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INSIGHT: Energy Explosion–10 Trends to Watch in Energy Restructurings



By Matthew Warren, Sarah Primrose, and Taylor Armstrong

U.S. benchmark crude traded negative for the first time in history on April 20. While prices recently ''rallied'' to above $30 a barrel (still less than half of the average price in 2018), the market is unlikely to see a recovery in the near term.

Th e drastic drop in price was caused by the perfect storm of the Saudi Arabia-Russia price war and the novel coronavirus. The pandemic has halted demand for gasoline, jet fuel and diesel; bringing to a standstill the world's consumption of tens of millions of barrels of oil every day. Thus, simultaneously with the decrease in price, the decrease in demand on account of the pandemic increased the global supply of oil.

These two events have driven the oil and gas industry into economic crisis. On April 1, Whiting Petroleum became the first major shale bankruptcy filed in the current crisis. On April 26, Diamond Offshore Drilling became that second major victim of the oil market crash. The month of May has seen additional filings and more are expected to follow.

Here are the trends to watch and events to take note of as the energy industry turns to restructuring advisers to address the current crisis:

1. **Reduced Demand/Oversupply of Oil:** According to Reuters, fuel demand has declined approximately 30% worldwide—producing a glut of oil. This has left energy providers with millions of barrels in storage. Since storage is filling up, production will be reduced. More bankruptcies are predicted and interested parties should closely monitor their interests.

2. **Crude Futures Turned Negative:** In April, West Texas Intermediate crude futures turned negative for the first time in history. While analysts suggest that this is unlikely to happen again, at least in the near future, traders should still scrutinize their holdings.

3. **Refineries Slowed Down:** In the week of April 17, oil refiners in the U.S. processed the lowest amount in thirty years. Refineries are running at half rate across Europe and Asia.

4. **Reduced Production:** On April 12, oil-producing nations agreed to cut approximately ten percent of the world's output of oil—the largest production cut ever negotiated. Production cuts have continued in the U.S. with only 60% of oil rigs in operation. Domestic production levels are not predicted to recover this year.

5. **Shale Producers Are Especially in Trouble:** Already laden with heavy debt levels and operating costs that cannot be easily reduced, these producers are particularly susceptible due to narrow margins.

6. **Watch for Chain Reactions:** Service providers are at risk as demand for their services plummets in the face of decreased capital expenditures by upstream companies. In addition to Diamond Offshore Drilling, as noted above, Speedcast International Limited, a satellite-communications company, filed for bankruptcy relief on April 23 in the Southern District of Texas. Speedcast connects oil rigs to internet and phone. Diamondback Industries Inc., a manufacturer and seller of disposable setting tools, power charges, and igniters used in the completion of oil and gas wells, filed for bankruptcy in the Northern District of Texas on April 21. Additionally, Hornbeck Offshore, a provider of marine transportation for oil field operators in the Gulf of Mexico, filed a prepackaged bankruptcy in the Southern District of Texas on May 19.

7. **We Are Still in a Holding Pattern:** Lenders and bondholders in many distressed credits are delaying restructurings, sale processes or bankruptcies given the market situation and a lack of desire to own these dis-

tressed oil assets. However, liquidity pressures will continue to mount and lenders and bondholders will ultimately be reluctant to fund further new money in the current environment. Accordingly, we may eventually see more ''free fall'' bankruptcies and fewer prepackaged ones. Interested parties should consider seeking counsel now and getting their ducks in a row.

8. **Texas Courts Will Get Busier:** The Bankruptcy Courts for the Northern and Southern Districts of Texas—a popular destination for energy bankruptcies—are already seeing an increase in activity. In recent news, Whiting Petroleum, Speedcast, Victerra Energy, Ultra Petroleum, Gavilan Resources, Hornbeck Offshore, Freedom Oil and Gas, Unit Corp., Echo Energy Partners, Tri-Point Oil & Gas Production Systems, and Permico Midstream Partners filed in the Southern District of Texas while Diamondback and Yuma Energy filed in the Northern District of Texas. In addition to an uptick in industry filings, Texas has the been the chosen venue for other high-profile non-energy filings such as Gold's Gym and Stage Stores in the Northern District of Texas along with Neiman Marcus and J.C. Penney in the Southern District of Texas.

9. **Strategic Mergers & Focused Asset Sales:** Oil and gas M&A was nearly nonexistent in the first quarter of 2020. Still, the downturn may eventually push the market into healthy consolidation as buyers will have access to high-quality assets. Buyers may want to consider scouting for assets now with distressed lists as a guide.

10. **Coal Is Still in Trouble:** With so much going on with oil, coal hasn't been in the headlines. That doesn't mean, however, that its troubles have gone away. Moody's Investors Service wrote that it ''expects a very challenging year for the coal industry in 2020.'' The current economic downturn will likely only further accelerate the decline in demand in the coal industry. Moreover, renewable energy sources have been displacing coal. The summer seasons provides an influx of low-cost solar and hydro power generation that may prove problematic to the fossil fuel industry as a whole.

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