Structuring Energy Investments in 2025: Enhancing Yield to Attract Investment

December 18, 2024

Seyfarth Shaw LLP

Today's Agenda

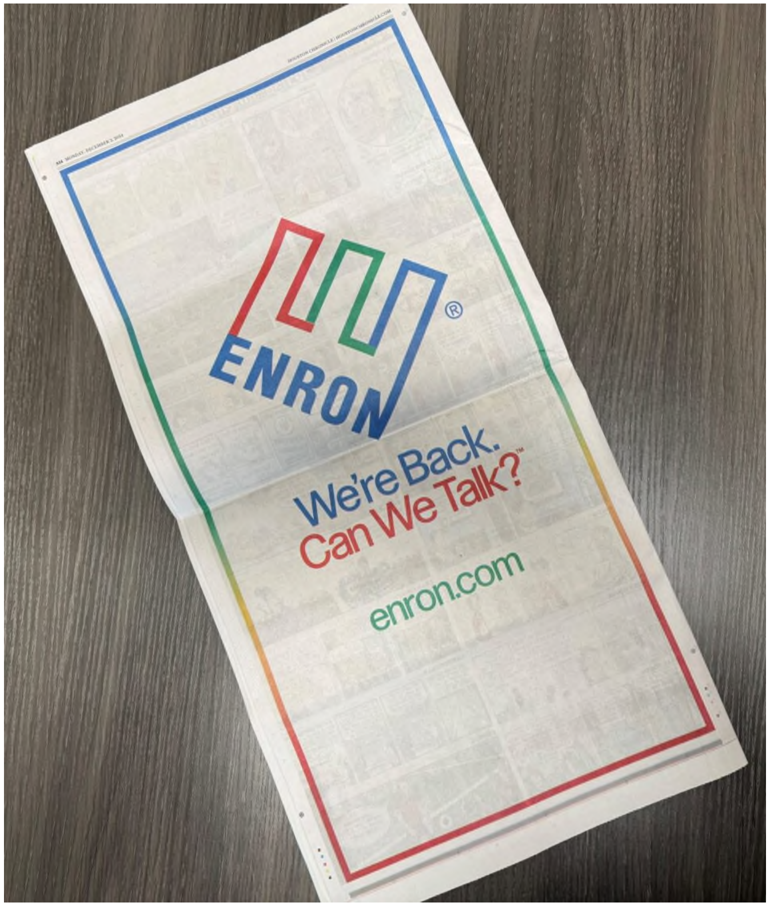
1 | Countdown of the top 10 energy deals that defined 2024

2 | Insights into market trends and deal structuring innovations

3 | Lively panel discussion about strategic joint ventures

4 | Audience Q&A and predictions for 2025!

Guess Who's Back?



Source: Houston Public Media

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Energy Meets Hollywood

Source: IMDb

Top 10 Energy Deals That Defined 2024

Top 10 Energy Deals in 2024

#10

Permian Power Move!

- Summary: Apache acquired Callon Petroleum in a strategic Permian Basin consolidation.
- Deal Value: ~$4.5 billion.
- Deal Structure: All-stock transaction.
- Location/Basin: Permian Basin, Texas.
- Yield Enhancing Themes:
  - Expected production increase by 103,000 boe/d.
  - Estimated overhead, operational and cost-of-capital synergies to exceed $150 million annually.
  - Enhances Apache's efficiency and ability to scale operations in the Permian Basin.

Top 10 Energy Deals in 2024

#9

Striking a High Note!

- Summary: Chord Energy and Enerplus combined operations to form a premier Williston Basin-focused E&P company.
- Deal Value: ~$4 billion.
- Deal Structure: All-stock transaction.
- Location/Basin: Williston Basin, North Dakota.
- Yield Enhancing Themes:
  - Expected to generate administrative, capital and overhead cost synergies of up to $150 million annually.
  - Enhanced operating scale to drive return of capital at 75%+ free cash flow.
  - Combination establishes approximately 10 years of low-breakeven inventory with significant opportunities to enhance returns.

