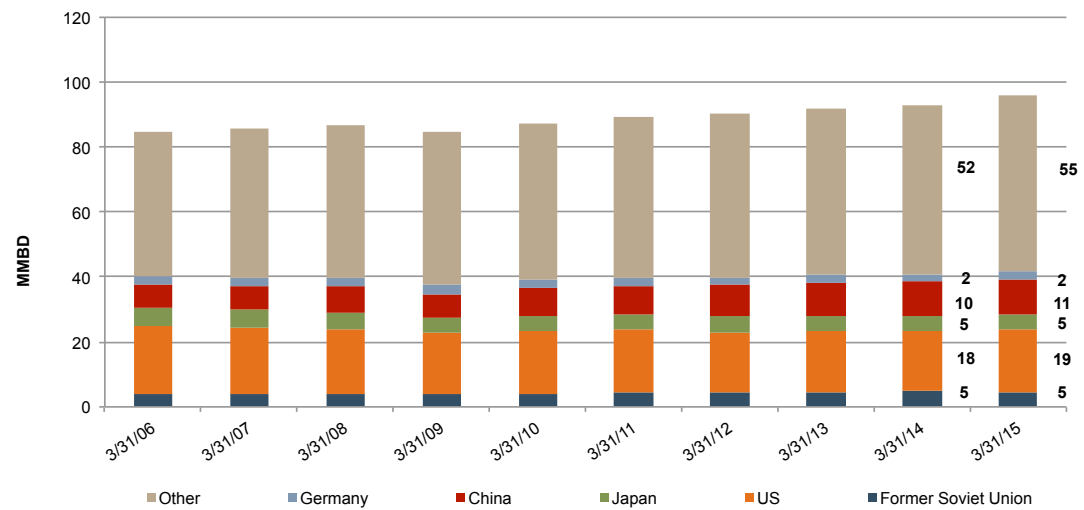
## World Daily Consumption of Crude Oil and Liquid Fuels: March 2015

As of March 31, 2015, total world daily consumption equaled 92.44 million barrels per day.



Source: Bloomberg

## World Daily Consumption of Crude Oil and Liquid Fuels



Source: Bloomberg

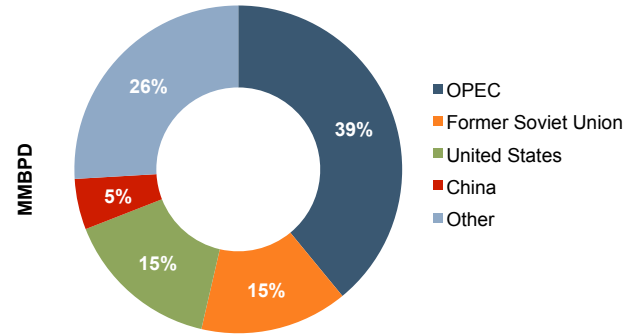
# World Oil Supply

Crude Oil & Natural Gas

96 mboe/d

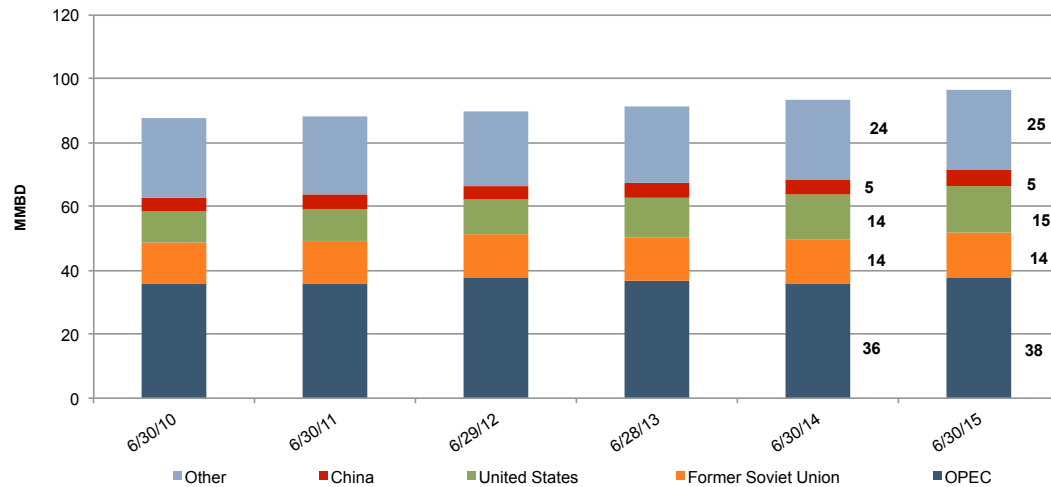
## World Daily Production of Crude Oil: June 2015

As of June 31, 2015, world daily production totaled 96.47 million barrels per day.



Source: Bloomberg

## World Daily Production of Crude Oil



Source: Bloomberg

## World Oil Supply

### Crude Oil & Natural Gas

---

4 mboe/d  
oversupplied

As indicated in the "World Daily Production of Crude Oil" chart on the prior page, industry experts believe OPEC has increased production to maintain market share and drive the price of oil down. As of August, OPEC surpassed its 30 mmbd production quota for the 15th month in a row. Iraq, OPEC's second largest producers of crude, boosted output 17% compared to this month last year.<sup>1</sup> Many have speculated that OPEC's target is U.S. shale oil producers, who face higher costs of production.

- » In OPEC's *September Monthly Oil Market Report*, forecasted U.S. oil production for 2015 dropped from 13.86 mmbd, as predicted in August, to 13.75 mmbd.<sup>2</sup>
- » "But through the collapse in prices, OPEC has continued to pump oil in a fight to maintain the market share it enjoyed for years. With this new forecast, OPEC is more or less claiming victory over shale producers in this stage of the oil price war."<sup>3</sup>
- » OPEC's new forecast echoes a recent report from the International Energy Agency that said low oil prices could bring U.S. oil production from new drilling to a grinding halt. The IEA said, "On the face of it, the Saudi led OPEC strategy to defend market share regardless of price appears to be having the intended effect of driving out costly, 'inefficient' production."<sup>4</sup>
- » OPEC writes: "In North America, there are signs that U.S. production has started to respond to reduced investment and activity. Indeed, all eyes are on how quickly U.S. production falls."<sup>5</sup>
- » U.S. Production is coming down faster than anticipated: "The U.S. production is coming down faster than even I thought... it's starting to correct already" per John Kulduff, on CNBC. Goldman Sachs projected oil prices into the \$20s.<sup>6</sup>
- » Federal data released in September shows that U.S. production has finally started to fall to about 9.3 million barrels a day in June, down roughly 3% since 2015 oil output peaked in April. Capital constraints could help push output down by 500,000 barrels a day by the end of 2015, Citi Research estimates.<sup>7</sup>
- » To put a reduction of 500,000 barrels per day into context, "[T]hat would be like Exxon Mobil Corp, the largest energy company in America, halting its U.S. oil production and then some. Put another way, it would require nearly 20 publicly traded U.S. Independent oil companies with a market capitalization of \$2 billion or less to stop pumping crude all together."<sup>8</sup>

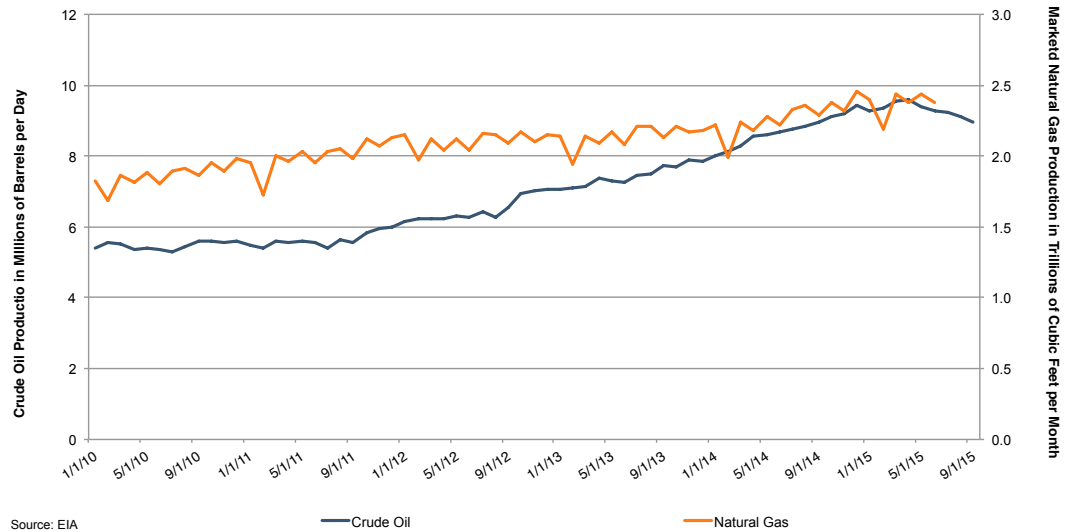
# World Oil Supply

## Crude Oil & Natural Gas

U.S. E&P restricts oil production

The oversupply of crude oil worldwide has caused significant downward pressure on price. U.S. producers have responded by cur-tailing and restricting production of existing wells and cutting capital expenditure budgets for the drilling of new wells.

U.S. Crude Oil and Natural Gas Production



# World Oil Price

## Proved Reserves

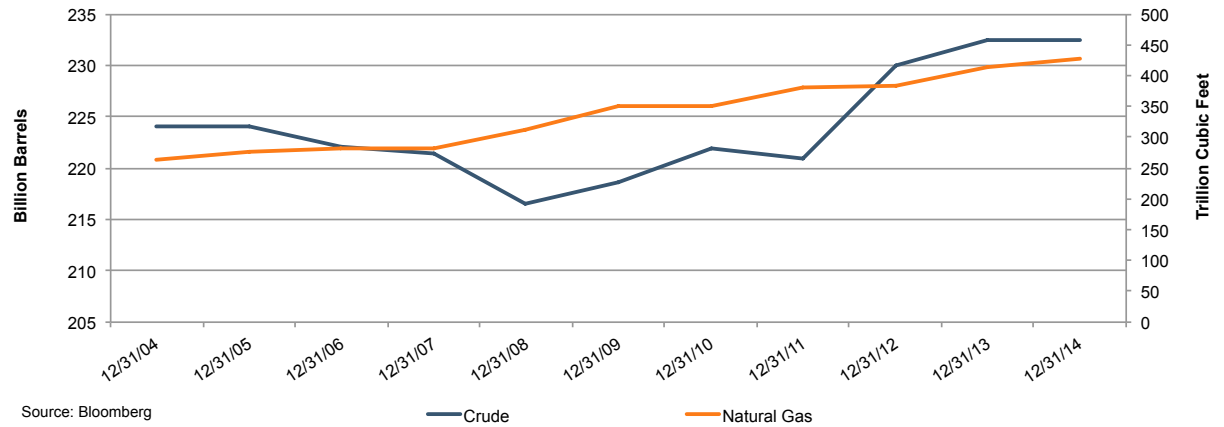
The U.S. Energy and Information Agency (EIA) defines proved reserves as the “estimated volumes of hydrocarbon resources that analysis of geologic and engineering data demonstrates with reasonable certainty are recoverable under existing economic and operating conditions.” The top chart shows recent trends in North America oil and natural gas proved reserves. The chart “World Proved Oil Reserves” details changes in global and domestic proved reserves between 2004 and 2014 (the most recent date for which information was available).<sup>9</sup>

With the expected demand for oil worldwide falling, most oil suppliers not slowing their production rates (sans the U.S.), and the world’s total oil reserves growing, the result is lower oil prices. The question is: How long will prices stay here and what does the future hold?

