In our recent study, we surveyed senior executives from across the oil and gas industry to determine the trends, issues and challenges for 2017 and beyond. These industry leaders weighed in on such topics as talent-related challenges, oil & gas price expectations, company headcount trends, capital spending, M&A activity and more. We investigated their expectations for company performance, industry segment performance and the macro-economic environment.

Contents:

Reinsvold & Associates

Overview - Optimism Returns To The Oil Patch

Short-Term

On multiple dimensions, the short-term outlook has shifted from negative in last year's study to a cautious optimism this year. Expectations for short-term industry segment performance, company performance, hiring, capital spending and oil & gas prices are all positive.

Here are the short-term highlights:

- 60% of the executives believe that their industry segment will perform better in 2017
- 66% believe their own companies will perform better
- 34% expect their companies to increase their headcount
- 40% feel that their companies will increase their capital spending
- 68% believe oil prices will average greater than $50 for 2017
- 32% expect natural gas prices to average greater than $3.00 for 2017

Long-Term

The five-year outlook is even more optimistic than the short term. About 90% of the executives believe that both their industry segments and their companies will perform better over the next five years. These percentages are improvements on the already optimistic long-term view we saw in last year's study. Talent-related issues remain as one the top longer-term challenges over the next five years. Increasing regulation/taxes/restrictions, which was a top longer-term issue in last year's study, dropped in significance in this year's survey. The top two drivers of opportunity over the next five years are: increasing oil & gas prices and global economic recovery.

Short Term Expectations Have Improved

The oil & gas executives in our study have a much improved outlook for the forward 12 months when compared to a similar survey conducted last year. Most of them feel that their industry segments will fare better in 2017. The results are presented in Figure 1 along with the results from last year's study. For this question the executives were asked to rate the performance of their respective industry segments (e.g.: E&P company executives commented on the expected performance of all E&P companies) rather than the oil & gas industry as a whole.

About 60 percent of the executives expect their segment to perform better in 2017 and 12 percent expect to see their segments to perform worse. This is a significant improvement from the 12 month outlook at this time last year. Last year only 25 percent expected to see their industry segments perform better over the coming 12 months and 41 percent expected worse performance. The general feeling appears to be that the worst of this bust cycle is behind us.

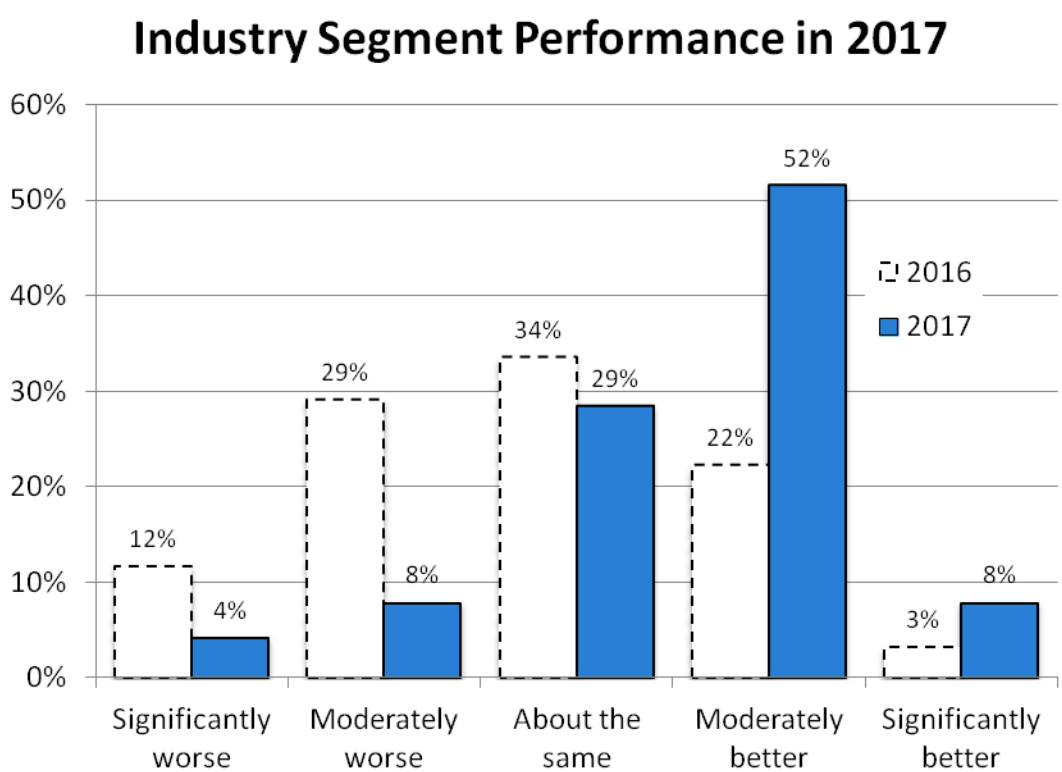

Figure 1

We also asked the executives to predict how their companies would perform in 2017 (Figure 2), rather than their industry segment. In this case, the outlook is even more positively skewed. About 66 percent of the executives expect to have a better year in 2017 and only 10 percent expect it to be worse. Of course, we would expect senior executives to have a positive bias regarding their own company's performance (since they play a major role in making that happen). However, the key take-away here is that the outlook is much more positive than last year's.

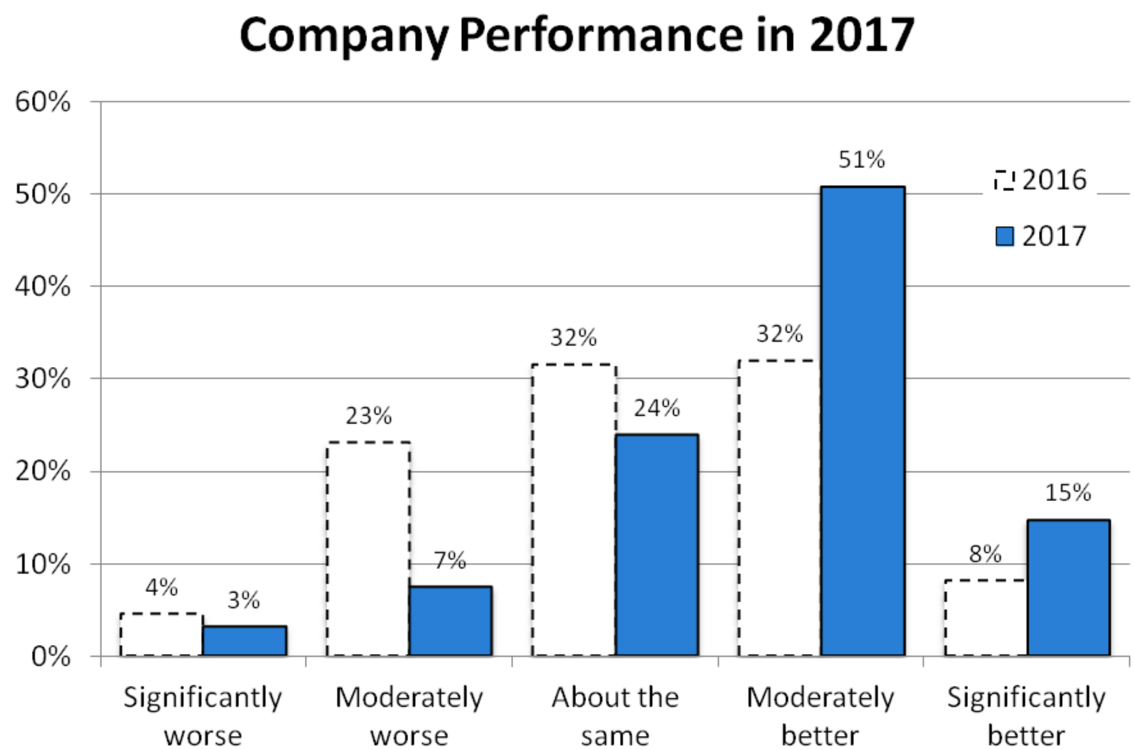

Figure 2

The generally optimistic outlook for 2017 continues in Figure 3. This chart shows the executives' expectations for employee headcount at their respective companies. While some companies may continue to reduce headcounts, more senior executives believe their companies will be growing. About 34 percent of the executives expect their respective companies to increase their employment numbers and 20 percent expect to see headcount reductions. A large number (46 percent) expect there to be little change. This year's study is a reversal in the negative trend of the last two years when 42 percent of the executives believed their companies would reduce their headcounts at the beginning of 2016 and 36 percent in 2015.

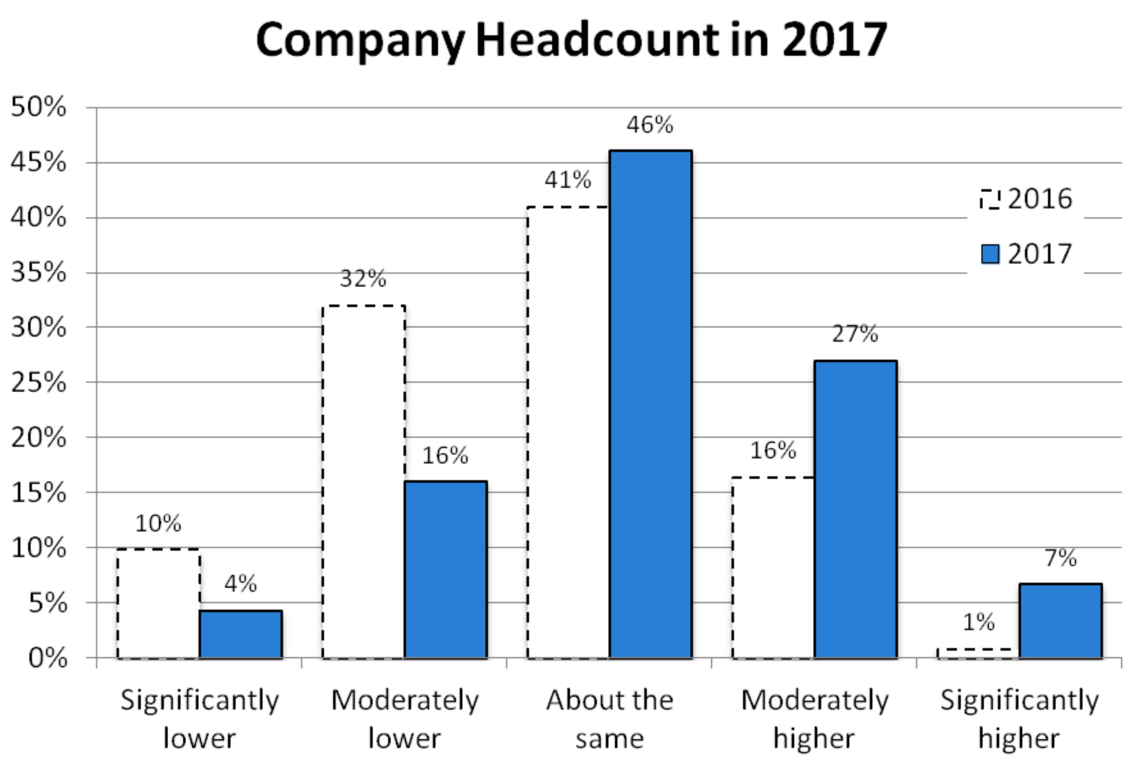

Figure 3

The short-term capital spending outlook has switched from negative to positive as well (Figure 4). About 40 percent of the executives expect capital spending at their companies to increase and 20 percent expect it to decrease. This strong shift in sentiment is probably the result of both an underinvestment during the last two years as well as a positive outlook for the coming year.

