A note from Andy Brogan, Global Oil & Gas Transaction Leader

Our 12th Capital Confidence Barometer characterizes the oil and gas M&A market once again as one of cautious optimism. There is increasing optimism around the global economy, but there are still big risks for the oil and gas sector from geopolitical instability and uncertainty (e.g., as usual, the Middle East and North Africa, the widening battle with Islamic extremists, the ongoing dispute between Russia and Ukraine, the unresolved Iranian sanctions issue), from commodity and currency volatility, in particular around crude oil prices and the strengthening of the US dollar.

Since last fall, sluggish oil demand growth has collided with strong supply and a repositioning by OPEC to create a sharp downward movement in global oil prices. Oil and gas companies have responded to the price collapse with an intense internal focus – aggressively cutting spending and costs, postponing new final investment decisions (FIDs), and improving operational efficiency.

Uncertainty about where oil prices will land after their months-long slide has dramatically disrupted the global market for oil and gas M&A activity. After a very strong second half of 2014, the first quarter of 2015 was the quietest in recent memory. But it’s not just the level of oil prices – it’s the volatility. As long as buyer and seller agree on pricing outlook, then a price at which to do a deal can be found. Sellers typically set price expectations based on the oil/gas price at the time they decided to sell, while buyers can be more current. Until the uncertainty diminishes and we have some clarity about the oil price trajectory, deals will be harder to do.

For most of the last three years, growth has led the strategic agenda for oil and gas companies. Now, unsurprisingly, it’s much more about optimizing the portfolio, managing the cost base and managing the risk profile. Only the US midstream, fed by the huge infrastructure requirements of the “shale revolution,” remains a hot spot in an otherwise lackluster deal market.

Altogether this means more oil and gas assets on the market now than in many past years, and while what has been described as a “wall of money” waiting in the wings, in a buyer’s market, deals are taking longer to close. The megamerger of Shell and BG announced early in the second quarter has been seen by some as the harbinger of renewed strength in the M&A market for oil and gas. While we think that the deal is reflective of a specific clear strategic fit, rather than a definitive shift in the market, we do, however, see grounds for some optimism performance oriented oil and gas dealmaking, in the second half of the year.

A note from Pip McCrostie, EY Global Vice Chair, Transaction Advisory Services

Our 12th Global Capital Confidence Barometer finds the global M&A market maintaining 2014’s positive momentum with more than half our respondents globally planning acquisitions. Economic optimism, combined with steady confidence in market indicators, is fuelling M&A moves as companies look to generate future value.

Our survey reveals three key reasons for these dealmaking intentions. First is the arrival of new entrants – both start-ups and companies returning to the market. Second, divergent economic conditions are accelerating cross-border M&A. Third, disruptive innovation is driving dealmaking at every level of the enterprise.

Of course, challenges remain on the boardroom agenda – volatility in commodities and currencies, geographic divergence in economies and monetary policies, and lingering geopolitical concerns. Rapid technological change is also creating new risks, such as cybersecurity, which must be managed by dealmakers.

Notwithstanding these risks, the overall view is of a global M&A market on an upswing. After a half-decade of stagnation, we are seeing the bold beginnings of a new kind of deal market – one marked by innovation, complexity and disruptive change.
97% expect that the global economy will improve or at least be stable over the next 12 months.

34% see increased volatility in commodities and currencies as a big economic risk over the next 12 months. Geopolitical risk remains the greatest economic risk.

94% are primarily focused on raising/optimizing capital, as opposed to investing or merely preserving capital; this is a sharp reversal from 2013 when companies were primarily focused on investing.

99% are expecting the oil and gas deal market to improve or at least remain stable over the next 12 months.

56% expect their companies to actively pursue acquisitions over the next 12 months, more than double compared to expectations in November 2014.

85% of oil and gas executives view the global economy as improving.

**Middle-market is expected to lead the M&A rebound**

Leverage regulatory/legislative opportunities

Gain market share in existing geographical markets

Move into new geographical markets

Improve structural tax efficiencies

Move into new product/service areas

**Top drivers impacting M&A strategy**

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