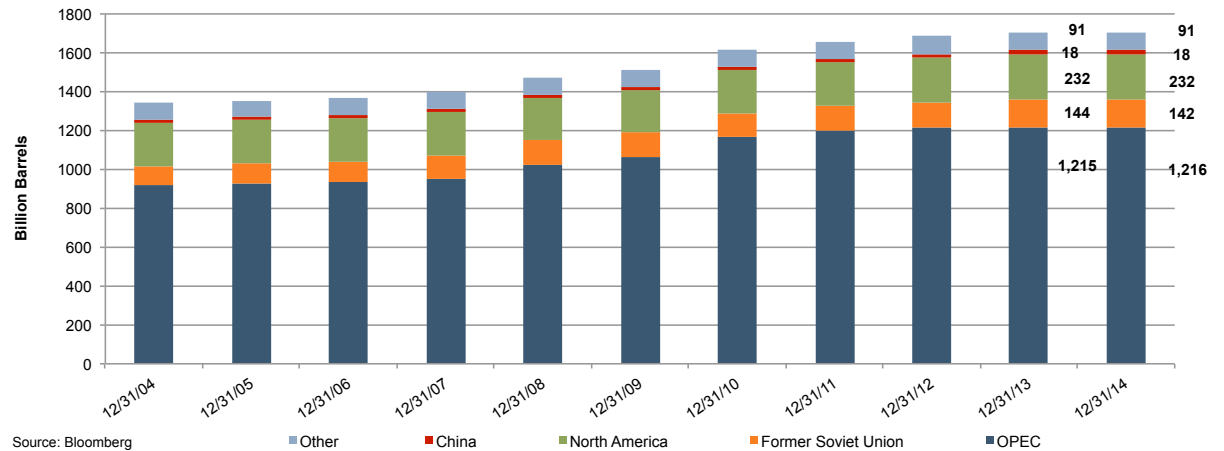
Al Walker, Chief executive of Anadarko Petroleum Corp., one of the biggest oil companies in the U.S., recently told the audience at a Barclays energy conference, “Frankly at the end of the day, none of us have a great sense for where oil prices are going.”<sup>10</sup>

This perspective has been shared by many industry participants, from oil and gas executives of large public entities, down to independent private E&P operators. We were visiting with one of our clients recently, who has been active in oil and gas for the past 30+ years. His experience is extensive and

North America Proved Reserves



World Proved Oil Reserves



# World Oil Price

## Low Price Implications

littered with successes. For example, he sold an E&P company in early 2014, which hindsight tells us that he had great timing on that divestiture. On our most recent visit, we asked where he thinks the price of oil is going? His response: "I have no idea." This is a humbling reminder for us observers of the industry that if CEO's of large public entities and owners of very active independent E&P's do not have a feel for where oil prices are headed next, what hope is there for the rest of us in the prediction game?

Now that oil prices have been "low" for the last 12+ months, with no predictable time frame on when a rebound may occur, there are several issues beginning to work their way through the industry: (1) liquidity issues; (2) leverage issues; and (3) valuation issues.

### 1. LIQUIDITY

» Statement from the President of Clayton Williams – a Texas based exploration and production company:

"We are in the process of coming up with a plan to maintain liquidity. This could be a challenging period of time for some time to come. We all know that the landscape for oil is a big question mark right now. We are trying to come up with a plan that is not dilutive to our shareholder base. And so we have been very actively involved and talking to private equity to put together capital to go forward drilling. They would obviously be at a - we'd like to see a little higher oil prices. We are making money with the rigs we are running now, but not the type of returns we'd like to see ultimately."<sup>11</sup>

» Jim Flores, vice chairman of Freeport-McMoran Inc., which pumps oil in the Gulf of Mexico, explained the industry's conundrum this way: "It's raining and it's going to rain for a long time. We're all going to get wet. A few people are going to drown. You just have to make it to the other side."<sup>12</sup>

» More distress is probably in store for many companies because the insurance they purchased as protection against low oil prices is increasingly expiring. Simmons & Company International estimates that 36 U.S. drillers have hedges to sell 33% of their oil for an average of \$80 a barrel this year; next year, hedges would cover just 18% of their oil at \$67 a barrel.<sup>13</sup>

### 2. LEVERAGE

» Smaller drillers are bracing for cuts to their credit lines in October as banks re-evaluate how much energy companies' oil and gas properties are worth. But with oil trading below \$45 a barrel, bigger oil outfits are struggling to stay profitable too.<sup>14</sup>

» "With eight bankruptcies already announced this year, weaker producers could live or die by the whims of capital providers," Citi analysts wrote recently, predicting that banks will reduce borrowing bases by as much as 15%.<sup>15</sup>

The combination of the above two factors may force a significant number of companies to divest oil and gas assets, sell their entire company, or file for bankruptcy. All of which creates an unstable environment for anticipating the price at which these assets and companies can be sold, i.e. Fair Value.

## World Oil Price

### Low Price Implications

### 3. VALUATIONS

Due to the significant drop in oil prices, the M&A industry has been in a holding pattern over the last 12 months. The number of transactions and the total deal value of the transactions is the lowest in the last five years.

We may consider this the calm before the storm as many industry experts have shared that when an industry experiences a significant shock to the system, most activity, including M&A activity, freezes until more certainty is experienced or predicted. The conundrum in this case is the “shock” has lasted more than 12 months, which is leading to the liquidity and leverage pressures forcing companies to act before any predictability can be foreseen with confidence. This pressure, along with lower oil prices, is leading to lower valuations.

W&T Offshore, Inc. said it would sell a prized Texas shale oil prospect for \$376.1 million, half what analysts projected it could fetch when the company first weighed selling it last year. W&T, which operates in West Texas and the Gulf of Mexico, said it plans to use the cash to pay back money it has borrowed on its credit line.<sup>16</sup>

With asset sales looming in the future as a way for companies to create liquidity, the figure below presents the acreage lease pricing for the Permian Basin and Eagle Ford Shale plays in the state of Texas.

#### Top Five Lease Sales for Permian Basin and Eagle Ford

YTD August 2015

Bidder	County	Price/Acre	Bid Date
<b>Permian Basin</b>			
Silver Hill Energy Partners, LLC	Loving	\$7,101	Aug-15
Panther Energy Company II, LLC	Reeves	\$5,100	Aug-15
CL&F Operating LLC	Reeves	\$11,221	Aug-15
Carrizo (Permian) LLC	Reeves	\$2,510	Aug-15
Carrizo (Permian) LLC	Reeves	\$2,510	Aug-15
<b>Eagle Ford</b>			
Marathon Oil EF LLC	Atascosa	\$5,000	Jan-15
Murphy Exploration and Production Company-USA	Karnes	\$2,000	Aug-15
Marathon Oil EF LLC	Atascosa	\$5,000	Jan-15
Ammonite Oil & Gas Corp	Gonzales	\$1,151	Jan-15
Ammonite Oil & Gas Corp.	Zavla	\$1,088	Aug-15

Source: Texas RRC



## World Oil Price

### Low Price Implications

### 3. VALUATIONS (continued)

In our own experience, we routinely watched market participants price Proved Undeveloped reserves (PUDs) at approximately 50% to as high as 75% of Proved Developed Producing reserves (PDPs). Of course, this was before the price decline started in mid-2014. Since that time, Proved Undeveloped reserves have been significantly discounted to 10% to 30% or less of the PDP's.

Note: Although we have focused solely on E&P participants in the discussion above, we should note that not all areas of the oil and gas industry are negatively impacted by significant drops in oil price. Many refineries have benefited from lower crude oil prices and have cut costs and increased profit margins. For example, in August Warren Buffet accumulated a 10.8% stake in Phillips 66, valued approximately at \$4.5 billion.<sup>17</sup> This comes more than a year after Buffet traded almost two-thirds of his prior holding in Philips for a chemical business. Thus this recent transaction came as a surprise. Buffett is betting that "oil prices will remain low and Americans will keep filling their gas tanks."<sup>18</sup>

## M&A Transaction Activity

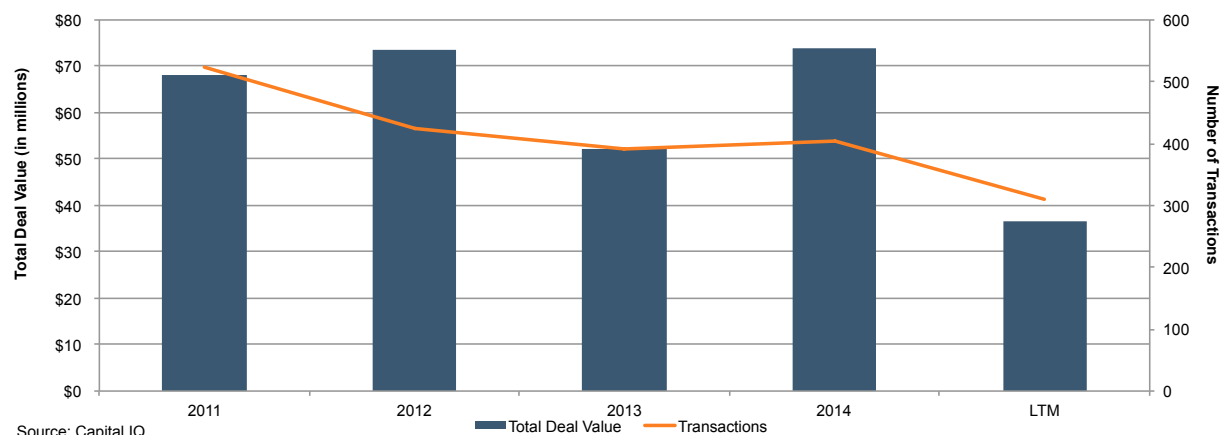
After peaking in 2011, transaction activity (in terms of announced transactions) declined over the next three years. While deal count in 2014 was on par with 2013 the total deal value increased to nearly \$74 billion.

Encana's \$7 billion acquisition of Athlon Energy will give the Canadian operator access to Athlon's Permian Basin acreage. The combination of Whiting Petroleum and Kodiak Oil & Gas will make the combined company the largest producer in the Bakken.

The merger of Rosetta Resources and Nobel Energy was the first major shale deal after the recent collapse of oil prices and is predicted to mark the beginning of a wave of M&A activity in the oil and gas space.<sup>19</sup> The merger of NewWoods Petroleum and RKI demonstrates this trend.

Selected individual transaction data (including implied valuation multiples) is shown in the table.

