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IPAA Private Capital Conference
Mid-Market Financing Options

January 2019

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Madava Financial is a private, energy-focused finance company that provides capital alternatives primarily through direct lending to oil and gas producers and midstream operators in the continental US and Canada. Madava was founded by Robb Turner, who was Senior Partner and co-founder of ArcLight Capital Partners until January of 2017.

Energy Lending Has Changed:

- Traditional lenders (banks) are retreating from energy lending due to increased regulatory requirements and recent loan underperformance
- Over $300 billion of existing public and private debt is maturing over the next seven years; SNC examination data as of 12/31/16 showed that $76 billion[(1)] needed to be reclassified under the new OCC lending regulations for banks[(2)], much of which will be seeking new non-bank financing

Growth of Energy Sector Requires Additional Financing:

- Significant ongoing capital is required to restructure the middle market E&P industry and fund the next stages of M&A and development activities

The Opportunity:

- We believe there is a large and unique opportunity for 'non-bank banks‘ to finance the next wave of energy capital needs

(1) Shared National Credit Review (SNC) Q1 2017
(2) Office of the Comptroller of the Currency

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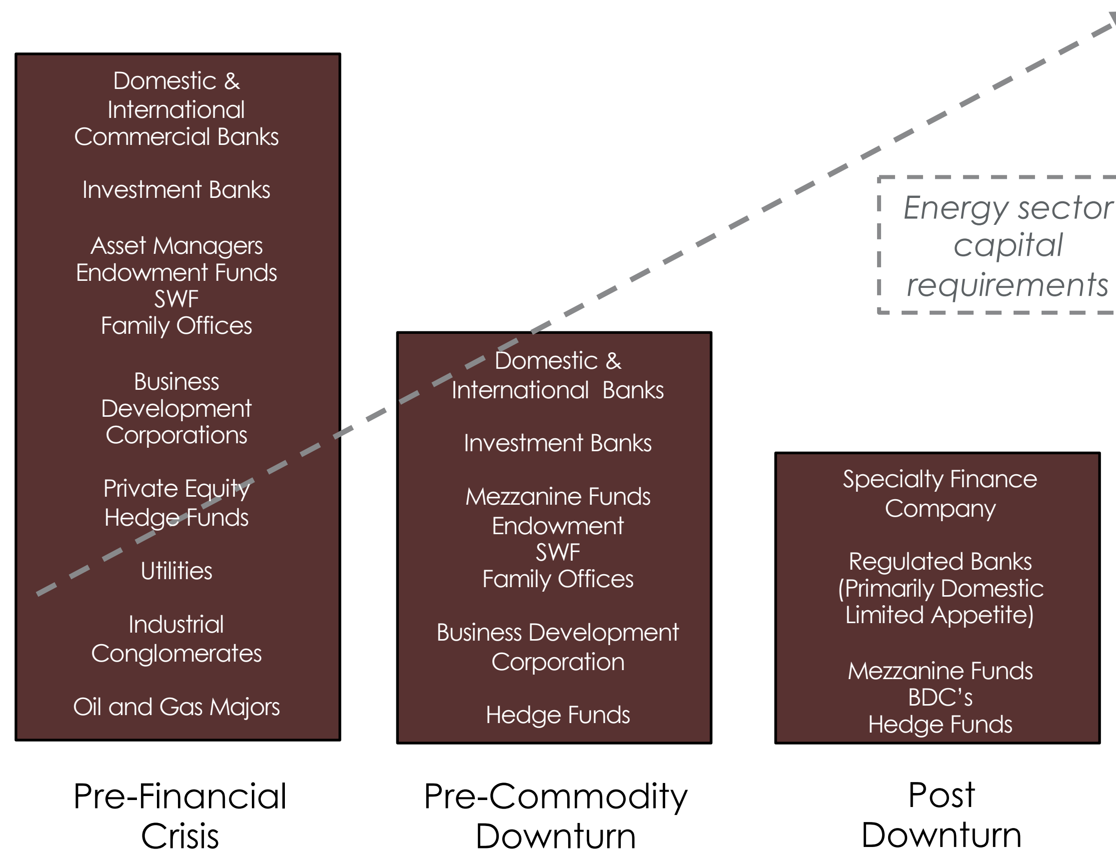
- Regulated lenders must reduce criticized / classified loan exposure, new OCC regulation is forcing significant disintermediation into the institutional market
- Private Equity activity is expected to pick-up boosting M&A and the associated balance sheet financing required to close these transactions
- Many deals are caught in financial purgatory, not in a position to be sold off by PE investors at a loss, but not in a position to receive incremental funding from lenders



