



Executive Q&A

With Terry Newendorp, Chairman and CEO, Taylor-DeJongh

Talking with
Ross Stewart Campbell, CEO, The Oil Council

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Ross Stewart Campbell (RSC) from The Oil Council: Terry, great to see you again, many thanks for joining us. As we usher in 2010 I thought we'd begin by gauging your general thoughts on 2009, and what was for many a rollercoaster year.

RSC: With the recent global economic and financial crises there's a need for us to learn from past mistakes, yet we are now witnessing more underinvestment in the industry, particularly in exploration. What are your thoughts on this and do you foresee another oil price spike and/or supply crunch in the future as a result?



Terry Newendorp (TN) from Taylor-DeJongh: Thanks, Ross. It's great to see you as well. Happy New Year. We did have a roller coaster in 2009, with oil rocketing down to the \$30's after hitting an all-time high just half a year before. With the banks dried up and capital markets closed, we expected a lot of deals to be transacted by mid-2009, but the widely diverse views as to the forward price curve, kept buyers and sellers of assets far apart. By the 3rd quarter, with oil stabilized around \$75/bbl, transactions started to get done. And the 4th quarter saw some moves on the buy side by ExxonMobil and portfolio rationalization by even big boys like ConocoPhillips.

TN: The smaller guys cut back very significantly in 2009, and their capital plans for 2010 are down again. There is heavy commitment to the shale gas plays in USA, so if total capital budgets are down by say, 20-25% overall, but the Marcellus shale commitments are a large part of what makes up even that spend plan, then a lot of places in the world are going without adequate investment. The oil industry is a long-term investment/reward industry. Under-investment doesn't show up for a few years and is manifest in reduced supply. So, as the global economy picks up speed over the next couple of years, the demand-supply gap will get closed, and the result will be another price spike within a couple years. I have seen plenty of articles opining that we'll never see \$100 oil again in our lifetimes, but the demand-supply balance will rapidly close and this 2-3 year period of underinvestment will catch up with us.

RSC: You and your team work at the coalface of finance, capital and investment. How has investor appetite for oil and gas changed over the past 12 months? Which companies / countries are now investing heaviest in tomorrow's industry and how might this affect future market dynamics?

RSC: Of course you need capital to invest and with only a few sources of capital currently being available what is your outlook on financing and capital raising in 2010? When, if at all, do you see sufficient access to the global capital markets re-opening to everyone?

TN: Oil (and gas) price volatility was scary for financial value investors. The IOCs, especially the super majors, held their budgets and spend plans pretty close to forecast. Large independents kept their spend-plans really focused on their highest value assets. The small caps have been hit hard with lack of access to capital markets such as AIM, and by an extended "freeze" at the banks. China, as we all know, was a more aggressive player for companies, not just single assets. Their pricing does not correlate with an IOC forward price curve, as it is access to and quantity of reserves (P1 and P2) that they are seeking, and that makes it difficult to compete with them on a price basis.

TN: The IOCs have access right now. Most Independents do as well. The smaller balance sheets are the ones with the impaired access to capital markets. If oil stays stable trading around \$75 +/- \$5 and we continue to pull the big economies out of recession, then some companies with well-placed assets and solid operating records, should be able to get back to some bank lending and some (less frothy) public market access in 2H10.

"Investment in E&P is holding the course only with the largest IOCs and a few large Independents."

RSC: We saw an increase in deal flow at the end of 2009, particularly in M&A and capital



placements, what volumes, sizes and types of deal flow are you and your team forecasting in 2010?

TN: We think that the M&A flow that many predicted would happen last year will finally show up in 2010. We think there will be some “needle-moving” deals by a few IOCs. There will be fewer “marginal” assets trading hands, because it is difficult to get investors to accept now that just because someone has lease rights somewhere, there will be an inevitable gain in value.

“I believe that Dubai is a real estate bubble, not a natural resource or commodity crash.”

RSC: *Risk is now front of mind with every investor and lender. How has the financial risk landscape evolved over the past 12 months? And do you think oil and gas company executives, as well as oil and gas investors and financiers, completely understand this landscape when approaching new financing, investments and acquisitions?*

TN: I think that’s the extension of my preceding comment. While it is true that a number of investors are moving their dollars into commodities, especially oil, that doesn’t mean that they are willing anymore to just buy into undeveloped prospects. I think that the IOC managements certainly understand this. I think that a lot of mid-market companies may be thinking that “pretty soon” the banks will be back lending to them. I think that the closure of the CDO market is still going to be problematic for the commercial banks who seek to package large sized debt financings for development projects. As for Private Equity going into the oil & gas sector, there is still a lot of money out there looking for deals, but they are much more “picky” about the transactions than in 2007-2008. Mezzanine debt with warrants and kickers are getting to be pretty common now, as financial investors insist on steady cash flow on their investments.