### U.S. Exploration & Production Transaction Activity



### Selected Exploration and Production Transactions

Target Name	Trans. Closing Date	Trans. Value	Implied Enterprise Value	LTM Revenue	LTM EBITDA	EBITDA Margin	Enterprise Value to:	
							Rev.	EBITDA
BG Group	04/08/2015	\$86,372.5	\$81,328.5	\$18,131.0	\$7,973.0	44.0%	4x	10x
Dragon Oil	05/21/2015	2,828.2	4,279.0	995.9	777.9	78.1%	4.3	5.5
Williams Companies, Inc.	06/21/2015	81,793.1	81,452.1	7,604.0	2,890.0	38.0%	10.7	28.2
Oil Search Limited	09/08/2015	12,529.3	11,686.3	1,964.1	1,383.8	70.5%	5.9	8.4
Cairn India Limited	06/14/2015	2,275.26	3,160.39	2,342.83	1,543.46	65.9%	1.3	2.0
<b>Average</b>		<b>\$45,880.7</b>	<b>\$44,686.5</b>	<b>\$7,173.8</b>	<b>\$3,256.2</b>	<b>57.6%</b>	<b>6.4x</b>	<b>13.1x</b>
<b>Median</b>		<b>\$47,161.2</b>	<b>\$46,507.4</b>	<b>\$4,784.1</b>	<b>\$2,136.9</b>	<b>57.2%</b>	<b>5.2x</b>	<b>9.3x</b>

KMG Kashagan BV was excluded from the summary of the largest E&P transactions because they did not report LTM Revenues or LTM EBITDA at announcement.

Presented in \$000,000s

Source: Capital IQ

## Market Valuations and Transaction Activity

Over the last twelve months, M&A reflected the following:

- » 1,174 deals closed worldwide in the oil and gas space.
- » 359 transactions have been announced globally, but have not yet closed.
- » 474 transactions closed in the U.S. in oil and gas. 109 transactions have been announced, but have not yet closed.
- » 53 oil and gas companies worldwide went bankrupt. 52 of those companies were primarily located in the U.S.
- » 756 transactions (both closed and announced) occurred globally in the Exploration and Production space. 329 of those had U.S. target companies.
- » 25 companies operating in Exploration and Production went bankrupt. 24 of those were located in the U.S.

## Guideline Public Company Valuation Multiples

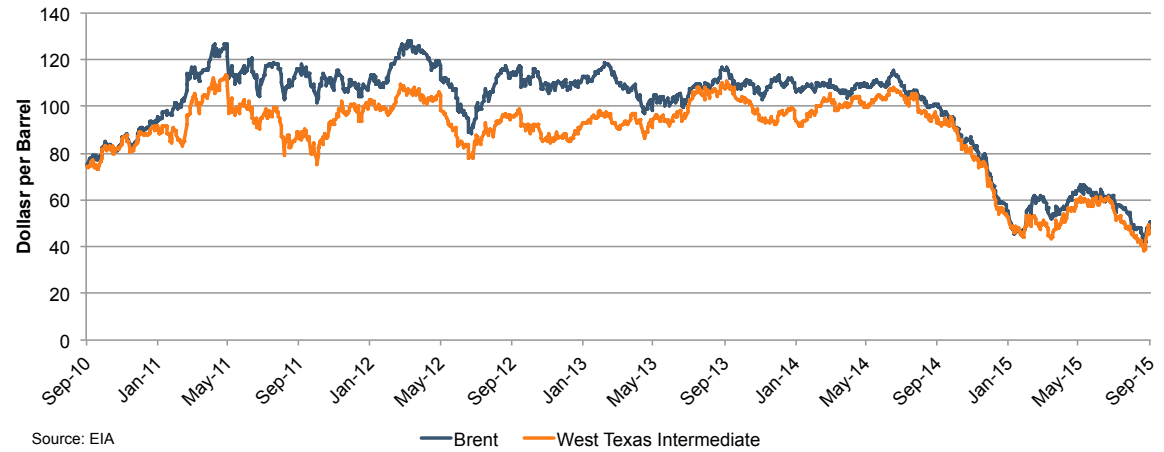
As shown in Appendix B, valuation multiples for exploration & production companies are widely dispersed, and measures of central tendency range from approximately 9.1x to 54.8x (on an enterprise value to EBITDAX basis).

As shown in Appendix C, valuation multiples were compressed going into year-end 2014 but have rebounded in the first three quarters of 2015.

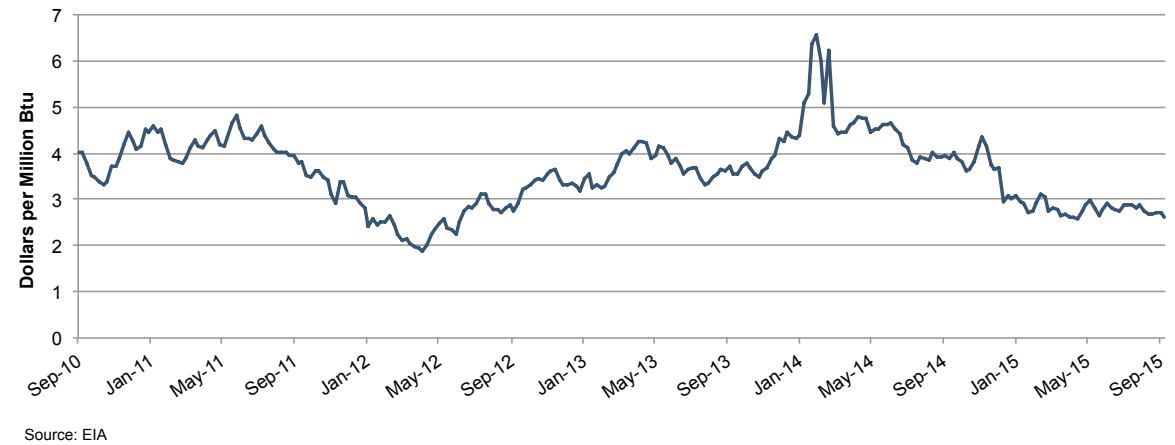
Appendix A

# Commodity Prices

Crude Oil Spot Prices



Henry Hub Natural Gas Spot Price



## Appendix B

## Selected Public Company Information // Exploration &amp; Production

Company Name	Ticker	LTM		EBITDA Margin	Enterprise Value @ 9/30/15	YOY Change in EV	EV/EBITDA Multiple	EV/Total Production (\$/MMBOE/D)
		Revenues	EBITDA					
Anadarko Petroleum Corp	APC	\$13,316.0	\$2,121.0	15.9%	\$47,533.9	-20.3%	22.4x	59,630x
Apache Corp	APA	10,214.0	-13807.0	-135.2%	23,739.0	-51.0%	nmd	44,162x
Approach Resources Inc	AREX	227.3	148.5	65.3%	574.2	-36.8%	3.9x	36,906x
Antero Resources Corp	AR	2,325.9	1105.8	47.5%	11,309.2	-38.9%	10.2x	48,809x
Bill Barrett Corp	BBG	413.4	112.8	27.3%	870.4	-46.5%	7.7x	51,960x
Bonanza Creek Energy Inc	BCEI	514.1	132.8	25.8%	1,037.1	-66.1%	7.8x	36,240x
Cabot Oil & Gas Corp	COG	1,780.0	298.8	16.8%	11,025.6	-26.2%	36.9x	43,789x
Carrizo Oil & Gas Inc	CRZO	681.5	486.3	71.4%	2,957.8	-15.2%	6.1x	85,996x
Chesapeake Energy Corp	CHK	15,583.0	-6552.0	-42.0%	18,717.1	-40.0%	nmd	28,392x
Cimarex Energy Co	XEC	1,987.0	-356.1	-17.9%	10,323.0	-13.6%	nmd	65,485x
Comstock Resources Inc	CRK	425.9	42.6	10.0%	1,340.4	-28.9%	31.5x	42,457x
Concho Resources Inc	CXO	2,637.7	1163.0	44.1%	15,488.8	-11.2%	13.3x	106,309x
Continental Resources Inc/OK	CLR	3,994.4	2410.6	60.3%	17,773.5	-41.6%	7.4x	81,359x
Denbury Resources Inc	DNR	2,143.5	-660.4	-30.8%	4,372.1	-50.7%	nmd	59,750x
Devon Energy Corp	DVN	16,605.0	-5512.0	-33.2%	30,392.0	-26.1%	nmd	45,664x
Diamondback Energy Inc	FANG	531.6	59.9	11.3%	5,182.0	3.2%	86.5x	162,956x
Energen Corp	EGN	1,044.6	527.4	50.5%	4,614.0	-21.8%	8.7x	73,098x
EOG Resources Inc	EOG	13,165.4	5856.8	44.5%	45,012.8	-23.2%	7.7x	80,796x
EV Energy Partners LP	EVEP	246.4	-101.8	-41.3%	733.9	-74.4%	nmd	26,313x

Presented in \$000,000s  
Source: Bloomberg L.P.

## Appendix B

## Selected Public Company Information // Exploration &amp; Production

Company Name	Ticker	LTM		EBITDA Margin	Enterprise Value @ 9/30/15	YOY Change in EV	EV/EBITDA Multiple	EV/Total Production (\$/MMBOE/D)
		Revenues	EBITDA					
EXCO Resources Inc	XCO	472.1	-444.6	-94.2%	1,699.6	-29.5%	nmd	29,560x
Gulfport Energy Corp	GPOR	727.1	506.1	69.6%	3,651.5	-27.4%	7.2x	37,354x
Halcon Resources Corp	HK	1,080.4	-984.0	-91.1%	4,090.4	-21.6%	nmd	100,827x
Hess Corp	HES	8,793.0	3400.0	38.7%	19,396.1	-37.5%	5.7x	52,689x
Laredo Petroleum Inc	LPI	914.4	3.0	0.3%	3,384.2	-28.6%	1,131.5x	77,481x
Magnum Hunter Resources Corp	MHR	238.1	-372.2	-156.3%	1,426.6	-45.2%	nmd	49,522x
Marathon Oil Corp	MRO	8,306.0	2539.0	30.6%	16,287.6	-47.5%	6.4x	38,526x
Matador Resources Co	MTDR	382.1	-51.4	-13.5%	2,108.4	-1.4%	nmd	84,678x
Murphy Oil Corp	MUR	\$4,306.4	\$2,488.5	\$0.58	\$6,155.6	-52.6%	2.5x	31,089x
Newfield Exploration Co	NFX	2,215.0	-922.0	-\$0.42	7,770.3	0.7%	nmd	51,533x
Noble Energy Inc	NBL	4,240.0	1,929.0	\$0.45	18,166.1	-37.6%	9.4x	50,049x
Northern Oil and Gas Inc	NOG	408.4	-359.3	-\$0.88	1,150.7	-27.9%	nmd	72,978x
Oasis Petroleum Inc	OAS	1,312.5	804.2	\$0.61	3,549.2	-47.1%	4.4x	71,803x
PDC Energy Inc	PDCE	512.4	133.6	\$0.26	2,789.1	13.3%	20.9x	62,722x
Pioneer Natural Resources Co	PXD	4,079.0	1,629.0	\$0.40	20,621.8	-32.0%	12.7x	99,765x
QEP Resources Inc	QEP	3,067.6	122.2	\$0.04	3,986.5	-56.4%	32.6x	28,004x
Range Resources Corp	RRC	1,803.4	922.6	\$0.51	8,903.4	-38.3%	9.7x	38,057x
Rex Energy Corp	REXX	295.3	-139.0	-\$0.47	1,043.3	-91.4%	nmd	31,222x
Rosetta Resources Inc	ROSE	913.4	-458.2	-\$0.50	3,305.5	-72.6%	nmd	58,655x

Presented in \$000,000s  
Source: Bloomberg L.P.