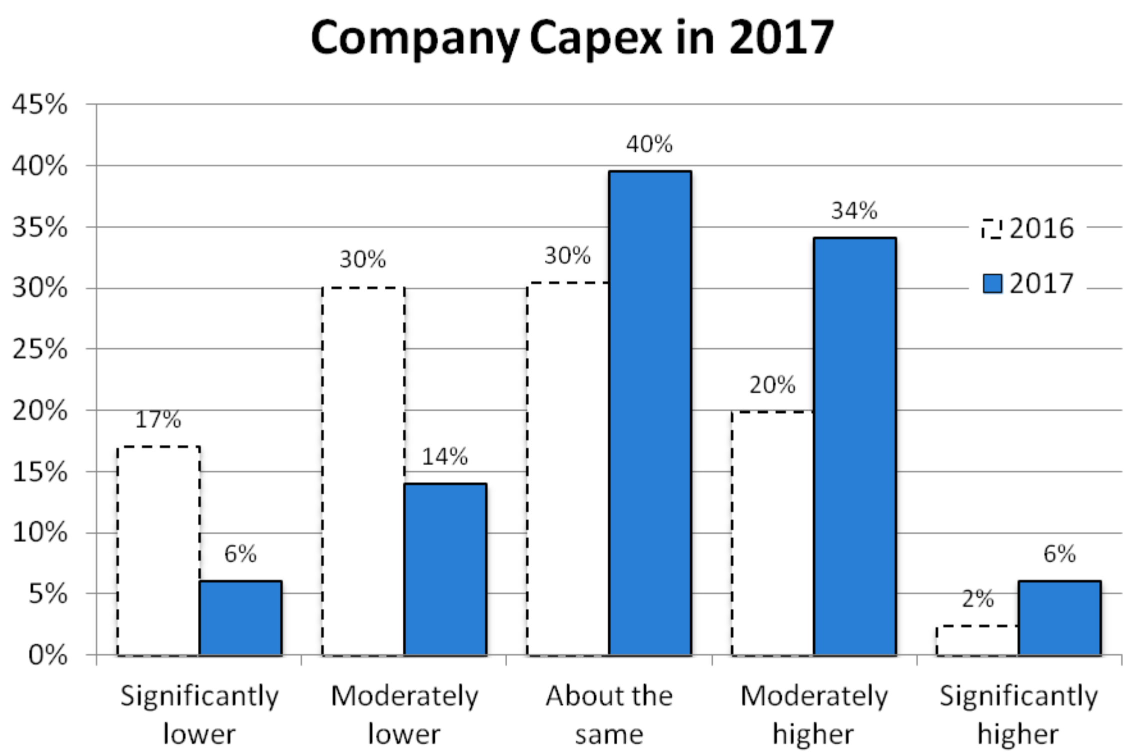

Figure 4

Of the executives surveyed, 73 percent expect 2017 to be a year of moderately or significantly more M&A activity in their industry segment, while only 5 percent expect less. There was a similarly strong M&A outlook at this time last year, but the actual deal flow did not turn out to be as strong in 2016 as many expected.

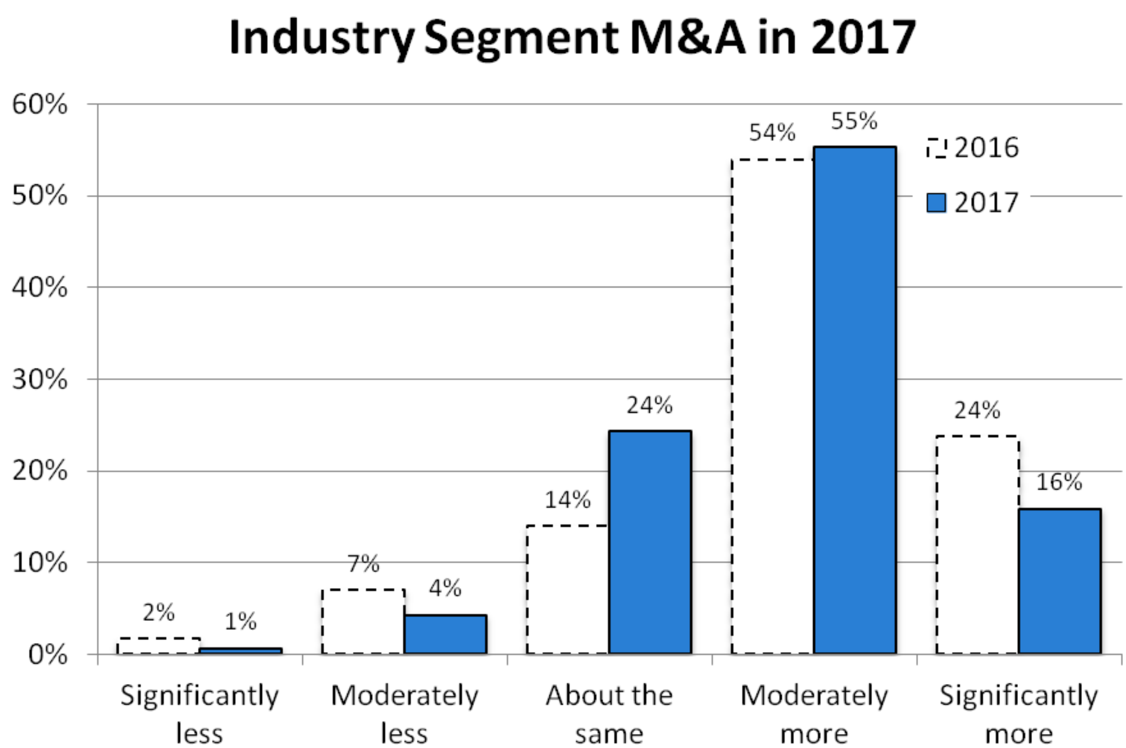

Figure 5

In addition to asking the executives how their industry segments and companies will perform in 2017, we asked them to identify which segments they believe will outperform all the other industry segments in 2017 (Figure 6). The survey participants were allowed to choose up to three segments. The results show that the independent E&P companies and the major integrated companies are expected to be the best performing segments in 2017.

Offshore drilling contractors and EPC companies are at the bottom of the list of expected best performers for 2017. Both of these segments are linked to larger capital projects with longer lead times. Many of these projects have been delayed or cancelled, so it is not surprising to see these segments low on the attached chart.

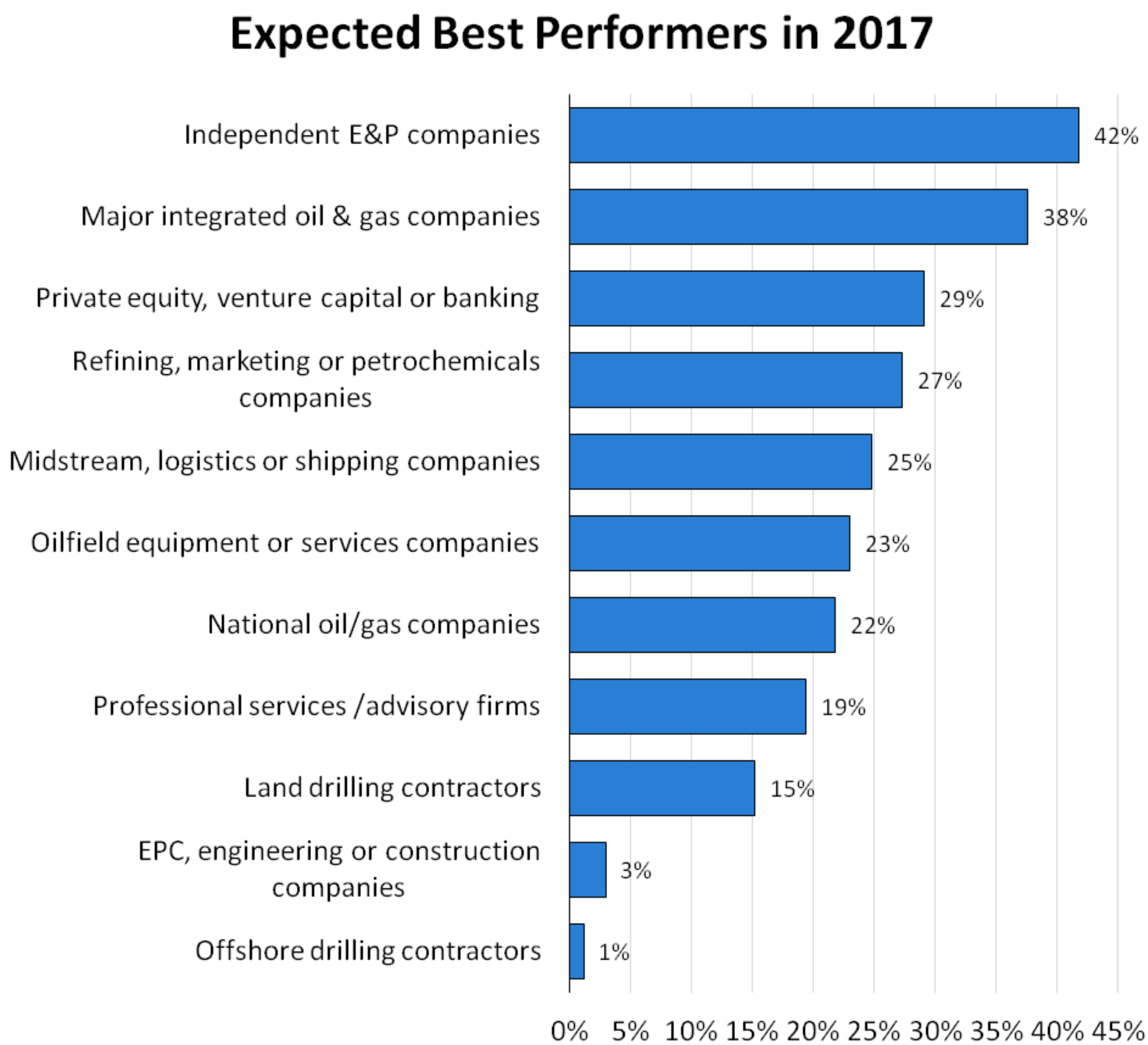

Figure 6

2017 Oil & Gas Price Outlook Improves

About two thirds of the survey participants (66 percent) expect the average price of WTI oil to be in the range of $50 to $65 per barrel in 2017 (see figure 7). About 31 percent of the executives believe the average price for 2017 will be in the range of $35 to $50. This is an improvement from last year's outlook when 51 percent expected the average price to be in the $50 to $65 range and 42 percent expected the price to be between $35 and $50.

As a matter of reference, according to the EIA, the 2016 average price for WTI was $42.50 per barrel for the first 11 months of the year. In 2015, the average price was $48.66 for the entire year. Also, during the 10 days in November 2016 that the survey was conducted, the price of oil averaged $44.87 per barrel. This survey was conducted before the November 2016 OPEC meetings at which OPEC had agreed to cut production. However, during the survey period, there was certainly speculation that OPEC might reach a deal.

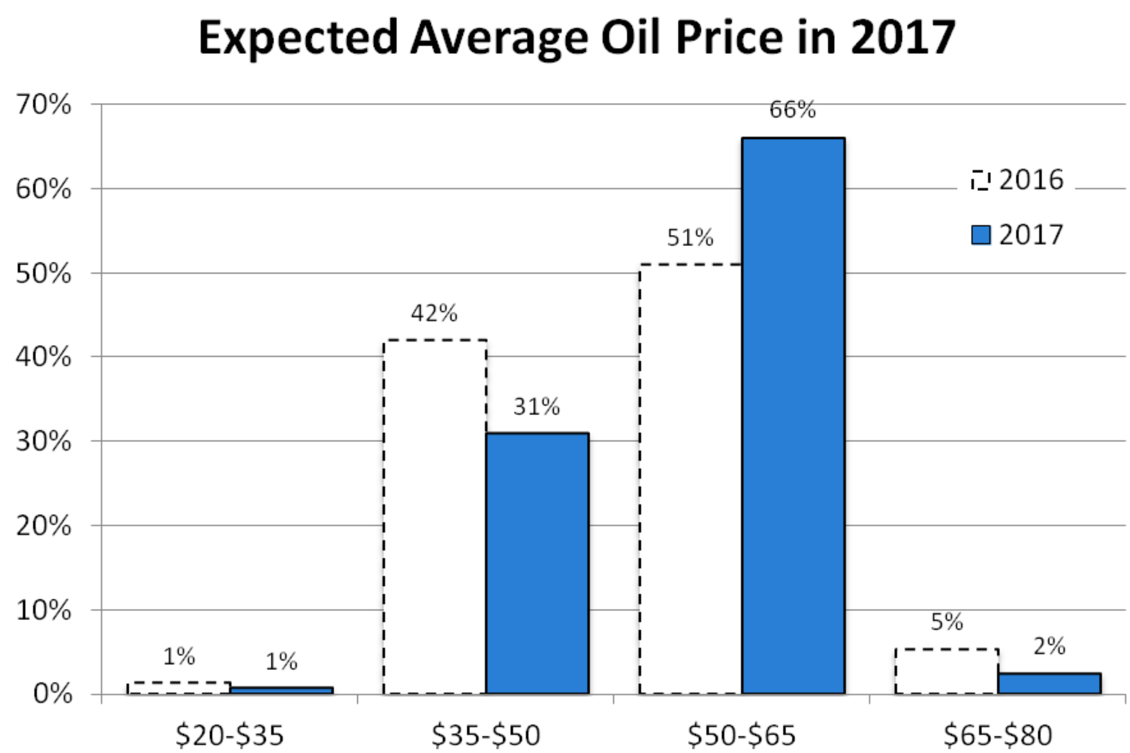

Figure 7

Regarding natural gas prices, expectations have shifted slightly higher for 2017 (Figure 8). About two thirds of survey participants (65 percent) expect the average 2017 spot price of Henry Hub natural gas to be in the range of $2.00 to $3.00 per thousand cubic feet. The number of executives expecting natural gas prices to be in the range of $3.00 to $4.00 has increased to 30 percent from 13 percent last year. Very few (6 percent) expect gas prices to be greater than $4.00 or less than $2.00 (4 percent).

