Finding True Market Value of Assets

By Josh Robbins

When historic oil companies/families like Yates, Clayton Williams and Bass sold out in the first quarter of 2017, it started a wave of transactions that we expect to carry through the rest of the year and deep into 2018. The oil business is very much an extended family, and when the families start to cash their chips in, those around them start to wonder what their chips are worth as well. But what is the true market value of an asset? Judging by the amount of deals at NAPE that were asking far too much, the answer to that questions seems to be "it depends…"

Josh Robbins, Beachwood Marketing Group. Credit: Edgar Lance Photography

First, it's very important to know that in the oil and gas world there are two very different paradigms taking place. These paradigms are radically changing the approach many publicly traded companies are taking to purchasing assets. The two ends of the spectrums are the finance/stock value and the traditional value.

On the one side of the spectrum, traditional value is very common, which is based solely on the actual reserves of an asset, the production decline curve, and the costs of running the well, including the expenses and taxes associated with it. Focus for additional value can be found in PUD locations, potential reworks, and increased net revenue. Increased or decreased value of an asset depends on geographic location, depths held within that geographic location and size of the acreage block.

On the other side of the spectrum, the finance/stock value of the market is removing nearly all of the data above when valuing an asset, position or company purchase. The value is not actually based on the oil and gas assets. The value is created on Wall Street, allowing companies to purchase in the buzzword areas that help raise their stock. The stock increase, in some cases, completely wipes out the cost of purchasing the assets.

As these assets or entire companies are purchased, the asset decline curve still exists, and therefore forces the new owner to cut costs. With these company acquisitions, that usually means the employees from the recently bought out company will be integrated, or removed, if the position is already filled. By cutting the workforce, the buying company is removing operating expenses, and will show an immediate increase in profitability, which will in turn, in theory, increase the stock value even more.

When the two paradigms face each other, there is no way to evenly equate value of an asset. This causes price increases in specific areas, which will soon spread through most of the oil patch. New buzzwords will continue to be created throughout the year. The deal flow therefore, will continue to be high among publicly traded organizations for an extended time. Actual transactional volume with independent oil and gas firms will slowly decline as we enter into the third and fourth quarter as the money gained from increased price per barrel and MCF will be reallocated to infield development.

We expect service prices to continue to rise but with some pushback from operators. Instead of allowing a 20% hike in prices, independent operators will switch vendors, because higher oil will bring additional vendors to the market. With service companies competing for business, the oilfield will continue to grow throughout all of 2017.

The true market value of an asset depends on many things, but it comes down to just one. Who's buying it?