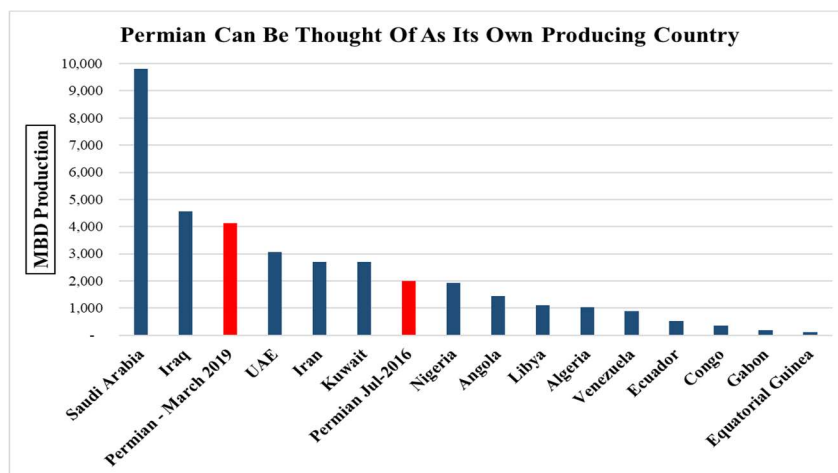


## The Country Permian: A Refresh

### The Country Permian

The volatility of commodity prices and resulting challenges accessing capital markets has led companies within the energy patch to allocate investment dollars to known resource plays (development) which generate the greatest returns on invested capital. The Permian is the lowest-cost producing basin in North America. The volumes (crude oil, natural gas and natural gas liquids) that the Permian Basin produces has made the US gulf coast, the home of the most complex refining center in the world (RCH Energy Midstream letter, January 2017, page 4), a net exporter of all liquid hydrocarbons (crude oil, gasoline, diesel) and propelled the US ethane market to the low end of the global cost-curve for petrochemicals. We believe that this export dynamic is likely to continue to grow as billions of dollars of new infrastructure (LNG, Petchem, Refining, and export takeaway capacity) continues to be built – by end-users in most cases, not the midstream service providers.

In our mid-year 2016 letter (page 7), we coined the phrase *“The Country Permian”* and shared the following excerpt, *“For perspective on the Permian, it can almost be thought of as its own producing country when compared to other OPEC and non-OPEC producing nations. The basin currently produces more oil than Venezuela, Nigeria, Angola, and close to all of Mexico where just five years ago it produced significantly less than all of these countries.”*



Since sharing our “Country Permian” theme, we have seen some significant M&A transactions: ExxonMobil acquired privately held BOPCO (\$6.6 Bn), Diamondback acquired Brigham (\$2.5 Bn), Concho acquired RSP Permian (\$9.5 Bn), and Cimarex / Resolute Energy (\$1.6 Bn). The most recent transaction was announced last Friday (April 12<sup>th</sup>) when Chevron (CVX) revealed its intention to acquire Anadarko Petroleum (APC). According to several sources including CNBC, Occidental Petroleum also bid for Anadarko before the Chevron deal disrupted talks. Occidental’s next move is unknown, but in our opinion, the Chevron / Anadarko transaction is a precursor of more Permian M&A as only a few players of note remain. By our estimation, only five companies (public and private), have attractive Tier 1 or Tier 2 contiguous positions of scale within the Permian Basin to be potential acquisition candidates.

M&A Is Accelerating And Likely to Get Larger					
Permian M&A	2019	2018	2017	2016	2015
Number of transactions	21	74	98	93	80
Annualized	75				
Amount	\$3,300	\$26,000	\$23,000	\$27,000	\$7,900
APC / CVX	\$33,000				
	<b>\$36,300</b>				

\*Property, acreage and royalty interests in transactions

Source: Evercore ISI, FactSet Data Systems, RCH Energy

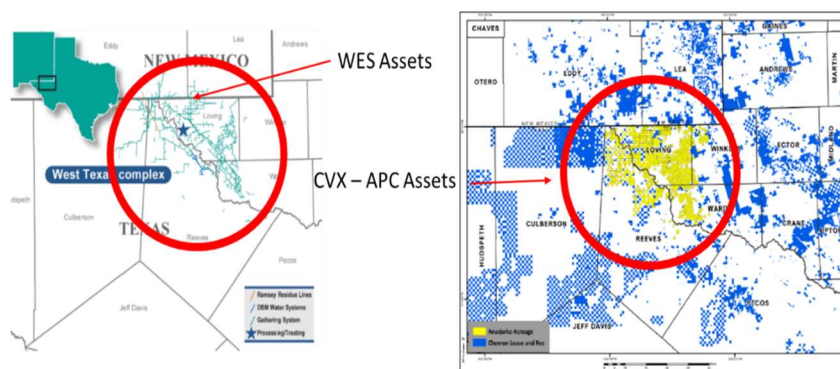
ExxonMobil, another large integrated energy company may also become more acquisitive as they only have approximately five years of drilling inventory in the Permian Basin according to our calculations (see table below).

