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Q&A: Keith Behrens

Keith Behrens
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Mr. Behrens has over 23 years of investment banking experience with major investment banking firms including Bear Stearns and Wasserstein Perella. He has focused most of his career in covering primarily exploration and production companies as well as other energy-related companies. Mr. Behrens has generated and led the execution of various M&A, public & private equity and senior & mezzanine debt transactions representing 150 transactions and approximately $27 billion in transaction volume. Mr. Behrens received his BBA and MBA from the University of Texas at Austin.

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Mr. Behrens joined Stephens in May 2009 as a Managing Director and serves as the group head of the Energy division. Below, he answers questions and offers insight into some of the surprising dynamics in the oil and energy sector.

Are you surprised by the dramatic drop in energy prices?

Prices have certainly fallen further and quicker than most had anticipated. It felt like there was some softness in oil when it was in the $80s, but most people probably thought that meant it was going to drop gradually into the $70s, not into the $40s.

There has been a lot of talk about how this is good news for consumers, even if it hasn't really shown up yet in spending, and how it is hurting the stock valuations of big oil companies. What is the bottom line on who benefits?

The consumer benefit is for sure. Even if they aren't spending those savings yet, they're seeing them. You hear people talking all the time about how low their gas bill is when they fuel up.

Businesses that have fuel costs as a large operating expense are also benefiting, such as airlines and transportation companies. A number of airlines are reporting strong earnings; some are even removing fuel surcharges from their fares, which is another benefit for consumers.

What about the oil companies?

There are a couple of nuances around this situation that people need to recognize. One is that there are still a lot of companies selling oil at much higher prices than the current market rates as a result of hedging strategies. There are numerous companies that have strong hedges in place for most if not all of 2015, so cash flows are probably stronger than what people expect.

And while there have been reductions in capital budgets, that doesn't necessarily mean production will fall near term, particularly with unconventional production, like shale, where you typically get a lot of the production in the first year and diminishing production in outer years. These wells with high initial production rates are typically better-return drilling projects. So companies will likely high grade their reduced capital budgets and focus on the higher-return wells, which means near-term production will fall less than corresponding decreases in capital budgets.

So while most U.S. producers have been pretty disciplined with their capital budgets, a lot of them are still projecting production increases for 2015. I think it's more likely to be 2016 when we will see production levels begin to fall.

What affect will lower prices have on alternative energy development?

Costs are only one side of the equation. So yes, with oil and gas prices lower, there may not be as much financial incentive to explore alternative energy, but there will always be the environmental incentive. You are even seeing more attention around the environment in practices of the traditional oil and gas companies.

Are you seeing any effect around M&A activity related to the sector?

Given the volatility in prices it's hard to nail down valuations for the buyer and the seller because there's still a wide gap in the bid/ask spread.

I think it will pick up first on the services side. Companies that are over-levered are going to have to look at their options. On the E&P side, it's going to take some price stability for M&A activity to accelerate and for companies to really feel the fall in their revenues and the pain of having to service debt.

We'll likely see some small deals done on the public equity side, in little subsectors that are lower risk in the value chain. There are companies that have done some creative deals, like spinning out an override and putting it into a new vehicle and taking that public I think you're going to see more deals like that done.

And there is a lot of private equity money to be deployed. This is the kind of environment they like, because they think they can buy low.