Agenda

Capital Flows
What’s driving recent energy market performance?

Valuation & Fundamentals
Why is deep value money still on the sidelines?

Looking Ahead: 2020-2021
What macro & sector developments can we expect?

Conclusion
How to craft a winning strategy
Capital Flows
What’s Driving Performance &
What Does That Tell Us?
After Being The Worst Performer In 2018, Energy Is One Of The Better Performers In 2019

2018 Equity Sector Performance

<table>
<thead>
<tr>
<th>Sector</th>
<th>YTD Equity % Chg.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Healthcare</td>
<td>5%</td>
</tr>
<tr>
<td>Utilities</td>
<td>0.46%</td>
</tr>
<tr>
<td>Cons. Disc.</td>
<td>0.32%</td>
</tr>
<tr>
<td>Technology</td>
<td>(3%)</td>
</tr>
<tr>
<td>Real Estate</td>
<td>(6%)</td>
</tr>
<tr>
<td>Cons. Staples</td>
<td>(11%)</td>
</tr>
<tr>
<td>Financials</td>
<td>(15%)</td>
</tr>
<tr>
<td>Industrial</td>
<td>(15%)</td>
</tr>
<tr>
<td>Materials</td>
<td>(17%)</td>
</tr>
<tr>
<td>Energy</td>
<td>(21%)</td>
</tr>
</tbody>
</table>

Q1'2019 Equity Sector Performance

<table>
<thead>
<tr>
<th>Sector</th>
<th>YTD Equity % Chg.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Technology</td>
<td>19%</td>
</tr>
<tr>
<td>Real Estate</td>
<td>17%</td>
</tr>
<tr>
<td>Industrial</td>
<td>16%</td>
</tr>
<tr>
<td>Energy</td>
<td>15%</td>
</tr>
<tr>
<td>Cons. Disc.</td>
<td>15%</td>
</tr>
<tr>
<td>Comm. Svcs.</td>
<td>13%</td>
</tr>
<tr>
<td>Cons. Staples</td>
<td>10%</td>
</tr>
<tr>
<td>Utilities</td>
<td>10%</td>
</tr>
<tr>
<td>Materials</td>
<td>10%</td>
</tr>
<tr>
<td>Financials</td>
<td>8%</td>
</tr>
<tr>
<td>Healthcare</td>
<td>6%</td>
</tr>
</tbody>
</table>
Even With Strong Gains, Energy Stocks Continue to Disappoint

E&P Stocks vs. Oil Prices in Q1'19: Despite the Strength, E&Ps Continue to Lag Oil Prices

Even With Strong Gains, Energy Stocks Continue to Disappoint
Energy Continues to Lag Other Sectors in Fund Flows

2018 Fund Flows by Sector: Energy's Equity Losses Corresponded with the Exodus of Invested Capital

Utilities: 14%  
Healthcare: 7%  
Real Estate: 6%  
Cons. Staples: 2%  
Cons. Disc.: (10%)  
Technology: (12%)  
Industrial: (19%)  
Energy: (26%)  
Materials: (27%)  
Financials: (32%)

YTD Fund Flows % Chg.

2019 Fund Flows by Sector: Despite Energy's Solid Equity Gains, Fund Flows Trail Other Sectors

Comm. Svcs.: 91%  
Real Estate: 21%  
Materials: 13%  
Technology: 12%  
Cons. Staples: 12%  
Healthcare: 9%  
Utilities: 9%  
Cons. Disc.: 8%  
Energy: 3%  
Industrial: (0.45%)  
Financials: (3%)

YTD Fund Flows % Chg.

Source: Lipper
Q1’19 Energy Performance vs. Short Interest Positioning

Short covering played a role in the Q1 gains of the Energy sector
The 3 highlighted sub-sectors account for ~75% of the S&P Energy Index
Valuation & Fundamentals
What Is Keeping The Long/Value Money On The Sidelines?
Sector Breakdown of S&P 500 by Market Cap Over Past Decade:
While Energy’s Absolute Market Cap Has Gone Up, the Sector’s Relative Weighting Has Lost Share To Technology

Energy dropped 62% in Relative Market Cap Weight - from 13% to 5%
S&P 500 Sector View: Market Cap Weightings vs. Percentage of Earnings

Energy has 5% stock value relative to 7% earnings contribution, suggesting the sector is undervalued.