Top 10 Energy Deals in 2024

#8

Crowning Glory!

- Summary: Occidental Petroleum acquired CrownRock L.P. to bolster its position in the Permian Basin with a focus on low-carbon oil production.
- Deal Value: ~$12 billion.
- Deal Structure: Cash-and-stock.
- Location/Basin: Permian Basin, Texas.
- Yield Enhancing Themes:
  - Adds high-margin, lower-decline unconventional production of 170 MMboe/d in 2024.
  - Quarterly dividend increases of 22% to $0.22 per share.
  - **Increased cash flow and $4.5-$6.0 billion in divestiture proceeds allow Oxy to reduce debt by at least $4.5 billion within 12 months.**

Top 10 Energy Deals in 2024

#7

Renewable Dream Team!

- Summary: BP and JERA have agree to form a $5.8 billion joint venture to become a leading global offshore wind developer.
- Deal Value: Up to $5.8 billion — BP will contribute up to $3.25 billion, while JERA will provide up to $2.55 billion.
- Deal Structure: 50:50 joint venture.
- Location/Basin: Europe, Australia, and Japan.
- Yield Enhancing Themes:
  - Long-term PPAs ensure predictable revenue streams.
  - A mix of operating assets and a strong development pipeline provides immediate returns and future growth potential.

Top 10 Energy Deals in 2024

#6

Fueled by Green!

- Summary: KKR has agreed to acquire a 25% stake in Eni's biofuels subsidiary, aiming to capitalize on the rising demand for sustainable energy.
- Deal Value: ~$3.2 billion.
- Deal Structure: Partial divestiture through a minority equity investment.
- Location/Basin: Europe.
- Yield Enhancing Themes:
  - Strengthen Eni's capital structure and lowers its debt.
  - KKR's infrastructure expertise supports Enilive's expansion and operational growth.
  - Improved cash flow from the deal supports potential dividend growth and shareholder returns.

Top 10 Energy Deals in 2024

#5

The North Sea's Scottish Brogue!

- Summary: Shell and Equinor have agreed to combine their UK offshore oil and gas assets to form UK's largest independent E&P company.
- Deal Value: Equinor's UK production stands at ~ 38,000 boe/d, and Shell UK produces more than 100,000 boe/d.
- Deal Structure: 50:50 joint venture.
- Location/Basin: North Sea, UK.
- Yield Enhancing Themes:
  - Strengthens Equinor's near-term cash flow through significant increase in production volumes.
  - Synergies anticipated to increase cash flows by reducing overall costs.
  - The joint venture creates a cost-competitive way of realizing additional value from the prolific, but naturally declining, basin.

Top 10 Energy Deals in 2024

#4

Pipeline Power Play!

- Summary: EQT Corporation and Blackstone Credit and Insurance (BXCI) have agreed to form a midstream joint venture consisting of EQT's ownership interest in high-quality contracted infrastructure assets.
- Deal Value: $3.5 billion (implied total JV value of $8.8 billion).
- Deal Structure: Corporate Joint Venture.
- Location/Basin: Appalachian Basin, Pennsylvania.
- Yield Enhancing Themes:
  - Recurring cash flows secured by long-term midstream contracts.
  - Higher JV valuation due to fixed returns.
  - High-quality assets with growth and scalability upside.
  - Retainment of asset operations to capture synergies and efficiency.

Top 10 Energy Deals in 2024

#3

Big Gains in Big Games!

Chevron

HESS

- Summary: Chevron's acquisition of Hess enhances its global upstream portfolio, driven by Hess's stake in Guyana's Stabroek Block, positioning Chevron for significant long-term production growth.
- Deal Value: $53 billion.
- Deal Structure: All-stock transaction.
- Location/Basin: Guyana and Bakken Basin.
- Yield Enhancing Themes:
  - Anticipated run-rate cost synergies of ~$1 billion before tax within a year of closing.
  - Gaining a 30% ownership interest in more than 11 billion BOE in the prolific Stabroek block offshore Guyana.
  - The combination is expected to grow production and free cash flow faster than Chevron's prior 5-year guidance.