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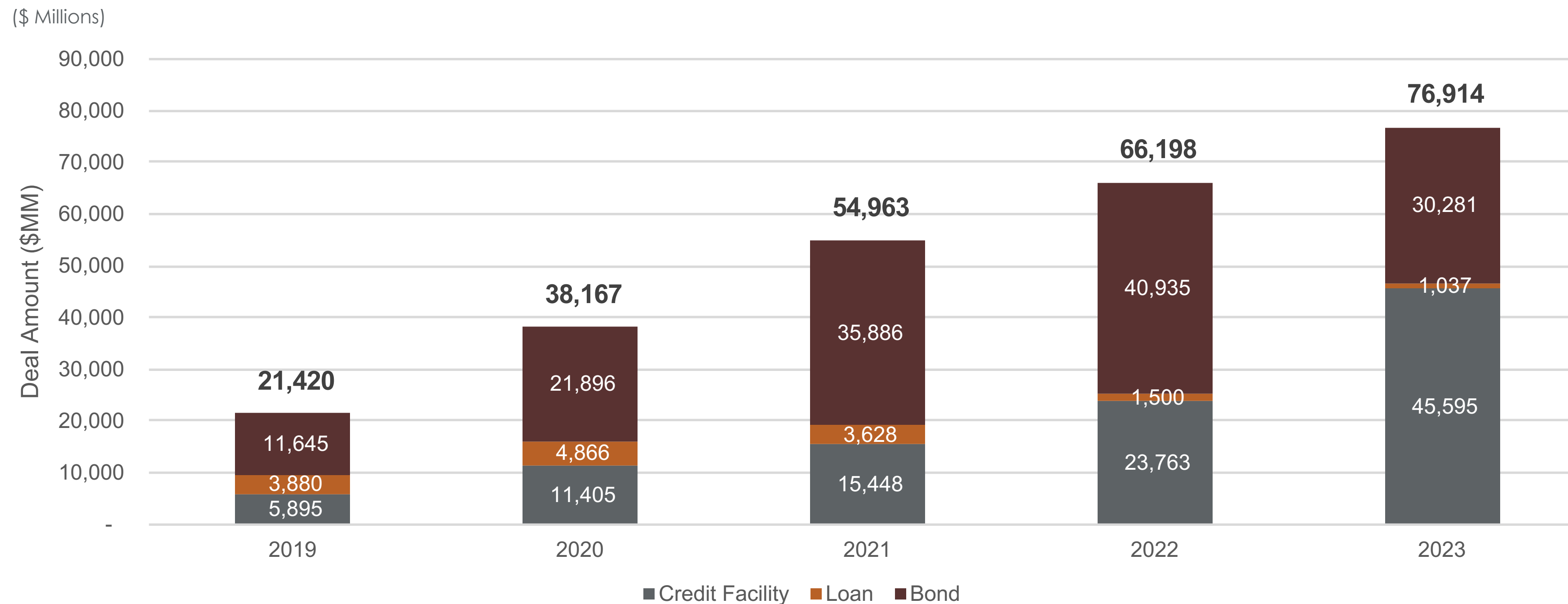
Upstream debt market by the numbers …

- Over $300 billion - committed revolvers/borrowing bases & HY/term debt scheduled to mature through 2023
- Over $76 billion – non-compliant at 12/31/16 according to Q1 2017 SNC review and will need refinancing / restructuring

Upstream Funded Debt Maturities (1)

