

Debt has the power to refocus, redefine or destroy energy companies

By **ROD WALTON** World Business Editor | Posted: Sunday, May 10, 2015 12:00 am

Quicksilver Resources, Dune Energy, Cal Dive International, BPZ Energy.

The average reader in Tulsa may not know those names, but seasoned oil and gas industry insiders certainly do. They are some of the firms that have filed for bankruptcy in the wake of this latest oil bust.

Tulsa's energy sector so far has been spared the specter of high-profile Chapter 11 reorganizations. Instead, many energy companies have slashed budgets and payrolls.

But that grace period may not last for long.

Privately held Samson Resources Co., founded by the Schusterman family 44 years ago and sold to private equity firm KKR & Co. for the steep price of \$7.2 billion in 2011, is on the brink of bankruptcy, by many accounts. The company has nearly \$4 billion in long-term debt, has stopped its drilling, has hired restructuring firms and was down to its last \$175 million in cash as of last month, according to a Samson conference call in April.

“I don't see that they have many options,” longtime Tulsa money manager Fred Russell said. “Samson is probably spending most of its time with its restructuring advisers conferring to see when and how they do it. I think that's probably consuming all of their energy right now.”

Samson, when it's drilling, remains one of the nation's biggest private oil and gas producers. What is choking the company, along with high debt and interest payments, are low oil and gas prices — now at about \$60 per barrel, but still off 40 percent from last summer.

It's making it virtually impossible to generate enough revenue to offset the leverage of lenders.

Leverage cuts two ways

During good times, corporate debt can fuel growth by helping to buy new rigs and drilling new wells. In bad times, debt can kill.

"Companies borrow money and invest in properties to generate good returns," said Rick Buterbaugh, chief financial officer for Tulsa-based producer Laredo Petroleum Inc., which itself is trying to adapt to low prices by lowering its long-term debt, getting some lower interest rates on senior notes and pushing maturities out several years.

"You don't want the bulk of your cash-flow stream just going to service your debt. That doesn't give you any funds to reinvest in your business."

Worse yet, it can gut that company in Chapter 11 reorganization or force it to sell assets at a relatively desperate discount.

No Tulsa energy company has sought bankruptcy protection since the oil downturn started last summer, but many are doing what they can to quit digging the holes. WPX Energy was sustaining regular net losses in its first few years but recently tightened up its core focus, sold \$1.5 billion in non-core assets and cut its capital budget by half to \$725 million this year.

WPX Energy reported a \$67 million profit for the first quarter.

"We had the wheels turning even before the downturn happened," WPX spokesman Kelly Swan said.

Debt-to-capital and other high-wire ratios

Midstates Petroleum is a relative newcomer to the Tulsa energy scene, having spent about \$1.3 billion to buy assets from Tulsa-based Eagle Energy and Panther Energy several years ago. Even company leaders previously admitted that perhaps they paid too much for some assets.

The company moved its headquarters from Houston to Tulsa late last year to focus on those core assets in Oklahoma and Texas while it sold virtually everything else.

But Midstates, which is much smaller than Samson and WPX, still has \$1.7 billion in long-term debt and suffered a \$193.6 million net loss for the first quarter due to accounting impairments on the value of its assets.

Midstates has changed CEOs twice in the past 15 months while it deals with huge debt and fallen commodity prices. It has a debt-to-capital ratio of 78.8 percent, perhaps the highest among local, publicly traded energy companies.

Moody's investor service in January lowered its various debt-worthy ratings.

The rating service warned "as Midstates continues to outspend cash flow, albeit at a reduced pace going forward, and as bank price decks begin to reflect a lower crude oil price and lower hedged production, Midstates' tight liquidity likely will shrink further over the next 12 months," the Moody's report reads.

"The negative outlook reflects the company's highly leveraged balance sheet, which impedes its ability to raise additional liquidity with which to sustain production, as well as Midstates' likely need to seek covenant relief early in 2015."

Randy Foutch, who founded Laredo after starting and selling numerous other companies, knows the boom-and-bust nature of the oil business. In his career, he has seen six cycles in which the price of oil has dropped more than 50 percent.

His company, which is focused in the Permian Basin of west Texas, has stepped up its pace in cutting debt and trying to reduce its debt-to-capital ratio, which is relatively high at 53.54.

Laredo's long-term debt rose from \$636 million at the end of 2011 to \$1.8 billion as of Dec. 31, 2014, according to its filings with the U.S. Securities and Exchange Commission. Dramatic, evasive action was taken to pare down that debt. Laredo sold 69 million shares, at only \$11.05 per share, in a public offering, to repay the balance of its senior secured-credit facility and redeem \$550 million of senior notes which had a 9.5 interest rate and were due to mature in 2019.

Instead, Laredo issued new senior notes at a lower interest rate and pushed the maturity out to 2023. "It's not as much how much you owe but when it's due," a wise oilman once said.

"It gave us more flexibility," Laredo CFO Buterbaugh noted about cutting the company's long-term debt to \$1.3 billion. "It gave us the ability to reduce our cash interest costs."

