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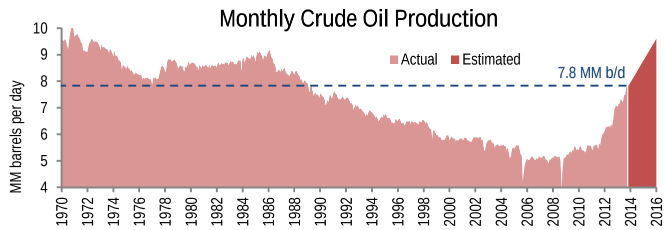
Energy Bulletin
Oil and Gas Midstream, Equipment and Services
Q1 2014

Shale Revolution Continues to Call for Capital

U.S. has reached highest oil production level in 25 years. In the midst of an energy revolution unlocked by innovations in hydraulic fracturing and horizontal drilling, U.S. crude oil production increased 1 million barrels per day in 2013, the largest annual increase in the country's history and more than the aggregate increases in the rest of the world. By 2016, U.S. crude oil production is expected to reach the historical high achieved in 1970 of 9.6 million barrels per day, according to the U.S. Energy Information Administration.

U.S. will be close to energy self sufficiency within two decades. By 2015, the U.S. is expected to surpass Russia and Saudi Arabia as the world's top oil producer. While crude oil production is expected to level off and then slowly decline after 2020, natural gas production is expected to grow 56% from 2012 to 2040. Increased production of oil and gas will enable the U.S. to continue reducing its use of imported fuels, which was previously at 30% (net) in 2005, declined to 16% in 2012 and is expected to decline to 4% by 2040, according to the EIA.

Sources: U.S. Energy Information Administration; International Energy Association; Mergermarket



Source: U.S. Energy Information Administration

Projected high growth will require capital investments of $5 trillion over next 20 years. The International Energy Association estimates that through 2035, a cumulative investment of over $5 trillion is needed to finance the U.S. shale revolution's growth needs. This includes investment to expand supply capacity (including production, storage/transportation and processing/refining) and to replace existing and future supply facilities. To date, 60,000 unconventional oil and gas wells have been drilled in the U.S., but 500,000 drilling locations remain. The development of shale resources will be contingent on the ability of companies to raise funds.

Private Equity Answering Call for Capital

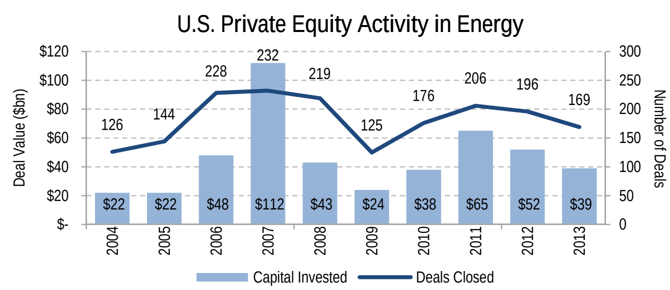
Private equity (PE) activity is expected to pick up in 2014. Mega deals of $1 billion or more in the energy sector declined sharply in 2013, which pushed capital invested down by 24% to $39 billion; however, middle market deals saw an uptick. A turnaround in energy PE activity is forthcoming as (1) the shale revolution continues to transform the industry, (2) significant dry powder needs to be deployed, (3) 2012-2013 was a very robust fundraising period for energy-focused funds, and (4) overseas strategic buyers are not as active for U.S. energy projects. In 2013, international companies invested into U.S. energy less than half of that in 2012.

Energy expected to be most attractive sector for acquisition targets in 2014. According to a Mergermarket survey of deal professionals, 100% of respondents believe that PE buyouts will increase this year, and 86% believe that the energy sector will have the most attractive targets. Case in point: KKR & Co. will open its first Canadian office in February 2014 in Calgary, the capital of Canada's oil patch, with the intentions of deploying $500 million to several billion dollars over the next five years.