ExxonMobil: A "Have" in the Permian Battle, Still Needs More					
		XOM	CVX	CXO	FANG
A	Acres	250,000.0	1,700,000	640,000	364,000
B	Sections	640.0	640.0	640.0	640.0
A/B = C	Acres / Sections	390.6	2,656.3	1,000.0	568.8
D	Benches	2.0	2.0	2.0	2.0
E	Assumed Wells / Section	6.0	6.0	6.0	6.0
C*D*E=F	Drilling Locations	4,687.5	31,875.0	12,000.0	6,825.0
G	Rigs Per Year	55.0	55.0	55.0	55.0
H	Locations Per Rig Per Year	15.0	15.0	15.0	15.0
G*H=I	Wells Per Year Drilled	825.0	825.0	825.0	825.0
F / I	Years of Permian inventory	5.7	38.6	14.5	8.3

Source: RCH Energy, Company Data

Our RCH midstream portfolio is supported by volumes from what we believe to be the best in class E&P and integrated oils (the acquired and the acquirers). Our midstream investments provide the key transportation, fractionation and storage logistics for all these entities. We often say, “you cannot understand the midstream without understanding the upstream”. This is playing out before our eyes in the upstream capital markets.

We view the Chevron / Anadarko transaction as a positive for Western Gas (WES), one of our portfolio holdings. Anadarko is the general partner of WES and owns ~55% of its outstanding units. Per the chart below, Chevron has a significant footprint behind and around Anadarko’s acreage and Western Gas’s infrastructure. As such, we expect Chevron to further drive additional volumes through this system and augment WES’s growth profile. We continue to believe in the value of the “Country Permian” and ownership of midstream assets, run by best in class operators, who service the lowest cost basins in North America, will deliver real fundamental cash flows and investment returns.



Source: RCH Energy, Company Data

### The Valuation Opportunity: Haves versus Have Nots not Differentiated; Yet

The structural outlook for best in class midstream continues to be constructive as upstream (E&P) capital is deployed into the Permian basin, downstream (refining and petrochemical) invests in the downstream vertical and midstream companies carry the molecules and capitalize on bottlenecks. Our midstream companies continue to demonstrate and communicate an increased level of focus on ROIC (return on invested capital) and capital discipline. In our view, the midstream investment opportunity remains compelling as the best in class operators have thus far not generated the best returns.

		Current	EV	18-'21	2019E	2020E	2019
		Yield	EBITDA	Growth	EV/EBITDA	EV/EBITDA	Q1 Return
GROUP 1	Large C-Corp 1	4.0%	10.4x	2.7%	10.1x	9.7x	31.5%
	Large C-Corp 2	5.4%	12.2x	7.0%	11.2x	10.6x	32.1%
	Large C-Corp 3	4.9%	15.6x	12.2%	14.6x	12.1x	31.2%
	Large C-Corp 4	6.0%	11.0x	6.5%	10.7x	9.9x	18.5%
	Large C-Corp 5	4.8%	11.2x	6.7%	10.0x	9.6x	27.5%
		5.0%	12.1x	7.0%	11.3x	10.4x	28.2%
		Current	EV	18-'21	2019E	2020E	2019
		Yield	EBITDA	Growth	EV/EBITDA	EV/EBITDA	Q1 Return
GROUP 2	RCH 1	6.0%	12.4x	4.9%	12.0x	11.3x	20.2%
	RCH 2	7.9%	9.4x	6.0%	8.2x	8.0x	18.8%
	RCH 3	9.5%	9.5x	5.2%	9.0x	8.5x	29.4%
	RCH 4	11.0%	9.6x	5.0%	9.8x	8.9x	51.4%
	RCH 5	4.9%	15.6x	12.2%	14.6x	12.1x	31.2%
	RCH 6	5.9%	10.6x	5.1%	9.7x	9.6x	23.9%
	RCH 7	6.6%	8.6x	11.7%	7.6x	6.7x	26.4%
	RCH 8	7.8%	10.3x	15.6%	8.8x	7.5x	27.2%
	RCH 9	8.6%	8.2x	5.8%	7.2x	7.3x	5.5%
	RCH 10	9.2%	11.0x	15.3%	10.7x	8.4x	17.8%
	RCH 11	7.0%	17.3x	25.1%	11.2x	9.9x	15.2%
		7.5%	11.1x	9.8%	9.9x	9.0x	24.4%

Source: RCH Energy, Bloomberg, Company Data

Per the table above, Group 1 represents the largest, most liquid midstream companies which tend to receive the greatest capital flows when “generalists” seek midstream exposure. These companies now trade at levels close to “historical midstream valuations” and offer little near-term equity appreciation in our opinion. The RCH Midstream portfolio has less than 4% invested in the large C-Corps listed in Group 1. We believe cash flows will drive attractive returns on a go-forward basis – not access to indiscriminate capital flows. As such, we believe our Group 2 holdings are positioned to deliver outsized returns versus the peer group.

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