Laredo has decades' worth of drilling opportunities to sustain it now and when the oil price rallies. The company's assets and liabilities are equal at \$4.655 billion, according to its most recent earnings report.

FlexRigs and flexibility

Another company, which is a driller and not a producer, is known for surviving busts by keeping debt relatively low even during growth periods.

Tulsa-based Helmerich & Payne laid off 2,000 employees earlier this year, but its bottom line is solid. The contract driller and rig maker has one of the industry's lowest debt-to-capital ratios at 1.6, with long-term debt of just more than \$500 million.

Money manager Fred Russell touted Helmerich & Payne as one of those companies that is always prepared for the downturn. Company Chief Financial Officer Juan Pablo Tardio said the last time H&P reached a 20 percent debt-to-capital ratio was in 2007, to finance growth through construction of its popular FlexRigs.

Since then, Helmerich & Payne has used proceeds from FlexRig contracts to pay down that debt and reduce the ratio below 2 percent.

“This is a very competitive business, and only by effectively managing costs and by innovating, applying new technologies and continuously improving its ability to deliver top performance can a company prosper while delivering customer satisfaction and a fair and reasonable return on invested capital for its shareholders,” Tardio said in a statement.

Company boxed into the corner

Samson Resources, then known as Samson Investment Co. loomed large in the energy landscape when the Schusterman family sold it to KKR and a group of partners for \$7.2 billion. The plan was to eventually take the oil and gas giant public at a profit for its investors.

KKR is known historically for using debt leverage to finance its acquisitions, and Samson was treated no differently. Twin strokes of bad luck, market-wise, almost imperiled the company's planned ascent as natural gas and oil prices floundered and debt levels rose by \$500 million in only three years.

Samson officials declined to comment for this story, on advice of its attorneys. Even so, it's unfair to imply that the company hasn't worked hard to overcome its debt ailments.

One of those moves, unfortunately, was laying off more than 270 employees, nearly a third of its workforce. Samson also reworked its covenant with lenders, reduced its borrowing base by \$50 million and sold \$48 million in Arkoma Basin assets.

The wiggle room is seen as almost non-existent for Samson. It has to maintain \$150 million in liquidity by July 1 while relying on revenues from current producing wells since new drilling and completions have stopped.

And then there's those restructuring firms, Kirkland & Ellis LLP and Blackstone Group. Kirkland & Ellis has handled bankruptcies for General Growth Properties Inc., Flying J and Tronox, among many others.

"I think they see the writing on the wall," Russell said of Samson in April. "They figure they might as well go into bankruptcy and put their finger in the dike."

Chapter 11 can breath new life into a company by cutting out unsecured debt. SemGroup LP looked like it was headed to a selloff of assets when it filed in July 2008, but it emerged as publicly traded SemGroup Corp. in late 2009 and has been stronger ever since.

A killer dose of debt can put companies in corners at times like these. All of those — from Samson to WPX, Midstates and Laredo — are trying to fight out of that corner as best that they can.

"If you haven't done that, for whatever reason, then there's companies that are going to be stressed," Buterbaugh said. "I've already seen companies file for bankruptcy in the industry that were not well-prepared."

And others are sure to follow, whether in Tulsa or not.

Tulsa companies and debt-to-capital ratios

Company	Debt-to-Capital Ratio*
Midstates Petroleum	78.83 percent
Laredo Petroleum	53.54
Mid-Con Energy Partners	46.82
WPX Energy	34.55
Unit Corp.	25.83

Helmerich & Payne 1.61
Samson Resources N/A**

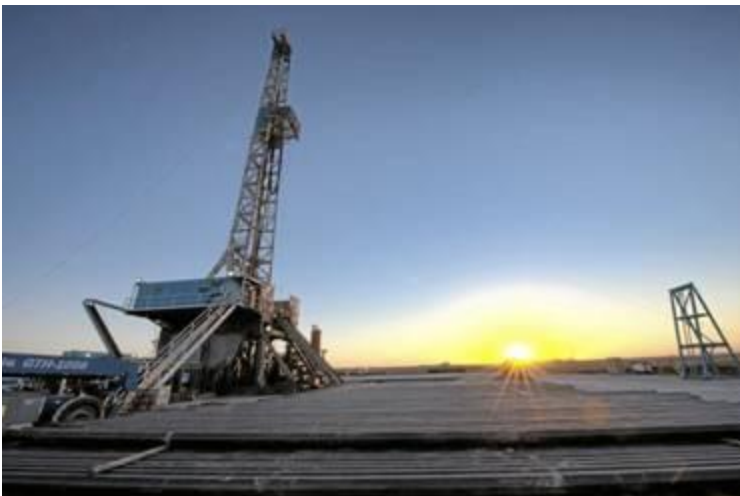
* ratio is percentage of total debt to total capital (equity and debt)

** Samson is privately held company

Source: marketwatch.com



Money manager Fred Russell, CEO of Fredric E. Russell Investment Management Co., for mug. Taken on May 5, 2015. CORY YOUNG/Tulsa World



Midstates Petroleum drilling rig

Midstates Petroleum has \$1.7 billion in long-term debt and a debt-to-capital ratio of 78.83, among the highest among local, publicly traded energy companies. Courtesy