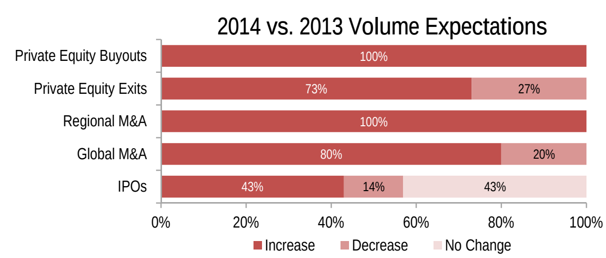
Over $10 billion of new private equity funding flowed into oil and gas in 2013. PE firms have been competing to raise multi-billion-dollar funds to take advantage of the expansion of the energy industry. Ridgewood Energy, Energy & Minerals Group, White Deer Management and American Energy each closed over $1 billion in commitments for their latest energy funds, while EIG Global Partners secured $6 billion, creating one of the industry's largest energy funds.

Energy-focused fundraising will continue to heat up in 2014. First Reserve Corp. has set a $5 billion cap for its latest energy fund, Warburg Pincus has set a $3 billion fundraising target for its first energy fund, and Carlyle Group has announced plans to raise $7 billion for energy funds over the next two years, with more than $3 billion for middle market energy transactions.

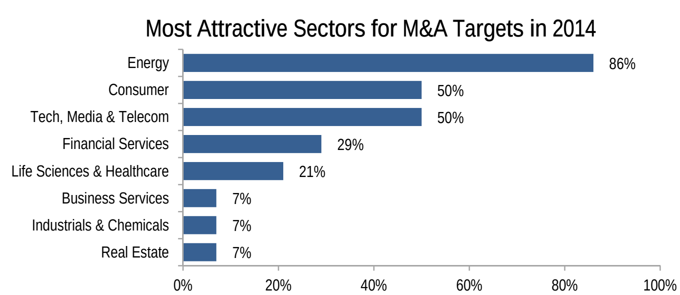
Sources: Mergermarket, Pitchbook, Wall Street Journal



Source: Pitchbook (January 2014)



Source: Mergermarket Survey (December 2013)



Source: Mergermarket Survey (December 2013)

Canadian Oil Sands: Capital Continues to Pour In

World's third largest source of crude reserves. Canada's oil sands in Alberta are the world's third largest source of crude reserves and the starting point for TransCanada Corp.'s proposed Keystone XL pipeline to the U.S. Gulf Coast. This pipeline is the highest profile among a spate of pipeline projects that would be needed to carry all of the growing Canadian oil production to distant markets. Amid a boom in oil sands production, Canada's output of heavy oil is expected to more than double by 2030 to over five million barrels per day, while annual capital expenditures in the oil sands have more than doubled since the recession of 2009 to currently over C$20 billion per year and is expected to reach C$23.4 billion by 2015.

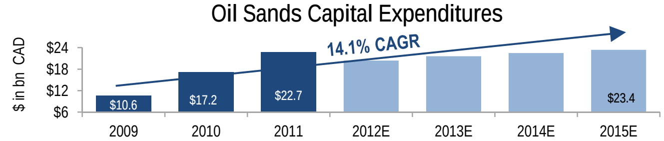
Keystone XL pipeline can trigger more growth. Currently, there are four major pipelines moving crude out of Alberta—the Enbridge Mainline, the Kinder Morgan Trans Mountain, the TransCanada Keystone and the Spectra Express pipelines—that facilitate the flow of approximately 3.7 million barrels per day out of Western Canada. The proposed Keystone XL pipeline will allow about 830,000 barrels per day to be moved from Western Canada down to the Gulf Coast, where the oil could compete on a more global scale (and command a higher price), triggering another significant growth period in the region. The Keystone XL is still in the approval process entering its sixth year of review by U.S. regulators and has been hotly contested by environmental groups. In addition to TransCanada, Enbridge and Kinder Morgan have also begun or are exploring options to expand their existing pipelines over the next four years by an additional 1.5 million barrels per day.

