As energy companies look ahead, some owe debt to the oil bust

By Collin Eaton May 30, 2018 Updated: May 30, 2018 11:24am

EnerVest CEO John Walker works Geoscience tech Maria Wedding at the company's headquarters downtown Tuesday May 08 ,2018.(Dave Rossman Photo)

John Walker, the CEO of EnerVest, at the company's headquarters downtown Tuesday May 08 ,2018.(Dave Rossman Photo)

This is the Patterson 248 oil well operated by the recent Magnolia Oil & Gas EnerVest merger located in south central Texas.

That night in February 2016 was a long one for John Walker, the chief executive of the Houston driller EnerVest. The next day, he and his company would hand out some 200 pink slips as oil prices sank to their lowest level in a dozen years.

EnerVest, Walker realized, had borrowed too much. When oil was racing to $100 a barrel in 2014, the strategy seemed prudent and the possibility that oil prices would plunge by 75 percent far-fetched. . But now, he was unable to sleep, thinking about the impact on the employees about to lose their jobs.

“It was the worst day of my career,” Walker said in a recent interview. “All the mistakes made during that period, I take the responsibility for it.”

More than two years after that restless night and the grim day that followed, Walker and the company are heeding the lessons of the worst oil bust in a generation. The collapse of the oil market, which led to scores of bankruptcies and tens of thousands of job cuts in the U.S. oil industry, has dramatically changed how companies like EnerVest raise and spend money in the oil patch

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Many are relying on debt far less, instead raising money from equity investors to buy, explore and operate oil and gas prospects, while borrowing more cautiously. Oil producers issued $35 billion in bonds last year, down from $40.3 billion the previous year, according to Houston consultancy Petroleum Listing Service.

Enervest, for example, had debt levels of 35 percent of its capital in the run-up to the oil bust. A portion of its debt came from high-yield bonds, known as junk bonds, which are considered riskier than many forms of debt and exact high interest rates from the borrowers.

Today, EnerVest plans to keep its debt levels to 25 percent of its capital, and roughly 15 percent of that debt will come from bank loans based on the value of the company's oil and gas reserves - a far more conservative strategy than its previous one. It'll cost more money, Walker said, but will make the company less vulnerable when the next downturn hits.

"The reality is, you can either sit around and say it's the other guy's fault, this that and the other," Walker said. "Or you could really look at it and say, 'I screwed up, we're going to make permanent changes and stay disciplined with those permanent changes.'"

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EnerVest has built a large position across U.S. oil and fields since its inception in 1992. It invests in oil and gas properties, managing both funds and oil field operations. It has some $7 billion in assets under management, and operates 35,000 wells. Walker, the company's longtime CEO and co-founder, is well-known in Houston's energy sector, having served as chairman of a trade group for independent U.S. producers and as a regent of the Texas Tech University System.

EnerVest, like many investors, lenders and oil companies, got caught up in the alluring story of American engineering and ingenuity that became known as the shale revolution — a story made even more seductive by the availability of cheap abundant credit. Before oil markets began their slide, EnerVest invested some $3 billion in oil and gas operations.

"We felt like we were disciplined in what we did," Walker said. "But when you lose 80 percent of your revenues, that's too much debt."

The reliance on high levels of debt came at a high price. A $2 billion fund EnerVest raised in 2013 was decimated. A key oil-production affiliate, EV Energy Partners, filed for Chapter 11 bankruptcy in Delaware last month. High-yield debt owners received 95 percent of the equity in EV Energy

Partners,and EnerVest relinquished control of the firm to a separate board, though it will continue to operate the oil and gas wells.

EnerVest also turned to another private equity firm, Mountain Capital Management, to replenish another one of its funds. It cut about 250 jobs, 20 percent of its workforce. during the worst of the downturn.

As oil prices have climbed, crossing $70 a barrel before retreating recently, Walker has been optimistic. Some of the properties EnerVest acquired at a lower price during the downturn - such as hundreds of thousands of acres in Virginia’s Nora natural gas field - could provide a cushion to profits. The company collected $1.6 billion in revenue last year, up $300 million from the previous year.

EnerVest is not the only company ditching a business model that relies heavily on debt. Fieldwood Energy, a private Houston oil producer that drills almost exclusively in the Gulf of Mexico, is another such firm. During the downturn, its offshore platforms in the Gulf paid for themselves, but the money generated was far from enough to support its debt load.

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In the heyday of $100 a barrel oil, Fieldwood borrowed $3.3 billion to pay for $4.4 billion in acquisitions. When crude prices crashed and revenues followed, half of the cash the company made from its offshore wells went to interest payments.

"That's a hard thing to sustain," Fieldwood CEO Matt McCarroll said in a recent interview. "Did we think $100 oil would last longer than it did? Yeah, probably so. Would we do that again? No way."

Fieldwood, which paid $260 million in interest last year alone, has joined scores of other U.S. oil companies ditching debt in favor of raising money by selling equity, or ownership stakes, and funding purchases with cash. In the oil market meltdown, more than 140 North American oil producers filed for bankruptcy with a combined $90 billion in debt, according to law firm Haynes & Boone.

Fieldwood, a private equity-backed oil producer, emerged last month from the U.S. oil industry's largest bankruptcy case since mid-2016. But McCarroll, Fieldwood's lawyers and advisers don’t view it as a traditional bankruptcy.

Its lenders and equity holders contributed $525 million in new capital in part to fund the acquisition of deep-water Gulf assets owned by Houston's Noble Energy - a deal it closed as it came out of bankruptcy. And how did it pay for the Noble deal?

"One-hundred percent equity," McCarroll said.

In the downturn, even when oil prices fell to $26 a barrel in February, the cost to operate Fieldwood's offshore wells only came to $15 a barrel. The oil and gas wells acquired from Noble generate $300 million in cash a year.

Now, Fieldwood is looking ahead to a more profitable year as U.S. crude prices rise. The company plans to spend $350 million this year and more than $400 million next year to dispatch more drilling rigs to the Gulf of Mexico, its first drilling program in more than two years. It has two rigs in Gulf, but will send two more soon. It plans drill other deep-water wells over the next few months.

"Without a heavy debt burden and without big capital commitments, we can be opportunistic," McCarroll said. "At these oil prices, we ought to be able to make pretty nice returns."