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Energy Research
Oil and Gas Exploration & Production
Industry Commentary

Taking the Pulse of Clients, Post-Launch and Pre-3Q Earnings

Summary

After two weeks of meetings/calls with clients following our recent launch, we present our summary takeaways. When re-engaging with investors after having our heads down for two months, we were most surprised by the degree investors favored oil over gas through 2017. Given that mindset, investors understand our caution on valuations for Permian Basin pure-plays, but feel content to hide in them knowing they are unlikely to underperform the broader industry in anything but a sharply accelerating oil price environment. Summary thoughts on two main topics and popular / unpopular ratings are below.

Company	Symbol	Price (10/24)	Rating Prior	Rating Curr	PT
Callon Petroleum Company	CPE	$14.88	–	Neutral	$17.00
Diamondback Energy, Inc.	FANG	$99.60	–	Buy	$124.00
Energen Corporation	EGN	$53.61	–	Buy	$72.00
Gulfport Energy Corporation	GPOR	$25.96	–	Buy	$36.00
Matador Resources Company	MTDR	$24.11	–	Neutral	$26.00
Noble Energy, Inc.	NBL	$35.38	–	Buy	$44.00
Oasis Petroleum Inc.	OAS	$11.56	–	Buy	$17.00
Southwestern Energy Co.	SWN	$11.20	–	Buy	$20.00

Source: Bloomberg and Mizuho Securities USA

Key Points

It's lonely here on Gas Bull Island. Our constructive view on natural gas through '18 was met with pushback from trading-oriented and long-only accounts. The pushback is more in a relative sense - investors have a more constructive view on a sustainable 10+% increase in oil prices than a similar rally in gas. But there remains concern on gas prices, which is two-pronged. First, investors are concerned that a bounce in non-Appalachia gas production (Permian, SCOOP/STACK, Haynesville) may offset broader declines in lower 48 production. Second, investors are increasingly less comfortable with the timeline of pipeline construction projects in Appalachia, and reviewing thoughts on what they are willing to pay for gassy Appalachian producers. Our counter has been that a minor disruption in the Atlantic Sunrise pipeline does not indicate the "end of days" for all regional pipeline projects. And we remain constructive on secular improvements in natural gas demand, which we expect to keep a bid for gas in the $3/mcf range, assuming a normal winter.

Investors understand Permian caution, but are still happy to hide there. Our caution on the Permian-levered names was received favorably, with investors questioning how much more relative multiple expansion the group will merit. But with that said, many Permian operators have announced '17 guidance already that demonstrates that capital efficient growth possible in a $50/b oil world. Investors largely feel comfortable owning names where there is a high level of certainty on 2017 production/spending. We have told clients that there is no need to take a bull/bear case on Permian-focused names as a whole. But they should look at each on a bottoms-up basis, as differences in '17 growth, balance sheets and inventory depth will differentiate winners and losers. Our two Buy-rated Permian Basin names remain Energen and Diamondback Energy.

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Calls getting the most pushback. We highlight select ratings/views on coverage companies that generated healthy debates between us and clients.

Callon Petroleum (CPE, $17 PT, Neutral). Our Neutral stance on Callon has gotten significant pushback, as clients see upside to multiples to align better with larger Permian players. Investors share our favorable view on management, which has done a strong job of both financial engineering and field execution to grow and preserve the balance sheet. Investors did agree that shares had been a significant outperformer in the industry, and need to show that they can absorb two recent deals and manage infrastructure needs

Southwestern Energy (SWN, $20 PT, Buy). We received pushback on Southwestern, with investors questioning our above-consensus '17 growth outlook in the face of guarded commentary from management on last Friday's earnings call. Despite the negative price action in SWN shares, we reiterate the fact that our '17 earnings/leverage outlook is more constructive after 3Q earnings than it was before. We continue to believe Street modeling is too conservative.

Gulfport Energy (GPOR, $36 PT, Buy). Another name that has become a major debate stock is Gulfport. Our Buy rating reflects confidence in the near-term growth outlook, strong hedges, and attractive relative valuations. Pushback has centered on curiously low inventory numbers (~600 dry gas Utica Shale locations left) despite a 230,000+ net acre footprint, execution uncertainty, management changes and a perceived necessary acquisition to bolster Utica Shale inventory.