Top 10 Energy Deals in 2024

#2

Pioneering Permian M&A!

ExxonMobil PIONEER NATURAL RESOURCES

- Summary: ExxonMobil's acquisition of Pioneer strengthens its position in the Permian Basin, significantly boosting its production capacity and resource base
- Deal Value: ~$60 billion.
- Deal Structure: All-stock transaction.
- Location/Basin: Permian Basin, Texas.
- Yield Enhancing Themes:
  - More than doubles ExxonMobil's production volume in the Permian.
  - Creates synergies by combining Pioneer's sizeable acreage with ExxonMobil's advanced technology and industry-leading project development capabilities.
  - Significant opportunities to grow Permian production from 1.3 MMboe/d to 2 MMboe/d by 2027.

Top 10 Energy Deals in 2024

#1

Marathon to Victory!

ConocoPhillips Marathon Oil

- Summary: ConocoPhillips acquired Marathon Oil, reshaping U.S. energy production and delivering significant shareholder returns.
- Deal Value: $22.5 billion.
- Deal Structure: All-stock transaction.
- Location/Basin: Eagle Ford and Bakken Basins.
- Yield Enhancing Themes:
  - Added high-quality, low cost of supply inventory adjacent to Conoco's existing unconventional positions.
  - Strong history of seamless asset integration.
  - Anticipate delivering synergies of over $1 billion on a run rate basis during the first 12 months.

