North American E&Ps: Dispelling debt bubble fears-an issue for a few, but not the many

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During the oil boom, upstream companies financed rocketing production growth and sizable cash flow deficits with cheap money during a low interest rate environment.

Who would not?

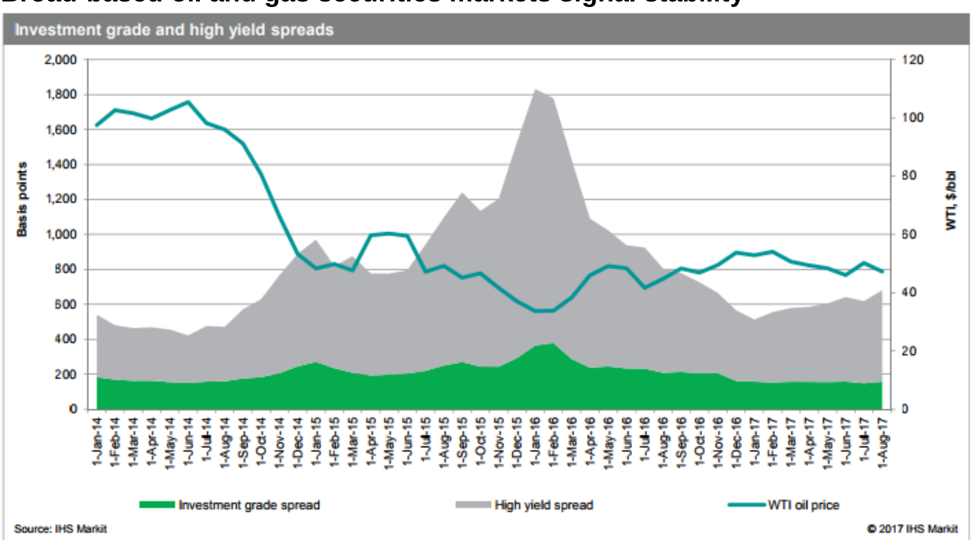
Debt ballooned to unprecedented levels, and as oil prices collapsed, as many as 160 North American upstream companies declared bankruptcy or commenced strategic reviews.

As we emerge from the rubble of the 2014 oil price collapse, there remains a significant amount of debt on North American upstream oil and gas company balance sheets, raising investor concerns that companies might not be able to sustain capital spending and production growth. This report, utilizing IHS Markit fixed-income data, dispels the notion that serious debt issues are broad based. Instead, we believe that relatively few companies on our IHS Markit North American E&P coverage list are at high risk.

Our analysis finds high yield-to-maturity (YTM) rates on only 20% of our coverage list, with the vast majority of operators incurring yields similar to 2014, when oil prices were $100 per bbl. Our analysis also shows that for roughly 25% of operators, yields are actually lower than in 2014.

Surprisingly, these select producers are small-cap companies with acreage primarily focused on the Permian and Marcellus. Analysis of debt maturity schedules indicates that companies have prudently refinanced near-term debt, taking advantage of low interest rates and preparing for a low-commodity-price environment. Collectively, the Large, Mid-sized and Small E&P peer subgroups reduced principal debt due in the next five years by nearly 20%, from $80 billion to $65 billion.

Broad-based oil and gas securities markets signal stability



IHS Markit proprietary indices that track oil and gas-focused company yield spreads to U.S. Treasuries confirm stability in the markets for both investment and noninvestment grade fixed-income securities.

YTM peaked at 1,800 basis points for noninvestment grade securities in early 2016, which coincided with the bottoming of oil prices at $33 per bbl. Yields for investment grade securities also peaked at that time, at 377 basis points.

Currently, with oil prices rallying and stabilizing in the $45–50 per bbl range, investment grade securities yields are lower than yields in early 2014 despite 50% lower oil prices. Yields on noninvestment grade securities are materially lower as well, at 525 basis points, but higher than the 400 basis point spread in early-to-mid-2014.

For more information on our Companies & Transactions Research, contact us.

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