



HOULIHAN LOKEY

ENERGY SERVICES: CHALLENGES AND OPPORTUNITIES

Situation Overview and Real-Time Considerations



Energy Services Market Update

Houlihan Lokey presents an assessment of the impact of recent macro events on the energy services industry, immediate strategic/financial challenges and priorities for companies and investors, near- to immediate-term transaction considerations, and how the firm can assist in this evolving and dynamic market.

Observations







In recent weeks, COVID-19 (better known as coronavirus) has globally sent shock waves through markets and captured the attention of the world. Since mid-February, the outbreak has accelerated and infections have become widespread, resulting in significant market volatility that is expected to continue in the near term. Substantial disruption to business operations has occurred, and all sectors of the economy have been impacted, including the energy services and general oil and gas industries. On March 27, 2020, Congress approved the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) to provide financial assistance to individuals and businesses, which, in aggregate, greatly exceeds the financial package Congress previously enacted to address the 2008 financial crisis. The act, which is the third major piece of bipartisan legislation to address the crisis created by the COVID-19 pandemic, includes approximately \$2 trillion in assistance to individual and businesses. While stimulus efforts are progressing, it is impossible to predict how long the outbreak will last, as well as the lingering effects on businesses, the economy, and the credit and M&A markets.

On the supply side of the equation, in March 2020, Saudi Arabia retaliated against Russia's refusal to join other OPEC members in cutting production by reducing its crude oil price and increasing output. As a result, both Brent and WTI spot prices dropped precipitously into the sub-\$25/bbl range.

With concerns of the extent and duration of the March 2020 commodity price collapse and demand impacts related to COVID-19, U.S. operators are cutting production, and both E&P companies and oilfield service firms are reducing capital spending. The general near-term outlook of the energy services industry is varied to some degree by subsector. However, one certainty is that volatility will likely persist until the overall impact of COVID-19 and other macro events can be determined.

As industry participants navigate these unprecedented times, there are clearly a number of challenges and opportunities that will arise. The most immediate considerations for companies and investors in the space are:

Defensive/Stabilization Priorities

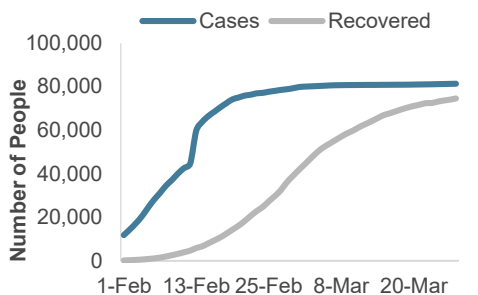
-  Ensuring employee/partner health and safety
-  Assessing near- to intermediate-term business impact and evaluating "downside" scenarios
-  Optimizing the cost structure
-  Managing liquidity, maturities, and covenants
-  Evaluating debt restructuring alternatives
-  Evaluating activist takeover-defense considerations

Offensive/Optimization Priorities

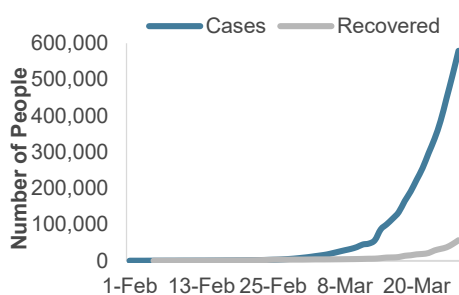
-  Identifying potential new sources of capital
-  Evaluating value-enhancing liability management strategies
-  Pursuing opportunistic M&A, including potential consolidation opportunities and strategic add-ons
-  Evaluating divestiture opportunities, particularly for noncore assets

Energy Services Market Update (cont.)