Source: FactSet April 2019
Energy Returns Have Improved But Still Lag Other Sectors

S&P Mid Cap ROCE by Sector

S&P 500 ROCE by Sector

Source: FactSet April 2019. ROCE Estimates based upon data as of April 3, 2019
Refiners Continue To Outpace All Other Energy Sub-sectors In Returns

Return on Capital Employed By Energy Sub-Sector

<table>
<thead>
<tr>
<th>Sub-Sector</th>
<th>2017</th>
<th>2018</th>
<th>2019 Est.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Refiner</td>
<td>12.7%</td>
<td>11.8%</td>
<td></td>
</tr>
<tr>
<td>Midstream</td>
<td>8.8%</td>
<td>8.1%</td>
<td>10.1%</td>
</tr>
<tr>
<td>Integrateds</td>
<td>9.9%</td>
<td>9.6%</td>
<td>9.9%</td>
</tr>
<tr>
<td>E&amp;P - Large</td>
<td>2.4%</td>
<td>7.5%</td>
<td>9.3%</td>
</tr>
<tr>
<td>E&amp;P - Mid</td>
<td>6.1%</td>
<td>7.6%</td>
<td>8.7%</td>
</tr>
<tr>
<td>E&amp;P - Small</td>
<td>4.0%</td>
<td>6.9%</td>
<td>7.8%</td>
</tr>
<tr>
<td>Services - Large</td>
<td>3.2%</td>
<td>6.5%</td>
<td>7.5%</td>
</tr>
<tr>
<td>Services - Mid/Small</td>
<td>1.8%</td>
<td>0.1%</td>
<td></td>
</tr>
</tbody>
</table>

ROCE = EBIT / (Total Assets - Current Liabilities)

Source: FactSet April 2019. ROCE Estimates based upon data as of April 3, 2019
Looking Ahead
What Developments Can We Expect in 2020 – 2021?
What Can We Expect in 2019-2020?
Challenges from the Macro Environment

Regulation on Corporate Access →
Unbundling of Research & Trading

- Contraction of sell-side
- Small & Mid-caps will receive less research coverage
- Decrease in conference & meeting quality
- International marketing particularly difficult
- Issuers will need to set up their own investor meetings

Increased Dominance of ETFs and Index Funds

- Passive assets are poised to surpass actively managed assets in the U.S. in 2021 according to Moody’s Investor Services
- Passive assets already hold 35% of S&P 500
- How to make the nuances of your investment thesis matter in a market with less discretionary capital?
More Macro Headwinds
Less Exclusive Focus On Energy

Increased Importance of Generalist Investors

- Analysts covering multiple unrelated sectors
- Issuers need to simplify the investment thesis
- Think in investment themes vs. sectors
- How do you compete outside of your sector?
Sector Trends & Developments in 2020-2021

Tailwinds

- US Becomes Net Energy Exporter On Consistent Basis
- IMO 2020
- Improved Financial Results
- Uptick in Reverse Mergers
  - IPO Market & Pipeline
  - Public M&A

Headwinds

- No Conviction On Sustainability Of Oil Prices +$60
- Perception That Energy Is The New Tobacco
- Aramco IPO Planned For 2021
- 2020 Election Year
E&P Equity Performance Post Acquisition Announcement Date Through Q1’19: Markets Have Penalized Companies for Buying Other Public Companies

- CXO: (29%)
- ECA: (29%)
- XEC: (21%)
- CHK: (17%)
- FANG: (6%)
Sector Trends & Developments in 2020-2021

Tailwinds

- US Becomes Net Energy Exporter On Consistent Basis
- International Maritime Organization (IMO) 2020
- Improved Financial Results
- Uptick in Reverse Mergers
  - IPO Market & Pipeline
  - Public M&A
- 2020 Election Year

Headwinds

- No Conviction On Sustainability Of Oil Prices +$60
- Perception That Energy Is The New Tobacco
- Aramco IPO Planned For 2021
Other trends for 2020-2021
Increased Focus on Environmental, Social & Governance (ESG):
A Challenge → Opportunity

Institutions embrace responsible investing

ranks of investment managers that have signed the UN Principles of Responsible Investing, committing to consider ESG issues in portfolio decisions.

- Assets under management (U.S. $ trillion)
- Number of signatories

PRI | Principles for Responsible Investment
Investors Across All Strategies Are Focusing On ESG

- No longer just a European phenomenon
- No longer only the domain of small pension funds/religious endowments
Sustainable Investing Rarely Implies Divesting: Being Best in Class within Oil & Gas Can Help Issuers Attract New Money

$1 of Every $4 institutional assets are invested sustainably

$23T institutional assets are invested sustainably
The “G” is the Most Important Part of ESG: Top Governance Priorities for Investors

1. Board Composition, with a particular focus on enhanced diversity
2. Board-level expertise that is more aligned with business goals
3. Increased attention to climate risk and the environment
4. Enhanced attention to talent and human capital management
5. Compensation that is more aligned with performance and strategy
In Conclusion
How To Craft A Winning Strategy
In Conclusion: How Should Issuers Position Themselves to Win?

- Acknowledge past performance as a steward of capital
- Simplify the investment case
- Demonstrate competitiveness relative to stocks in other sectors
- Focus on returns rather than growth
- Cut costs, reduce debt & compensate shareholders
- Be transparent about managing risk for the future
  - Stress test around carbon tax and reserves write downs
- Focus on lowering carbon intensity
- Institute incentive metrics that align with long-term strategy
- Increase female representation at board and management level
Thank You!

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