PINE BROOK

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The Rigzone Interview: Private Equity Cash Focuses on Oil, Gas Development

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by Deon Daugherty

Upstream private equity focuses on developing oil and gas assets, energy investment pro Claire Harvey tells Rigzone in exclusive interview.

Plenty of private equity capital is willing to play in the oil and gas space, and Claire Harvey, principal on Pine Brook Partners' energy investment team, shares with Rigzone how companies can make a deal.

Rigzone: How does Pine Brook's 'line of equity' approach work in private equity investing?

Harvey: Pine Brook invests capital to build businesses. This typically comes in two forms: growth capital in existing businesses, or in start-up businesses. In both instances, we may utilize a line of equity approach. This means that we allocate capital to a management team or company, but we don't invest all of that money on day one. We do it as capital is needed. Over the life of an investment, the risk profile of the investment proposition changes, and the line of equity allows us to contemplate decisions after taking these changes into account. From a management team's perspective, the line of equity gives teams room to grow without the need to continuously fundraise. In addition, the cost of capital to a management team is mitigated by the fact that capital goes in over time, versus all-at-once.

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- Claire Harvey,
Principal, energy investment team,
Pine Brook Partners

Rigzone: What do you look for when considering whether to invest with a management team?

Harvey: There are multiple things that catch our eye. When it comes to an existing business or a start-up business, it really comes down to the people. As markets change, different things seem more and more important. Ten years ago, you saw a lot of land-flip investments where prospectors were looking for the next big play – the next place to find single wells that produce 5-plus Bcf of gas, or 500,000-plus barrels of oil – it was a different skill set than what is required now. During that time, public company valuations were driven by inventory and companies were active aggregators of inventory. Private equity-backed companies were ripe targets for that inventory. As a result, a lot of private equity capital was deployed to teams with really talented geologic and geophysical staffs.

In today's market, public companies are driven by something different. The industry is in development mode, rather than explore mode, partially driven by the amount of resource we have found and partially driven by the global macro level supply issues and dislocations we've seen in the last couple of years. Our capital generally is being used more for development rather than exploration.

For that, you need more engineering expertise and that comes more in the form of operations – How can I extract 1 percent more from a reservoir? How can I do it for cheaper and faster? Taking something from a $40 resource to a $35 resource is really important in our industry in today's world.

Rigzone: Has the downturn changed Pine Brook's investment strategy?

Harvey: Absolutely. The call on U.S. oil has contracted, causing folks to move to core areas that work at today's prices, with less risk of success. In order to continue to do business, you've got to change your philosophy and change the types of tools you might think are important.

We're not looking for the next big play so we're not looking at exploration much anymore. We've really focused our efforts on the top few basins – the Anadarko basin, the Permian, the Eagle Ford, and certain parts of the Rockies – that is where most of our capital today is going. And most of the business ideas we have backed include the extension or development of those plays. As I mentioned earlier, the management team's skill sets need to fit these plans.

Rigzone: How has acreage cost in the Permian impacted the appetite to develop it?

Harvey: The Permian, the Anadarko Basin and in some cases portions of the Rockies are all moving in the same direction from an acreage cost side. They are ripe with stacked pay, which makes headline acreage valuations striking to some people. You really have to think of it on a per zone basis. $30,000-plus per acre is the combination of three to four zones in some cases, but an acre or section can provide a tremendous amount of inventory for companies. On a human note, I think it's human nature that when you pay a lot for something, you want to see it get developed. That, combined with the public capital market's perception of value, provides a tailwind for development. And, a lot of times there are leasehold issues that might require that development to occur. If you're going to go out and pay $30,000-plus an acre for something and within 24 months you might start losing some of that asset that you just paid for, you're likely to start developing it.

Rigzone: What trends do you anticipate in the next 18 to 24 months?

Harvey: I think you'll continue to see a trend in people raising development capital. There is a lot of capital out there, and not just from private equity funds.

As the supply equation contracts, basins will continue to consolidate and there's going to be a real need for development capital. Different types of capital will fill all of those needs. It will be interesting to see how it's all structured on a go-forward basis, especially as companies continue to evolve and get larger. You might see some management changes in the process, because the team five or 10 years ago doesn't necessarily fit the asset today. We're consistently watching all of the consolidators to see how we can play in the evolution of the capital side, as well as to understand what management teams might get pried loose in the future. It's an ever-evolving industry.

OPEC, in rhetoric, drives a lot of what we do. But on the flip side, the U.S. is in a really good position to control its destiny.

An award-winning journalist, Deon has reported on energy, business and politics for almost 20 years.