Oil & Gas Mergers and Acquisitions Report
Year-end 2012

Deloitte Oil & Gas Mergers and Acquisitions
Stable oil prices support a healthy deal market

Deloitte Center for Energy Solutions

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Vice Chairman's introductory comments

A few major transactions near the end of the year pushed the oil and gas industry’s overall deal value to $321.5 billion, about 7% higher than 2011 levels. Driven by Rosneft’s $61.6 billion purchase of TNK-BP, the focus of buyers’ attention remained in the upstream space. Excluding the Rosneft transaction, much of the activity once again was concentrated in North America around unconventional plays. National oil companies (NOCs) and other large international buyers continue to be active in the North American market and elsewhere as they work to expand their resource base around the globe.

A relatively stable oil price environment set the stage for greater confidence around upstream oil investments. Crude oil prices have settled into a stable range, which gives people more confidence in deal valuations. The same cannot be said of natural gas where prices, although up from their very depressed levels at the beginning of 2012, remain weak. U.S. natural gas supply growth is outpacing demand growth, resulting in continuing low prices and peak inventory levels. Natural gas liquids prices, which had held up while dry gas prices fell, declined during the second half of 2012. Liquids prices are responding to a glut of product in the market, and that oversupply could continue to dampen activity in the coming year.

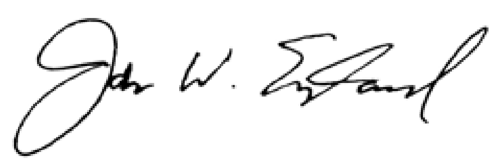
Deal activity in 2012 slowed from the rapid pace in 2011 in the midstream and oilfield services sectors. However, midstream activity remained at historically high levels, and continued to revolve around transactions that will facilitate serving of the shale plays in North America. Growth in midstream pipeline and processing infrastructure has not kept pace with growth in the unconventional resource plays, providing many opportunities for capital investment that we expect to lead to more midstream deal activity in 2013.

The downstream sector has been through a major reshuffling the past couple of years with the spin-off of the downstream businesses of two large integrated oil companies and two significant refinery dispositions by BP. The North American refining industry, once controlled by large integrated firms, is now mostly dominated by independent companies.

Uncertainty and inaction in Washington has led to some hesitancy among potential energy industry executives and investors. The oil and gas industry has been the target of some groups in Washington looking for sources of new tax revenues, and whether they achieve the desired results could affect activity in the coming year. Investors are still waiting to get clarity from Washington on the direction of overall tax reform, and the specific changes that will affect the economics of oil and gas deals in the future.

Industry executives and other deal market participants should keep an eye on regulatory direction in the upcoming second term of the Obama administration. As the U.S. oil and gas industry and its activities become larger and more publicly visible across the multiple shale and tight oil basins, it is incumbent upon companies to be particularly diligent in following the evolving regulations and be sensitive to environmental concerns as these new plays are developed. Continued vigilance and adherence to leading operational practices will go far to take steps that the country’s energy renaissance is not derailed.

Oil and gas companies continue to make significant technological advancements in drilling and production, and as we see completions rise in an increasing number of North American fields, we expect to see continued improvements not only in cost effectiveness, but in safety as well. For the past five years, the world has witnessed the dramatic development of unconventional oil and gas in North America. Unlocked by technology and innovation, development of these domestic resources continues to change the global energy landscape.