As a matter of reference, according to the EIA, the 2016 average Henry Hub spot price for natural gas was $2.50 per thousand cubic feet for the first 11 months of the year. In 2015, the average price was $2.70. Also, during the week in November 2016 that the survey was conducted, the natural gas spot price averaged $2.39 per thousand cubic feet.

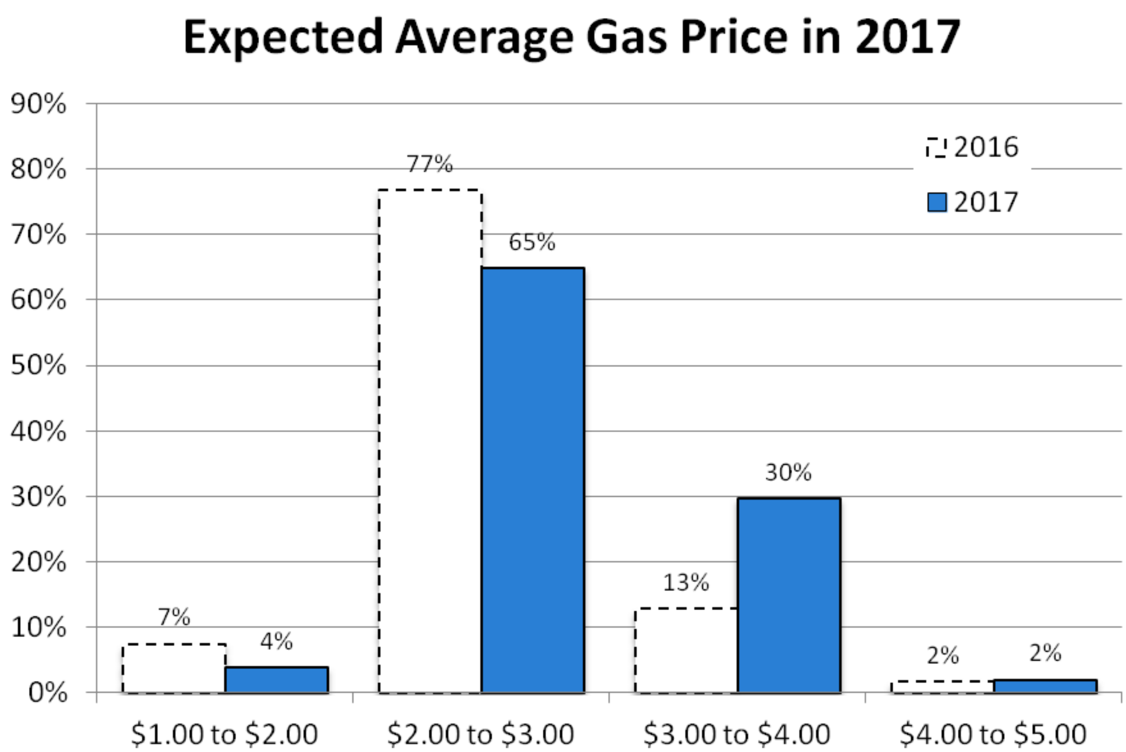

Figure 8

The Long-Term Outlook Is Even Stronger

Switching to a longer-term view, we asked the survey participants to rate their industry segment performance over the next five years (Figure 9). A large majority of the executives (90 percent) believe their industry segment will perform moderately or significantly better. Most importantly, 39 percent believe their segments will perform significantly better over the next five years. This is a substantial improvement in the longer-term outlook when compared to this time last year.

We believe it is important to consider both the short term and long term horizons when accessing the outlook for the oil & gas industry. This helps us to separate year-on-year cycles from the longer-term business cycles. However, we also believe there will always be a positive bias built into any longer-term forecast (oil & gas executives tend to be optimists). For this reason, we pay more attention to relative shifts in the long-term outlook rather than the absolute percentages.

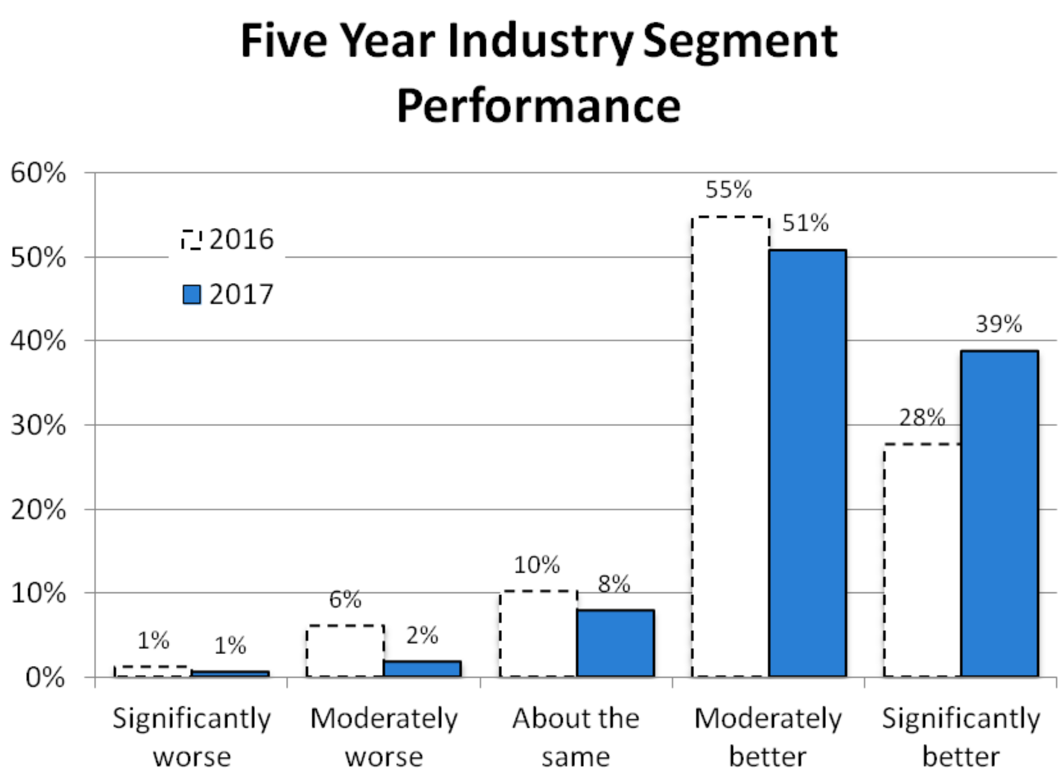

Figure 9

In addition to industry segment performance, we asked the executives to comment on the longer-term performance of their own companies. An overwhelming number of the executives (90 percent) believe that their companies will perform better over the next five years (Figure 10). Included in that number is 48 percent that believe their companies will perform significantly better. Only 3 percent believe their companies will perform worse over the next five years. Just like the positive view of industry segment performance illustrated in Figure 9, long-term individual company performance expectations have improved.

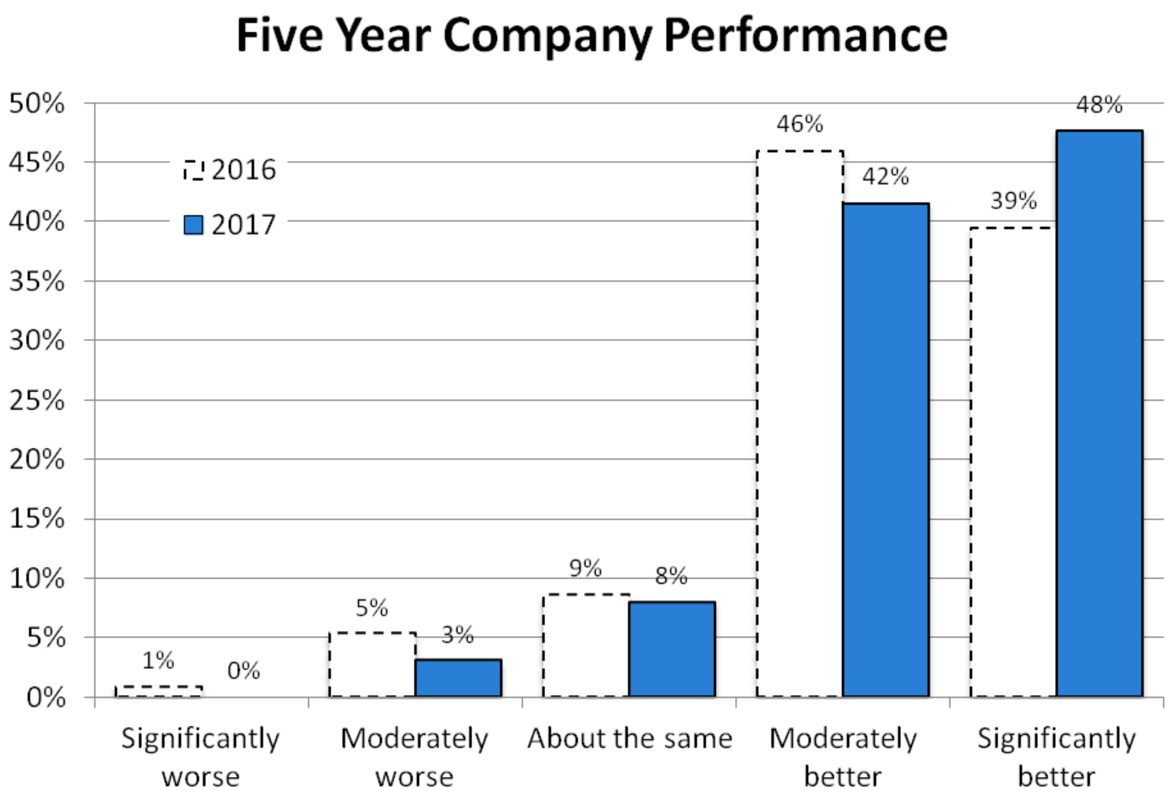

Figure 10

Figure 11 shows the expected best performing industry segments over the next five years (survey participants were able to choose their top three). Comparing this to the short-term industry performance in Figure 6, we see that the top two short-term performers are also expected to be the best long-term performers. However, the oilfield equipment/services segment is expected to be the third best performing segment over the next five years, moving up from sixth place for the 12 month outlook.

