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## Buoyed by higher oil prices, Houston PE funds load coffers

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Liquid gold selling for more than \$100 a barrel is driving a surge in energy-sector private equity activity in Houston and other key oil and gas markets, experts say.

Continued high commodity prices in turn generates more oil drilling, while also encouraging service companies to advance development of technology to make the drilling faster and less expensive.

As a result, Houston PE players say more private equity funding is being pumped into oilfield services firms as 2012 unfolds, as well as continued PE investment in the more traditional exploration and production companies. In short, the entire energy industry is reaping the rewards from the infusion of capital.

"It takes capital to capture the acreage and to drill the wells. The services provider needs more equipment, bigger equipment and to replace old equipment. It's a cascading effect from the upstream to the service sectors. All parts of the value chain need capital to make oil production," said Frost Cochran, managing director of Houston's Post Oak Energy Capital LP.

Post Oak made three private equity investments during 2011. To date in 2012, the company has one investment on the books and intends to make at least three additional deals this year.

"It's an increase in activity for us over the last year, to be sure," Cochran said.

During the first quarter of 2012, U.S. private equity funds raised \$38.1 billion for 136 funds, an increase of 4 percent above last year's first quarter, according to information from Dow Jones LP.

For Houston, home to many energy companies and investment firms, that increased activity in PE investments puts even more people back to work, said Michael Pierce, a managing partner at the Houston office of Thompson Knight LLP. Pierce advises oil and gas clients on equity, debt financing and mergers and acquisitions.

The challenge going forward, Pierce said, is how to price deals given the historic highs in oil prices and historic lows on natural gas prices. Also, he said, investors have to be wary, given that a lot of capital exists within the same space. Investors are chasing the same deals and must be very selective.

Many private equity investors like "repeat transactions," Pierce said. In those cases, a management team acquires assets, develops them to add cash to the balance sheet and then sell them. That's typically a three-to five-year lifespan between the initial investment and the sale, or monetization, of the company.

Just this month, a \$600 million private equity deal was announced by two New York investment firms, Apollo Global

Management LLC (NYSE: APO) and Riverstone Holdings LLC, with the formation of Talos Energy in Houston.

Talos President Tim Duncan, and his team managed Phoenix Exploration Company LP, which was sold to Apache Corp. (NYSE: APC) in Houston for an undisclosed amount last year. Prior to that, Duncan's team led Houston's Gryphon Exploration Co., which was sold to Woodside Petroleum Ltd., which is based in Perth, Australia.

All told, the success of shale plays, the heightened awareness of high oil prices and the need for capital to develop reserves now make the oil patch function in some ways like a manufacturing operation.

"What the shale plays have done for the industry is almost turn oil and gas production into a factory model," said John Graves, founder and president of Houston-based Graves & Co., a transaction advisory, service and support firm to the oil and gas industry.

"There is a lot of money to be made, especially given the decline of other potential investments, the dynamics of moving the industry to almost a factory model of getting things done and reducing risk factors ..., The energy industry has become a lot more attractive to a lot more investors," Graves said.

Private equity investments are also made more attractive by the regulations ushered in by the Sarbanes-Oxley Act of 2002 that have hamstrung some public companies, he said.

"Even small companies say they are spending \$2 million a year to make sure they comply with the law," Graves said. "It makes some people who might have taken their company public want to deal in other ways to finance their operations."

### HOUSTON ENERGY PE DEALS AT A GLANCE

Here's a quick look at some of the high-profile Houston private equity-backed deals rolled out this year in the energy space:

- In January, EnCap Investments LP of Houston and Pine Brook Road Partners LLC in New York put together \$400 million in capital to back a new oil-and-gas acquisitions company, Forge Energy LLC, in San Antonio.
- Houston-based Quantum Energy Partners said in February it had made a \$300 million equity commitment to form to develop shallow water assets in the Gulf of Mexico.
- In late March, Post Oak Energy Capital LP in Houston closed a \$60 million equity deal with Crown Oil Partners IV LP in Midland. Funds will be used as corporate growth capital, development acceleration and for acquisitions.
- Denham Capital Management, a Boston-based lender that houses its oil and gas division in Houston, said this month it had closed its sixth fund, having raised \$3 billion in commitments inside of eight months for deals in the oil and gas space.