Noble Energy (NBL, $44 PT, Buy). Many investors are content to wait to get involved in what they agree is a high quality company until: 1) clarity emerges on the regulatory environment in Israel AND 2) the company pulls the trigger on the bolt-on Permian Basin acquisition that even they have admitted is a necessary precursor to a large-scale development program. There was also major pushback on potential declines in Gulf of Mexico oil production in '18, and on the lack of more oil growth from the DJ Basin, given strong drilling economics.

Calls investors have largely agreed with. Ratings/views that were shared by most investors are highlighted below.

Oasis Petroleum (OAS, $17 PT, Buy). Our Buy rating on Oasis was met favorably by investors who largely shared our view that the pivot to Wild Basin and improving leverage profile means OAS shares should not be viewed as merely oil beta. Conversations since last Tuesday's acquisition revealed an incrementally bullish view, given the accretive nature of the deal to both traditional valuation multiples and leverage metrics.

Energen (EGN, $72 PT, Buy). Investors warmed up to our thesis that the company's soft guide of "mid teens" production growth is a low hurdle, especially given improving well productivity from new proppant-heavy completions. The favorable investor reception to Diamondback's recent '17 guidance release should embolden the company to display the productive potential of the portfolio. We acknowledged to investors that our modeling does not reflect the growth the company may deliver with a six-rig program in '17, although management may accelerate activity to that level in a $50/b WTI environment.

Matador Resources (MTDR, $26 PT, Neutral). Investors largely shared our cautious outlook on the name. Many questioned the delay on the long-expected sale of the Rustler Breaks cryogenic gas processing plant. We share their concerns and note that with leverage expected to end '17 at over 3x, the company may not be able to increase drilling activity into strengthening oil prices, something most peers are doing, without a capital raise and/or asset sale.

Glossary

AMI	Area of mutual interest
b	Barrel
Bcf	Billion cubic feet
Bcf/d	Billion cubic feet per day
Bcfe	Billion cubic feet equivalent
b/d	Barrels per day
boe	Barrel of oil equivalent
boe/d	Barrel of oil equivalent per day
BTU	British thermal units
CAGR	Compound annual growth rate
CEO	Chief executive officer
CF	Cash flow
CFO	Chief financial officer
CO_2	Carbon dioxide
Discretionary CF	Discretionary Cash Flow (Adjusted EBITDA less interest expense)
DD&A	Depletion, depreciation, and amortization
DUCs	Drilled uncompleted wells
EBITDA	Earnings before interest, taxes, depreciation, and amortization
EBITDAX	Earnings before interest, taxes, depreciation, amortization, and exploration
EBITDX	Earnings before interest, taxes, depreciation, and exploration
E&P	Exploration and production
EPS	Earnings per share
ET	Eastern time
ETF	Exchange traded fund
EUR	Estimated ultimate recovery
EV	Enterprise value
F&D	Finding & Development
FCF	Free cash flow
FT	Firm transportation
FY	Fiscal year
G&A	General and administrative
GP	General partner
IDR	Incentive distribution right
IP	Initial production
IPAA	Independent Petroleum Association of America
IPO	Initial public offering
IRR	Internal rates of return
JDA	Joint development agreement
JV	Joint venture
K	Thousand
LOE	Lease operating expense
LLS	Light Louisiana Sweet
LNG	Liquefied natural gas
LP	Limited partner
M&A	Mergers and acquisitions
mb	Thousand barrels
mb/d	Thousand barrels per day
mboe	Thousand barrels of oil equivalent
mboe/d	Thousand barrels of oil equivalent per day
mcf	Thousand cubic feet
mcf/d	Thousand cubic feet per day
mcfe	Thousand cubic feet equivalent
mcfe/d	Thousand cubic feet equivalent per day
Mdth/d	Decatherms per day
MENA	Middle East North Africa
MLP	Master limited partnership
mmb	Million barrels
mmb/d	Million barrels per day
mmboe	Million barrels of oil equivalent
mmboe/d	Million barrels of oil equivalent per day
mmbtu/d	Million British thermal units per day
mmcf/d	Million cubic feet per day
mmcfe/d	Million cubic feet equivalent per day
MTD	Month to date
MVC	Minimum volume commitments
NAV	Net asset value
NGL	Natural gas liquids
NOL	Net operating loss tax carryforward
NR	Not rated
NYMEX	New York Mercantile Exchange
Opex	Operating expense
PDP	Proved developed producing reserves
PIK	Payment in kind
PT	Price target
PUD	Proved undeveloped reserves
PV-10	Present value of proved reserves, discounted at 10% per annum
Q	quarter
q/q	Quarter over quarter
ROACE	Return on average capital employed
SCOOP	South Central Oklahoma Oil Province
STACK	Sooner Trend Anadarko Canadian and Kingfisher
SEC	Securities and Exchange Commission
SOTP	Sum of the parts
Tcf	Trillion cubic feet
Tcfe	Trillion cubic feet equivalent
TTM	Trailing twelve months
VP	Vice President
WEHLU	West Edmund Hunton Limestone Unit
WI	Working interest
WTD	Week to date
WTI	West Texas Intermediate
Y/E	Year-end
YTD	Year to date
y/y	Year over year
1H	First half
2H	Second half
1P Reserves	Proved reserves
2P Reserves	Probable reserves
3P Reserves	Possible reserves