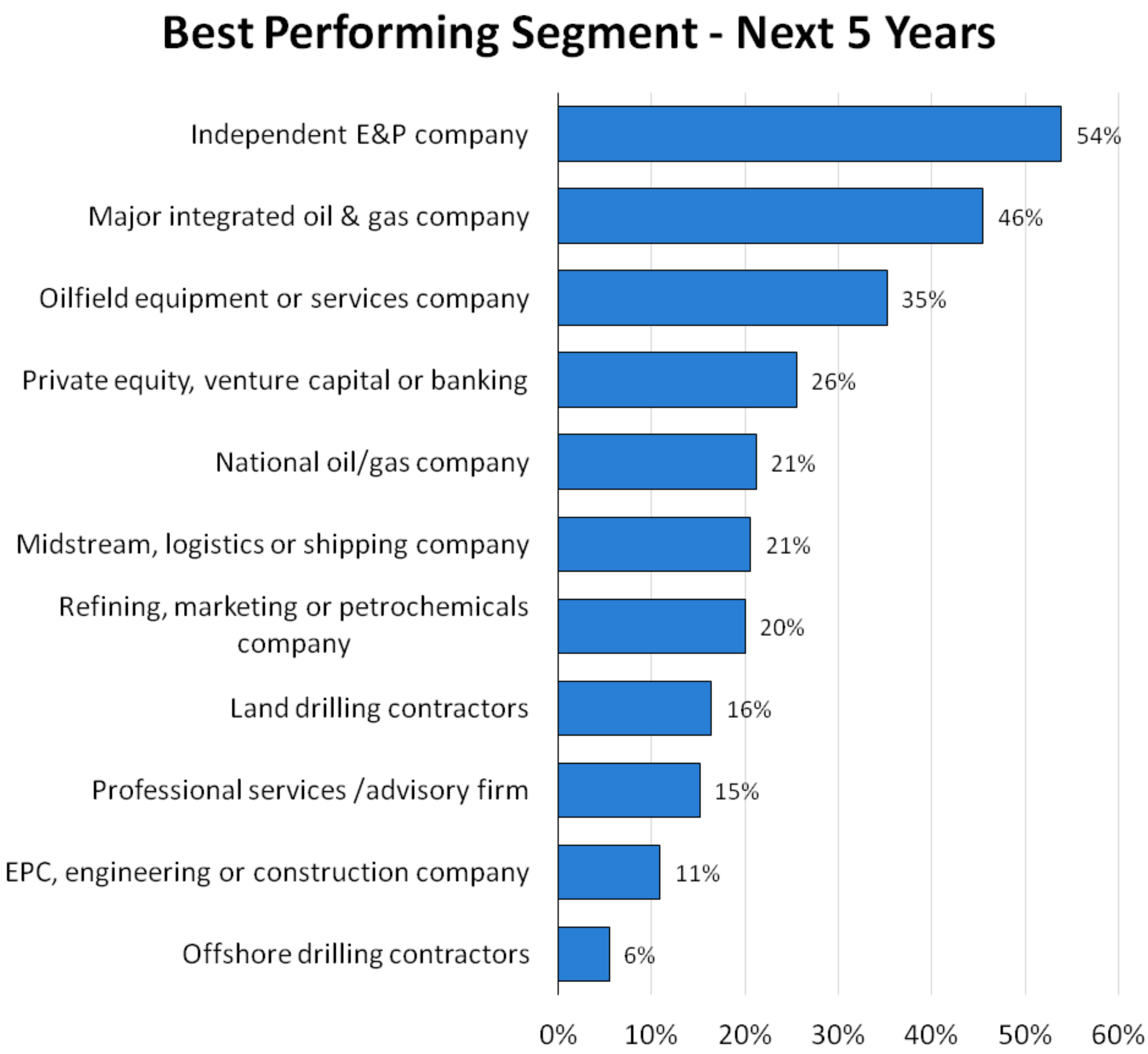

Figure 11

Industry Tailwinds Over The Next Five Years

Moving beyond just company and segment performance, we asked the executives to weigh in on the tailwinds or important drivers of opportunity (Figure 12) as well as the headwinds or challenges (Figure 19) for their segments over the next five years. For this question the participants were able to select their top three choices. The survey results show that, like last year's survey, the top two drivers of opportunity are macro-economic in nature: improving oil/gas prices and global economic recovery. The third, fourth and fifth opportunity drivers are all very close at 28 percent to 30 percent. They are: increased use of natural gas, lower costs and new technology developments.

For many of these tailwinds, survey participants were given follow-on questions to learn more about their thoughts on these particular drivers. For example, the follow-on details for the increased natural gas use driver can be found in Figure 13.

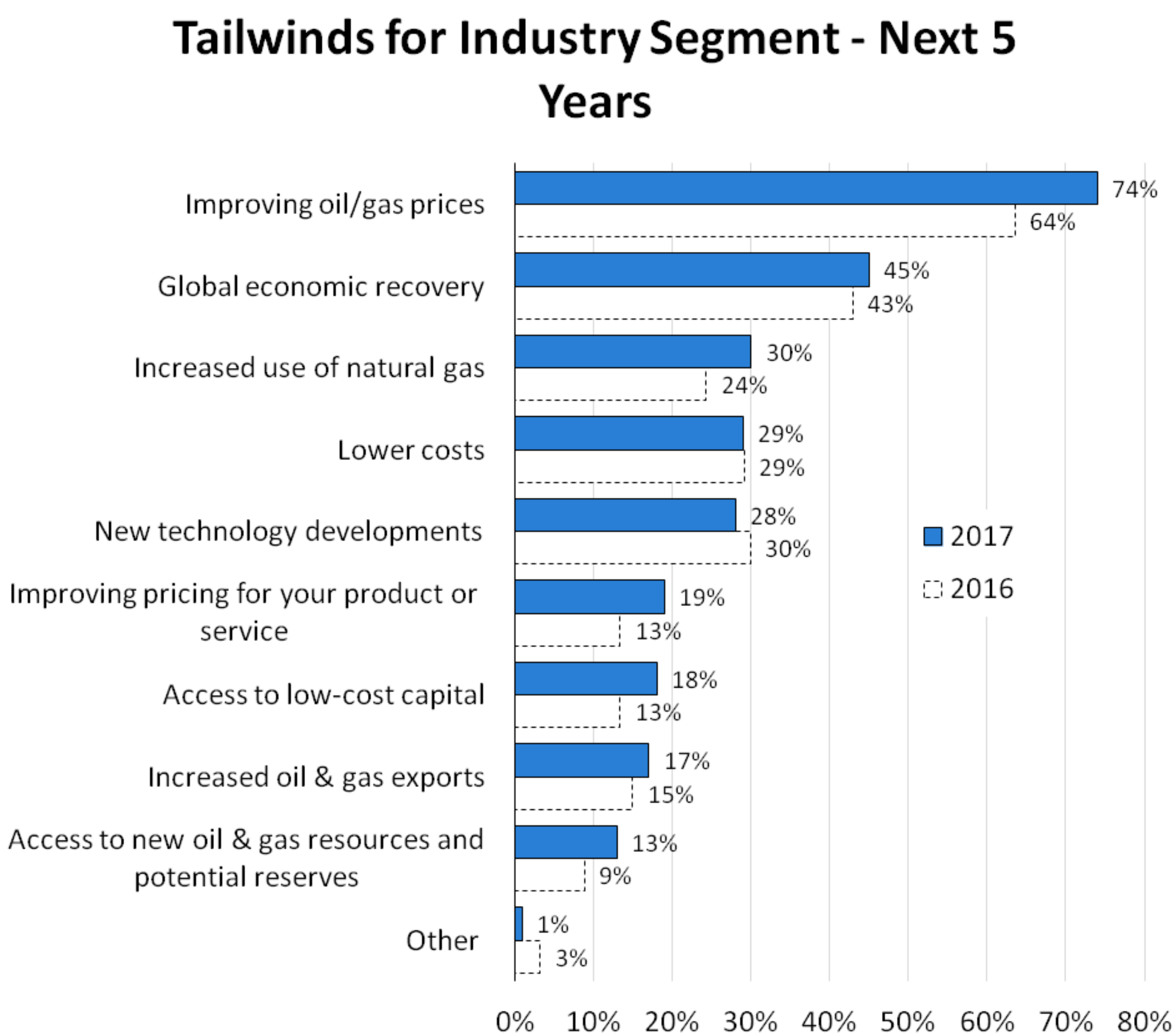

Figure 12

One of the factors cited in the opportunity drivers (Figure 12) was the increased use of natural gas. The chart below (Figure 13) shows how the survey participants answered the follow-on question as to what is the biggest factor driving a long-term increase in the use of natural gas. Certainly, the economics of inexpensive natural gas has led to a significant increase in its use for power generation (at the expense of coal).

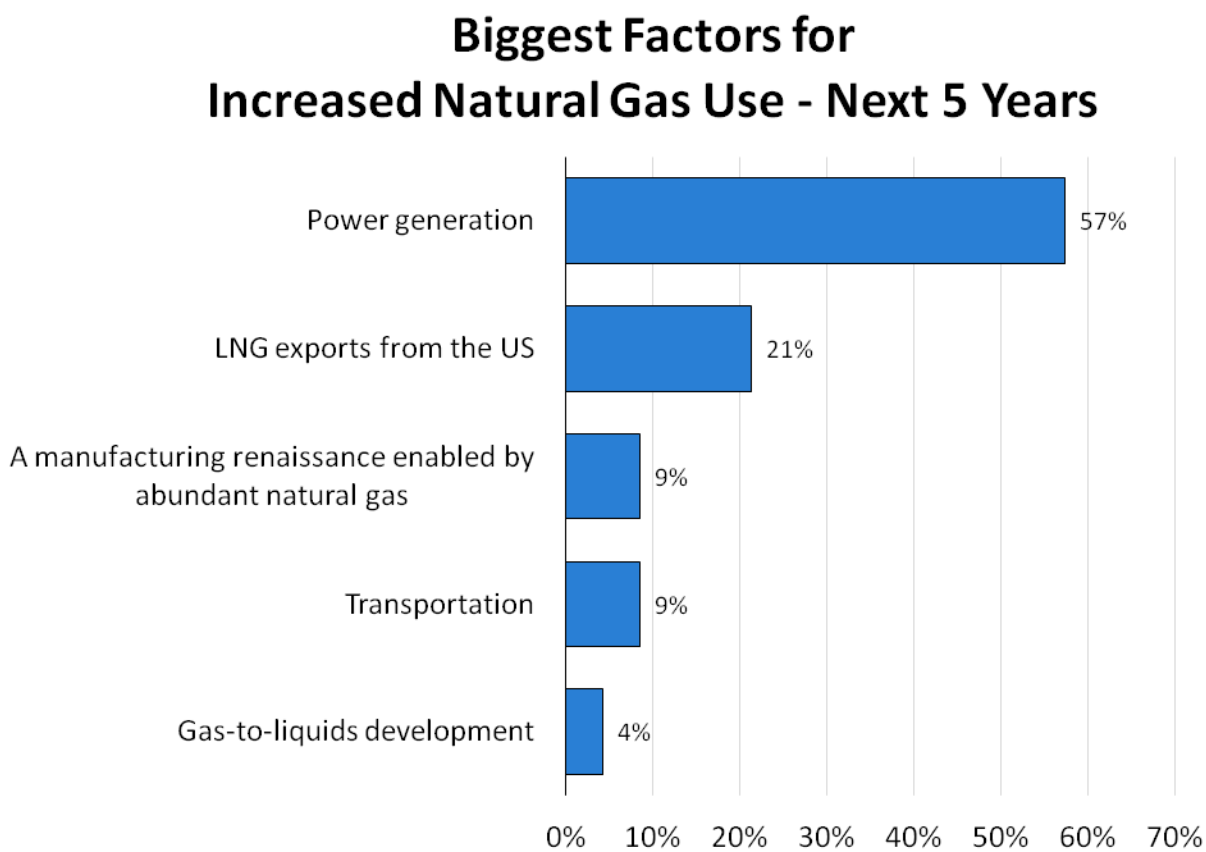

Figure 13

The fourth-ranked long-term opportunity driver cited in Figure 12 is lower costs. Figure 14 gives additional detail on the factors that the survey participants believe will lead to lower costs over the next five years. The top two factors for reducing costs are: 1) reduced costs for purchased equipment and/or services, and 2) improved operating efficiency.

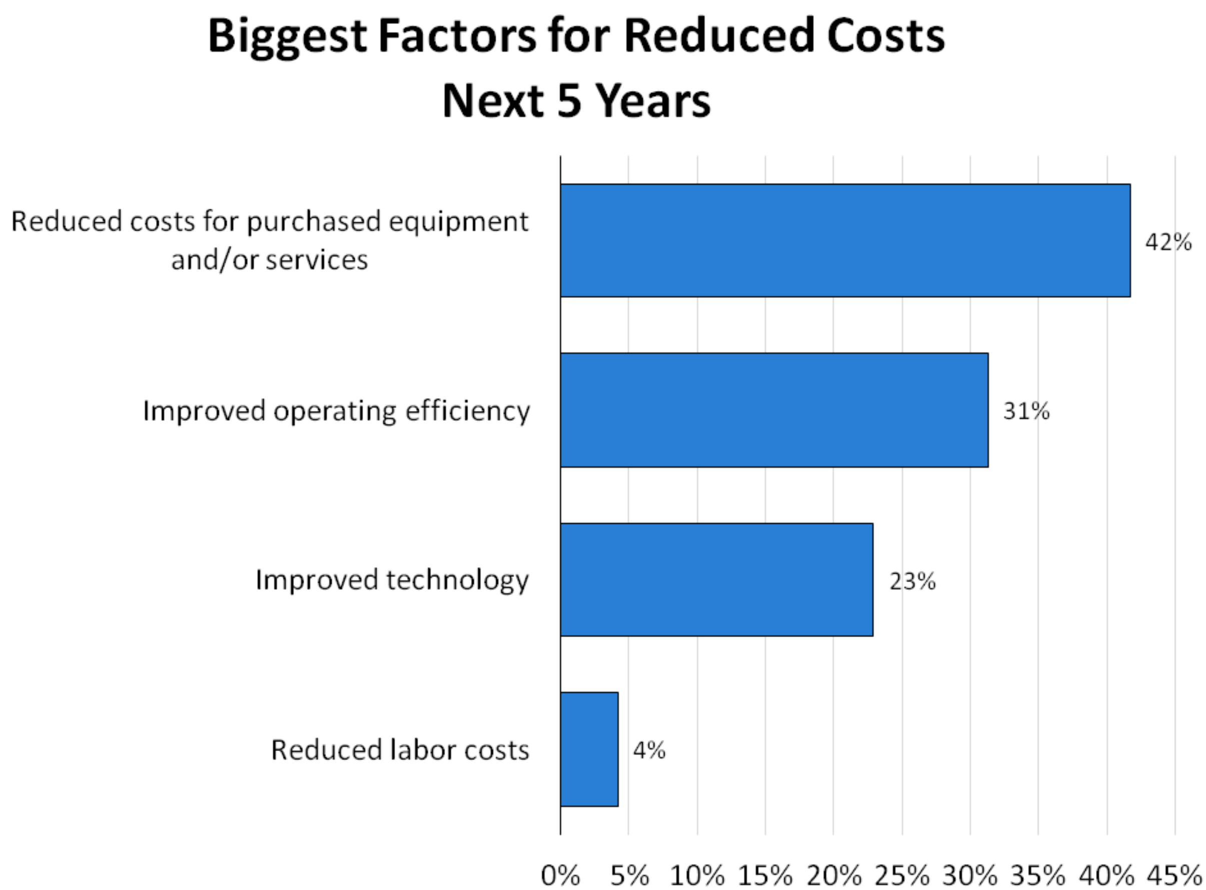

Figure 14

Technology improvement was listed as the fifth highest overall opportunity driver (in Figure 12). Those survey participants that cited this driver were given a follow-on question to better understand which technology drivers they thought would have the biggest impact (choosing their top three).