## Appendix B

## Selected Public Company Information // Exploration &amp; Production

Company Name	Ticker	LTM		EBITDA Margin	Enterprise Value @ 9/30/15	YOY Change in EV	EV/EBITDA Multiple	EV/Total Production (\$/MMBOE/D)
		Revenues	EBITDA					
Sanchez Energy Corp	SN	702.7	-650.6	-\$0.93	2,124.0	-82.0%	nmd	41,934x
SandRidge Energy Inc	SD	1,461.3	-1,719.5	-\$1.18	4,973.3	-44.1%	nmd	61,398x
SM Energy Co	SM	2,053.4	1,649.8	\$0.80	4,649.0	345.6%	2.8x	27,261x
Southwestern Energy Co	SWN	3,587.0	542.0	\$0.15	11,107.1	236.0%	20.5x	24,701x
Stone Energy Corp	SGY	645.4	-742.6	-\$1.15	1,190.7	-80.5%	nmd	30,579x
Ultra Petroleum Corp	UPL	1,115.5	724.3	\$0.65	4,403.9	-21.1%	6.1x	33,557x
Vanguard Natural Resources LLC	VNR	766.3	-318.4	-\$0.42	2,897.7	-37.7%	nmd	47,519x
W&T Offshore Inc	WTI	708.2	-137.5	-\$0.19	1,691.2	-52.1%	nmd	37,412x
Whiting Petroleum Corp	WLL	2,689.6	727.0	\$0.3	8,310.5	143.7%	11.4x	51,332x
<b>Average</b>		<b>\$3,098.6</b>	<b>-\$36.2</b>	<b>-3.5%</b>	<b>\$9,017.7</b>	<b>-19.2%</b>	<b>54.8x</b>	<b>55,368x</b>
<b>Median</b>		<b>\$1,312.5</b>	<b>\$122.2</b>	<b>15.1%</b>	<b>\$4,403.9</b>	<b>-36.8%</b>	<b>9.1x</b>	<b>49,522x</b>

Presented in \$000,000s  
Source: Bloomberg L.P.

## Appendix B

## Selected Public Company Information // Oil Field Services and Equipment

Company Name	Ticker	LTM			Enterprise Value @ 9/30/15	YOY Change in EV	EV/EBITDA Multiple
		Revenues	EBITDA	EBITDA Margin			
<b>Diversified</b>							
Baker Hughes Inc	BHI	na	\$2,575.0	na	\$24,853.3	-21.6%	9.7x
Halliburton Co	HAL	\$30,440.0	4,747.0	15.6%	35,323.4	-41.8%	7.4x
Schlumberger Ltd	SLB	44,545.0	10,250.0	23.0%	93,565.0	-32.4%	9.1x
Weatherford International PLC	WFT	12,788.0	1,228.0	9.6%	13,876.0	-42.9%	11.3x
<b>Average</b>		<b>\$29,257.7</b>	<b>\$4,700.0</b>	<b>16.1%</b>	<b>\$41,904.4</b>	<b>-34.7%</b>	<b>9.4x</b>
<b>Median</b>		<b>\$30,440.0</b>	<b>\$3,661.0</b>	<b>15.6%</b>	<b>\$30,088.3</b>	<b>-37.1%</b>	<b>9.4x</b>
<b>Contract Drilling</b>							
Atwood Oceanics Inc	ATW	\$1,356.0	\$664.8	49.0%	\$2,599.3	58.0%	3.9x
Diamond Offshore Drilling Inc	DO	2,667.1	618.3	23.2%	4,880.7	83.1%	7.9x
EnSCO PLC	ESV	4,643.9	-1,056.9	-22.8%	7,957.1	55.0%	nmd
Helmerich & Payne Inc	HP	3,584.4	1,537.3	42.9%	4,893.0	47.5%	3.2x
Hercules Offshore Inc	HERO	602.4	-124.5	-20.7%	na	na	nmd
Nabors Industries Ltd	NBR	5,875.6	588.5	10.0%	6,419.7	60.4%	10.9x
Noble Corp plc	NE	3,231.4	937.8	29.0%	7,947.4	71.0%	8.5x
Parker Drilling Co	PKD	875.2	224.4	25.6%	797.1	69.7%	3.6x
Patterson-UTI Energy Inc	PTEN	2,877.3	911.8	31.7%	2,730.2	50.6%	3.0x

Presented in \$000,000s  
Source: Bloomberg L.P.



## Appendix B

## Selected Public Company Information // Oil Field Services and Equipment

Company Name	Ticker	LTM			Enterprise Value @ 9/30/15	YOY Change in EV	EV/EBITDA Multiple
		Revenues	EBITDA	EBITDA Margin			
Pioneer Energy Services Corp	PES	885.2	71.7	8.1%	483.0	36.5%	6.7x
Rowan Cos Plc	RDC	2,079.7	351.2	16.9%	4,673.8	89.0%	13.3x
Transocean Ltd	RIG	8,434.0	-1,523.0	-18.1%	11,262.4	58.0%	nmd
Unit Corp	UNT	1,250.0	-423.8	-33.9%	1,497.2	41.7%	nmd
Vantage Drilling Co	VTG	853.3	405.6	47.5%	na	na	na
<b>Average</b>		<b>\$2,801.1</b>	<b>\$227.4</b>	<b>13.5%</b>	<b>\$4,678.4</b>	<b>60.0%</b>	<b>6.8x</b>
<b>Median</b>		<b>\$2,373.4</b>	<b>\$378.4</b>	<b>20.0%</b>	<b>\$4,777.2</b>	<b>58.0%</b>	<b>6.7x</b>
<b>Equipment</b>							
Cameron International Corp	CAM	\$9,977.0	\$1,055.0	10.6%	\$13,749.7	83.24%	13.0x
Dril-Quip Inc	DRQ	937.8	306.7	32.7%	1,870.7	57.40%	6.1x
Exterran Holdings Inc	EXH	2,930.4	na	na	3,421.4	67.60%	na
FMC Technologies Inc	FTI	7,523.3	1,192.4	15.8%	7,831.0	57.54%	6.6x
Forbes Energy Services Ltd	FES	373.3	56.1	15.0%	258.0	71.70%	4.6x
Forum Energy Technologies Inc	FET	1,540.0	246.6	16.0%	1,483.3	46.06%	6.0x
National Oilwell Varco Inc	NOV	20,025.0	3,628.0	18.1%	16,289.4	51.08%	4.5x
Tesco Corp	TESO	442.6	41.2	9.3%	215.8	30.48%	5.2x
<b>Average</b>		<b>\$5,468.7</b>	<b>\$932.3</b>	<b>16.8%</b>	<b>\$5,639.9</b>	<b>58.1%</b>	<b>6.6x</b>
<b>Median</b>		<b>\$2,235.2</b>	<b>\$306.7</b>	<b>15.8%</b>	<b>\$2,646.1</b>	<b>57.5%</b>	<b>6.0x</b>

Presented in \$000,000s  
Source: Bloomberg L.P.

## Appendix B

## Selected Public Company Information // Oil Field Services and Equipment

Company Name	Ticker	LTM			Enterprise Value @ 9/30/15	YOY Change in EV	EV/EBITDA Multiple
		Revenues	EBITDA	EBITDA Margin			
<b>Services</b>							
Basic Energy Services Inc	BAS	\$1,250.2	\$165.9	13.3%	\$946.0	52.9%	5.7x
Helix Energy Solutions Group I	HLX	903.7	256.1	28.3%	801.5	34.3%	3.1x
Hornbeck Offshore Services Inc	HOS	598.2	306.4	51.2%	1,299.8	64.5%	4.2x
Key Energy Services Inc	KEG	1,185.9	-108.7	-9.2%	812.8	56.3%	nmd
McDermott International Inc	MDR	2,818.0	177.7	6.3%	1,360.2	79.6%	7.7x
Newpark Resources Inc	NR	975.2	125.3	12.8%	489.3	41.4%	3.9x
Oceaneering International Inc	OII	3,489.1	790.6	22.7%	4,445.6	61.6%	5.6x
RPC Inc	RES	1,956.7	443.9	22.7%	1,960.7	39.6%	4.4x
Superior Energy Services Inc	SPN	4,015.7	125.0	3.1%	3,048.6	47.5%	24.4x
TETRA Technologies Inc	TTI	1,189.6	150.2	12.6%	1,747.7	80.8%	11.6x
Willbros Group Inc	WG	1,644.3	53.1	3.2%	225.4	36.7%	4.2x
<b>Average</b>		<b>\$1,820.6</b>	<b>\$226.0</b>	<b>15.2%</b>	<b>\$1,558.0</b>	<b>54.1%</b>	<b>7.5x</b>
<b>Median</b>		<b>\$1,250.2</b>	<b>\$165.9</b>	<b>12.8%</b>	<b>\$1,299.8</b>	<b>52.9%</b>	<b>5.0x</b>

Presented in \$000,000s  
Source: Bloomberg L.P.

## Appendix B

## Selected Public Company Information // Oil Field Services and Equipment

Company Name	Ticker	LTM			Enterprise Value @ 9/30/15	YOY Change in EV	EV/EBITDA Multiple
		Revenues	EBITDA	EBITDA Margin			
<b>Geophysical Services</b>							
Dawson Geophysical Co	DWSN	\$168.9	-\$9.4	-5.5%	\$40.3	-47.1%	nmd
Geospace Technologies Corp	GEOS	95.1	-14.7	-15.5%	136.4	-66.6%	nmd
ION Geophysical Corp	IO	320.8	-161.3	-50.3%	136.4	-73.5%	nmd
<b>Average</b>		<b>\$194.9</b>	<b>-\$61.8</b>	<b>-23.8%</b>	<b>\$104.4</b>	<b>-62.4%</b>	<b>nmd</b>
<b>Median</b>		<b>\$168.9</b>	<b>-\$14.7</b>	<b>-15.5%</b>	<b>\$136.4</b>	<b>-66.6%</b>	<b>nmd</b>
<b>Oilfield Services &amp; Equipment Overall</b>							
<b>Average</b>		<b>\$4,906.4</b>	<b>\$790.0</b>	<b>11.8%</b>	<b>\$7,535.0</b>	<b>38.3%</b>	<b>7.3x</b>
<b>Median</b>		<b>\$1,644.3</b>	<b>\$256.1</b>	<b>14.1%</b>	<b>\$2,280.0</b>	<b>52.0%</b>	<b>6.1x</b>

Presented in \$000,000s

Source: Bloomberg L.P.