Price Target Calculation and Key Risks

Callon Petroleum Company

PT Calculation

Our methodology for assessing ratings and a price target (PT) includes qualitative and quantitative factors, and both a "top down" and "bottoms up" process. Continuing assessment of industry conditions and metrics is done. Management philosophy and actions are examined for effectiveness. Historical and estimated balance sheets, cash flows, earnings, returns, valuation multiples, dividend yields, and other metrics are compared to peers. The market capitalizations of various energy companies sometimes makes them candidates for either acquiring other companies or being a target of an acquiring company.

For Callon, we rely on a combination of multiples-based analysis and sum-of-the-parts (SOTP) work. Our SOTP work acknowledges much of the value in CPE shares reflects unbooked resource potential that is not reflected in current earnings or cash flow.

Our $17 PT reflects a target 10x 2017E EV/EBITDA multiple, slightly above the group average, reflecting: 1) the company's core Permian Basin footprint, and 2) a more conservative target multiple than Permian Basin peers, due to the company's smaller size and inferior balance sheet.

Key Risks include but are not limited to:

1) Callon has commodity price risk on its unhedged production. A sustained decrease in crude oil prices could make its drilling program economically unfeasible. Callon has approximately half of 2016E oil production hedged, but only at $52/b. And the company only has 14% of 2017E oil hedged at $45/b. Callon currently has 30% of 2016E natural gas production hedged at $2.52/mcf, but nothing in place for 2017.

2) Callon faces execution risk. The company has grown rapidly through three major acquisitions that have totaled over $530 million since 2014 and increased the company's acreage position over 34,000 net acres. While the acquisitions have increased inventory, they have also created a more disparate Midland Basin position. Much of the growth in CPE shares has been from the company's strong execution and savvy acquisition history.

3) Callon also faces exploration risk across some of its acreage, which has not been fully derisked. The inability to de-risk zones outside of those that have already been tested, or the inability to tighten spacing assumptions, may limit upside to current inventory counts. Given Callon's relatively small inventory count (< 1,000 delineated locations) relative to other pure-play Permian Basin peers, the company's ability to increase inventory without shareholder dilution from an acquisition will be a key driver of multiple expansion, in our opinion.

Diamondback Energy, Inc.

PT Calculation

Our methodology for assessing ratings and a price target (PT) includes qualitative and quantitative factors, and both a "top down" and "bottoms up" process. Continuing

assessment of industry conditions and metrics is done. Management philosophy and actions are examined for effectiveness. Historical and estimated balance sheets, cash flows, earnings, returns, valuation multiples, dividend yields, and other metrics are compared to peers. The market capitalizations of various energy companies sometimes makes them candidates for either acquiring other companies or being a target of an acquiring company.

For Diamondback, we rely on a combination of multiples-based analysis and sum-of-the-parts (SOTP) work. Our SOTP work acknowledges a portion of the value in FANG shares reflects: 1) unbooked resource potential in the Permian Basin that is not reflected in current earnings or cash flow, and 2) Diamondback's ownership of 72 million LP units of Viper Energy Partners.

Our $124 PT reflects a target 14x 2017E EV/EBITDA multiple, a premium multiple among our coverage group. We believe a premium multiple to the group is warranted, given: 1) the company's high quality Permian Basin acreage footprint, 2) best-in-basin drilling results and efficiencies, 3) an industry leading low full-cycle cost structure, and 4) liquidity optionality from the company's ownership of LP units of Viper.

