

10th Annual  
**Private Company  
Energy Conference**  
**Recap**



SIMMONS ENERGY

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## OIL SERVICE 10TH ANNUAL PRIVATE COMPANY CONFERENCE RECAP

### Conclusion

We recently convened for our 10th Annual Private Energy Conference at the Pierre Hotel in New York City. This event originated as a small ~16 company conference in the basement of the New York Hilton, but as investor appetite for private company perspectives blossomed during the 2011-2014 time frame, so too did the size/scale of this event. Now, however, the investor registration list, while still commendable, has transitioned largely to private equity and credit investors, a sign of the times as oil service is not at the top of most equity-investors' Christmas wish-lists. That said, industry attendance remains solid as we are thankful for the over 80 energy companies who attended this highly unique and differentiated event. Moreover, we are always appreciative of the candor conveyed by our panelists.

**What Did We Learn? First and no surprise, market conditions remain weak.** Leading edge pricing commentary for pressure pumping and other L48 services confirmed our previously published views, including a ~10% decline in pumping pricing, relative to Q3'19 rates, for new dedicated-type arrangements. The broader theme of a seasonal slowdown is also very real with multiple panelists noting customers pushing jobs from Q4 to Q1. Many panelists do, however, anticipate a rebound in activity in Q1, although the magnitude of such rebound remains unclear. Compressing capital spend on the part of oil service enterprises is also beginning to take its toll on our OEM and packager contacts. To that point, one has witnessed a ~90% reduction in EBITDA y/y in 2019. Stocks, we suspect, largely recognize this.

**While the market backdrop remains challenging, many of our panelists are still growing their respective enterprises.** Some are adding capacity due to strong performance and customer relationships, while others are introducing new products which further drive drilling and completion efficiencies. Collectively, a basket of our OFS panelists will enjoy a better 2019 than 2018 and some anticipate further improvement in 2020. In other words, the OFS market remains nuanced and casting an entirely negative view on the industry is likely inappropriate. Rather, knowing which pole to tie your horse to remains the right strategy.

**For service companies, the most concerning view conveyed at the conference came from our E&P attendees, all of which expect the mantra of capital discipline to remain should oil prices migrate to the \$60-65/bbl range heading into 2021.** They anticipate their budgets would still be based on a \$50-\$55/bbl price deck, despite higher oil prices. In other words, higher cash flows attendant to higher commodity prices would likely be returned to shareholders or used to reduce debt, as opposed to increasing activity. This commentary, if applied broadly to all E&P's, would suggest a flattish environment for the foreseeable future.

**Attendees reported somewhat diverging views regarding leading-edge interest in e-frac.** Some report slowing inquires as E&P clients manage cash flow and are unwilling to engage in LT commitments. Others, notably OEMS, disagree. Most, however, did agree with respect to medium-term prospects for electric, concurring that e-frac will comprise ~10-15% of the total frac market over the coming years (although one believes that estimate is conservative), not ~25-30%, as espoused by some earlier this year.

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### INDUSTRY RISKS

Cannibalized equipment, costs of rebuilds, and the oversupply of frac fleets. The oversupply of frac sand and the potential for declining service intensity.

### Additional E-Frac Thoughts

The depressed state of the frac market does not lend itself to E&P's embracing take-or-pay frac contracts, a necessity for pressure pumping companies wishing to build electric fleets. To that point, one pumping panelist stated it would not build a new fleet without a contract and could not justify building a fleet at today's spot prices.

Fuel savings are real according to one contact. It noted 40-50% savings using CNG and as much as 80-90% using field gas. Similarly, an E&P panelist who has used an e-fleet claimed it saved ~\$250k in fuel per well. There are still skeptics, however, another attendee (without experience operating an electric fleet) questioned whether advertised results corresponded with reality.

The E&P company who has used an e-fleet did acknowledge move times were an issue, one exacerbated by its 2-3 well pad design. With more wells per pad, it believes move times would have been less of a challenge. Our sense is the technology worked, but perhaps it would have been more effective with a different pad design. To that point, one e-frac company stated it has an average move time of ~17 hours.

Running e-fleets off of the grid is not an option according to multiple players because of the magnitude and timeliness of power needs. A turbine OEM stated the start-up of a frac operation creates a power surge, which could be at risk of overpowering a localized electric grid. Frac fleets would also likely not be a priority for power companies, relative to schools/hospitals. If E&P companies were to construct their own grids, it could solve some of these potential issues. But this type of investment is expensive. One panelist believes it is cheaper to run off a natural gas generator than off of the grid and attests ~10% of fleets today can operate using natural gas.

The time required to set up a gas turbine has improved for one panelist and now takes just one hour. It believes the total cost of ownership is lower for an electric fleet than a conventional one over time, in part due to the need to replace diesel engines for conventional fleets. It expects start-up rental turbine players to enter the market next year. Purportedly, massive companies which offer temporary power to other industries view this as an opportunity.



Ben Bodishbaugh, CEO, Evolution Well Services



Curtis Philippon, CEO, Certarus Ltd.