## Appendix B

## Selected Public Company Information // Midstream Operations

Company Name	Ticker	LTM			Enterprise Value @ 9/30/15	YOY Change in EV	EV/EBITDA Multiple
		Revenues	EBITDA	EBITDA Margin			
Blueknight Energy Partners LP	BKEP	\$183.3	\$61.9	33.8%	\$631.4	-7.8%	3.9x
Boardwalk Pipeline Partners LP	BWP	1,211.8	670.2	55.3%	6,420.3	-19.3%	9.6x
Buckeye Partners LP	BPL	4,704.4	754.2	16.0%	11,626.3	-17.5%	15.4x
Crestwood Midstream Partners L	CMLP	2,286.3	393.1	17.2%	3,973.5	-40.7%	10.1x
DCP Midstream Partners LP	DPM	2,706.0	423.0	15.6%	5,193.4	-37.1%	12.3x
Enbridge Energy Partners LP	EEP	6,755.7	1,420.0	21.0%	20,079.2	-13.2%	14.1x
Energy Transfer Partners LP	ETP	46,967.0	4,098.0	8.7%	54,939.8	15.2%	13.4x
EnLink Midstream Partners LP	ENLK	4,039.2	644.5	16.0%	8,000.3	-18.5%	12.4x
Enterprise Products Partners L	EPD	37,085.5	4,886.7	13.2%	71,858.2	-24.0%	14.7x
EQT Midstream Partners LP	EQM	507.4	406.3	80.1%	5,738.6	-4.8%	14.1x
Genesis Energy LP	GEL	2,994.6	226.6	7.6%	5,891.6	-5.7%	26.0x
Holly Energy Partners LP	HEP	343.8	222.0	64.6%	2,687.8	-12.8%	12.1x
Magellan Midstream Partners LP	MMP	2,198.3	1,108.0	50.4%	16,968.6	-23.2%	15.3x
MarkWest Energy Partners LP	MWE	2,052.9	821.5	40.0%	14,072.2	-25.7%	17.1x
Martin Midstream Partners LP	MMLP	1,282.6	157.2	12.3%	1,705.3	-22.8%	10.8x
Memorial Production Partners L	MEMP	460.8	0.9	0.2%	2,228.2	-27.4%	2484.1x
MPLX LP	MPLX	562.2	242.1	43.1%	3,719.5	-24.8%	15.4x
NuStar Energy LP	NS	2,601.7	570.9	21.9%	6,536.7	-17.2%	11.4x
ONEOK Inc	OKE	9,898.3	1,395.4	14.1%	18,813.4	-21.0%	13.5x

Presented in \$000,000s  
Source: Bloomberg L.P.

## Appendix B

## Selected Public Company Information // Midstream Operations

Company Name	Ticker	LTM			Enterprise Value @ 9/30/15	YOY Change in EV	EV/EBITDA Multiple
		Revenues	EBITDA	EBITDA Margin			
Phillips 66 Partners LP	PSXP	245.4	156.6	63.8%	5,029.7	-0.5%	32.1x
Plains All American Pipeline L	PAA	33,191.0	1,925.0	5.8%	22,163.5	-26.9%	11.5x
SemGroup Corp	SEMG	1,817.0	142.5	7.8%	2,844.2	-34.6%	20.0x
Spectra Energy Partners LP	SEP	2,366.0	1,510.0	63.8%	18,638.1	-14.1%	12.3x
Sunoco Logistics Partners LP	SXL	\$14,564.0	\$1,020.0	7.0%	\$11,865.1	-17.4%	11.63x
Tallgrass Energy Partners LP	TEP	447.1	187.4	41.9%	3,509.5	-1.3%	18.72x
Targa Resources Partners LP	NGLS	7,700.3	1,057.9	13.7%	10,758.4	-6.0%	10.17x
TC PipeLines LP	TCP	339.0	255.0	75.2%	4,915.0	-19.2%	19.27x
Teekay LNG Partners LP	TGP	396.0	274.6	69.3%	3,988.5	-31.1%	14.52x
Teekay Offshore Partners LP	TOO	1,025.6	542.9	52.9%	4,076.9	-25.0%	7.51x
Tesoro Logistics LP	TLLP	878.4	447.8	51.0%	6,970.4	31.1%	15.56x
TransMontaigne Partners LP	TLP	147.6	69.4	47.0%	690.5	-24.6%	9.96x
Western Gas Partners LP	WES	1,441.9	662.3	45.9%	8,791.2	-21.5%	13.27x
Williams Partners LP	WPZ	4,349.9	1,904.8	43.8%	39,549.2	126.5%	20.76x
<b>Average</b>		<b>\$5,992.5</b>	<b>\$868.4</b>	<b>33.9%</b>	<b>\$12,268.9</b>	<b>-12.5%</b>	<b>89.19x</b>
<b>Median</b>		<b>\$2,052.9</b>	<b>\$542.9</b>	<b>33.8%</b>	<b>\$6,420.3</b>	<b>-19.2%</b>	<b>13.48x</b>

Presented in \$000,000s  
Source: Bloomberg L.P.

## Appendix B

## Selected Public Company Information // Alternative Energy

Company Name	Ticker	LTM			Enterprise Value @ 9/30/15	YOY Change in EV	EV/EBITDA Multiple
		Revenues	EBITDA	EBITDA Margin			
<b>Solar</b>							
Enphase Energy Inc	ENPH	\$393.1	\$7.3	1.9%	\$150.0	-75.2%	20.4x
First Solar Inc	FSLR	3,262.7	521.6	16.0%	2,838.1	-50.2%	5.4x
Real Goods Solar Inc	RGSE	62.7	-32.4	-51.7%	13.2	-86.2%	nmd
SolarCity Corp	SCTY	300.4	-320.1	-106.6%	6,456.3	-2.2%	nmd
SunEdison Inc	SUNE	2,069.7	-330.4	-16.0%	14,366.1	25.2%	nmd
SunPower Corp	SPWR	2,648.9	247.0	9.3%	3,143.4	-33.0%	12.7x
<b>Average</b>		<b>1,456.2</b>	<b>15.5</b>	<b>-24.5%</b>	<b>\$4,494.5</b>	<b>-36.9%</b>	<b>12.9x</b>
<b>Median</b>		<b>1,231.4</b>	<b>-12.5</b>	<b>-7.0%</b>	<b>\$2,990.8</b>	<b>-41.6%</b>	<b>12.7x</b>
<b>Wind Turbine Manufacturing</b>							
Suzlon Energy Ltd	SUEL	\$177,994.8	\$10,472.9	5.9%	\$0.0	-100.0%	.0x
Gamesa Corp Tecnologica SA	GAM	\$3,234.8	na	na	3,375.4	23.7%	na
Xinjiang Goldwind Science & Te	2208 HK	\$22,565.9	na	na	57,529.3	25.0%	na
Sinovel Wind Group Co Ltd	601558 CH	\$2,048.1	na	na	21,477.6	17.6%	na
<b>Average</b>		<b>\$51,460.9</b>	<b>\$10,472.9</b>	<b>5.9%</b>	<b>\$20,595.6</b>	<b>-8.4%</b>	<b>.0x</b>
<b>Median</b>		<b>\$12,900.3</b>	<b>\$10,472.9</b>	<b>5.9%</b>	<b>\$12,426.5</b>	<b>20.6%</b>	<b>.0x</b>

Presented in \$000,000s  
Source: Bloomberg L.P.

## Appendix B

## Selected Public Company Information // Alternative Energy

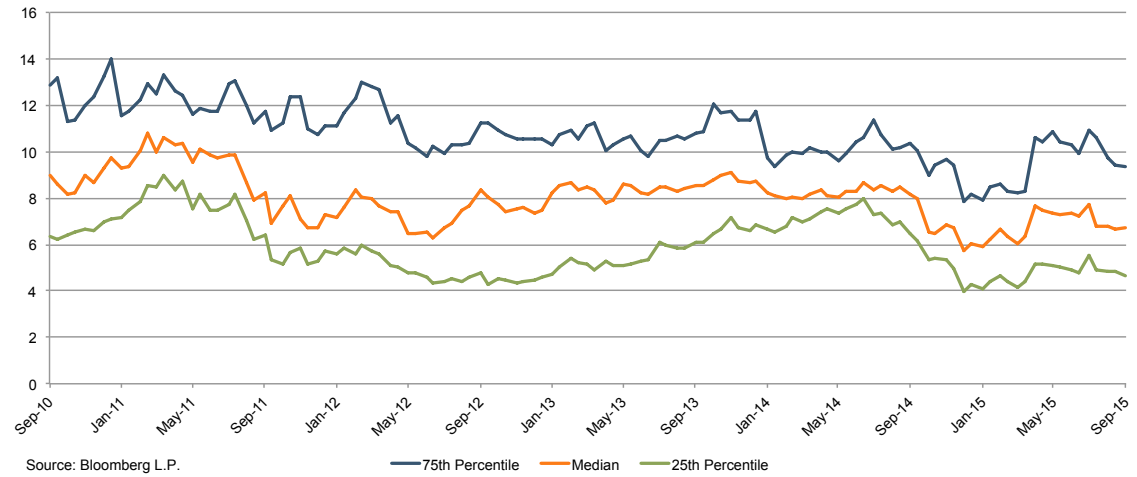
Company Name	Ticker	LTM			Enterprise Value @ 9/30/15	YOY Change in EV	EV/EBITDA Multiple
		Revenues	EBITDA	EBITDA Margin			
<b>Biofuels</b>							
Amyris Inc	AMRS	\$43.6	-\$88.3	-202.3%	\$588.7	27.9%	nmd
FutureFuel Corp	FF	350.3	67.8	19.4%	203.7	-37.1%	3.0x
Gevo Inc	GEVO	34.5	-27.3	-79.3%	42.8	-27.7%	nmd
Green Plains Inc	GPRE	3146.7	239.6	7.6%	994.1	-38.6%	4.1x
Pacific Ethanol Inc	PEIX	965.5	37.1	3.8%	273.8	-19.3%	7.4x
Renewable Energy Group Inc	REGI	1326.6	68.3	5.1%	458.5	1.0%	6.7x
REX American Resources Corp	REX	484.8	92.9	19.2%	256.8	-49.6%	2.8x
Solazyme Inc	SZYM	56.4	-117.6	-208.5%	262.9	-51.1%	nmd
<b>Average</b>		<b>\$801.0</b>	<b>\$34.1</b>	<b>-54.4%</b>	<b>\$385.2</b>	<b>-24.3%</b>	<b>4.8x</b>
<b>Median</b>		<b>\$417.5</b>	<b>\$52.4</b>	<b>4.5%</b>	<b>\$268.3</b>	<b>-32.4%</b>	<b>4.1x</b>
<b>Alternative Energy Overall</b>							
<b>Average</b>		<b>\$12,277.2</b>	<b>\$722.6</b>	<b>-38.4%</b>	<b>\$6,246.1</b>	<b>-25.0%</b>	<b>7.0x</b>
<b>Median</b>		<b>\$1,146.0</b>	<b>\$37.1</b>	<b>3.8%</b>	<b>\$523.6</b>	<b>-30.3%</b>	<b>5.4x</b>

Presented in \$000,000s  
Source: Bloomberg L.P.