John England
Leader, U.S. Oil & Gas
Vice Chairman, Deloitte LLP

Source: PLS Inc. and Derrick Petroleum Services Global M&A Database

Industry overview

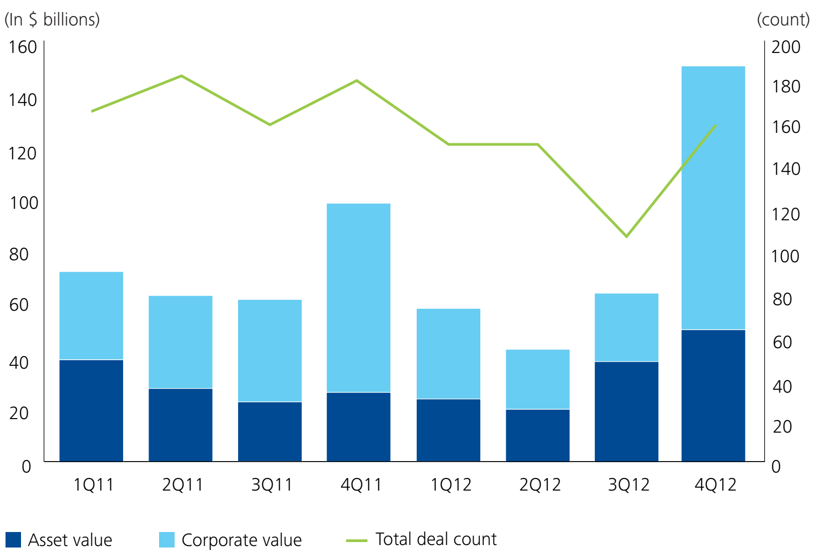
North America remains the center of merger and acquisition (M&A) interest and activity

Although the headline transaction for 2012 was Rosneft's $61.6 billion acquisition of TNK-BP, the North American oil and gas industry continued to drive strong M&A activity in 2012, centering on unconventional and deepwater oil and gas resources. In spite of depressed natural gas prices in North America, the opportunities in oil and natural gas liquids created a robust investment environment ranging from deepwater deposits in the Gulf of Mexico to the Bakken formation in North Dakota to the oil sands of Alberta. Much of the new investment came from outside the region from NOCs and other international buyers who are attracted to the North American market for several reasons. These include a) the political stability and maturity of the investment environment, b) ability to invest in resource plays that are well known with predictable results, c) access to the technology and workforce expertise that have driven the boom in exploration and production (E&P) of unconventional and deepwater sources of oil and gas in North America, and d) the potential that continued growth could lead to an export market for North American resources.

The total 2012 value of global energy deals reached $321.5 billion, compared to $300.6 billion in 2011, despite a drop in the number of deals from 698 to 576. This decline in deal volume was experienced in the lion's share of segments except the downstream area. (NOTE: This deal data excludes transactions less than $10 million and also excludes transactions between affiliates.) While the substantial percentage gain in transaction value reflects the inclusion of a few very large international transactions during the fourth quarter, overall deal activity remained healthy and continued to be driven by the exploration for and development of unconventional oil and gas resources. "The unconventional trend has had ripple effects throughout the industry value chain," said Trevear Thomas, Principal, Deloitte Consulting LLP. "First E&P assets, then midstream and even downstream refinery activities have responded to the shale and tight oil boom in North America."

Note: M&A activity examined in this report represents mergers and acquisitions involving oil and gas companies between the first quarter 2011 and the fourth quarter 2012 with values greater than $10 million, including transactions with no disclosures on reserves and/or production. Our analysis has excluded several transactions between affiliated companies to provide a more accurate picture of M&A activity in the sector. Deloitte's methodology takes a deeper look into the M&A transaction data.

Oil and gas M&A deals by value and count



Source: PLS Inc. and Derrick Petroleum Services Global M&A Database

Oil prices were relatively stable during 2012, held back by the economic slowdown in Europe and the sluggish nature of the U.S. recovery, among other factors. "Some of the moderation in oil prices also has to do with the significant increase in North American supplies," said Jim Dillavou, Partner, Deloitte & Touche LLP. "North America is importing less oil and this helped to moderate global prices in spite of the embargo on Iranian oil. Also, because of supply bottlenecks with the new North American supplies, U.S. oil prices are often below those in the rest of the world, creating a price differential that has traditionally not existed."