RSC: *Looking at the old adage of ‘size matters’ how important is size for today’s oil and gas companies? Is bigger really better?*

TN: If “big” means “portfolio diversity”, then it definitely matters. One of the key reasons that small cap companies have been hit so hard by this market, is that they tend to have relatively few prospects or assets, and those may not be in production and therefore generating cash flow. Operational optionality is really crucial.

RSC: *With this in mind Terry what advantages do small and mid-cap independents have over large IOCs and NOCs in today’s markets?*

TN: Well, in order to seize their traditional advantage of being small and nimble and able to “take chances” and find new fields that the IOCs haven’t been able to

tap yet, many small and mid-cap companies are going to have to strengthen banking relationships, shed peripheral assets, and focus on cash-producing deals. Right now, the small cap guys are mostly in a pretty rough spot, if they haven’t had time to get assets into production.

RSC: *Recent problems in the Middle East and specifically in Dubai have stirred investors’ concerns about the future of the region. Taylor-DeJongh have a proud history of operating in the Middle East now for over 20 years. What in your opinion went wrong in Dubai and do you see any long-term ramifications on the region’s oil and gas industry and its dynamics?*

TN: I believe that Dubai is a real estate bubble, not a natural resource or commodity crash. It is noteworthy that Abu Dhabi, which is where the bulk of UAE’s oil is, has been able to provide liquidity and stability in the face of a banking crisis driven by crashing real estate prices. The new private oil & gas companies formed in the Gulf during the oil price boom have been hurt by the collapse of Dubai’s stock market and the illiquidity of the banks there – but these companies did not cause the problem; over-exuberant real estate development was the cause. The good ones are already bouncing back, and the NOCs are doing just fine, although both Mubadala and TAQA are being threatened with downgrades, the latter primarily because of the heavy debt load it took on in order to rapidly expand.

RSC: *2009 of course ended with the UN Climate Change Conference in Copenhagen. Do you have confidence in the future of renewables and alternative energy? Are you seeing increased appetite or increased scepticism from investors looking at this part of the industry?*

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TN: Europe has been about 10 years ahead of the US in the renewables arena, because public policy embraced alternative energy and provided incentives such as the Spanish feed-in tariffs. Now in the US, the Obama administration has provided some real incentives at the federal level, and many states have created “Renewable Portfolio Standards”, setting targets for percentage of total electricity supply from renewables. Even with the Department of Energy loan guarantees, the accelerated depreciation treatment, cash from Treasury in lieu of investment tax credits, what I see are large capital gaps between the technology creation and the technology deployment. There was a lot of venture capital money that poured into renewables in the US. But the traditional VC model of spending about \$20mm to get a technology ready for market and then doing an IPO (to both



provide liquidity to the VC firms and also capital for running the company) just doesn't work when the technology deployment requires \$500mm-\$800mm-even \$1.5bn in capital in order to achieve utility-scale power generation project. This capital gap is an interesting opportunity.

RSC: Looking ahead now at 2010, a lot can change in a year as we all know. What is your outlook for oil and gas in 2010? Will there be winners and losers? And what must companies do to ensure not only survival but growth in this new era?

TN: There are winners and losers in up markets and in down markets. 2010 will see plenty of winners. Focus on cash flow. I don't mean to sound rudimentary, but the fact is that companies are going to have to look to themselves to stay afloat, and that means production, production, production. New leases and raw exploration plays will have to wait a year or so.

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RSC: To conclude Terry I'll ask your one-word opinion on some key market components. Are you bullish, bearish or uncertain about The US Dollar?

TN: Bearish.

RSC: China?

TN: Bullish.

RSC: Dubai?

TN: Still bearish for another year.

RSC: Oil Service Companies?

TN: Bullish for specialty services that are required in shale and unconventional plays.

RSC: Unconventional Oil?

TN: Bullish over the long term, especially in US and China.

RSC: As always Terry many thanks for your time and your insight, we wish you and the Taylor-DeJongh team a prosperous 2010.

*** A paper discussing if 2010 will be the year for the return of the IOCs has been written by Taylor-DeJongh executives and can be found on our website and in *Drillers and Dealers*.***

About Terry:

Terry Newendorp, founder, Chairman and CEO of Taylor-DeJongh, has more than 35 years of experience in international and cross-border capital investments, financial structuring, project financing, debt and equity raising and private placements of capital. He has negotiated and closed deals in 75 countries, aggregating more than US\$70 billion.

About Taylor-DeJongh:

Taylor-DeJongh (TDJ) is an independent, specialist investment banking firm that focuses on conventional and renewable energy, oil & gas, industrial and infrastructure business globally. The firm has over 28 years of success in providing investment banking services, including debt and equity raising, project financing advisory, project development and structuring services for energy and infrastructure sectors worldwide. TDJ has successfully structured and advised on over US\$70 billion worth of debt and equity investments in 100 countries, for power, renewable energy, oil & gas, LNG, petrochemical, industrial, transportation and other infrastructure projects. TDJ also advises clients on corporate finance, M&A and capital raising.