Figure 15 shows the top technology developments. The top two are: 1) increasing use of Big Data, the Digital Oilfield or the Internet of Things, and 2) improvements in hydraulic fracturing and completions. These are the same top two from last year, but the order changed with Big Data, the Digital Oilfield or the Internet of Things coming out on top.

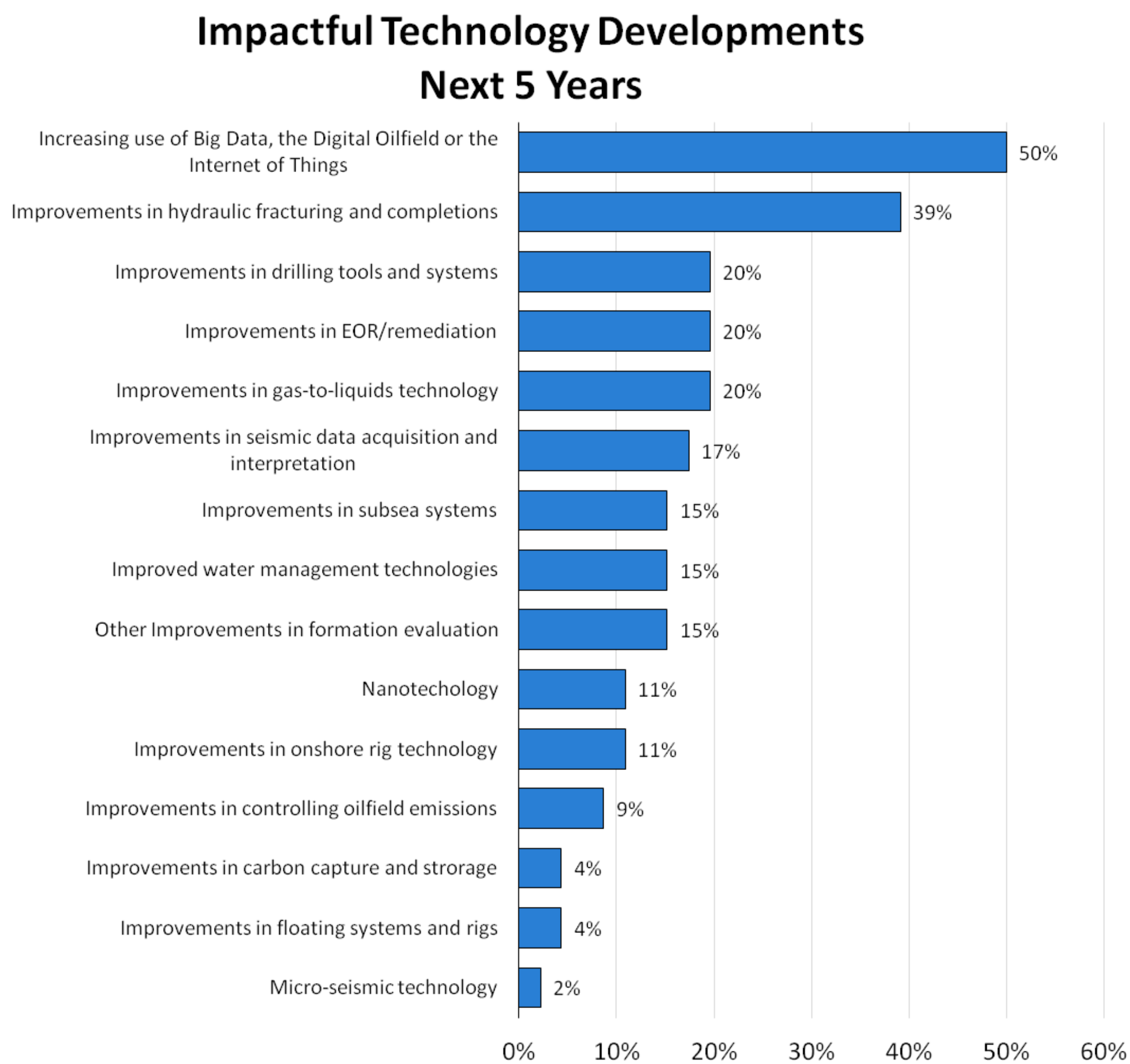

Figure 15

The seventh most cited long-term opportunity driver in Figure 12 was access to low cost capital. Certainly this was a key driver for the rapid U.S. oil and gas growth over the last five years. Figure 16 gives additional detail on which capital sources are expected to play a major role over the next five years. MLPs, which were cited in the past, failed to make the list this year.

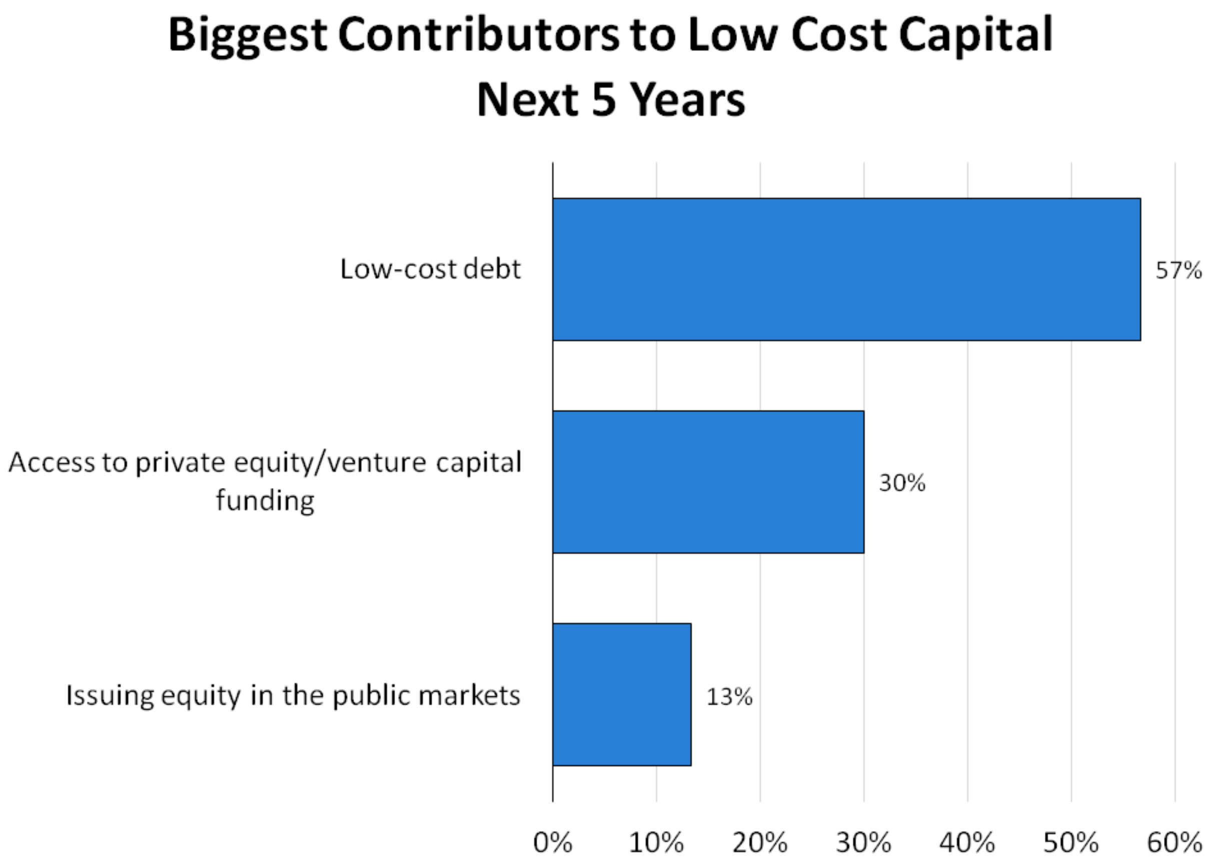

Figure 16

Another factor cited as a long-term opportunity driver in Figure 12 was increased oil & gas exports. The chart below (Figure 17) shows how the survey participants answered the follow-on question as to what is the biggest factor driving the increase in oil & gas exports. LNG exports was cited as the top factor with U.S. crude oil exports a distant second.

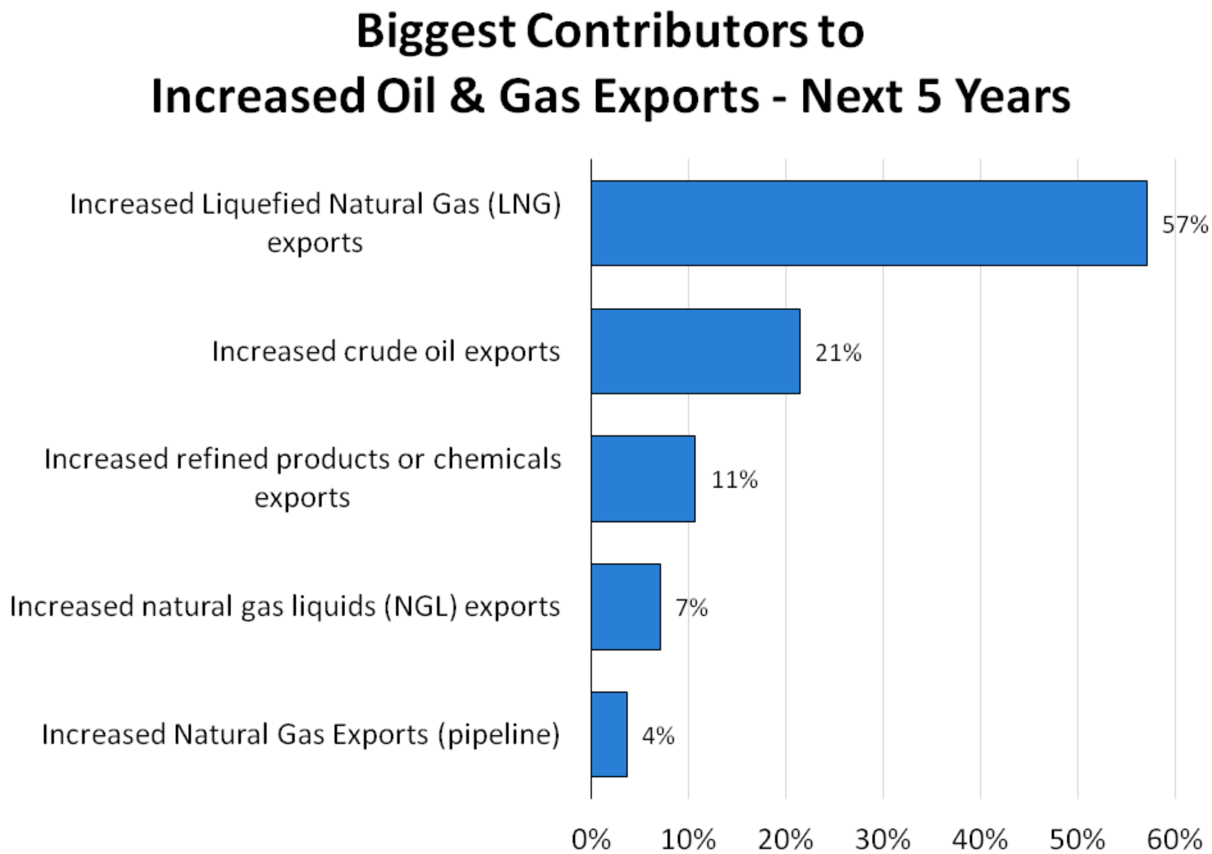

Figure 17

Rounding out the list of potential long-term opportunity drivers (see Figure 12) is: access to new oil & gas resources and potential reserves. Figure 18 provides additional insights into which areas the survey participants believe will be the most impactful for the long-term development of new oil & gas resources.