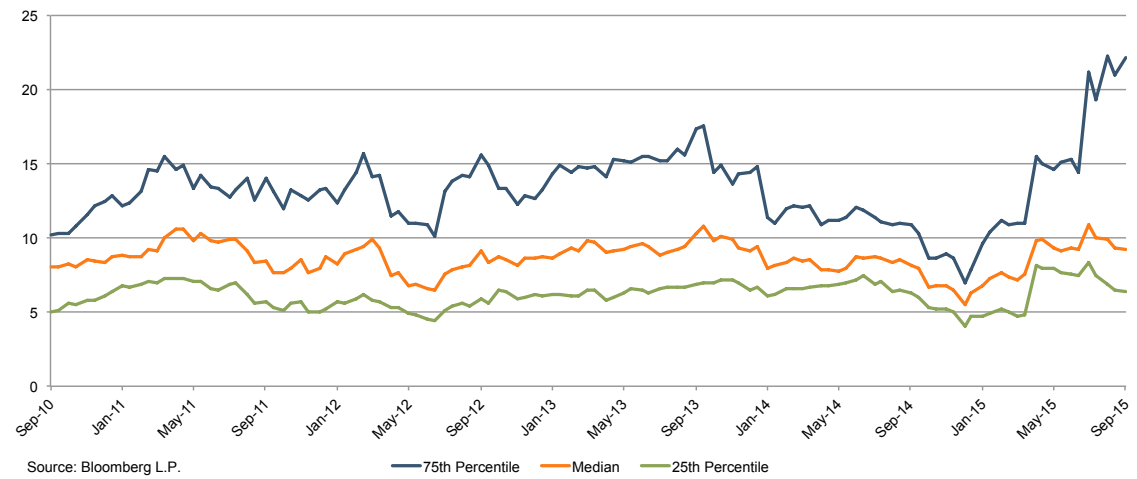
Appendix C

# Historical Valuations

**Oilfield Services & Equipment EV/EBITDA Multiples**



**Exploration & Production EV/EBITDA Multiples**

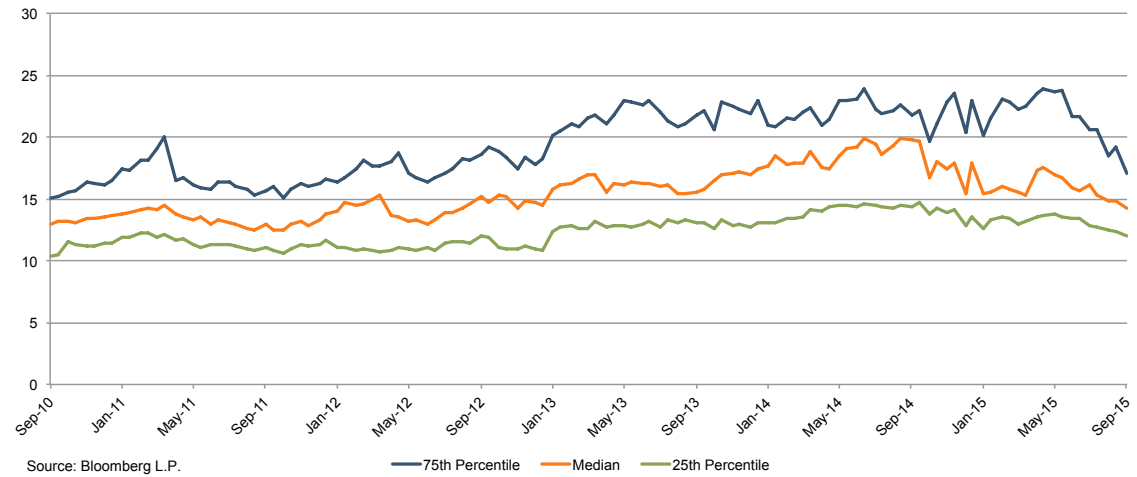




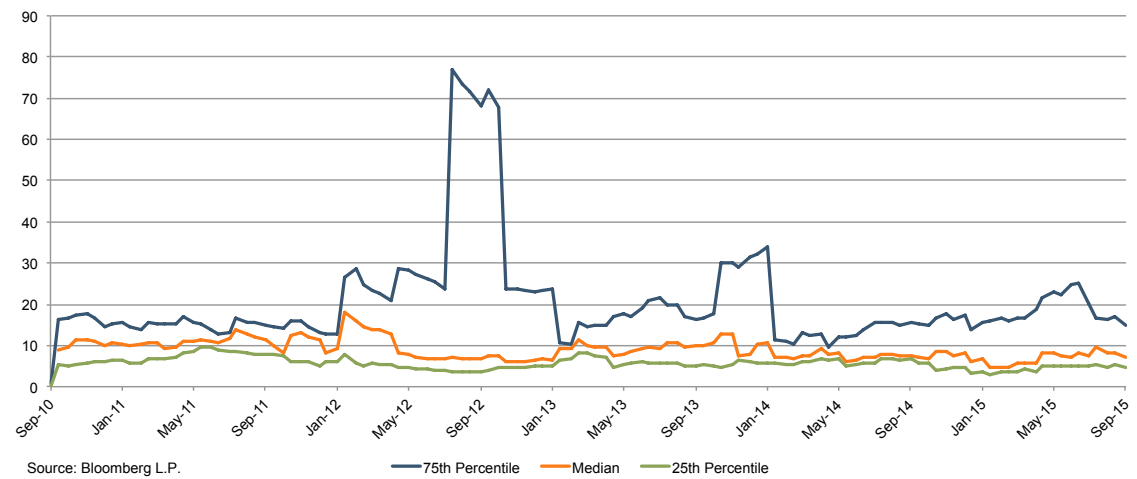
Appendix C

# Historical Valuations

Midstream EV/EBITDA Multiples



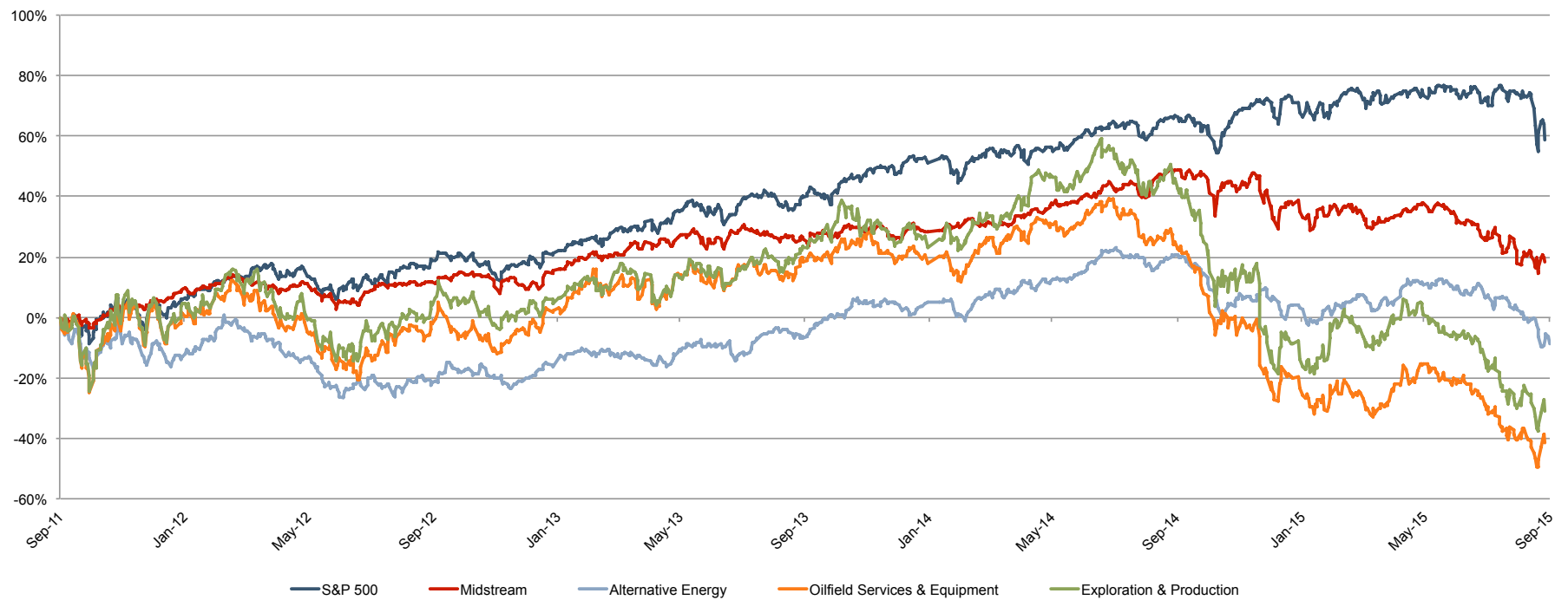
Alternative Energy EV/EBITDA Multiples



Appendix D

# Stock Performance

Mercer Capital's Energy Indice Stock Performance



Source: Bloomberg L.P.  
 Note: Performance shown on a total return basis

Appendix E

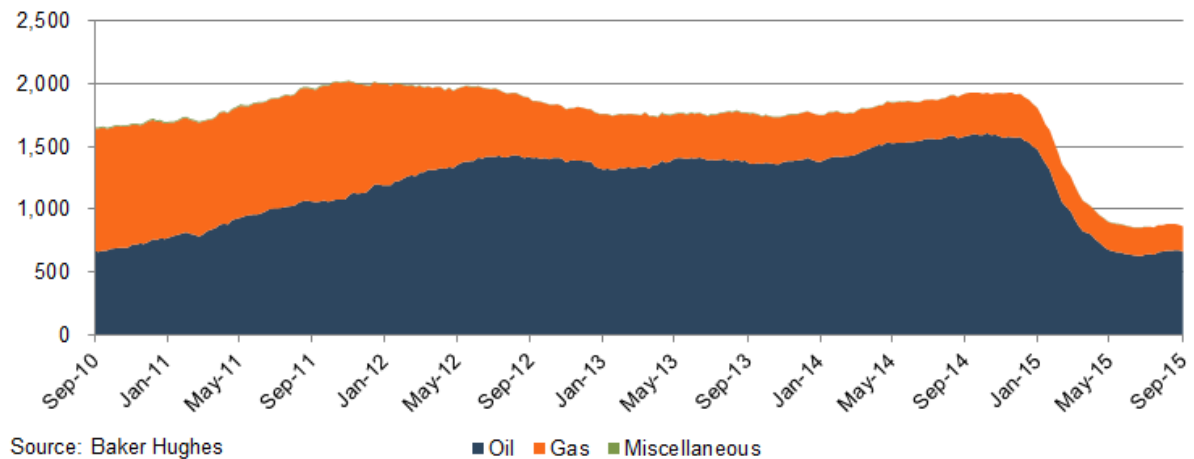
# Rig Count

Baker Hughes collects and publishes information regarding active drilling rigs in the United States and internationally. The number of active rigs is a key indicator of demand for oilfield services & equipment. Factors influencing rig counts include energy prices, investment climate, technological changes, regulatory activity, weather, and seasonality. The number of active rigs in the United States as of September 4, 2015, stood at 864, representing a 55% decrease from the same period in 2014. The decline reflects a slowdown in activity due to lower oil prices.<sup>20</sup>

Texas remains the most active state for drilling, followed by Oklahoma. North Dakota saw the largest increase in activity over the past five years. This was primarily due to drilling in the Bakken formation.

The increase in active drilling rigs over the past several years was driven by horizontal drilling. Horizontal wells, coupled with hydraulic fracturing, are particularly well suited for many of the tight oil and gas plays recently discovered in the United States. Unlike traditional vertical drilling, in which wells are drilled down to a pooled reservoir of hydrocarbons, in tight oil and gas plays the hydrocarbons are trapped in rock formations. Horizontal drilling allows for greater exposure to the formations containing oil and gas, and thus more efficient production.

