IMT Exam – Chapter 6

Analysis of Resource Companies

Professor's Comment:
It is possible that you will see 3 questions specifically related to this material. This summary is intended to provide coverage of the 10 key need to know items so that you can boost your score by 2 or 3 points…which may be the difference to push you over the passing mark.

Oil and Gas Industry
Equity valuation in the oil and gas industry focuses on ***"reserves"***. Reserves are the natural resources owned by the company that are still in the ground.

Terms to Know:

Proved reserves: 90% chance that they will be recovered, also called ***"P90"*** or ***"1P"***.

Probable reserves: 50% chance that they will be recovered, also called ***"P50"*** or ***"2P"*** or ***"Proved + Probable"***.

Possible reserves: 10% chance that they will be recovered, also called ***"P10"*** or ***"3P"*** or ***"Proved + Probable + Possible"***.

We can further breakdown the proved reserves category into:

1) Proved developed reserves (PDP) - producing reserves that are currently generating cash flow. PDP assets are not discounted for valuation purposes.

2) Proved developed not producing (PDNP) - same as PDP reserves but no cash flow yet. PDNP assets are discounted by 25% for valuation purposes.

3) Proved underdeveloped reserves (PUD) - questionable recovery due to legal, regulatory or political risks. PUD assets are discounted by 35% for valuation purposes.

Reserves
A ***barrel of oil equivalent (BOE)*** is the basic unit of measurement for reserves.

1 BOE = 1 barrel of oil (bbls)
1 BOE = 6,000 standard cubic feet (scf) of natural gas (NGL)

<u>Quick Example:</u>
Stampede Oil has the following 1P reserves:

1) 5 million bbls of oil
2) 600 million scf of natural gas

Calculate the BOE of Stampede's entire reserves:

Solution:
5 million bbls of oil = 5 million BOE

600 million scf of natural gas / 6,000 = 100,000 BOE

Total reserves = 5,100,000 BOE