DOLLISON SEES NICHE OPPORTUNITY AMID DEPRESSED OIL SECTOR

An Interview with J.B. Dollison, Principal, Crutchfield Capital Corporation

J.B. Dollison is a principal with the Houston-based private investment banking firm Crutchfield Capital Corporation. Middle Market Growth Magazine previously asked for his take on how depressed worldwide oil prices are affecting midsize deals in the energy sector. This is the October 2015 update to that interview.

Q. How is the downturn in global energy prices impacting your business at Crutchfield?

With clients that are close to the wellhead, meaning companies providing services associated particularly with drilling activities, those deals are in peril right now. Other than that, Crutchfield Capital is relatively well-diversified. However, there's clearly a lot of uncertainty in the oilfield services arena, and as a result deals are much more difficult to close.

Q. Is there a lot of opportunity in this market?

I definitely think there's opportunity—there are many buyers that were on the sidelines hoping that valuation metrics would become more rational in the oil and gas sector, and I think you're starting to see that.

Conversely, companies with an attractive niche in the segment will remain in great demand. For example, we sold Chemtec Energy Services to a public company out of Pittsburgh called L.B. Foster. Our client, Chemtec, is involved in manufacturing measurement solutions used in the midstream sector; every time there is a sale of a hydrocarbon, you've got to measure it. Chemtec provided measurement systems for that exchange—basically the cash register for the oil and gas industry. This is a sector where you know there is going to be continual buying and selling of product; it's not like you don't have molecules being exchanged, you're just not drilling for as many molecules.

A business that is sustainable through a downturn is also attractive. We're currently representing a company that provides information technology services for the oil and gas industry. We always need to manage this information, and much of it is stored on legacy systems. If oil companies are going to survive, they've got to access and manage that data, so this company will be a very at- tractive company in the capital markets.

Q. Are PE firms in the energy space right now having a hard time raising funds?

I don't think so. I think the success of fundraising is more attributable to historical returns of a fund, rather than a particular focus. I think, if anything, it might be actually a little bit easier to raise capital in the sector because target companies are trading at lower valuation multiples, and can be bought at more attractive prices.

Q. What kind of valuations are you seeing for pure energy deals, and where were they prior to the downturn, maybe three months ago?

Obviously, multiples vary by company, and it's really difficult to generalize as a whole. For attractive niche players such as those I described, multiples may be down by maybe a quarter to half a turn. For companies very closely tied to drilling operations, those valuation metrics probably have declined by one turn of EBITDA at least.

Q. How long do you think this depression in oil pricing is going to last?

It is very difficult to know; the one thing for sure—there's an awakening if there wasn't before—that commodity prices are cyclical and clearly we're seeing that in the oil and gas sector. I think several things have to happen before oil prices begin to rise. First, there has to be at least a perception that world demand has stabilized and is increasing. We still have declining growth rates in Asia and Europe—when you see that, you think of less demand for commodities like oil and gas, so the bias is to the downside of prices. Second, we need to see the supply of crude from the U.S. decline. We are finally seeing increased domestic imports of oil which suggests that U.S. producers are scaling back production. This should help stabilize oil prices.

Q. When should owners think about selling their companies?

For those clients heavily tied to the extraction of crude oil, I think the valuation metrics are going to be depressed and it might be best to wait to sell the business. On the other hand, if you have an attractive niche, I think there are still some very nice valuations and I wouldn't hesitate at all to explore the markets. Timing is everything and there's still a lot of liquidity in the market looking for great deals. If you've got that niche, I think you're going to get a lot of attention.

Q. What about opportunities in the natural gas market?

In the natural gas segment, most of the activity is designed to increase demand for molecules. We continue to build infrastructure on the Gulf Coast that will accommodate natural gas as a feedstock and as a power source. Therefore, longer-term, I would anticipate demand for natural gas will increase. This causes me to be bullish on the continued fortunes of companies tied to the extraction of natural gas. Additionally, I am bullish on transportation infrastructure—an example would be master limited partnerships involved in the transportation of crude and other hydrocarbons; we have to move the molecules and most MLPs earn a tariff for this service.

J.B. Dollison is a principal with Crutchfield Capital Corporation and a member of the Association for Corporate Growth's Global Board of Directors, where he co-chairs the Public Policy Committee. Previously, he enjoyed an extended career with Exxon Corporation, holding a variety of management positions in finance, marketing and operations.

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