



Friday Morning Coffee

Nr. 9 – Value Investing in the Energy sector

As a bottom-up value investor, we do not claim to have an edge into forecasting the future direction of the oil price. Indeed, the factors dictating supply and demand of black gold are very complex: how can we possibly make a reasonable assumption on the next move by OPEC, their ability to cut supplies, potential geopolitical tensions, supply of shale oil, inventories, harshness of a winter season or the success of alternative energy sources?

So, **why do we** however **invest in the Energy sector**? **Because** we think that **a successful investment case in this sector is not automatically related to a correct prediction of oil price** and that **it is possible to look at the sector through a different angle**: instead of building an investment case on an assumption of the future oil price, we thrive to identify companies and business models that are less dependent on these prices.

In line with this approach, our current investment ideas are all service providers to the oil and gas industry and within this segment, we are avoiding companies that are first in line and purely dependent on the activity level in oil exploration. So, we are avoiding not only the Exploration & Production companies (E&Ps) but also the E&P service providers, for example the seismic companies.

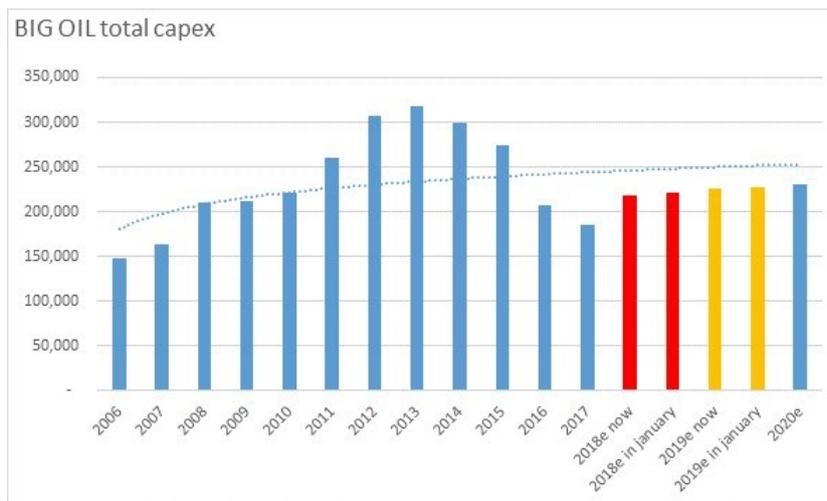
We thus focus on 2 types of oil companies.

- * **Firstly, the one's who offer products and services that are linked to the operating expenditures of the oil majors.** In other words, in order to have their production going and continue to pump oil, the oil majors need to continue to invest in these services. So, even at the bottom of the cycle these suppliers will continue to get orders and will continue to show a certain level of earnings power. Wood Group is a good example of this type of company.
- * **Secondly, we like the oil service providers that have a substantial competitive advantage that makes their products desirable.** For example, Subsea 7 is one of the top 3 players worldwide in subsea installation work. Any company, being it an oil major or a national oil company will sooner or later require its services if they want to run deep-sea oil production.

The following note gives the opinion of the Investment team at the time of the publication. Please refer to important notice at the end of the document.

Friday Morning Coffee - Nr. 9 – Value Investing in the Energy sector

Independently of the oil price that has been rebounding from its lows, we believe that the stars are aligned again for the oil service industry.



Source: Bloomberg

Indeed, the cycle is improving after 4 years of underinvestment while demand for oil and well depletion has continued. That means that finally the order books of the companies we look at are filling up again. We focus on companies with strong balance sheets at very low valuations. For example, 14.8% of the market cap of Subsea 7 is net cash and the company trades at 4.8 times EV/EBITDA. The company has continued to generate cash through the downturn. We believe, **now that the oil majors are starting to spend again, this represents a clear undervaluation for the earnings power at hand.**

Have a great weekend,

Léon Kirch, CFA
Partner & Chief Investment Officer
May 4th, 2018

Important notice

European Capital Partners (Luxembourg) SA ("ECP") is responsible for the publication of this promotional document. ECP is an asset management company based in Luxembourg, registered at JF Kennedy avenue 35a, L-1855 Luxembourg (RCS Luxembourg, B 134.746) authorized as an Alternative Investment Fund Manager ("AIFM") of the Luxembourg law of 12 July 2013 and supervised by the Commission de Surveillance du Secteur Financier (CSSF). This document is published for information purposes only and gives the opinion of the Investment team at the time of the publication. It does not constitute an offer to buy or sell financial instruments or investment advice and does not confirm any transaction unless expressly agreed otherwise. Although ECP carefully selects the data and sources used, errors or omissions cannot be excluded a priori. ECP cannot be held liable for any direct or indirect damage resulting from the use of this document. The intellectual property rights of ECP must be respected at all times; The contents of this document may not be reproduced without prior written consent. Any investment involves risks, such as the risk of loss of initial capital. Please read the Prospectus of Selected Funds, their Key Investor Information Documents (KIIDs) and financial reports before making an investment decision to understand their specific risks, costs and conditions. Those documents are available on www.ecp.lu. Past performance does not guarantee future performance. Please refer to an independent tax advisor for country tax information that can change at any time and analyze the tax impacts of any investment on your personal situation.