The approximate $15 to $20 per barrel oil price differential between the U.S. benchmark WTI prices and international markets could be considered small if compared to the large spread between domestic natural gas prices and those overseas, especially in Asia. While North American gas prices recovered somewhat by the end of the year, they remain at historically depressed levels, which are less than half of those in most parts of the world. In many cases, prices are below where many North American producers in the unconventional space can operate profitably. The industry as a whole responded to this by effectively applying the horizontal drilling and fracturing techniques used to create the boom in natural gas production to more profitable natural gas liquids and oil resource plays, a trend that began in 2011. Once again, producers fell victim to their own effectiveness as natural gas liquids prices reacted to the resulting increased supply by weakening in 2012, creating further pressure on gas producers. The oilfield services side of the business was most affected by the sustained weakness of natural gas prices, with rig counts declining and margins under pressure from weakening services pricing environment. Natural gas prices are not expected to rebound significantly in 2013; however, deal activity may pick up in the E&P and service areas as industry consolidation takes place and buyers with a longer-term time horizon are attracted to the lowered asset valuations and long-term potential of U.S. natural gas.

Source: PLS Inc. and Derrick Petroleum Services Global M&A Database

Political uncertainty over the direction of tax and fiscal policy in Washington may have had a negative impact on the deal market during 2012. "Some buyers and sellers did push to get deals done, driven by the changes to the tax law," said Jason Spann, Partner, Deloitte Tax LLP. "A few people were incentivized to get deals completed in 2012 at more favorable tax rates." Looking ahead, U.S. lawmakers left a significant deal undone at the end of 2012, creating lingering uncertainty. "For an investor, the uncertainty has an impact on transactions and how much they are willing to pay," said Mr. Dillavou. "The uncertainty makes it more difficult for buyers and sellers to reach an agreement on pricing." The domestic energy industry has so far avoided any drastic changes in regulation or taxation, but the risk of change still exists. "A disproportionate or extreme change in regulatory oversight or taxation could put at risk the energy renaissance that North America is experiencing," cautioned Roger Ihne, Principal, Deloitte Consulting LLP. "The shale gas revolution initially benefited the oil and gas industry, and is now largely responsible for potentially hundreds of billions of dollars in investment slated over the next decade for midstream infrastructure, added petrochemical capacity, LNG export facilities, and other manufacturing related capital outlays. The impact is nothing short of phenomenal."

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– Jason Spann
Partner
Deloitte Tax LLP

Source: PLS Inc. and Derrick Petroleum Services Global M&A Database

Exploration and production

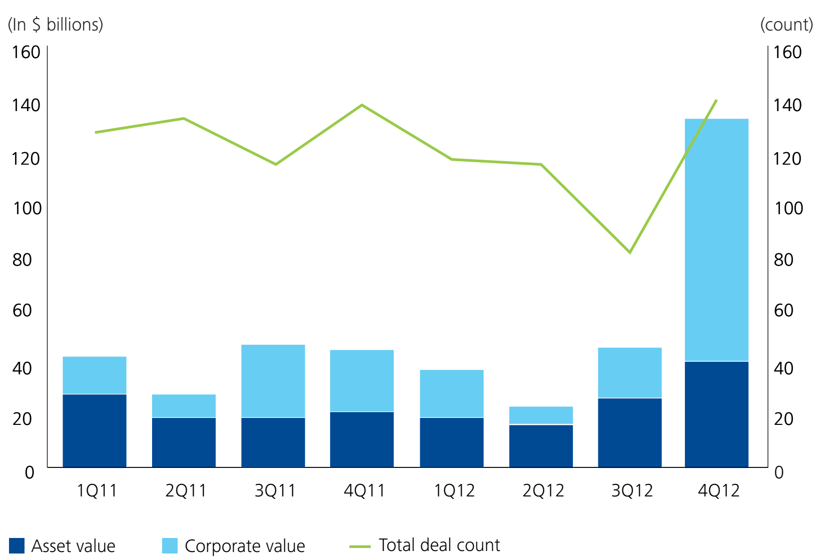
Continued global interest in North American unconventional plays

Interest in North American assets supported a healthy upstream transaction market in 2012. Globally, total deal value in this segment rose 50% to $253.4 billion in 2012, compared to $167.9 billion in 2011, even as the number of deals declined 11% from 518 to 461. The upsurge in 2012 activity took place almost entirely in the fourth quarter, as Rosneft's acquisition of TNK-BP alone contributed $61.6 billion to total deal value. NOCs in particular showed continued interest in North American E&P assets. "We continued to see strong interest from foreign buyers, including state-owned enterprises," commented Mr. Dillavou. "Those companies are getting involved in North America's oil and gas markets in order to better understand shale and tight oil resources." Mr. Thomas agrees. "NOCs want to be a part of the North American energy business," he said. "It is where a lot of the technology is based, and where many skilled workers reside. NOCs want to leverage that technology and skill in other parts of the world."