**U.S. Rig Count by Oil vs. Natural Gas**



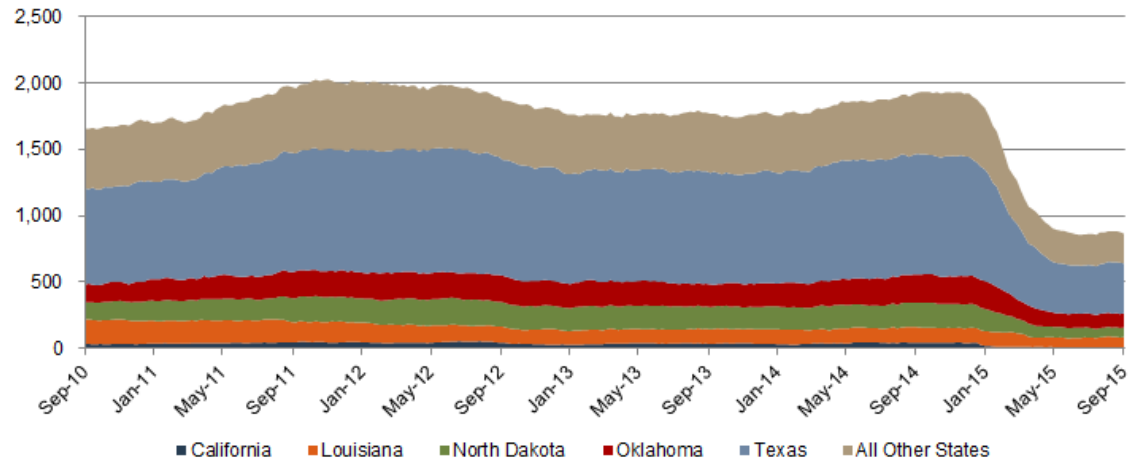
Source: Baker Hughes

■ Oil ■ Gas ■ Miscellaneous

Appendix E

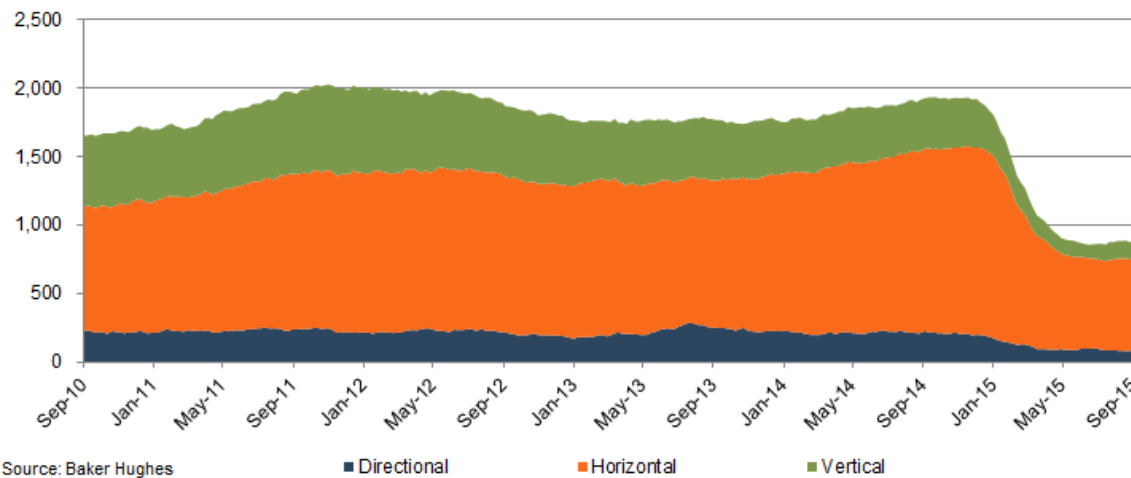
# Rig Count

**U.S. Rig Count by State**



Source: Baker Hughes

**U.S. Rig Count by Trajectory**

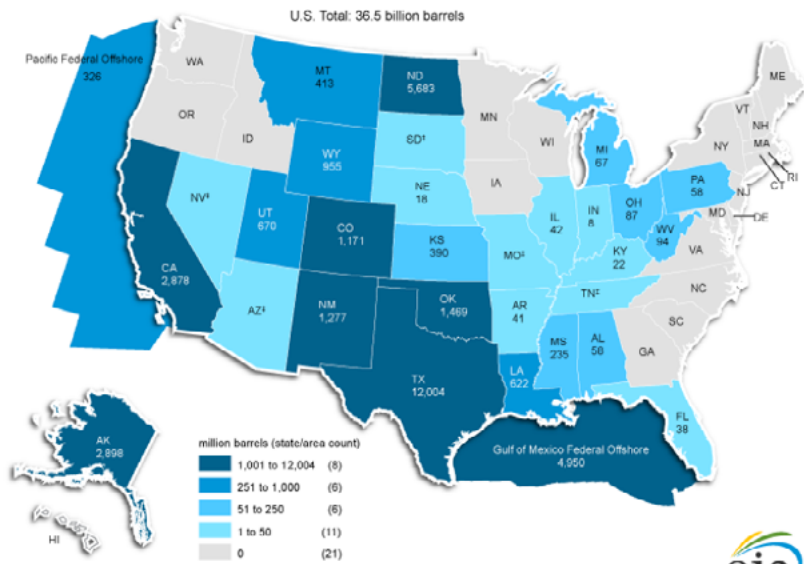


Source: Baker Hughes

Appendix F

# U.S. Oil and Gas Resources

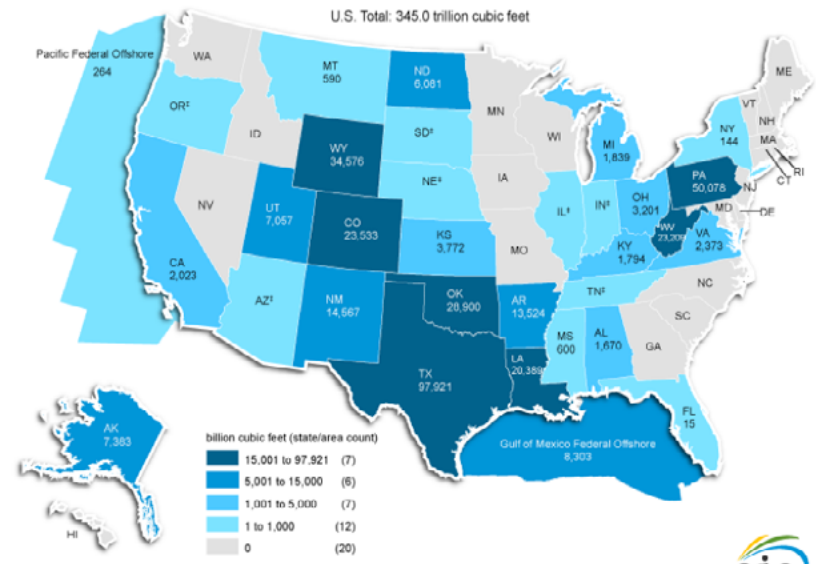
U.S. Crude Oil and Lease Condensate Proved Reserves Map



<sup>1</sup> Data withheld to avoid disclosure of individual company data  
Source: U.S. Energy Information Administration, Form EIA-23L, Annual Survey of Domestic Oil and Gas Reserves.



U.S. Wet Natural Gas Proved Reserves Map



<sup>1</sup> Data withheld to avoid disclosure of individual company data  
Source: U.S. Energy Information Administration, Form EIA-23L, Annual Survey of Domestic Oil and Gas Reserves.



## Sources

- <sup>1</sup> "Oil set for Weakest Quarter Since 2009 as Glut Seen Expanding," *Bloomberg*, September 30, 2015.
- <sup>2</sup> *OPEC Monthly Oil Market Report*, September 14, 2015 & August 14, 2015, ([http://www.opec.org/opec\\_web/en/publications/338.htm](http://www.opec.org/opec_web/en/publications/338.htm)).
- <sup>3</sup> "OPEC: The U.S. Shale Boom is Over," *Business Insider*, September 14, 2015, (<http://www.businessinsider.com/opec-monthly-outlook-september-2015-9>).
- <sup>4</sup> "Oil Market Report", IEA, September 11, 2015, (<https://www.iea.org/oilmarketreport/omrpublic/>).
- <sup>5</sup> "Monthly Oil Market Report", OPEC, September 14, 2015, ([http://www.opec.org/opec\\_web/static\\_files\\_project/media/downloads/publications/MOMR\\_September\\_2015.pdf](http://www.opec.org/opec_web/static_files_project/media/downloads/publications/MOMR_September_2015.pdf)).
- <sup>6</sup> "Oil Oversupply May Finally Be Correcting: Kilduff," *CNBC*, September 14, 2015, (<http://www.cnbc.com/2015/09/14/oil-over-supply-may-finally-be-correcting-kilduff.html>).
- <sup>7</sup> "Oil Patch Braces for Financial Reckoning," *WSJ*, September 16, 2015 (<http://www.wsj.com/articles/oil-patch-braces-for-financial-reckoning-1442274651>).
- <sup>8</sup> Ibid.
- <sup>9</sup> *Bloomberg*, World Proved Reserves, December 31, 2014.
- <sup>10</sup> "Oil Patch Braces for Financial Reckoning," *WSJ*, September 16, 2015 (<http://www.wsj.com/articles/oil-patch-braces-for-financial-reckoning-1442274651>).
- <sup>11</sup> CWEI Earnings Conference Call, August 5, 2015.
- <sup>12</sup> "Oil Patch Braces for Financial Reckoning," *WSJ*, September 16, 2015 (<http://www.wsj.com/articles/oil-patch-braces-for-financial-reckoning-1442274651>).
- <sup>13</sup> Ibid.
- <sup>14</sup> Ibid.
- <sup>15</sup> Ibid.
- <sup>16</sup> "Oil Patch Braces for Financial Reckoning," *WSJ*, September 16, 2015 (<http://www.wsj.com/articles/oil-patch-braces-for-financial-reckoning-1442274651>).
- <sup>17</sup> "Statement of Changes in Beneficial Ownership of Securities", *Bloomberg*, September 9, 2015.
- <sup>18</sup> "Buffett's \$4.5 Billion Bet on Phillips 66 a Winner," *Barron's*, August 31, 2015, (<http://www.barrons.com/articles/buffetts-4-5-billion-bet-on-phillips-66-a-winner-1441048835>).
- <sup>19</sup> "This \$2.1 Billion Shale Deal Will be the First of Many," *Bloomberg News*, May 11, 2015, (<http://www.bloomberg.com/news/articles/2015-05-11/noble-energy-buys-rosetta-resources-for-2-1-billion>).
- <sup>20</sup> Data provided by Baker Hughes. See <http://www.bakerhughes.com/rig-count>.

# Mercer Capital

Energy Industry Services

Mercer Capital has expertise providing business valuation and financial advisory services to companies in the energy industry.

## Industry Segments

Mercer Capital serves the following industry segments:

- Exploration & Production
- Oil Field Services
- Midstream Operations
- Alternative Energy

## Services Provided

- Valuation of energy companies
- Transaction advisory for acquisitions and divestitures
- Valuations for purchase accounting and impairment testing
- Fairness and solvency opinions
- Litigation support for economic damages and valuation and shareholder disputes

Contact a Mercer Capital professional to discuss your needs in confidence.