Sources: Wall Street Journal; Bloomberg; Statistics Canada; Assoc. of American Railroads; Canadian Assoc. of Petroleum Producers

Significant opportunities in crude-by-rail. Burgeoning railroad capacity will also give Canadian crude an alternative way to reach global markets, as crude-by-rail has become one of the largest beneficiaries of the shale revolution. In 2013, carloads of fuel oil and crude shipped along Canadian rail lines are expected to have more than double from 68,000 carloads in 2011. In the U.S., railroad cars carried 234,000 carloads of crude in 2012, up from 5,912 in 2007. Recently announced investments further support the growing importance of crude-by-rail, including KKR's December 2013 C$250 million investment in Torq Energy Logistics, an operator of transloading terminals in Western Canada, as well as Kinder Morgan and Imperial Oil's December 2013 announcement of a 50-50 joint venture to build a C$180 million crude oil rail-loading facility in Edmonton.

Multi-billion-dollar capital investments continue. Despite concerns about environmental risks and constraints on pipeline expansions, significant capital investments continue to flow into the oil sands. Canadian regulators recently approved a C$13.5 billion project by Suncor Energy and its JV partners for the biggest investment in an oil sands project to date. Imperial Oil has also applied for approval to develop a C$7 billion oil sands project.

Oil Sands Capital Expenditures



Sources: Statistics Canada; Energy Resources Conservation Board

Private Equity Providing Growth Capital

Capital requirements drive PE activity. The oil and gas sector is in a period of major capital investment, with $700 billion forecasted for projects currently under development. Three-quarters of these projects have an estimated cost of greater than $1 billion, underscoring the growing size, complexity and challenges the sector is facing. More than half of respondents to a December 2013 Mergermarket survey cite capital requirements as the primary driver to oil and gas PE investment, followed by the availability of financing and global expansion.

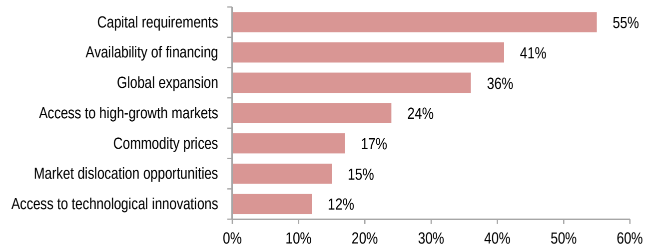
Oil and gas subsectors are characterized by different perceptions of potential risk and reward. While the capital needs of upstream and downstream companies are seen as strong drivers of PE activity in those subsectors, predictable returns and reduced exposure to volatile commodity prices are more important for midstream and oilfield services. Attractive valuations are also a very important driver in the midstream subsector. EV/EBITDA multiples of publicly traded midstream operators grew to 16.8x as of Q4 2013, nearly double most of its peer subsectors.

Organic investments and platform acquisitions are top PE priorities. Over the next two years, the top two priorities for PE firms will be to focus on existing portfolio company growth through organic investment and to make new platform acquisitions, according to approximately 40% of respondents to the Mergermarket survey. Raising new capital and exiting current investments were the bottom two priorities.

PE to add value through growth capital. Contributing to and managing the deployment of growth capital to help oil and gas firms restructure and grow is the primary way PE firms believe they can add value to prospective portfolio companies, according to the Mergermarket survey.

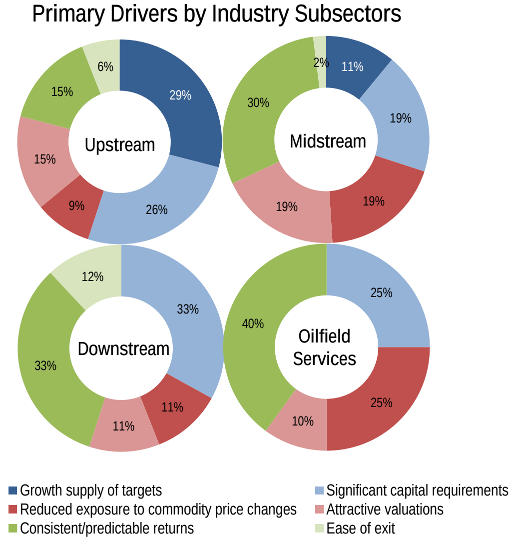
Source: Mergermarket; Capital IQ

Primary Drivers of PE Activity in Oil & Gas



Source: Mergermarket Survey (December 2013)