One of the larger E&P transactions during 2012 involved the announced acquisition of a Canadian public company by a Chinese NOC during 2012. U.S. laws make it more difficult to export oil and to a lesser extent, natural gas than Canada, partly reflecting that the U.S. is a large net importer while Canada is a net exporter of oil and gas resources. Many investments by NOCs in North America have been through noncontrolling interests in joint ventures. International firms' quest for North American properties—and South American as well—should continue as countries such as China and India address their growing energy demands and diversify their portfolios.

Large integrated companies should also be active buyers, as they look to the market for new properties to offset production declines that have been prevalent among the majority of the supermajor oil companies. "In the past, whenever we have encountered production declines, we have seen a big burst of M&A activity," noted Mr.

Exploration and production M&A deals by value and count



Source: PLS Inc. and Derrick Petroleum Services Global M&A Database

Ihne. "The large integrated companies need to increase production and one way to do that is through prudent acquisitions." North American natural gas assets may look particularly attractive to buyers with long-term time horizons, given depressed prices that may be putting pressure on smaller companies to sell. "At some point, the valuations in the natural gas area become so attractive that buyers with a long-term strategy can make a good deal of money," added Mr. Ihne.

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Principal
Deloitte Consulting LLP

Source: PLS Inc. and Derrick Petroleum Services Global M&A Database

Midstream

A once sleepy segment responds to growing U.S. infrastructure needs

Comparisons of year-over-year midstream transactions were skewed by the inclusion of a few extremely large deals that took place near the end of 2011—including Kinder Morgan's acquisition of El Paso Corporation. For a segment that recently was among the quietest in the energy industry in terms of major dealmaking, transaction activity remained relatively brisk in 2012, with the total value of M&A deals reaching $35.6 billion, but down significantly when compared to $84.5 billion in 2011.

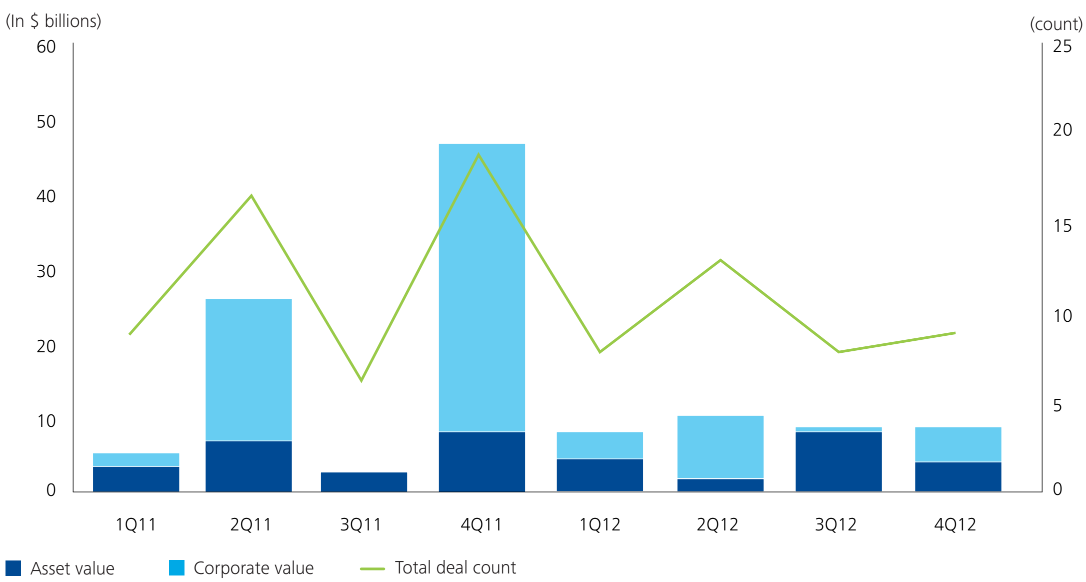
The transformation of the U.S. energy landscape of the past few years has created the need to move domestically produced oil and gas to market from new regions and in new directions. This will continue to drive capital spending and funding needs in the midstream sector for years to come. "Deloitte believes that, over the next few years, the size of capital expenditures in the midstream area could easily exceed the current market cap of those companies," noted Mr. England. "It is therefore reasonable to think that we could see some bigger players enter the market, some consolidation take place, or a combination of both, if the midstream segment is going to continue to support the shale and tight oil activity that is taking place in the United States."