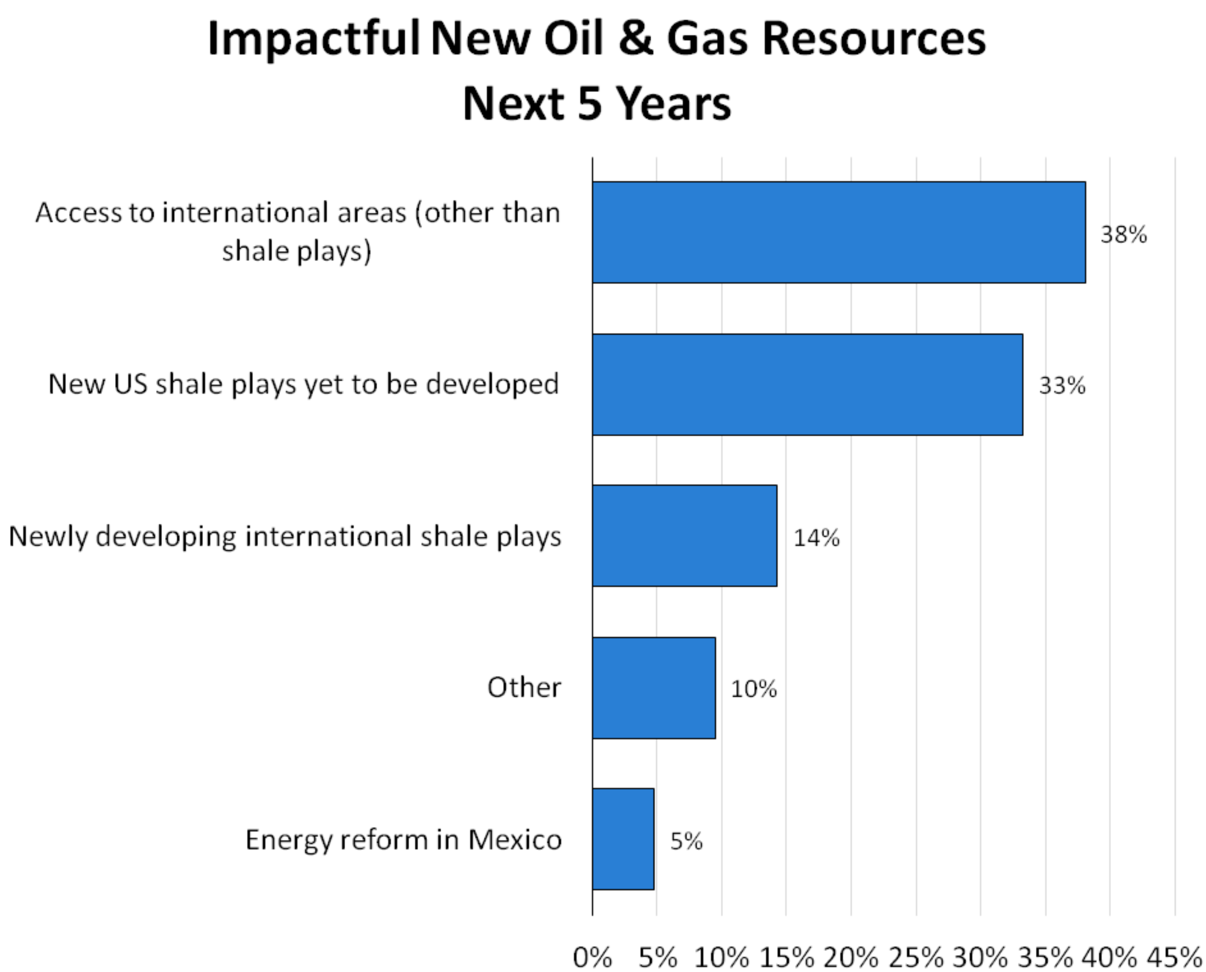

Figure 18

Industry Headwinds

In addition to asking about the most important drivers of opportunity (Figure 12) over the next five years, we asked the survey participants their view on the industry headwinds or challenges (Figure 19) their segments would face. In the chart below, the participants were able to select their top three choices. Like the Tailwinds question, survey participants were asked follow-on questions to gain additional detail into specific Headwinds choices. Except for Talent Shortages (more on this on page 26), the remainder of the top five industry headwinds are macro-economic in nature.

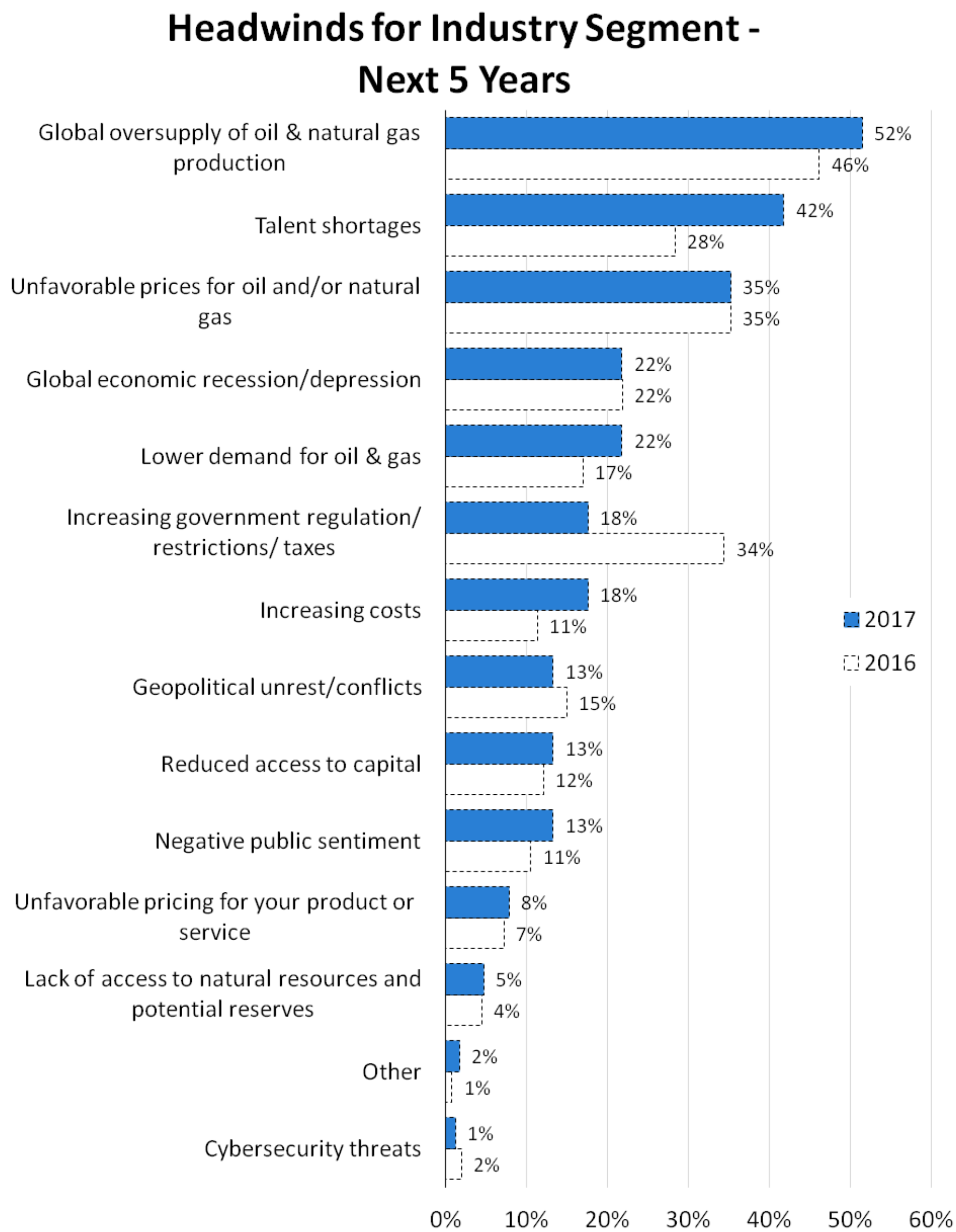

Figure 19

When asked for more detail on what would lead to lower demand for oil & gas (#5 in Figure 19), the following was cited (Figure 20). Lower oil & gas demand is seen as being primarily linked to global economic recession/depression, rather than competition from alternative energy sources (over the five year time horizon).

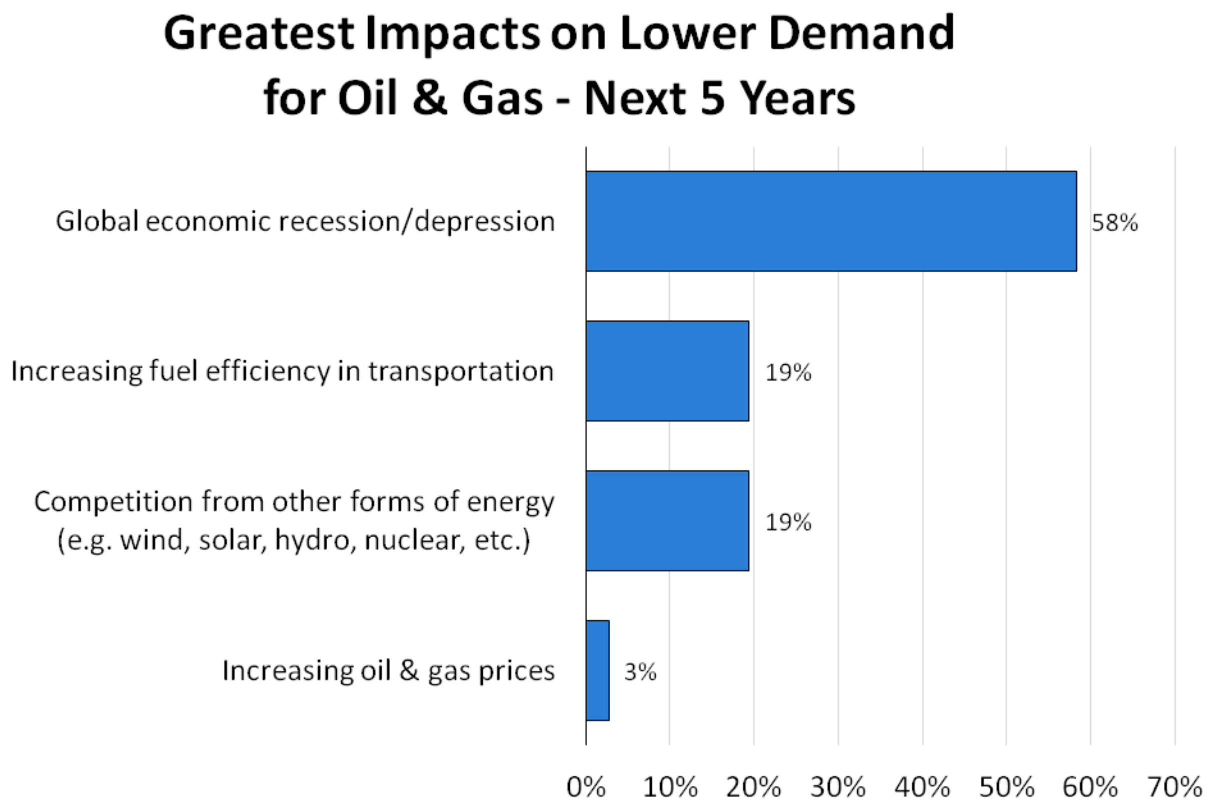

Figure 20

Last year, 34 percent of the survey participants cited increasing government regulation/ restriction/taxes as a key headwind. In a major shift this year, that number dropped to just 18 percent. Since the survey took place just after the recent U.S. elections, perhaps the feeling is that the industry will see less government interference.

When asked to elaborate on the challenge of increasing government regulation/restriction/taxes, the top response was: increasing regulation or restrictions by the EPA (Figure 21) with 54 percent of the responses (participants were allowed to select three choices). Local or regional bans on hydraulic fracturing was second with 50 percent. Last year, regulation uncertainty was the second highest response.