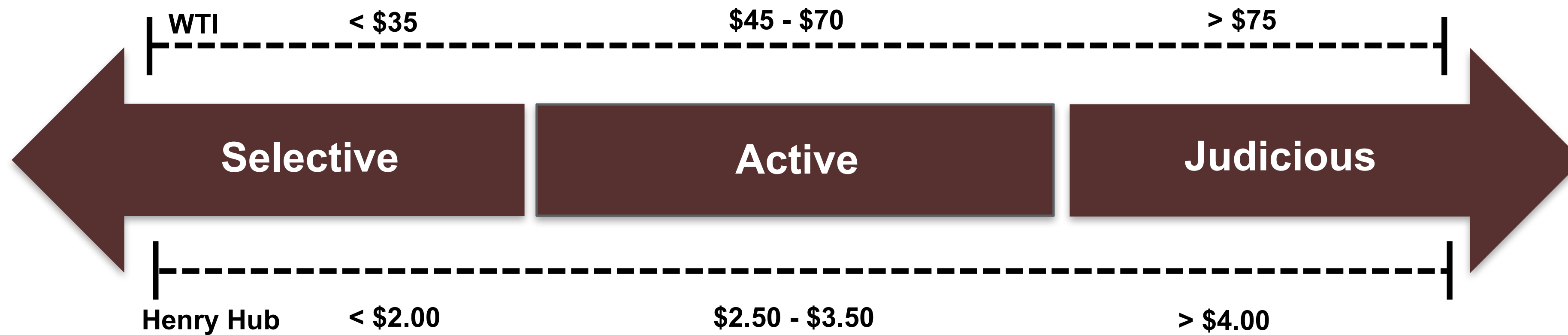


(1) DI Capitalize

- Capital for sub-$200 million deals (“middle market” lending) is primarily accessed via senior secured borrowing base facilities at one end of the capital structure and mezzanine capital and/or equity at the other
- Capital is required for situations that lie outside where the regulated financing entities can comfortably participate
- The advancement of horizontal drilling technologies and multistage hydraulic fracturing has created a large capital requirement for development vs. traditional single vertical wells. Pad development programs only exacerbate the need for liquidity as multiple wells are cash called at one time with completion after all wellbores are drilled

We believe significant unwinding of financial regulation after the 2008 financial crisis remains politically unpalatable for both sides of the house. In the current environment, unregulated capital is preferential in situations such as:

- E&P loan refinancing where the Bank Borrowing Bases are insufficient to meet on-going capital requirements
- M&A activity driven by larger independents divesting of assets to deploy capital into core high return areas such as the Permian and Scoop / Stack basins
- Companies currently stuck in “bank purgatory”. Lenders are unwilling to sell loans at a loss nor will they lend additional money to continue operations and undertake new drilling
- Many PE firms are unable to sell conventional assets which have depressed fund returns and has slowed subsequent fundraising activities



- **Selective:**
  - Many Basins become uneconomic to drill
  - Focus on core basins, existing production and strong sponsors
- **Active:**
  - Robust development activities and M&A market where capex requirements can exceed bank lending capacity
  - Focus on strong hedge programs to ensure cash flow to support development and debt service
- **Judicious:**
  - Elevated prices allow producers to “step out” into unproven areas
  - Degradation in loan terms/structures
  - Focus on proven borrowers and sponsors that exhibit cost controls and maintain reasonable drilling risk
  - Maintain hedge programs as the marginal basins can quickly become uneconomic