"Looking ahead, we expect continued growth in this area, and related acquisition activity, as MLPs search for quality assets to grow their distributions."

– Trevear Thomas
Principal
Deloitte Consulting LLP

Master Limited Partnerships (MLPs) continue to be the vehicle of choice for pipeline investment. Despite some lingering uncertainty over the future tax treatment of these vehicles, the number and size of MLPs should continue to grow. "We are witnessing the emergence of supermajors in the MLP sector, with big players getting bigger," noted Jed Shreve, Principal, Deloitte Financial Advisory Service LLP. "Looking ahead, we expect continued growth in this area, and related acquisition activity, as MLPs search for quality assets to grow their distributions." Mr. Thomas adds "several large deals have already been done, and we are likely to see a number of 'Tier 2' deals that will drive the next wave of consolidation, as companies shore up their competitive positions and strategies."

Midstream M&A deals by value and count



Source: PLS Inc. and Derrick Petroleum Services Global M&A Database

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– John England
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Source: PLS Inc. and Derrick Petroleum Services Global M&A Database

Oilfield equipment and services

Declining rig count is the backdrop for falloff in U.S. transaction activity

Transaction activity in the oilfield services sector was relatively quiet in 2012. The total value of transactions amounted to $17.9 billion, a $20.1 billion, or 54% decline from 2011 and the number of deals declined from 97 in 2011 to 57 in 2012. Activity dropped steadily as 2012 progressed, and only six transactions over $1 billion occurred during the year. For onshore oilfield services companies, the steadily declining U.S. rig count over the course of the year tells the tale; by year-end 2012, the U.S. land rig count had dropped 13%, according to the Baker Hughes rig count report, from 1,965 to 1,712 rigs. "Major oilfield service companies experienced softening demand in the second half of the year, as rig counts dropped," noted Mr. Shreve. That in turn put pressure on margins and on stock prices for publicly held companies. "It has made the companies less capable or interested in doing transactions," noted Mr. Dillavou. Additionally, with the shift in focus from dry gas to liquids by producers, the oilfield services companies have also been forced to relocate resources and services to match what the producers are doing. The shift has created inefficiencies and overcapacity in some areas and a struggle to reposition resources and labor to the emerging liquids areas. Sellers and buyers may have been far apart of valuations in 2012, with overcapacity and related margin issues arising rapidly following years of rapid growth. 2013 may be a year when M&A activity rebounds in the onshore oilfield services sector, as sellers become more realistic about pricing and consolidation takes place in what is still a fragmented industry.