## Contact Us

**Bryce Erickson, ASA, MRICS**  
214.468.8400  
ericksonb@mercercapital.com

**Timothy R. Lee, ASA**  
901.685.2120  
leet@mercercapital.com

### MERCER CAPITAL

**Memphis**  
5100 Poplar Avenue, Suite 2600  
Memphis, Tennessee 38137  
901.685.2120

**Grant M. Farrell, ASA, CPA, ABV, CFF, CGMA**  
214.468.8400  
farrellg@mercercapital.com

**Eden G. Stanton, CFA**  
901.270.7250  
stantone@mercercapital.com

**Dallas**  
12201 Merit Drive, Suite 480  
Dallas, Texas 75251  
214.468.8400

**Don Erickson, ASA**  
214.468.8400  
ericksond@mercercapital.com

**Taryn E. Burgess**  
901.322.9757  
burgessst@mercercapital.com

**Nashville**  
102 Woodmont Blvd., Suite 231  
Nashville, Tennessee 37205  
615.345.0350

[www.mercercapital.com](http://www.mercercapital.com)

# Erickson Partners

## Merges with Mercer Capital



**Mercer Capital**, a national business valuation and financial advisory firm specializing in Corporate Valuation, Litigation Support, Financial Reporting Valuation, and Transaction Advisory Consulting, and **Erickson Partners, Inc.**, a Texas-based Valuation and Litigation Support firm, announce their merger effective July 1, 2015.

Mercer Capital, with its strong presence throughout the Southeast and Midwest, and Erickson Partners, with its strong presence in Texas and Oklahoma, are a perfect fit.

Both firms maintain the highest standards of quality for financial analysis and client service and believe deeply in hiring and developing the best professionals.

“The culture of both firms is so similar and that was important to us. The professionals of Erickson Partners are well-known in the valuation profession as some of the best and brightest. Their work product and reputation are stellar. This merger not only allows us to broaden our geographic reach but also our industry expertise,” said **Matt Crow**, President of Mercer Capital.

Erickson Partners enhances Mercer Capital’s broad base of industry concentrations with their exceptional history working with and knowledge of professional sports franchises and the energy sector.

“Over our 30 plus year history, Mercer Capital has developed several industry concentrations. By adding the knowledge, insight, and expertise of Don Erickson, Bryce Erickson, and the rest of the professionals of Erickson Partners, we now bring deep experience and insight to a broader range of industries than we could as separate firms,” said **Chris Mercer**, CEO of Mercer Capital.

“Combining with Mercer Capital, we will now be able to offer new or expanded services that complement our existing services, as well as additional industry expertise,” said **Bryce Erickson**, Managing

Director of Erickson Partners. “In addition to our sports franchise and energy industry concentrations, we will be able to offer deep industry concentrations in construction and building materials, agribusiness, manufacturing and financial institutions, which includes depository institutions, insurance companies, fintech companies, asset management firms, and PE firms.”

“The combined firm will have over 40 valuation professionals positioned in five markets throughout the southwest and southeast. Such a deep bench will provide us with a tremendous opportunity to better serve the expanding needs of our clients,” said **Don Erickson**, President of Erickson Partners. “Joining with Mercer Capital gives us national resources that will benefit our clients in Texas and beyond.”

### About Mercer Capital

Mercer Capital is a national business valuation and financial advisory firm offering corporate valuation, litigation support, financial reporting valuation, and transaction advisory consulting services to a national client base. Clients include private and public operating companies, financial institutions, asset holding companies, high-net worth families, and private equity/hedge funds.

### About Erickson Partners, Inc.

Erickson Partners is a professional valuation and advisory firm specializing in business valuation, litigation support, financial investigations and strategic corporate advisory services. Founded by Don & Bryce Erickson, Erickson Partners has served large and small clients by providing complex financial and economic analysis, leading to reasonable valuation opinions that withstand scrutiny.

## CONTACT US

**Z. Christopher Mercer, ASA, CFA, ABAR**  
901.685.2120  
mercerc@mercercapital.com

**Matthew R. Crow, CFA, ASA**  
901.685.2120  
crowm@mercercapital.com

**Donald Erickson, ASA**  
214.468.8400  
ericksond@mercercapital.com

**Bryce Erickson, ASA, MRICS**  
214.468.8400  
ericksonb@mercercapital.com

## COMBINING CULTURES OF EXCELLENCE

### MERCER CAPITAL

#### Headquarters

5100 Poplar Avenue, Suite 2600  
Memphis, TN 38137  
901.685.2120

#### Dallas

12201 Merit Drive, Suite 480  
Dallas, TX 75251  
214.468.2120

#### Nashville

102 Woodmont Blvd., Suite 231  
Nashville, TN 37205  
615.345.0350

[www.mercercapital.com](http://www.mercercapital.com)



# Fairness Opinions and Down Markets

August has become the new October for markets in terms of increased volatility and downward pressure on equities and high yield credit. This year has seen similar volatility as was the case in some memorable years such as 1998 (Russian default; LTCM implosion), 2007 (tremors in credit markets), 2008 (earthquakes in credit and equity markets) and 2011 (European debt crisis; S&P's downgrade of the U.S.). Declining commodity markets, exchange rate volatility and a pronounced widening of credit spreads finally began to reverberate in global equity markets this year.

So far the downdraft in equities and widening high yield credit spreads has not slowed M&A activity. Preliminary data from Thomson Reuters for the third quarter indicates global M&A exceeded \$1 trillion, which represents the third highest quarter on record and an increase of 11% over the year ago quarter. Activity is less broad-based though as 8,989 deals were announced compared to 10,614 a year ago.

Immediately prior to intensified pressure on risk-assets, Thomson Reuters estimated that as of August 13 global M&A was on pace for a record year with \$2.9 trillion of announced transactions globally (+40% vs. LYTD) and \$1.4 trillion in the U.S. (+62%). Within the U.S., strategic buyer activity rose 53% to \$1.1 trillion while PE M&A rose 101% to \$326 billion.

LBO multiples have been trending higher since 2009. The median LBO EBITDA multiple for broadly syndicated large deals was 10.1x through September, while middle market multiples expanded to 10.3x. Debt to EBITDA multiples for LBOs were 6.0x for large deals YTD and 5.5x for middle market transactions.

No one knows what the future holds for markets. Deal activity could slow somewhat; however, a weak environment for organic revenue growth will keep many strategic buyers engaged, while lower prices for sellers if sustained will make more targets affordable for private equity provided debt financing costs do not rise too much. As of October 14, the option-adjusted-spread (OAS) on Bank of America Merrill Lynch's High Yield Index was 6.31%, up from 5.04% at year-end and 4.83% a year ago.

The role of the financial advisor becomes tougher too when markets are declining sharply. Obviously, sellers who do not have to sell may prefer to wait to see how market turmoil will play out while buyers may push to strike at a lower valuation. Questions of value and even fair dealing may be subjected to more scrutiny.

Fairness opinions seek to answer the question whether a proposed transaction is fair to a company's shareholders from a financial point of view. Process and especially value are at the core of the opinion. A fairness opinion does not predict where a security—e.g. an acquirer's shares—may trade in the future. Nor does a fairness opinion approve or disapprove a board's course of action. The opinion, backed by a rigorous valuation analysis and review of the process that led to the transaction, is just that: an opinion of fairness from a financial point of view. Nevertheless, declining markets in the context of negotiating and opining on a transaction will raise the question: How do current market conditions impact fairness?

There is no short answer; however, the advisor's role of reviewing the process, valuation, facts and circumstances of the transaction in a declining market should provide the board with confidence about its decision and the merits of the opinion. Some of the issues that may weigh on the decision process and the rendering of a fairness opinion in a falling market include the following:

- » **Process vs. Timing.** Process can always be tricky in a transaction. A review of fair dealing procedures when markets have fallen sharply should be sensitive to actions that may favor a particular shareholder or other party. A management-led LBO after the market has fallen or a board that agrees to buyback a significant shareholder's interest when prices were higher are examples. Even an auction of a company may be subject to second guessing if the auction occurred in a weak environment.
- » **Corporate Forecasts.** Like the market, no one knows how the economy will perform over the next several years; however, consideration should be given to whether declining equity markets and widening credit spreads point to a coming economic

slowdown. A baseline forecast that projects rising sales and earnings or even stable trends may be suspect if the target's sales and earnings typically fall when the economy enters recession. A board should consider the implications of any sustained economic slowdown on the subject's expected financial performance with follow-through implications for valuation.

- » **Valuation.** Unless markets experience a sharp drop from a valuation level that reflects a widely held view that multiples were excessive, a sharp pullback in the market will cause uncertainty about what's "fair" in terms of value. DCF valuations and guideline M&A transaction data may derive indications that are above what is obtainable in the current market. Transactions that were negotiated in mid-2007 and closed during 2008 may have felt wildly generous to the seller as conditions deteriorated. Likewise, deals negotiated in mid-2012 that closed in 2013 when markets were appreciating may have felt like sellers left money on the table. There is no right or wrong, only the perspective provided from the market's "bloodless verdict" of obtaining a robust market check if a company or significant asset is being sold. It is up to the board to decide what course of action to take, which is something a fairness opinion does not address.
- » **Exchange Ratios.** Acquisitions structured as share exchanges can be especially challenging when markets are falling. Sellers will tend to focus on a fixed price, while buyers will want to limit the number of shares to be issued. The exchange ratio can be (a) fixed when the agreement is signed; (b) fixed immediately prior to closing (usually based upon a 10 day volume-weighted average price of the buyer); or (c) a hybrid such as when the ratio floats based upon an agreed upon value for the seller provided the buyer's shares remain within a specified band. Floating exchange ratios can be seen as straightjackets for buyers and lifejackets for sellers in falling markets; rising markets entail opposite viewpoints.
- » **Buyer's Shares.** An evaluation of the buyer's shares in transactions that are structured as a share exchange is an important part of the fairness analysis. Like profitability, valuation of the buyer's shares should be judged relative to its history and a peer group presently and relative to a peer group through time to examine how investors' views of the shares may have evolved through market and profit cycles.

The historical perspective can then be compared with the current down market to make inferences about relative performance and valuation that is or is not consistent with comparable periods from the past.

- » **Financing.** If consummation of a transaction is dependent upon the buyer raising cash via selling shares or issuing debt, a sharp drop in the market may limit financing availability. If so, the board and the financial advisor will want to make sure the buyer has back-up financing lined-up from a bank. The absence of back-stop financing, no matter how remote, is an out-of-no-where potential that a board and an advisor should think through. Down markets make the highly unlikely possible if capital market conditions deteriorate unabated. While markets periodically become unhinged, a board entering into an agreement without a backstop plan may open itself to ill-informed deal making if events go awry.

A market saw states that bull markets take the escalator up and bear markets take the elevator down. Maybe the August sell-off will be the pause that refreshes, leading to new highs, tighter credit spreads, and more M&A. Maybe the October rebound in equities (but not credit, so far) will fade and the downtrend will resume. It is unknowable.

What is known is that boards that rely upon fairness opinions as one element of a decision process to evaluate a significant transaction are taking a step to create a safe harbor. Under U.S. case law, the concept of the "business judgment rule" presumes directors will make informed decisions that reflect good faith, care and loyalty to shareholders. The evaluation process is trickier when markets have or are falling sharply, but it is not unmanageable. We at Mercer Capital have extensive experience in valuing and evaluating the shares (and debt) of financial and non-financial service companies engaged in transactions during bull, bear and sideways markets garnered from over three decades of business.



**Jeff K. Davis, CFA**

jeffdavis@mercercapital.com

615.345.0350