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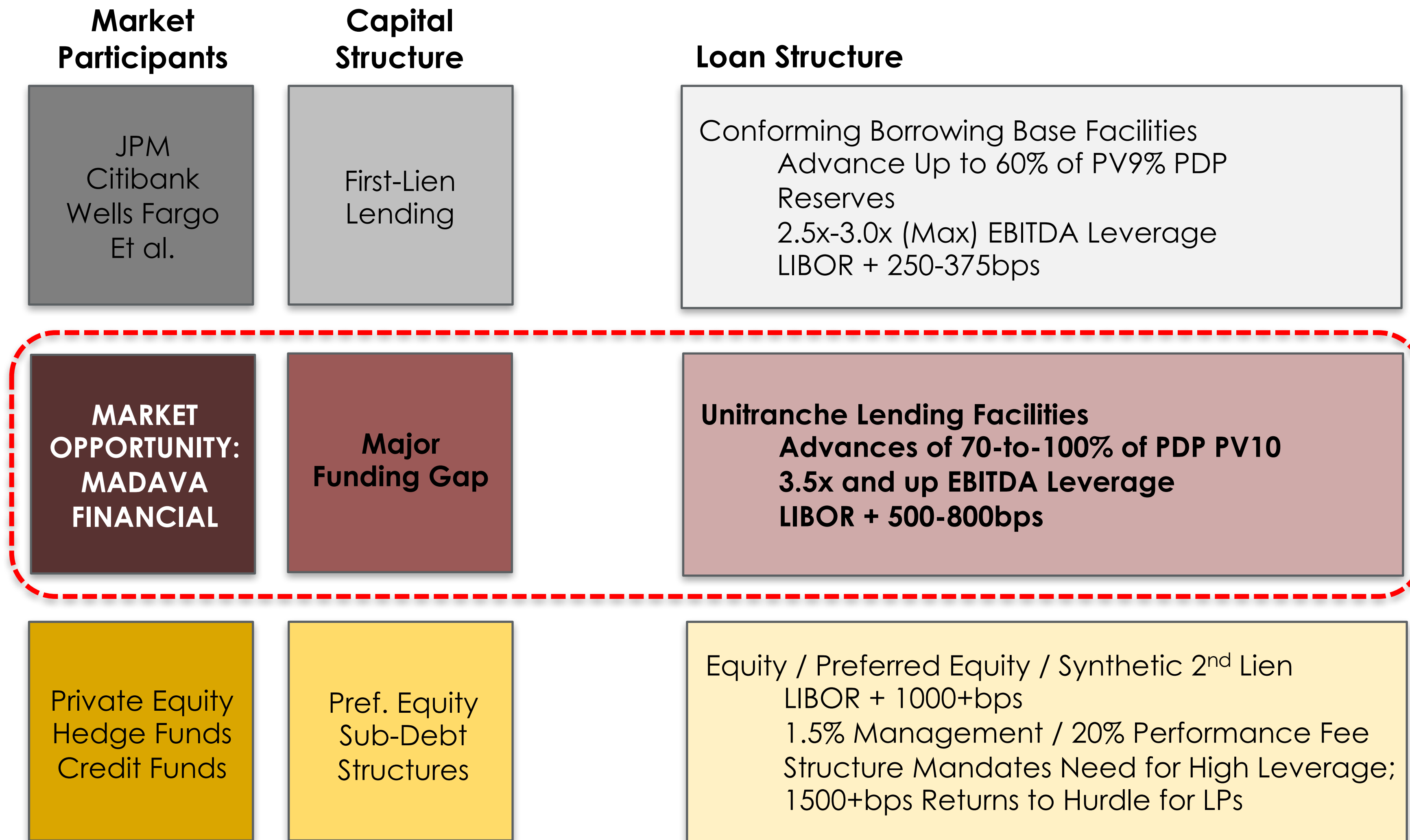


Information on this slide reflects the Company's best estimate of representative market participants and transaction terms based on a review of company filings, the team's transaction history, and ongoing industry dialogue. It is subject to change based on market developments.

ILLUSTRATIVE TRANSACTIONS – UNITRANCHE LOAN STRUCTURE

Notional: $200mm

Spread: LIBOR + 650 - 850bps (LIBOR floor: 100bps)

Upfront Fee: 200bps

Security: First Ranking Lien on all Assets, negative pledge on Equity

Semi-Annual / Quarterly Borrowing Base Redeterminations

Hedging Requirement:

75%+ of PDP for 36 months

75% of PDP rolling for 36 months tested quarterly

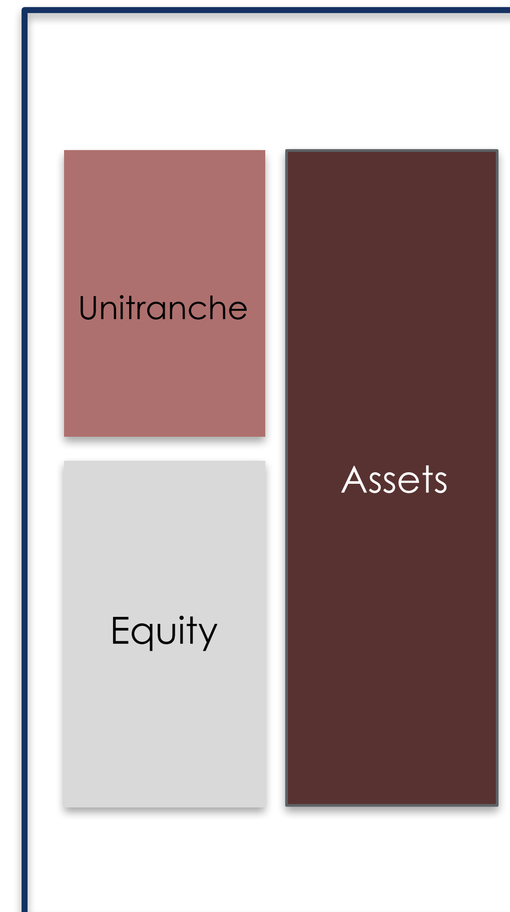
Financial Covenants:

Asset Coverage Test: Min PDP PV9% to Debt of 1.0x

Leverage Ratio: 12 month holiday then 4x thereafter

Current Ratio: 1.0 / 1.0

Call Protection: 1 year make whole; year 2 - 102%; year 3 – 101%



ILLUSTRATIVE TRANSACTIONS – STRUCTURED SYNTHETIC 2ND LIEN

<u>Senior Unsecured Loan (HoldCo):</u>

Notional: $125mm

Maturity: 5 years

Rate: 11.5% (8% cash pay / 3.5% PIK)

Upfront: 200 bps

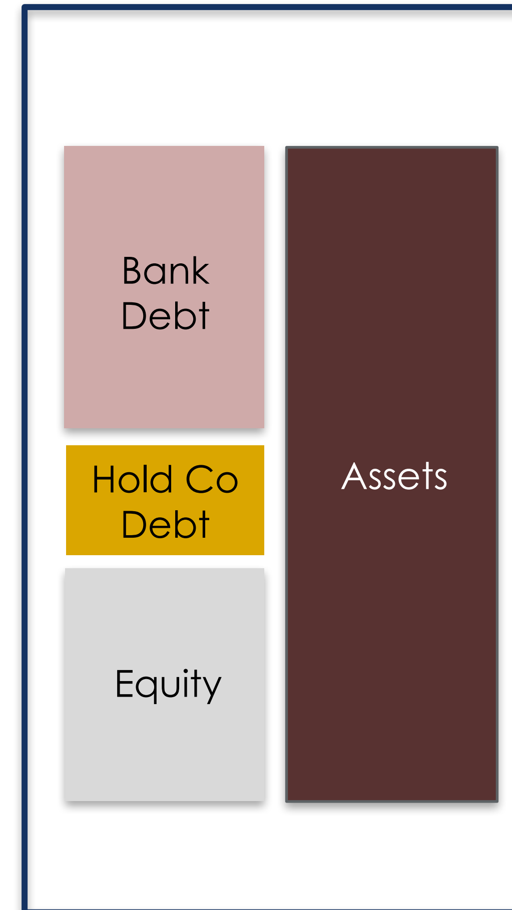
PDP Asset Coverage Ratio: 1.25x (80% of PDP's max total leverage)

Prepayment Penalties: First 2 years: Interest Make whole / Year 3: 3% penalty

Mandatory Hedging: 85% of PDP's first 3-5 years **Review:** The Holdco note caps any leverage beyond the First Lien, returns approx. 15% for less than 1 times PDP coverage with most oil and gas production hedged for the next 3-5 years