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– Jed Shreve
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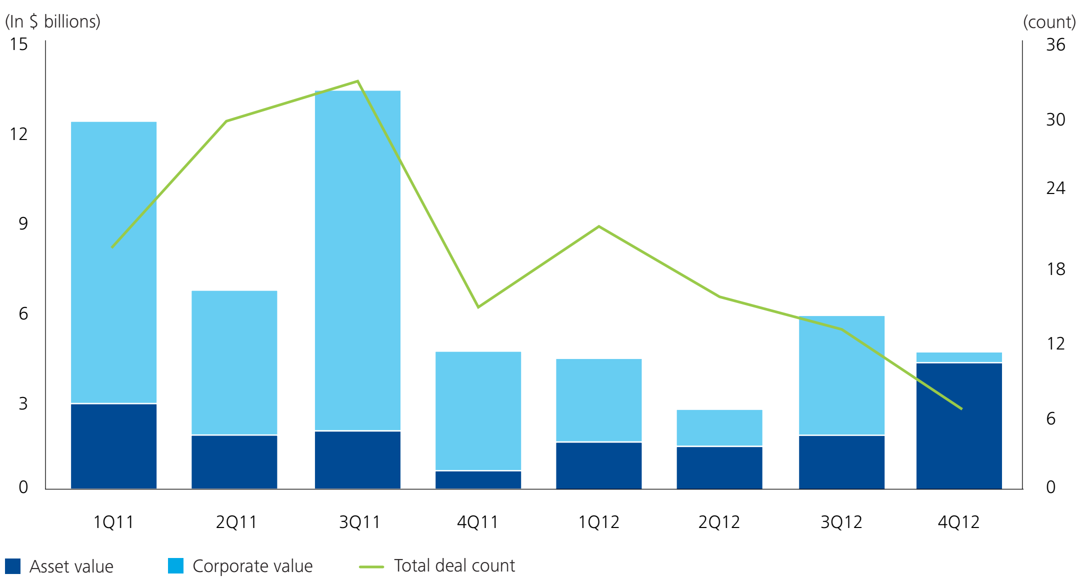
Deloitte Financial Advisory Services LLP

Oilfield equipment and services M&A deals by value and count



Source: PLS Inc. and Derrick Petroleum Services Global M&A Database

United States rotary rig count in the Gulf of Mexico

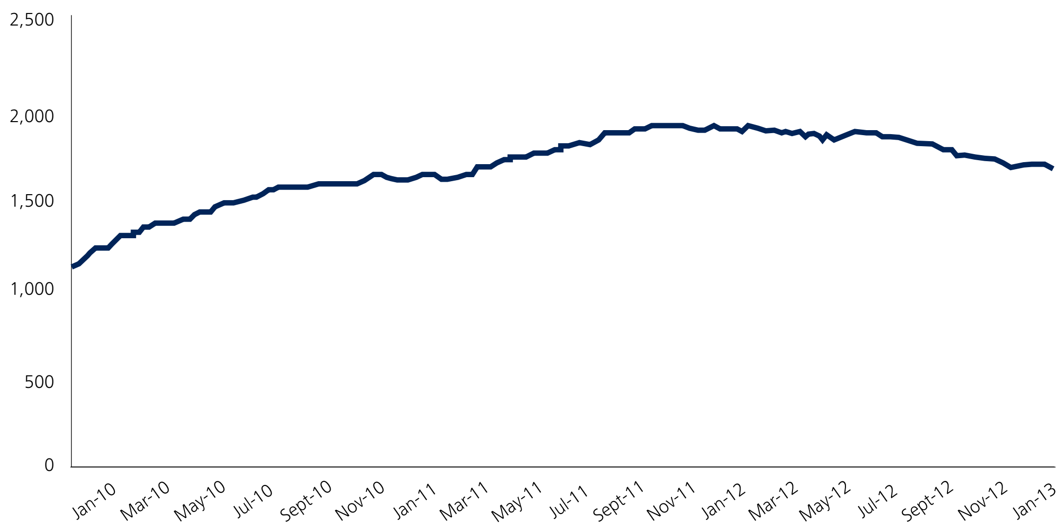
Source: Baker Hughes

"The potential in the Gulf is so great, even some independents are returning in spite of the increased costs, risks, and delays associated with the stricter permitting process."

– Jim Dillavou
Partner
Deloitte & Touche LLP

Source: PLS Inc. and Derrick Petroleum Services Global M&A Database

United States onshore rig count



Source: Baker Hughes

Offshore, an area inhabited primarily by larger companies with a growing emphasis on subsea development, activity has been steadier. "We still think this is an area where people are looking to invest in new technologies," said Mr. Spann. There are a number of significant offshore developments around the globe that will demand a high level of service as those fields are developed. This may create opportunities for service companies to add capacity and technology to serve these as the development pace increases. As activity in the Gulf picks up, one trend that Mr. Dillavou notes is the reentry of some smaller companies into that region. "It is harder for them after the Macondo incident, but we are definitely seeing smaller companies move back into the Gulf," he said. "The potential in the Gulf is so great, even some independents are returning in spite of the increased costs, risks, and delays associated with the stricter permitting process."

