THE UNCERTAINTY METRIC

Dry natural gas properties have declined in value enough that buyers who acquired based on high commodity prices in 2008-2009 are reentering the market to average down their portfolio's cost basis. Gas properties are selling in the range of PV-12 to PV-15. Conventional gas properties with natural gas liquids (NGLs) and oil-heavy properties are being sold to fund resource plays. Oil properties are garnering PV-8 values.

Commercial bank lending is finally increasing. Mezzanine financing is back, seeking a higher return. Capital sources, offering record-low interest rates, are contributing to the "race to liquids." Proved undeveloped reserves (PUDs) are being discounted to PV-25, which, with gas around $4 per thousand cubic feet (Mcf), translates to dry-gas PUDs receiving almost no value.

During the past 12 months, oil and gas prices have become more decoupled than ever, ranging to a ratio as high as 25:1, oil to gas.

The threat of capital-gains tax increases drove divestitures this past year. The November election results lessen these concerns; however, uncertainty remains. Increased and threatened government regulation has encouraged companies to take themselves private, as in the cases of Exco Resources Inc. and Quicksilver Resources Inc.

Private equity is re-loading as portfolio companies realign, exiting or consolidating with other portfolio companies.

Lease aggregators in resource plays are seeking funding and joint ventures. Currently, more than half a million acres of Eagle Ford shale leasehold is on the market. Implied acreage values are ranging from $1,500 per acre to more than $10,000 per acre, depending on how oily they are.

The competition for oil reserves is as fierce as it has been in years. Emerging as a successful buyer requires creating a tangible competitive advantage from special knowledge or commodity-price-risk acceptance. Commodity-price hedging is a required component of every deal, no matter the size. It is extremely difficult to be a competitive bidder without downside risk protection.

Major oil companies are selling conventional assets and increasing their exposure to resource plays. Large caps are realigning their holdings toward oil assets. Private-equity companies are seeking to buy conventional gas assets while prices hover around $4 per Mcf.

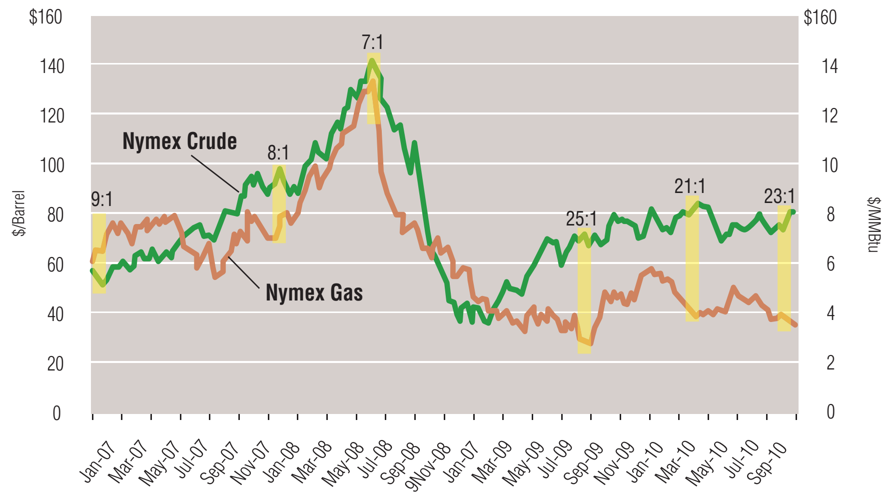
EnergyNet's engineering staff has analyzed proved developed producing (PDP) working-interest metrics in each of the producing regions. We then compared our auction metrics with PDP-only industry transaction metrics. With the exception of the Rockies, the auction metrics exceed negotiated-package values. The reason? When properties are sold at their lowest definable strategic unit (single well, lease or field), their maximum value will be derived. This assumes that the due diligence information presented is complete and accurate and that a maximum number of bidders compete.

The interesting finding for both working interests and royalty/overriding royalty interests, when normalized, is that they have not changed significantly from 2007 to the present. The cash-flow multiples and flowing-barrel results have remained relatively consistent amidst commodity-price swings when comparing property values.

No industry is more adept than the oil and gas industry at facing uncertainty and risk. The A&D winners have been and will continue to be those who create opportunity out of uncertainty.

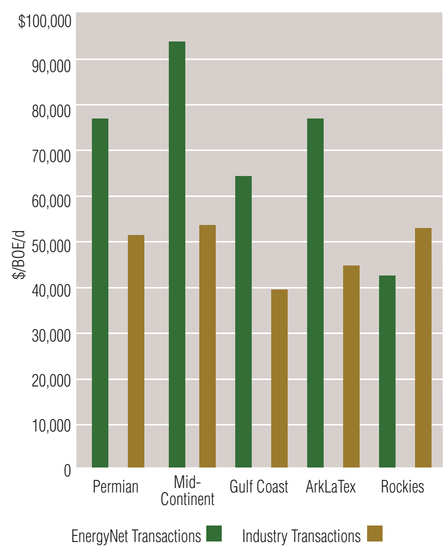
Bill Britain, president and chief executive, EnergyNet Inc., 806-242-1509

Price Collapse And Gas Disequilibrium



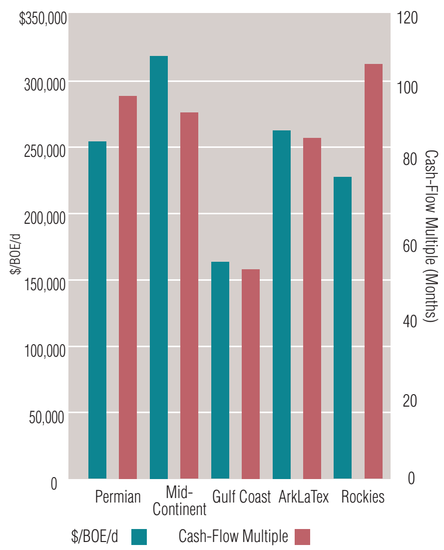
Source: Energy Information Administration

PDP Working-Interest Metrics: 1/07–6/10



Producing Working-Interest Properties Selling > $50,000-$10MM
Source: EnergyNet Inc.

Royalty/ORRI Metrics 2007-June 2010*



Producing Royalty/ORRI Properties Selling > $50,000-$10MM
* 20:1
Source: EnergyNet Inc.

For details on assets on the market, see A-Dcenter.com.