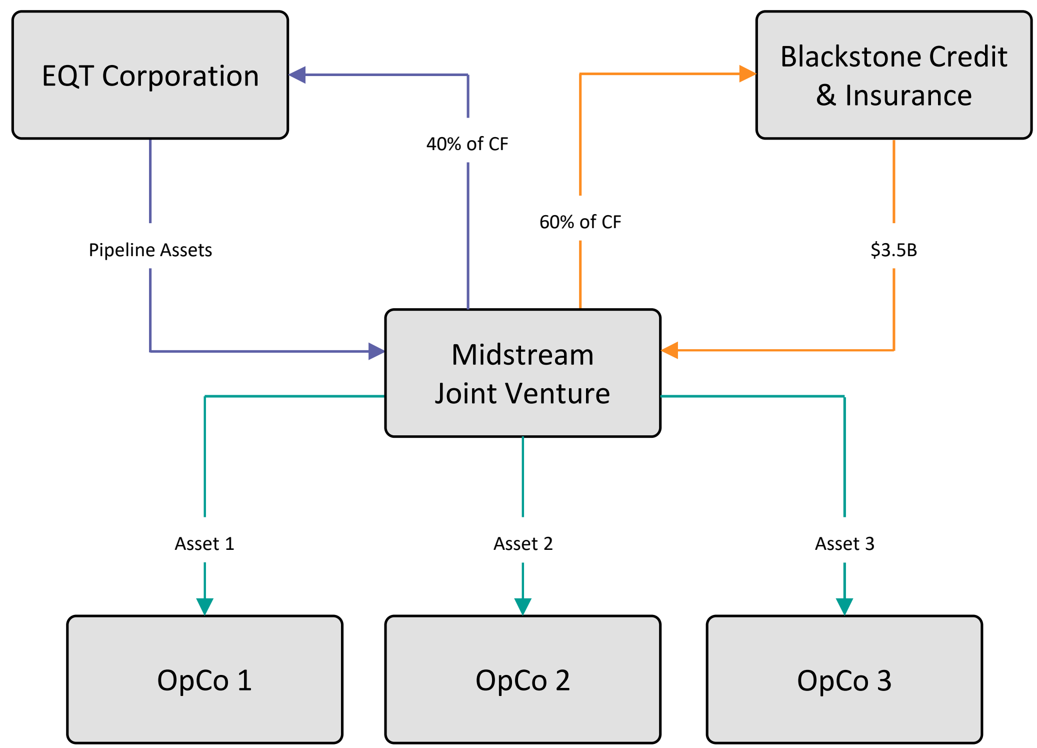
Deep Dive on Yield

Market Trends

1. Synergies and Cost Efficiencies
2. Increases in Production and Scale
3. Enhanced Cash Flows and Predictable Returns
4. Dividend Growth and Shareholder Returns
5. Strategic Asset Integration and Development

2025: Year of the Yield

Illustrated Asset Drop-Down and Organizational Structure



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Valuation Premiums

YieldCos are pass-through entities that own operating assets that produce predictable cash flows and are designed to allow for generous dividend yields and strong long-term dividend growth.

- EBITDA valuation multiples for YieldCos are significantly higher than that of non-YieldCo structured companies in the same industry.
  - The EQT/Blackstone midstream JV is valued at $8.8 billion or 12x EBITDA versus ~3.913x EBITDA (EQT's valuation multiple at year end December 31, 2023).
- Valuation premiums are driven by:
  - Long-term, contract-backed, recurring revenue streams supported by midstream assets that create **stable cash flows** and predictable earnings (*e.g.*, full Mountain Valley Pipeline capacity contracted for at least 20 years).
  - Low cost of equity (7.875%) provides investors with a **fixed, predictable yield** while allowing the JV to be valued at a higher multiple (12x EBITDA).
  - **High payout ratios** and structured cash flow distribution (*e.g.*, 40% to EQT and 60% to Blackstone) appeals to income-focused investors seeking reliable yield.
  - **Asset quality and scalability**, with growth opportunities such as the MVP Expansion and MVP Southgate, create upside for future earnings growth.

Key Takeaways

Owners of revenue generating assets have the opportunity to establish "sponsored" YieldCo's, enabling them to drop down the assets to fully capture the elevated EBITDA multiples exhibited in the YieldCo market.

- Allows for immediate partial monetization of the valuation disparity between YieldCo and non-YieldCo structured entities.
- Provides visibility and transparency to cash flows.
- Value creation is captured through:
  - ParentCo's ownership interest in the YieldCo; and
  - Cash flow from distributions made to YieldCo's shareholders, including dividends and potential sponsor-related agreements.
- Additional benefits could be realized in the M&A market through strategic third-party acquisitions.
- A YieldCo's flexible capital structure allows for cash and equity considerations to be offered to sellers, enhancing its attractiveness in competitive M&A markets.

What Should I Be Thinking About?

Transactional Considerations for Enhancing Your Own Yield

1. Focus on Synergies and Cost Efficiencies

- Combining operations, reducing redundancies, and achieving cost-of-capital efficiencies can significantly enhance cash flows.
- Synergies improve profitability post-close, resulting in accretive cost of capital.

Example:

- *ConocoPhillips/Marathon*: Projected **$1 billion in synergies** on a run-rate basis within the first 12 months.

2. Leverage Increased Production and Scale

- Achieving immediate scale and production increases improves operational efficiencies, spreads fixed costs, and drives revenue growth.
- Deals that increase production volumes often yield higher cash flows and long-term value creation.

Example:

- *Apache/Callon*: Production expected to immediately increase by **103,000 boe/d**.

Transactional Considerations for Enhancing Your Own Yield (cont'd)

3. Enhance Cash Flow Predictability

- Structuring deals to secure recurring cash flows - through long-term contracts, PPAs, or predictable revenue sources - reduces risk and enhances yield stability.
- This improves financing opportunities and enables capital deployment for growth and debt reduction.

Example:

- *EQT/Blackstone*: Secured **recurring cash flows** through long-term midstream contracts, supporting predictable yields.