Source: PLS Inc. and Derrick Petroleum Services Global M&A Database

Refining and marketing

Independent companies now dominate the downstream space

The major news in the refining and marketing sector during the past two years was the completion of downstream spin-offs by Marathon Oil and ConocoPhillips, to form two very large independent, public companies, Phillips 66 and Marathon Petroleum Company. "This along with the sale of two large refineries by BP, means that over 70% of the United States. refining capacity is controlled by independent refiners," noted Mr. Ihne. "There are now three publicly held, independent downstream companies with significant capacity operating in the United States which could have increasing influence over the domestic refining market." Additionally, there is a growing number of smaller publicly held independent refiners, which could help shape the future of the domestic market as possible consolidation among refiners occurs over subsequent business cycles.

Overall, deal activity remained steady, as the dollar value rose to $14.6 billion for the year compared to $11.0 billion in 2011. The two largest deals for the year occurred outside of the United States, one in Japan and one in Europe. In both these instances, large integrated companies continued to shed refining assets in mature OECD economies. However, the next largest deals

Refining and marketing M&A deals by value and count

Source: PLS Inc. and Derrick Petroleum Services Global M&A Database

occurred in the United States with the sale of two refineries by BP to Tesoro and Marathon Petroleum Company. While the domestic refining market remains an opportunistic one, with fundamental prospects and valuations highly dependent upon geographic location and access to cheap crude and pipeline capacity, U.S. refiners, in general, have seen their underlying business fundamentals greatly improve over the last two years. "At the beginning of 2011, many analysts were negative on the refining and marketing sector," said Mr. Dillavou. "The resurgence of U.S. oil and natural gas liquids production has changed that, and turned the sector around from a market value standpoint." Mr. Ihne notes that along with their access to price-advantaged oil from the Canadian oil sands and U.S. tight oil plays, domestic refiners are benefitting from weak U.S. natural gas prices. "Because of the shale gas boom, U.S. refiners now have much lower operating costs than refiners in the rest of the world," said Mr. Ihne. "Low natural gas prices obviously drive reduced energy costs, but they also provide a competitive advantage when used as a feedstock to produce hydrogen that is needed to remove impurities and increase yields of clean products."

Source: PLS Inc. and Derrick Petroleum Services Global M&A Database

Conclusion

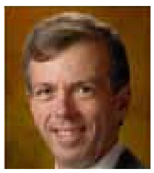
North American oil and gas, from promise to production

The International Energy Agency prediction in 2012 that U.S. oil production could surpass Saudi Arabian production for a period after 2020 drew enormous media attention in 2012. The prediction, while misinterpreted or exaggerated by some in the press, nevertheless helped raise public awareness that the promise of North American energy resources is now turning into production. Reserves and production levels from unconventional sources continue to surprise industry participants on the upside, and the largest players throughout the world have taken notice, and are pursuing North American unconventional assets. Continued low U.S. natural gas prices may only fuel buying interest, as those with the deepest pockets recognize a long-term bargain when they see it.

Looking ahead, we anticipate that M&A action will continue to focus upon the promise of the North American markets, where technological innovation and private ownership of reserves has created a promising future for the industry and related deal activity—as well as for the overall economy.

Source: PLS Inc. and Derrick Petroleum Services Global M&A Database

For more information, please contact a Deloitte Oil & Gas professional:



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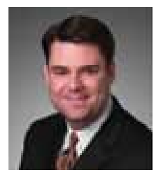

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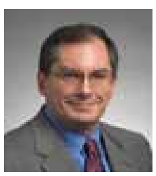

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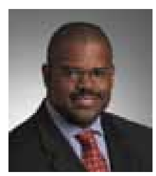

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