Key Risks include but are not limited to:

1) Diamondback has commodity price risk on its unhedged production. A sustained decrease in crude oil prices may impact drilling economics and drive the decision to reduce drilling activity, which will impact production/earnings/cash flow growth. Diamondback has less than 10% of oil production for the remainder of 2016 and 2017 hedged, and volumes are currently hedged between $45-$47/b.

2) Dilution risk is a concern for FANG shareholders. Diamondback has liberally used secondary equity issuances, instead of debt financing, to fund acreage acquisitions. Equity shareholders should be prepared for potential dilution as Diamondback pursues additional bolt-on acreage acquisitions.

3) Diamondback faces exploratory risk across some of its Midland Basin acreage. Diamondback has recently begun testing the stacked pay potential of acreage in Glasscock and Howard counties. Disappointing results from untested zones would weigh on the company's inventory in these areas.

4) Diamondback also has exploratory risk on its Delaware Basin acreage in Reeves and Ward counties, which it acquired in July 2016. Three zones in the area have been derisked by the industry, but Diamondback has yet to drill the area itself.

Energen Corporation

PT Calculation

Our methodology for assessing ratings and a price target (PT) includes qualitative and quantitative factors, and both a "top down" and "bottoms up" process. Continuing assessment of industry conditions and metrics is done. Management philosophy and actions are examined for effectiveness. Historical and estimated balance sheets, cash flows, earnings, returns, valuation multiples, dividend yields, and other metrics are compared to peers. The market capitalizations of various energy companies sometimes

makes them candidates for either acquiring other companies or being a target of an acquiring company.

For Energen, we rely on a combination of multiples-based analysis and sum-of-the-parts (SOTP) work. Our SOTP work acknowledges much of the value in EGN shares reflects unbooked resource potential that is not reflected in current earnings or cash flow. This resource potential equates to ~3,500 or more horizontal locations across the company's 136,000 net acre footprint in the Permian Basin, which excludes the potential acquisition of 10,000 net acres in Howard County.

Our $72 PT reflects a target 13x 2017E EV/EBITDA multiple, four turns above the group average, reflecting: 1) the company's core Permian Basin footprint across both sides of the Permian Basin, and 2) the strong balance sheet following $552 million of non-core asset divestitures in 3Q16.

Key Risks include but are not limited to:

1) Energen faces legal risk on the potential acquisition of a contiguous 10,000 net acre position in the northern core of the Midland Basin in southwest Howard County. The company is navigating through the courts to attempt to close the deal.

2) Energen has commodity price risk on its unhedged production. A sustained decrease in crude oil prices could make its drilling program economically unfeasible. Energen has typically been a robust hedger of its oil and gas production, but the firm was left largely exposed to spot pricing in 2016/2017. While the company has hedged nearly half of its oil production for both years, hedges are in the $45-$50/b range.

3) Energen faces execution risk. The company has struggled to deliver results in-line with guidance in recent quarters, which has led to some relative underperformance versus Permian Basin peers. Energen's ability to deliver dependable earnings/ production to the investment community will be a key factor determining the multiple investors are willing to put on the equity.

4) Energen also faces exploration risk across some of its acreage, which has not been fully derisked. The inability to de-risk zones outside of those that have already been tested, or the inability to tighten spacing assumptions, may limit upside to current inventory counts.

Gulfport Energy Corporation

PT Calculation

Our methodology for assessing ratings and a price target (PT) includes qualitative and quantitative factors, and both a "top down" and "bottoms up" process. Continuing assessment of industry conditions and metrics is done. Management philosophy and actions are examined for effectiveness. Historical and estimated balance sheets, cash flows, earnings, returns, valuation multiples, dividend yields, and other metrics are compared to peers. The market capitalizations of various energy companies sometimes makes them candidates for either acquiring other companies or being a target of an acquiring company.

For Gulfport Energy, we rely on a combination of multiples-based analysis and sum-of-the-parts (SOTP) work. Our SOTP work acknowledges much of the value in GPOR

shares reflects: 1) unbooked resource potential across its Utica Shale acreage position that is not reflected in current earnings or cash flow, 2) its interest in the Strike Force midstream gas gathering JV, and 3) the company's interests outside of the Utica Shale, including the Grizzly Oil Sands project and its legacy Gulf Coast production.

Our $36 PT reflects a target 10x 2017E EV/EBITDA multiple, in line with the midpoint of our coverage group. We believe a group-average multiple is warranted, given the company's strong organic growth potential in its core asset, its strong balance sheet, and our bullish outlook for natural gas prices into 2017.