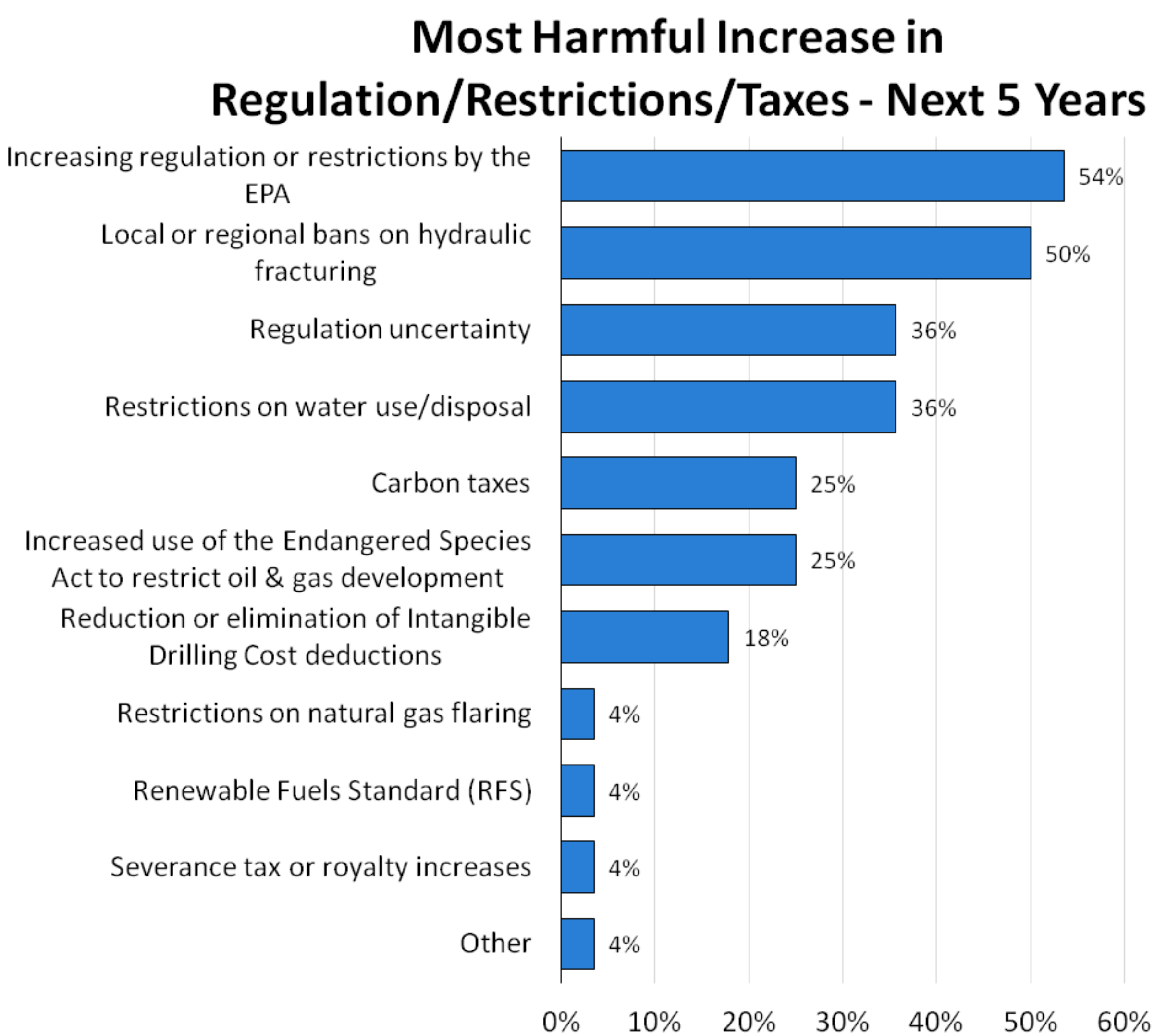

Figure 21

The seventh most cited headwind was increasing costs over the next five years (with 18 percent). Figure 22 gives additional detail on this issue. It is interesting to compare the responses from the tailwinds (Figure 12) and headwinds question (Figure 19) to see that lower costs over the next five years cited in the former and increasing costs cited in the latter. Digging a little deeper, we see purchased equipment and/or service costs decreasing as the top factor in one (Figure 14) and they are listed as increasing as the top factor in the other (Figure 22). The fundamental question here (and potential conflict) is how fast the service and equipment providers will be able to reverse the steep discounts of the last two years.

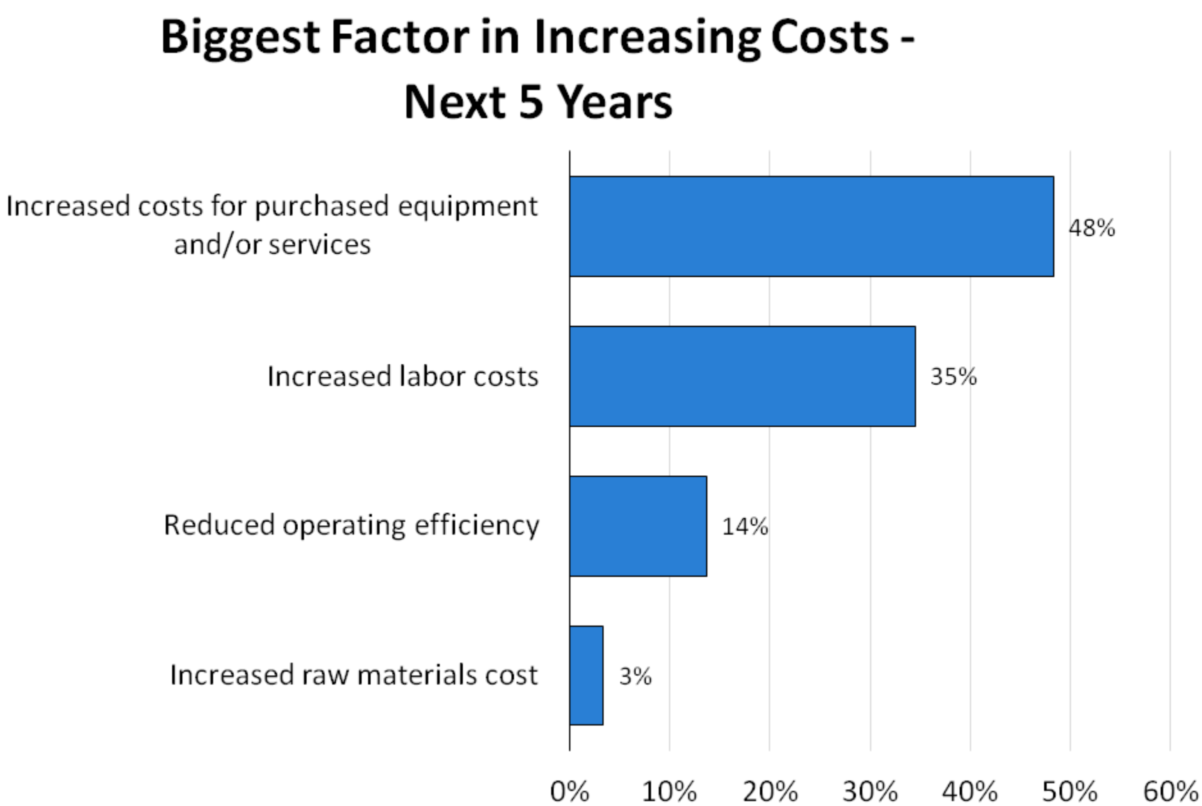

Figure 22

The tenth most often cited headwind was listed as increasing Negative Public Sentiment. Figure 23 gives additional detail into this issue. Survey participants were allowed to select their top three factors.

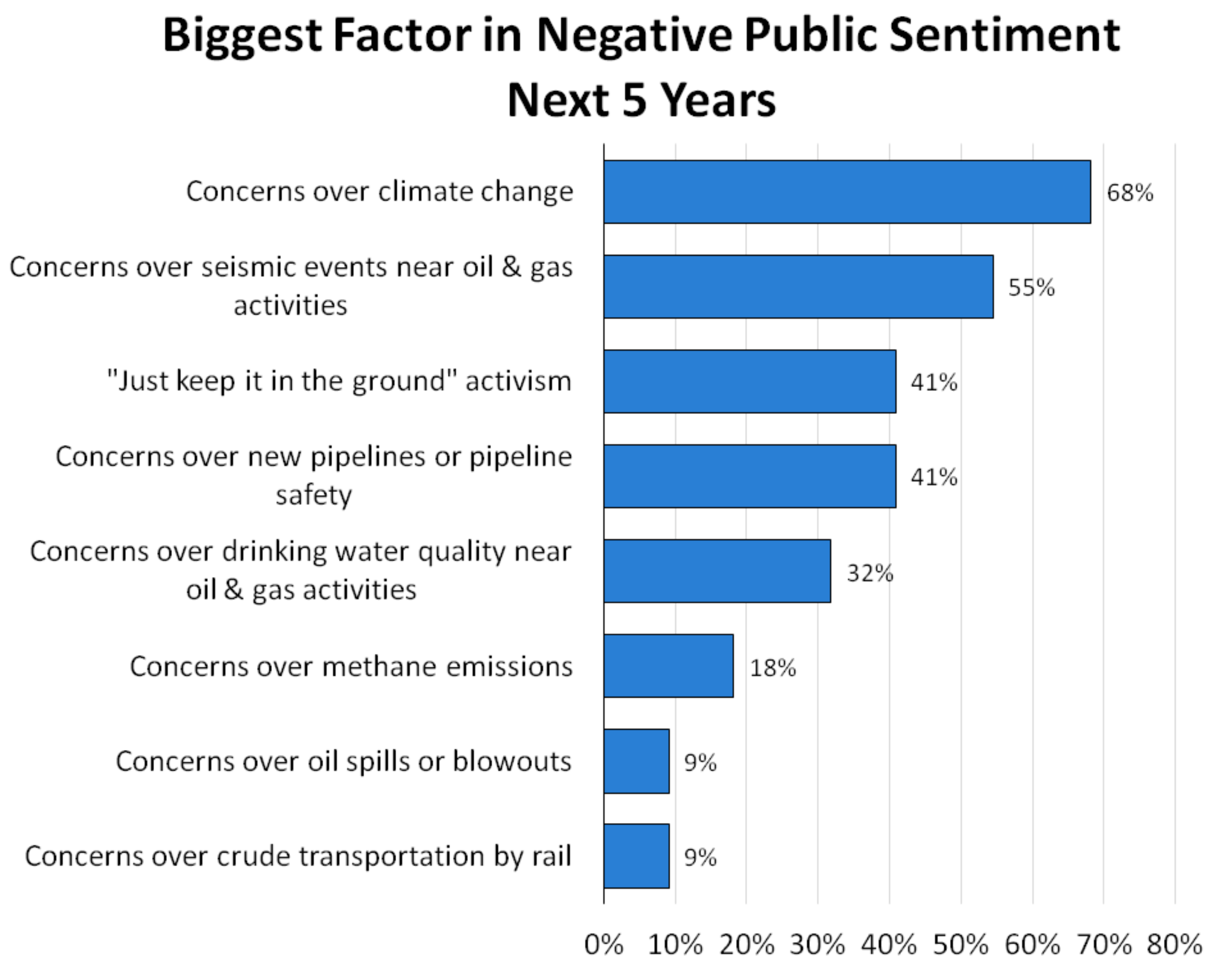

Figure 23

Talent-Related Issues

The survey participants were asked to identify the top talent-related challenges that they expect their industry segment to experience over the next five years (Figure 24). For the third year in a row, the most significant talent issue cited is the "Great Crew Change" – the retirement of key personnel expected in the near future. The second greatest talent-related challenge is the industry's attractiveness to new entrants (struggling industries are not very appealing) and the third is leadership talent. These are the same top three as last year's study.

As the industry recovers, it would not be surprising to see the technical talent move up the list in future surveys. Just two years ago this was the #2 talent-related issue.

