

## M&A Outlook 2018

### Oil & Gas

# AS WE ENTER THE CUSP OF SUMMER 2018, WE CAN TAKE THIS OPPORTUNITY TO REFLECT ON BOTH THE OIL AND GAS M&A INDUSTRY IN THE PREVIOUS YEAR OF 2017 WHILST SIMULTANEOUSLY LOOKING AHEAD TO WHAT WE CAN EXPECT FOR THE SECOND HALF OF 2018.

The oil and gas industry in 2017 can be summarised in three key factors. Firstly, oil prices hovered between \$50-60 per barrel reflecting a new found stability between supply and demand. Secondly, overall M&A deal values in 2017 were lower than 2016, indicating we should see more focus on internal organic growth through extraction of existing assets. Thirdly, the United States has seen a continued increase in oil production and exports. On the M&A side in 2017 we saw that consolidation was the key theme. Upstream transaction value in the US for instance was valued at \$64bn, falling short of the 2008-15 average of \$69bn. \$11bn of deals in the US were financed by private funding which was invested into 63 energy ventures. “Permania” was a highlight of the 2017 M&A year, with intense bidding to secure assets in the west basin of eastern New Mexico.

According to 1Derrick COO Mangesh Hirve, “A significant decline in E&P company stock prices made it more expensive for producers to use their equity to fund large acquisitions. However, sub-billion M&A activity level remained solid, with the number of transactions between \$100 million and \$1 billion increasing from 16 in 2Q2017 to 17 in 3Q2017 and 20 in 4Q2017.” Mid 2017 saw shale deals increase, one of which was EQT Corp’s \$8bn buyout of competitor Rice Energy to create the largest natural gas producer in the States, looking to triple their combined output. A second highlight of the year was China National Petroleum Company paying \$1.8bn and China Energy Company paying \$0.8bn for onshore concessions in Abu Dhabi. Another interesting development was the involvement of private equity in M&As, as they accounted for 28% of total acquisitions in 2017. The closing 2017 year ended strong with approximately 863 deals completed globally which amounted to a total of \$223bn.



If we follow 2017's activity and the continued strength in oil prices, we can expect the prices of oil to remain strong for Q2 of this year. Macro-economic as well as political factors such as the geopolitical tensions in Yemen, Syria and Iran will ensure the Brent benchmark for crude at \$68 will hold firm. Prices surged in the leadup to and execution of the missile strikes in Syria, spearheaded by the trifecta of the UK, France and the US. Donald Trump's decision on whether to renew sanctions on Iran later this month is expected to have further impact on prices. However, factors could cause the market to correct crude prices in the second half of the year. For example, US oil production consistently rising to record highs, and the expectation that the oil market will swing back into surplus by the end of the year and remain oversupplied into the next year.

OPEC are set to struggle for the rest of the year as well. Production cuts have been seen and are expected to continue until November 2018, but with an option to be reviewed in June. Saudi Arabia along with other OPEC members are currently looking to protect at minimum a \$60 benchmark price on oil to balance their economies. Competition from the United States however, will put pressure on OPEC's market share and influence, with US production increasing this year to 1.2 million barrels per day. We are seeing a struggle between the OPEC and Russia attempting to stabilise the market and keep oil prices consistent, against the United States flooding and oversupplying the market.

On the M&A front it is likely that we will see a continuation of a cautious and consolidated approach, with the optimization of existing assets. M&A's activity therefore looks to be timid and more strategic based on last year's data, larger companies will be searching for efficiencies of scale from high-return assets. We can also consider that over-leveraged smaller companies can create more inventory value by combining with larger producers, as development is accelerated, and output is increased.

The biggest players which we can expect to see in the M&A market this year include Total and BP, with the former looking for low cost-long term upstream assets. In 2017 Total acquired Maersk Oil \$7.45bn, which could set a precedent for further M&A activity this year. BP's current project pipeline is beginning to thin, and they may look to refresh their project portfolio this year. However, overall industry projections seem to suggest that oil companies place emphasis moves that improve long term output. There is also the possibility that state-run oil companies in China and Russia may be involved in deals, and private equity firms will continue to seek more investment opportunities in the US and Europe.

Overall there are several industry indicators that we can look out for in 2018. 2017's M&A precedent suggests we will see strategic moves across the industry, which are planning to maximise long term returns. Deals will likely continue to take place across the United States which is looking increasingly attractive for investors. Private equity, and state-run oil companies are also expected to be involved in acquisitions as well. There will be continued strong shale output from the United States alongside a sluggish performance from OPEC, which will attempt to protect oil prices and prevent oversaturation in the market.



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