The above deal would complement a more traditional and still available First Lien (OpCo) bank facility:

Notional: $650mm; Rate: LIBOR + 275 - 375 bps grid; Upfront: 75bps



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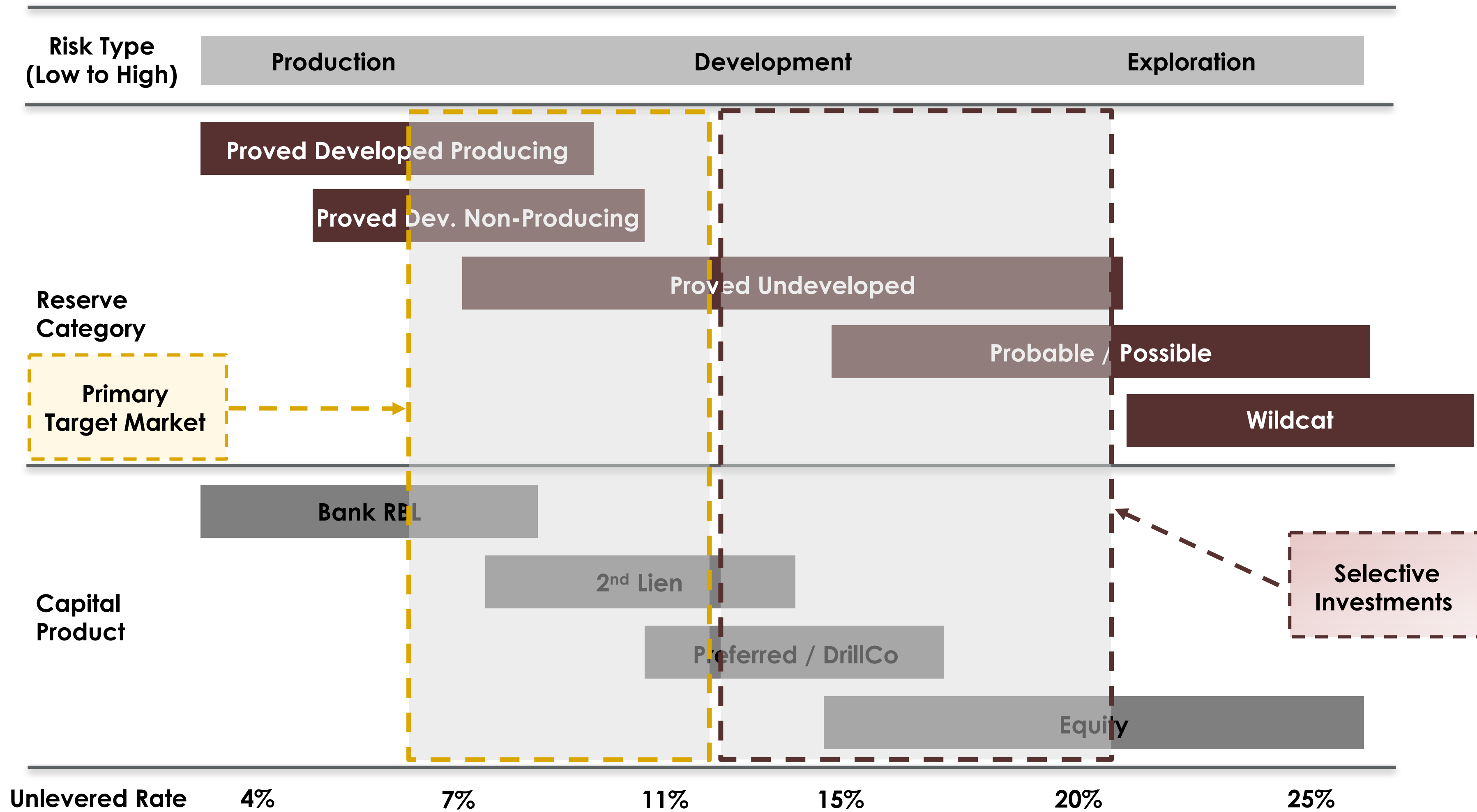

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