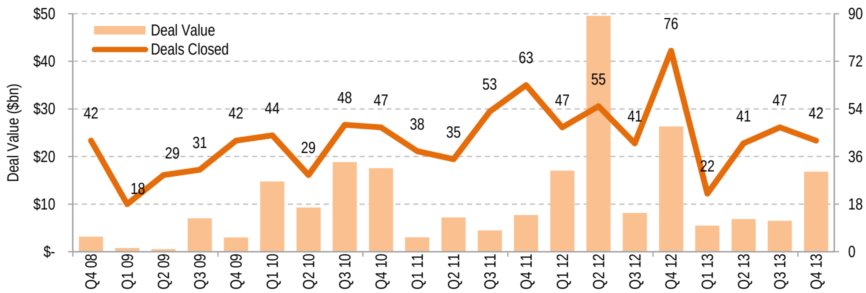
Primary Drivers by Industry Subsectors



Source: Mergermarket Survey (December 2013)

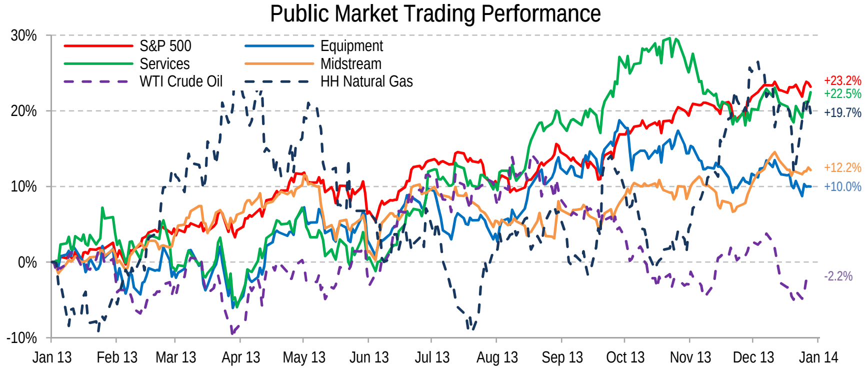
Historical Trends and Performance

North America M&A Activity: Midstream, Equipment & Services



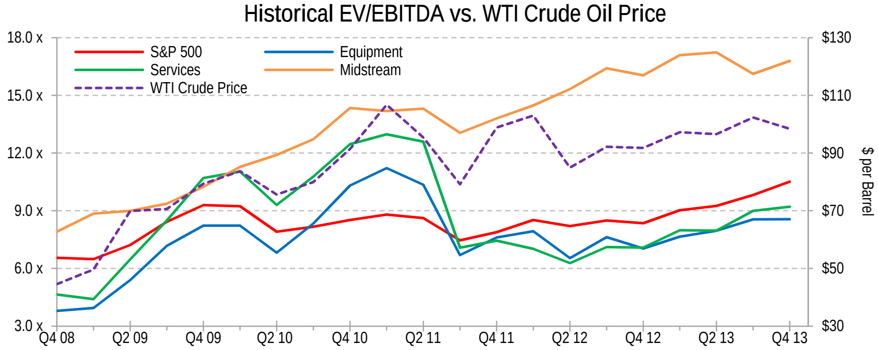
Source: Capital IQ

Public Market Trading Performance



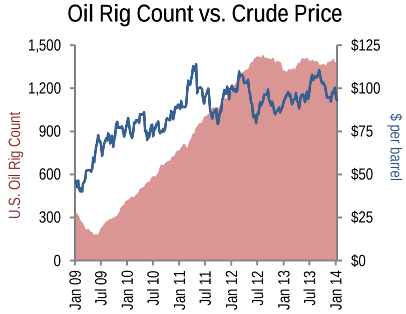
Sources: Capital IQ as of January 20, 2014; Wall Street Journal; Nasdaq