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### Activity & E&P Spending

Appalachian activity will be challenged in 1H'20, according to one attendee. Another feels better about Q1 bookings across its regions of operation than it did a few months ago. A third expects Q1 activity to improve sequentially, but does not expect a consequential bounce in the first few weeks of January. A compression panelist expects compression demand to decrease y/y, but to contract by a less meaningful percentage than completions and/or drilling activity.

While much is made of RFP “season”, our supply chain contacts are constantly reviewing their costs and essentially view RFP season as a year-long event.

### Service Pricing

One E&P panelist believes we are near the bottom with respect to frac pricing. One pumper has parked equipment due to low pricing. It expects the market to recover early in 2020 and more so by mid-2020 but still is not confident in a pricing rebound. More positively, the closure of a facility in El Reno by one prominent pumper sends a message that this company will not “burn the village down”, according to another.

In general, pricing is more volatile in the Permian versus Bakken, because of the steadiness in activity for the latter while a good service company in the Permian may not be a good service company in the Bakken - preferred vendors vary by basin.

CT and high spec drilling were tight markets in early 2019. Less so today, according to an E&P panelist. CT pricing has decreased in every month of 2019, according to a service company panelist. Another believes leading-edge high-spec day rates are now near \$20k (although it does acknowledge examples of pricing closer to the high teens) down from close to \$25k a year ago. This driller is one of a few which has constructed new build rigs over the past few years, in part because it serves as its own contractor and in part because it believes its modular design allows for faster rig moves as compared with a box-on-box design.

Last mile pricing has decreased 10-12% YTD, but has held flat of late, according to one market participant. Another's fishing and rental margins have remained robust.



*Tracie Stone, Director, Global Supply Chain, Marathon Oil Corporation (MRO)*

### Efficiencies

Days to spud for one player is down ~20% from 2017 levels while wells drilled per rig per year is up ~10% for another. Further efficiency improvement is expected in 2020 for multiple panelists, with more upside in completions efficiencies than drilling efficiencies. Specifically, one E&P does not expect completions efficiencies to improve in 2020 at the rate they did in 2019. Smaller sand and design changes were larger factors in its efficiency improvements than any specific action from a pumper.

According to a pumper, the range of acceptable pumping hours has increased from 12-14 hours per day to ~20. The implication: more efficient frac crews reduce the need for industry horsepower. Moreover, faster crews leads to expedited equipment attrition. One frac panelist believes the pressures in the Delaware are too high for pumpers to consider purchasing and refurbishing old frac equipment for deployment in that basin.

Operators noted a willingness to employ vendors in financial distress as long as they hit efficiency targets. That said, they are paying attention to the risk/reward of using such distressed providers.

### Water

According to one panelist, the ultimate water midstream business model will include long term agreements, hard pipe assets, treatment and recycling. As evidence, one water midstream player previously focused primarily on disposal is now less concerned about its business being

cannibalized by recycling. Instead, it views recycling as a margin accretive opportunity, enabled by legislation which dictates water midstream companies take title of water: land owners do not have any claim to water once it is transferred to a water midstream player. However, because of land owner interactions, some water midstream players do not want to enter the source water business, to avoid competing with their land owners who often sell fresh water.

Rising recycling demand has been enabled in part by both the volume of recycling on the fly facilities increasing and the time to construct such facilities decreasing, as well as more and more E&P's treating water less intensively than they used to. Two panelists claim the industry is shifting from utilizing small, mobile facilities for recycling to larger, semi-permanent ones.

In prior years, recycling was a hypothetical construct. Now it's a reality. Today beneficial reuse and alternative disposal are transforming from hypothetical construct to reality: one player is evaporating water for a super-major and believes it could eventually utilize the heat generated from electric frac fleets to assist in its evaporation efforts. Another highlighted that it evaporates 1-2% of its water volumes set for disposal and that it has removed ~300k trucks from the road, highlighting the ESG benefits of the water midstream industry.

With respect to CapEx, water midstream is likely an anomaly in 2020 with capital spending likely increasing y/y for most players. One in particular will triple its CapEx budget next year to keep up with its customers.



Aron Marquez, CEO, Wildcat Oil Tools

### Other

According to one wireline player, customers want to shoot integrated guns because they reduce runs per misrun, all else equal. But the cost of the guns and the constriction of the type of charges that can be used with some integrated gun options prevents this company from using these guns - the efficiency benefit is outweighed by the cost. It would be more likely to use integrated guns if it entered a new basin and did not establish a gun shop (gun shops are less necessary when using integrated guns).

One panelist believes dissolvable plugs are too expensive and too inconsistent to allow for a significant shift in adoption over the next 1-2 years.

There is an increasing focus from large operators on electric compression and automation, according to one panelist.

Reasons for limited service M&A to date: (1) balance sheet leverage; (2) egos and (3) relative valuation. Our take: a failure to consolidate = years of pain.



Danny Jimenez, CEO, Gradient Energy Services

IMAGES FROM THE PRIVATE COMPANY ENERGY CONFERENCE



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### Analyst Certification — John Daniel, Sr. Research Analyst

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