4. Prioritize Shareholder Returns and Dividend Growth

- Deals that unlock cash flow for dividends, share buybacks, or capital returns enhance shareholder value.
- Structuring transactions to focus on these outcomes makes deals attractive to investors and can boost stock performance.

Example:

- *Oxy/CrownRock*: Quarterly dividend increases of **22%** to $0.22 per share.

Transactional Considerations for Enhancing Your Own Yield (cont'd)

5. Integrate High-Quality, Scalable Assets

- Acquiring high-quality, low-cost assets with scalability potential ensures long-term growth opportunities.
- Seamless integration of these assets unlocks operational efficiencies and positions the acquirer for sustainable yield enhancement.

<u>Example</u>:

- *ExxonMobil/Pioneer*: Combination of Pioneer's sizeable Permian acreage with ExxonMobil's advanced technology and project development to unlock long-term production potential.

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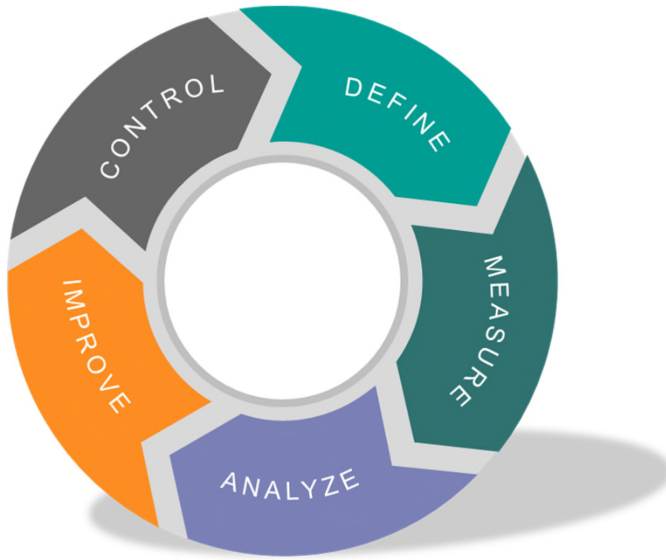

DEFINE

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MEASURE

Collect data on Seyfarth/ client experience: total cost, cost by task code, "voice of client"

ANALYZE

Gather experts in "Kaizen"; review current state and process map future

IMPROVE

Make changes in process; train attorneys/staff; support with technology and best practices

CONTROL

Supervise and measure to prevent return to the prior process

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This Day in Energy

This Day in Energy:

December 18, 1957

Source: Britannica

Shippingport Atomic Power Station (Pennsylvania)

- **Pioneering Nuclear Energy:** On December 18, 1957, Pennsylvania's Shippingport Atomic Power Station became the first full-scale U.S. nuclear power plant dedicated to commercial electricity generation.
- **Construction Cost:** Built at a cost of $72.5 million (equivalent to approximately $813.9 million today).
- **Technological Innovation:** Utilized a pressurized water reactor which introduced nuclear technology into a landscape dominated by coal and hydroelectric power.
- **Impact on Society:** The plant's success demonstrated nuclear energy's potential, influencing U.S. energy policy and encouraging further development of nuclear power.
- **Successful Decommissioning:** Shippingport set a precedent for safe nuclear plant dismantling when it was decommissioned in 1989, with all structures removed and the site restored.

Post-Merger Considerations

Post-Merger Considerations

1. Operational Integration

- Asset Consolidation: Streamline and integrate physical and digital assets to reduce redundancies.
- System and Process Alignment: Harmonize IT systems, supply chain management, and financial reporting platforms.
- Cultural Integration: Bridge cultural differences between organizations to foster employee alignment and shared purpose.

Example:

- *Shell/Equinor:* The Shell-Equinor JV streamlined operational integration by consolidating UK offshore oil and gas assets into a single independent entity, aligning financial reporting, IT systems, and production oversight under a unified management structure, while fostering cultural alignment through the establishment of a neutral headquarters in Aberdeen, Scotland.