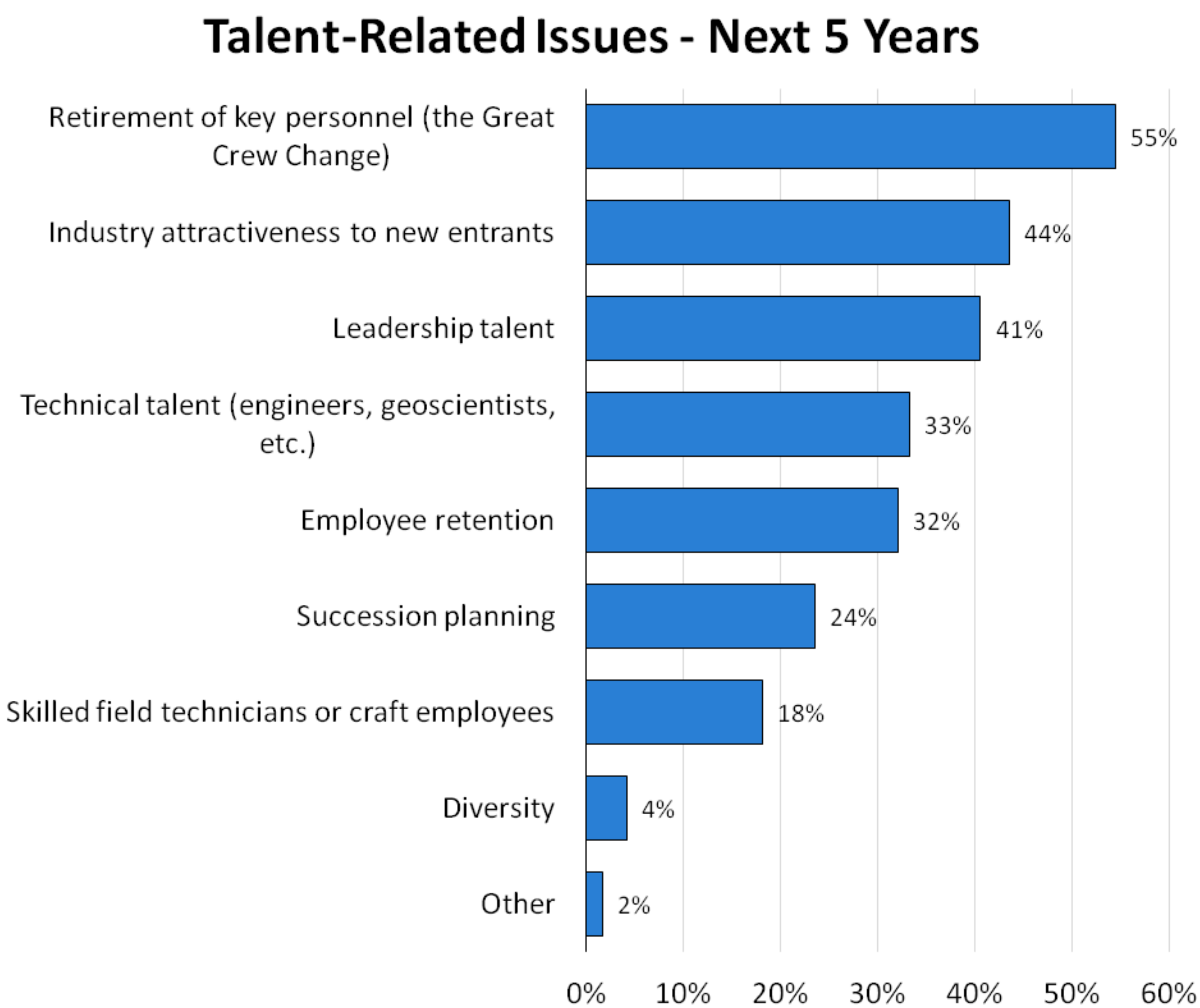

Figure 24

About The Survey

This survey was conducted November 9 to 18, 2016. Of the participants, 69 percent are at the Board, C-level (CEO, CFO, etc.) or VP level (Figure 25). Most of the participants represent the upstream side of the industry with the rest distributed amongst the many other segments. About 22 percent of the survey participants work for companies with greater than 5,000 employees (Figure 26). About 70 percent of the companies are headquartered in the U.S. (Figure 27) and 76 percent of the survey participants reside in the U.S. (Figure 28).

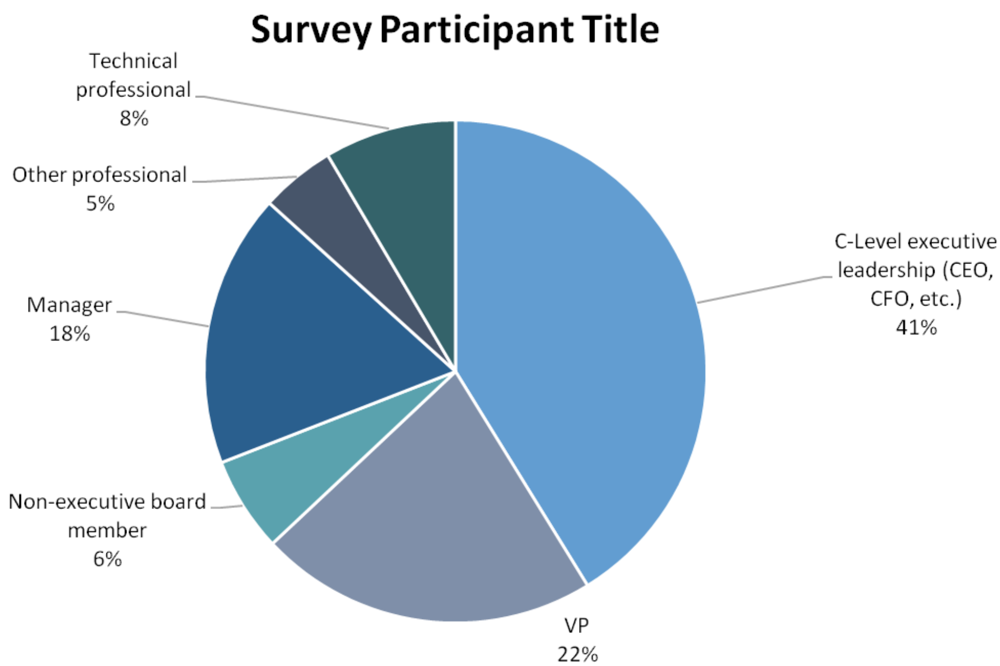

Figure 25

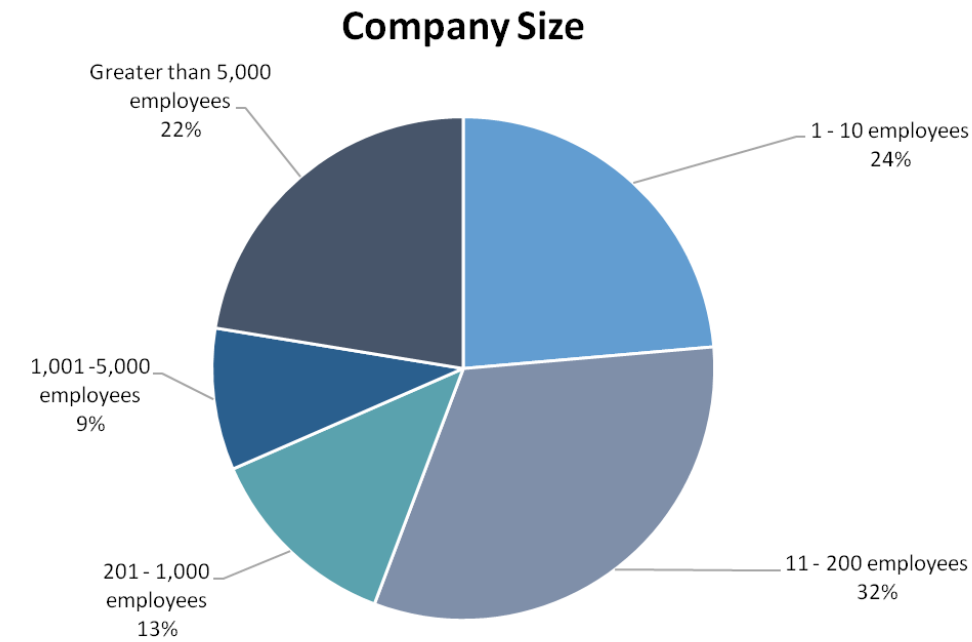

Figure 26

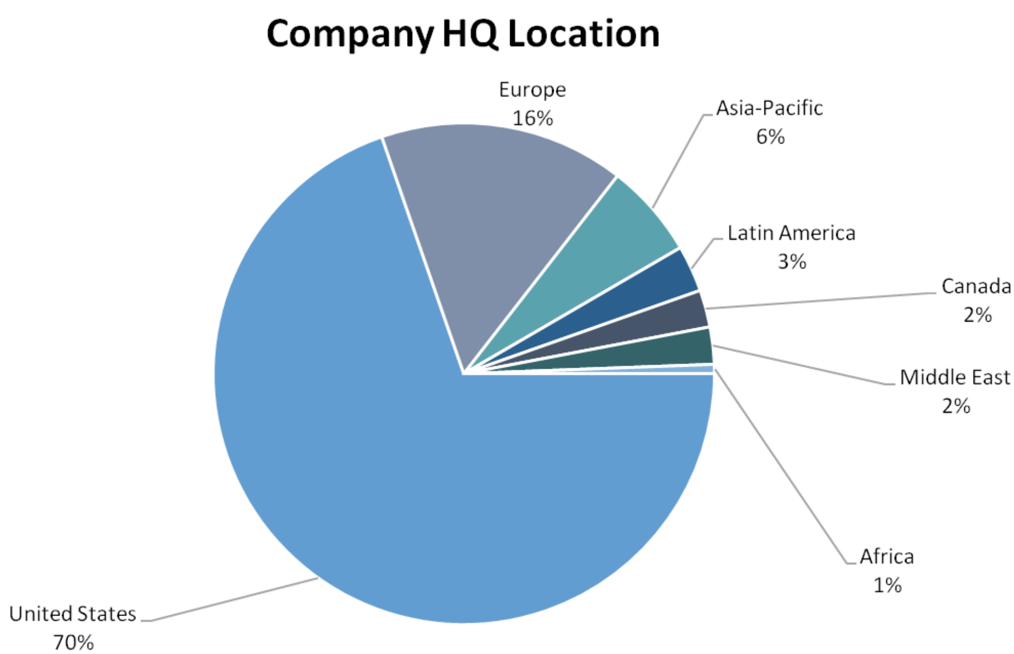

Figure 27

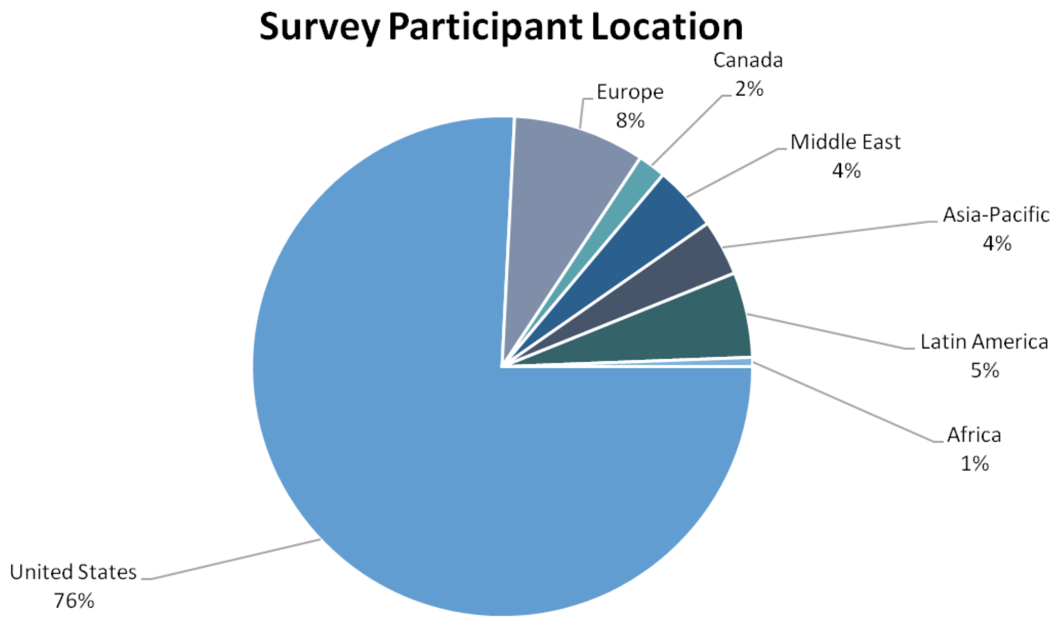
Survey Participant Location
Canada
2%
Europe
8%
Middle East
4%
Asia-Pacific
4%
Latin America
5%
Africa
1%
United States
76%

Figure 28

About The Author

Chris Reinsvold is the Founder and CEO of Reinsvold & Associates, a retained executive search and management consulting firm. Based in Houston, Chris has over 25 years of management experience in the energy industry. Chris helps his oil, gas and energy sector clients develop strategies and build leadership teams in the Board room, C-suite and senior executive management. The American Business Journals selected him for their 2014 Who's Who in Energy list.

Chris is active in the Independent Petroleum Association of America (IPAA), the Society of Petroleum Engineers (SPE), the National Association of Corporate Directors (NACD) and Mensa. He graduated from California State Polytechnic University, Pomona with a Bachelor of Science degree in mechanical engineering and earned an MBA from The University of Texas at Austin.

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