Historical EV/EBITDA vs. WTI Crude Oil Price

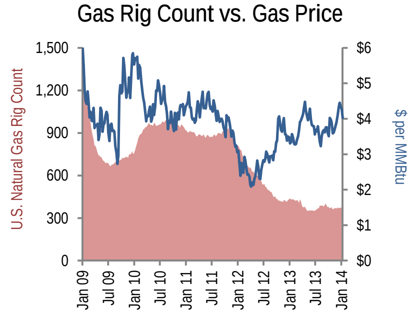


Source: Capital IQ as of January 20, 2014; historical EV/EBITDA multiples are enterprise value weighted

Oil Rig Count vs. Crude Price



Gas Rig Count vs. Gas Price



Sources: EIA; Baker Hughes

Oil and gas M&A activity declined in 2013. The slowdown in deal activity in early 2013 came after a record Q4 2012, driven by companies accelerating deals. In 2013, 152 deals were closed in the midstream, equipment & services sectors, compared to 219 deals in 2012. Aggregate deal value declined 65% year-over-year to $35.6 billion in 2013. Note that, in 2012, Kinder Morgan's $35.7 billion acquisition of El Paso was one of the largest energy deals in history, while Kinder Morgan's $4.5 billion acquisition of Copano Energy was one of the sector's largest deals in 2013. As industry capital requirements continue to grow, there is a robust opportunity for private equity capital and increased M&A activity in 2014.

Investment inflow into energy stocks reached a new high in 2013. A record $15.7 billion of net new investment money flowed into mutual funds and ETFs focused on energy master limited partnerships (MLPs), which generally own oil and gas infrastructure and pay out nearly all their cash flow in distributions, in 2013, more than triple the previous record of $5.2 billion set a year earlier. With the rising interest in the sector, there was a record 20 MLP IPOs in 2013 that raised roughly $7.5 billion in equity, topping the previous record of 17 set in 2007. By subsector, midstream MLPs were the most prevalent (38%), followed by terminals (14%) and marine (10%).

Valuations are on an upward trend in tandem with crude price. In Q4 2013, EBITDA multiples for energy stocks have reached their highest levels across each subsector since Q3 2011. Midstream operators have reached a record high 16.8x as of Q4 2013, growing to nearly double that of both oilfield services (9.2x) and equipment manufacturers (8.6x). Multiples across the industry are expected to continue to rise in 2014, as cash-rich corporates and dry powder-laden PE firms compete for the same quality target energy companies, coupled with recovering capital markets and increased market liquidity.

WTI crude oil spot price averaged $98 in 2013 but is expected to decline to an average $93 per barrel in 2014 and $90 per barrel in 2015, as a result of continued production growth.

Henry Hub natural gas spot price averaged $3.84 per MMBtu in 2013 and is expected to average $4.01 per MMBtu in 2014 and $4.23 per MMBtu in 2015.