Post-Merger Considerations (cont'd)

2. Governance and Leadership

- Management Structure: Define clear roles and responsibilities for key executives.
- Decision-Making Authority: Establish clear guidelines for decision-making, including escalation paths and approval protocols.

Example:

- *BP/JERA:* The BP-JERA JV established a balanced governance framework with JERA appointing the CEO and BP appointing the CFO, while implementing joint approval protocols for major decisions on capital allocation, project selection, and financing to ensure shared control and operational transparency.

Post-Merger Considerations (cont'd)

3. Financial and Legal Compliance

- Debt and Capital Structure: Restructure existing debt and optimize capital allocation to ensure financial stability.
- Regulatory Compliance: Address regulatory approvals and satisfy any imposed conditions.
- Contract and IP Review: Review and update contracts for change-of-control clauses and protect key intellectual property.

Example:

- *EQT/Blackstone*: The EQT-Blackstone JV restructured EQT's debt using a $3.5 billion cash infusion from Blackstone, reducing net debt to $9 billion, while addressing regulatory approvals for FERC-regulated assets and updating key contracts to reflect changes in ownership and protect operational rights.

Post-Merger Considerations (cont'd)

4. Employee and HR Management

- Employee Retention: Implement retention programs to secure key talent and critical operational staff.
- Change Management: Launch change management initiatives to promote transparency and employee engagement

Example:

- *Shell/Equinor:* The Shell-Equinor JV prioritized employee retention by maintaining operational independence and avoiding layoffs, thereby preserving key talent and critical staff essential to managing offshore assets. Change management initiatives included transparent communication and the establishment of a neutral headquarters in Aberdeen, fostering employee alignment and engagement during the transition.

Post-Merger Considerations (cont'd)

5. Customer and Market Positioning

- Customer Retention: Proactively engage key customers to maintain relationships and reduce churn.
- Brand Integration: Develop a unified market presence with consistent branding and customer messaging.

Example:

- *EQT/Blackstone*: The EQT-Blackstone JV maintained customer relationships by promoting scalability and growth opportunities, ensuring stable, long-term access to midstream infrastructure and capacity for key customers. The joint venture's unified market presence emphasized operational stability and future expansion, reinforcing customer confidence and support.

Post-Merger Considerations (cont'd)

6. Performance Measurement and Reporting

- KPI Tracking: Track key performance indicators (KPIs) to monitor integration success and identify gaps.
- Post-Closing Audits: Conduct post-closing audits to validate integration effectiveness and compliance with financial obligations.

General Comments:

- Most of the deals mentioned above have either recently announced or only recently closed, leaving the realization of proposed synergies unverified. Post-closing audits and KPI tracking will be essential to assess integration success, validate the achievement of anticipated synergies, and ensure compliance with financial obligations.

Integration Solutions

We partnered with our compliance subsidiary, Seyfarth at Work, to develop **The Merger Playbook** – a comprehensive solution with a high impact training program.

Clients can customize our playbook to fit their workplace needs and compliance goals. This approach minimizes future risks and supports successful integration post-merger.

Source: Seyfarth at Work

Audience Q&A

Source: Enron

Predictions for 2025

1. **Expect to see more hybrid structures combining YieldCo stability and flexibility.**
   - We will continue to see new approaches on old ideas to have line of sight on new development and ultimately cash flow (*e.g.* Landbridge's IPO pitching sponsored royalty affiliates).

2. **Joint Ventures will dominate in highly consolidated areas.**
   - This is especially true in regions like the Permian Basin, where existing operators remain hesitant to sell non-core assets, requiring prospective buyers to pursue strategic development and operational partnerships.

3. **Foreign investments into private equity will see a resurgence.**
   - Family offices and institutions are driving this trend, particularly in regions like Europe, where energy security concerns have created opportunities for strategic energy investments.

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