COVID-19 Cases (China)



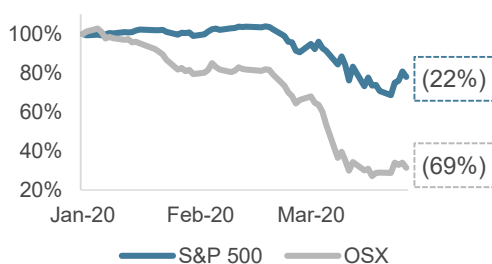
COVID-19 Cases (Ex-China)



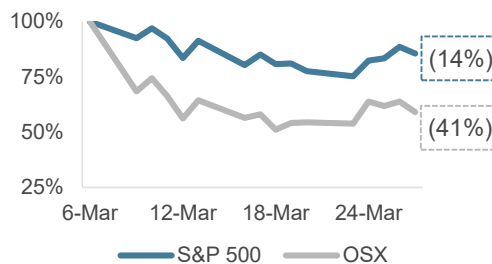
Considerations

- China, the origin of COVID-19, has stemmed the increase in cases
- Meanwhile, “flattening the curve” remains the order of the day, particularly in Europe and the U.S. Until the curve begins to flatten, market volatility will continue

S&P 500 and OSX YTD...

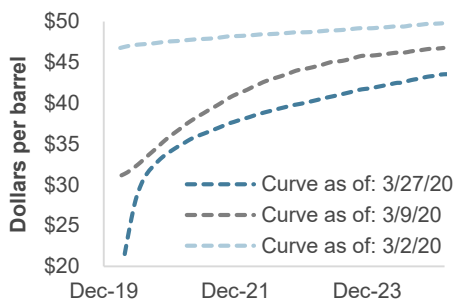


...and Since OPEC+ Policy Change

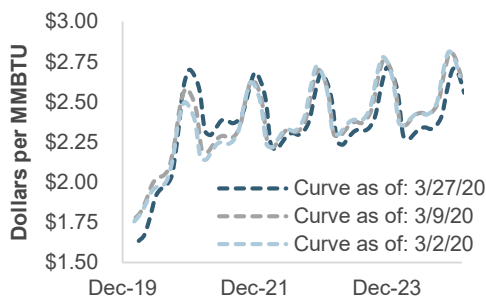


- The markets have seen extreme volatility in the past few weeks, which will likely continue until some degree of certainty sets in
- The OSX is down 69% YTD relative to the S&P 500, which is down 22% YTD

Oil Forward Curve

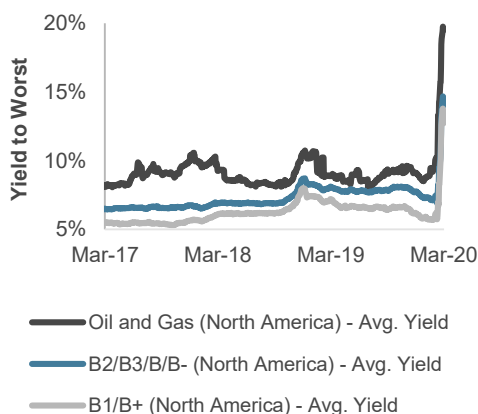


Natural Gas Forward Curve

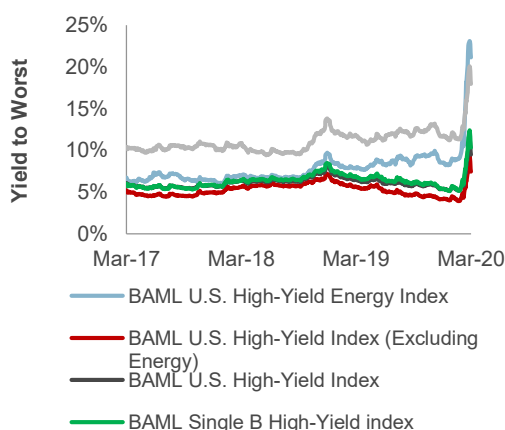


- Oil spot prices have wildly fluctuated in the past few weeks as news regarding COVID-19 and OPEC+ discussions have shocked the market
- Notably, the oil forward curve, which has significant valuation implications, has shifted significantly downward

U.S. Leveraged Loans—Energy



U.S. High-Yield—Energy



- Debt markets in the energy space were tenuous at best before the events of the past few weeks and are mostly closed for energy service issuers at this juncture
- Private debt options are extremely limited, as most investors who will lend to the space at all are in “wait-and-see” mode until the market finds stability

Real-Time Market Intelligence

Volatile market conditions have created a great deal of uncertainty for businesses, particularly in the energy services sector. Key market trends and observations are outlined below.