Select Oil and Gas Mergers and Acquisitions Activity

Date	Target	Acquirer	Enterprise Value	EV / Revenue	EV / EBITDA	Description
Equipment Manufacturing						
Jan 14A	Varel Intl Energy Services	Sandvik AB	$740	2.2 x	-	Downhole drilling tools
Aug 13	Galvanic Applied Sciences	Tuckerman Capital et al	18	1.1	4.1 x	Measurement equipment
Aug 13	S&R Compression, LLC	USA Compression Partners, LP	187	-	-	983 compression units
Jul 13	Wenzel Downhole Tools Ltd.	Basin Tools, LP	85	1.1	4.7	Downhole drilling tools
Jul 13	Lufkin Industries Inc.	GE Oil & Gas SpA	3,323	2.5	17.0	Lift and pumping products
Equipment Manufacturing Average				**1.7 x**	**8.6 x**	
Oilfield Services						
Nov 13	Bonnett's Energy Corp.	Babson Capital et al	$101	1.0 x	4.3 x	Completion and production
Oct 13A	TNT Crane and Rigging, Inc.	First Reserve Corporation	650	-	-	Lifting services and equipment
Oct 13	Mission Well Services, LLC	Calfrac Well Services Ltd.	147	-	-	Hydraulic fracturing services
Jun 13	IronGate Energy Services	Clearlake Capital Group, LLC	244	2.4	5.4	Tubing and tubular services
Apr 13	IROC Energy Services Corp.	Western Energy Services Corp.	173	1.8	6.0	Completion and production
Oilfield Services Average				**1.7 x**	**5.2 x**	
Midstream Operators						
Dec 13	PAA Natural Gas Storage, LP	Plains All American Pipeline	$2,269	5.5 x	19.1 x	Natural gas storage facilities
Dec 13	Hess Corp., 20 Terminals	Buckeye Partners, L.P.	850	-	-	20 liquid petroleum terminals
Nov 13	Arrow Midstream Holdings	Inergy Midstream, L.P.	808	0.6	31.5	Oil, gas and water pipeline
Nov 13	TGGT Holdings, LLC	Azure Midstream Holdings LLC	909	-	-	Midstream assets
May 13	Copano Energy LLC	Kinder Morgan Energy Partners	4,421	3.1	29.3	Midstream services
Midstream Operators Average				**3.1 x**	**26.6 x**	

Sources: Capital IQ; company press releases. Amounts in millions of U.S. dollars.

Public Company Valuation and Performance

Company	Ticker	Share Price	Market Cap	Enterprise Value	LTM EV/Revenue	LTM EV/EBITDA	LTM P/E
Equipment Manufacturing							
National Oilwell Varco, Inc.	NYSE:NOV	$76.97	$32,951	$34,057	1.5 x	8.3 x	14.1 x
Cameron International Corp.	NYSE:CAM	58.69	13,961	15,369	1.6	11.0	20.9
FMC Technologies, Inc.	NYSE:FTI	51.00	12,066	13,300	1.9	14.8	27.6
Weatherford International Ltd.	NYSE:WFT	14.68	11,295	20,315	1.3	8.7	NM
Dril-Quip, Inc.	NYSE:DRQ	106.51	4,334	3,953	4.8	17.2	28.2
Equipment Manufacturing Average					**2.2 x**	**12.0 x**	**22.7 x**
Oilfield Services							
Schlumberger Limited	NYSE:SLB	$90.21	$118,803	$123,609	2.7 x	10.3 x	17.7 x
Halliburton Company	NYSE:HAL	50.66	42,971	49,186	1.7	8.5	24.2
Baker Hughes Incorporated	NYSE:BHI	54.14	23,996	27,400	1.3	7.6	22.6
Oil States International Inc.	NYSE:OIS	100.03	5,517	5,750	1.3	6.6	15.0
Superior Energy Services, Inc.	NYSE:SPN	26.11	4,164	5,757	1.2	5.1	15.0
Oilfield Services Average					**1.6 x**	**7.6 x**	**18.9 x**
Midstream Operators							
Enterprise Products Partners L.P.	NYSE:EPD	$63.99	$58,942	$76,668	1.7 x	17.1 x	23.3 x
Kinder Morgan, Inc.	NYSE:KMI	35.57	36,845	87,659	6.2	15.2	30.9
TransCanada Corp.	TSX:TRP	44.14	31,206	55,548	7.1	14.5	21.4
Williams Partners L.P.	NYSE:WPZ	49.93	21,901	30,587	4.4	14.1	17.7
Energy Transfer Partners, L.P.	NYSE:ETP	52.99	20,153	40,669	0.9	12.9	25.9
Midstream Operators Average					**4.1 x**	**14.8 x**	**23.9 x**

Source: Capital IQ as of January 20, 2014. Amounts in millions of U.S. dollars, except share price.

MARCUM CRONUS PARTNERS LLC
www.MARCUMCRONUS.com
New York | New Haven | Boston

Contact:
Shane Campbell
Director, Marcum Cronus Partners LLC
212.485.5878
shane.campbell@marcumcronus.com