IPAA Private Capital Conference

Focus on Debt

February 24, 2011
Chambers Energy Capital

A Credit Opportunities Energy Fund

- Chambers Energy Capital seeks to provide debt capital to the energy industry across multiple sectors
  - Exploration & Production
  - Gas Gathering & Processing
  - Oilfield Services
  - Refining & Marketing

- Targeted investment sizes of $15 - $35 million

- Founders previously comprised the Investment Team of the Lehman Energy Fund, a proprietary credit-oriented energy investment portfolio of Lehman Brothers

- Invested more than $2 billion in capital over seven year period across 38 Transactions

- Cycle-tested investors focused exclusively on energy industry
Senior Lending Increased Materially in 2010

- Private lending rebounded sharply in 2010, but is still at fairly depressed levels
- Institutions (Hedge Funds, Mutual Funds, CLOs, etc.) were impacted more by the downturn than commercial banks but seem to have rebounded

**Total New Senior Loans**

![Total New Senior Loans Graph](Image)

Source: Standard & Poor’s Financial Services LLC

**Institutional Loans as % of New Senior Loans**

![Institutional Loans as % of New Senior Loans Graph](Image)

Source: Standard & Poor’s Financial Services LLC
Market Overview

Energy Banks Still Using Conservative Price Decks

- While bank price decks have gone up on a combined oil/gas basis.
- ...natural gas price forecasts have fallen considerably

Energy Lender Price Deck (60:40 Gas/Oil Ratio)

Source: Macquarie Tristone Energy Lender Price Survey

Energy Lender Gas Only Price Deck

Source: Macquarie Tristone Energy Lender Price Survey
Market Overview

Junior Loan Volume is Still Weak

- Second lien loan volume is up slightly but still down over 80% from the recent peak
- Commercial banks are less willing to share collateral with junior lenders
- New second lien rules-of-thumb:
  - Second lien amount cannot exceed 50% of the first lien amount
  - Caps on the amount of cash interest that can be paid to second lien lenders
  - Strict rules on when second lien lenders can exercise remedies

Total New Second Lien Loans

Source: Standard & Poor’s Financial Services LLC
Typical Private Debt Terms

Cost of Junior Debt Remains Relatively High

- Unfavorable intercreditor terms from commercial banks
- Reduced number of second lien/mezzanine debt providers
- Increased demand for junior debt to offset lower natural gas-oriented cash flow
- Mezzanine debt occasionally includes some form of return “kicker”

### Components of Mezzanine Debt Cost of Capital

<table>
<thead>
<tr>
<th>Component</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash Interest</td>
<td>10%</td>
</tr>
<tr>
<td>PIK Interest</td>
<td>5%</td>
</tr>
<tr>
<td>Fees</td>
<td>20%</td>
</tr>
<tr>
<td>Equity Kickers</td>
<td>30%</td>
</tr>
<tr>
<td>Total</td>
<td>100%</td>
</tr>
</tbody>
</table>
Typical Private Debt Terms

Junior Debt vs. Private Equity

- Despite the higher cost of private junior debt relative to bank debt, it can still be a competitive alternative to private equity

<table>
<thead>
<tr>
<th>Private Junior Debt</th>
<th>Private Equity</th>
</tr>
</thead>
<tbody>
<tr>
<td>High cost for a short period of time</td>
<td>Permanent equity dilution</td>
</tr>
<tr>
<td>“Silent Partner”</td>
<td>Board Control</td>
</tr>
<tr>
<td>Operational flexibility</td>
<td>“Mother may I …” management</td>
</tr>
<tr>
<td>Rules-based funding</td>
<td>Partner controlled advances</td>
</tr>
</tbody>
</table>

Vs.
Typical Private Debt Terms

Attributes Chambers Energy Capital Prefers for Junior Debt Financing

- While all transactions and sectors are different, some common attributes affect the cost and structure of junior debt capital

<table>
<thead>
<tr>
<th>Criteria</th>
<th>Chambers Energy Capital Preference</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash Flow</td>
<td>Company or project must have some demonstrated cash generation ability</td>
</tr>
<tr>
<td>Collateral Value</td>
<td>Collateral value must generally be at least 1.2x to 1.4x the total debt level</td>
</tr>
<tr>
<td>Earnings Predictability</td>
<td>Stable, predictable cash flows enhance amount of leverage allowed and reduce cost</td>
</tr>
<tr>
<td>Experienced Management</td>
<td>A demonstrable management track record increases the amount of structural flexibility</td>
</tr>
<tr>
<td>Geographic Location</td>
<td>Assets in well-known basins of the US and Canada are preferred</td>
</tr>
<tr>
<td>Risk Mitigation</td>
<td>Commodity price hedging or other contractual risk mitigation techniques can reduce the cost</td>
</tr>
</tbody>
</table>
Contact Chambers Energy Capital Team

Chambers Energy Capital

600 Travis Street
Suite 7330
Houston, Texas 77002
www.chambersenergycapital.com

J. Robert Chambers 713-554-6771 rchambers@chambersenergycapital.com
Guy Hoffman 713-554-6772 ghoffman@chambersenergycapital.com
Phillip Z. Pace 713-554-6773 pzpace@chambersenergycapital.com