M&A

- Deal volume and pace of execution have slowed dramatically
- No cash buyers; deals will require significant structured solutions to close (stock for stock, structured equity, seller paper, bridge financing, etc.)
- For the few deals that are currently in-market, terms are being reevaluated (economic and legal terms, particularly MAE/MAC clauses) with extended timelines and financing contingencies
- Many change-of-control transactions will be effectuated through secondary-market purchases of distressed debt
- Strategic consolidation and a rationalization of capacity is required across the industry. Newly restructured companies might lead the way, including post-reorganized companies

Capital Markets

- Economic implications of COVID-19 continue to manifest in the debt markets in the form of credit rating downgrades and an increase in debt trading at or below distressed levels
- Nontraditional sources of capital becoming more prevalent (direct lending funds, diversified asset managers, finance companies, insurance companies, family offices, mezzanine funds, mutual funds, pension funds, structured equity providers, and special situations/opportunity funds)
 - Limited dry powder for unlimited opportunities
- Capital providers looking for good companies with bad balance sheets; differentiated and defensible platforms
 - Near-term structured liquidity solutions/rescue financing
 - Opportunistic M&A
 - Private investments in public equities (PIPEs)
- Liability management strategies will be important to evaluate
 - Amendments, consents, repurchases, tenders, exchanges, etc.

Debt Restructurings

- Expect to see a wave of liability management, liquidity enhancing transactions, and comprehensive balance sheet restructurings within the near- to intermediate-term
- Capital structure challenges are exacerbated by the depressed commodity price environment
 - Liquidity, financial covenant compliance, upcoming debt maturities, and debt capacity are important considerations
- Current market conditions may limit out-of-court solutions, forcing many companies to pursue an in-court process
 - Chapter 11 plan of reorganization, Section 363 sale process, or liquidation
- Optimal solutions will reduce debt service and optimize asset base while positioning for post-reorganization strategic alternatives

How Houlihan Lokey Can Help

Our firm is extremely well equipped to help our clients navigate these uncertain times. We respond quickly to challenging situations and are constantly helping clients analyze, structure, negotiate, and execute the best possible solutions from both a strategic and a financial perspective.

Integrated Special Situations and Liability Management Approach

Financial Restructuring

- No. 1 Global Restructuring Advisor
 - Restructuring debt/equity
 - Debtor-in-possession (DIP) financing
 - Plans of reorganization, §363 M&A
- Worked on more than 175 restructuring-related transactions in 2019 on behalf of companies, their creditors and shareholders, and other constituents

Mergers and Acquisitions

- No. 1 M&A Advisor for All U.S. Transactions
 - Sellside and buy-side advisory
 - Partial sale or divestiture
 - Joint ventures
 - Strategic alliances
 - Special committee advisory



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Special Situations and Liability Management

- ***Combines relevant and diverse capabilities under one roof***
 - One firm ensures seamless execution
 - Independent advice
- Allows for simultaneous pursuit of multiple paths
 - Liability management, comprehensive refinancing, rescue financing, out-of-court restructuring, asset/business sales, etc.

Houlihan Lokey's approach to special situations and liability management is to utilize expertise across business units to best advise its clients in the most challenging of times

Capital Markets Solutions

- Largest capital markets team on Wall Street at a non-balance sheet bank with ~45 professionals
- Raised more than ~\$11.5 billion across ~55 transactions during 2019
 - Private placement of senior and subordinated debt, structured equity, off-balance sheet financing/sale leaseback transactions, and growth equity

Valuation and Diligence

- No. 1 Global M&A Fairness Opinion Advisor Over the Past 20 Years
 - Fund advisory
 - Transaction opinions
 - Financial and tax diligence
 - Opportunistic tax planning
 - Dispute consulting
 - GAAP and SEC advice
 - Corporate valuations

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