Key Risks include but are not limited to:

1) Gulfport faces natural gas takeaway risk. Near-term production growth has been limited by a lack of compression on gas gathering lines and interstate pipelines. Uncertainty on the duration of this issue creates some uncertainty on production growth. Gulfport is also reliant on the build-out of several interstate pipelines to take its Appalachia gas to markets providing stronger pricing. A significant delay in one or more projects could impact near-term growth, although the depth of the company's firm takeaway portfolio should be able to absorb some delays.

2) Gulfport also faces execution risk. 2Q16 production fell short of expectations and led to underperformance following earnings, and possibly reminded investors of the difficulty the company had executing to guidance in 2012/2013, when it began developing the Utica Shale. While full-year production guidance has been maintained, investors may now rely on Gulfport to be a "show me" story, as it relates to achieving key guidance metrics.

3) Gulfport has commodity price risk on its unhedged production. A sustained decrease in natural gas prices could make much of its inventory in the Utica Shale economically unfeasible to drill. The company has hedges on 61% of 2017E gas at $3.12/mcf and 21% of 2017E oil at $51/b.

Matador Resources Company

PT Calculation

Our methodology for assessing ratings and a price target (PT) includes qualitative and quantitative factors, and both a "top down" and "bottoms up" process. Continuing assessment of industry conditions and metrics is done. Management philosophy and actions are examined for effectiveness. Historical and estimated balance sheets, cash flows, earnings, returns, valuation multiples, dividend yields, and other metrics are compared to peers. The market capitalizations of various energy companies sometimes makes them candidates for either acquiring other companies or being a target of an acquiring company.

For Matador, we rely on a combination of multiples-based analysis and sum-of-the-parts (SOTP) work. Our SOTP work acknowledges much of the value in MTDR shares reflects unbooked resource potential that is not reflected in current earnings or cash flow.

Our current $26 PT reflects a target 13x 2017E EV/EBITDA multiple, four turns above the group average, reflecting: 1) the company's core Permian Basin footprint, and 2) imminent asset sales that should address leverage concerns.

Key Risks include but are not limited to:

1) Matador faces liquidity and capital markets risk. We forecast Matador will outspend discretionary cash flow by $310 million in 2016, which includes equity issuance proceeds. The company has a $375 million secured credit facility on which there is currently nothing drawn. A reduction in the borrowing base could constrain liquidity.

2) Matador has commodity price risk on its unhedged production. A sustained decrease in crude oil prices could make its drilling program economically unfeasible. The company hedged over 50% of 2016E oil at an average floor price of $43.31/b, and 29% of 2017E oil between $38.62/b and $47.62/b. The hedges provide some protection against a drop in oil prices, but Matador's current hedge exposure leaves 71% of 2017E oil exposed to spot pricing.

3) Matador faces midstream risk. Infrastructure in the Delaware Basin to handle oil and gas gathering and water transportation to/from well pads continues to lag the demand for these services. Matador made the decision to build out infrastructure in its core Wolf/Loving area, and is doing the same at Rustler Breaks now.

4) Matador faces exploration risk. At its exploratory northern Delaware Basin fields (Arrowhead, Ranger and Twin Lakes), Matador may not encounter commercially recoverable amounts of oil and natural gas, which could lead to asset impairment charges if the acreage is deemed uneconomic. In addition, undelineated zones within current development areas such as Rustler Breaks and Wolf/Loving may prove uneconomic for drilling.

Noble Energy, Inc.

PT Calculation

Our methodology for assessing ratings and a price target (PT) includes qualitative and quantitative factors, and both a "top down" and "bottoms up" process. Continuing assessment of industry conditions and metrics is done. Management philosophy and actions are examined for effectiveness. Historical and estimated balance sheets, cash flows, earnings, returns, valuation multiples, dividend yields, and other metrics are compared to peers. The market capitalizations of various energy companies sometimes makes them candidates for either acquiring other companies or being a target of an acquiring company.

For Noble Energy, we rely on multiples-based analysis. Our current $44 PT reflects a target 9x 2017E EV/EBITDA multiple, one turn below our coverage group. A discounted target multiple seems appropriate, given uncertainty on a potential Delaware Basin acquisition and uncertainty on Leviathan. We remain bullish on the development prospects for the Leviathan gas discovery offshore Israel, but acknowledge uncertainty on the ultimate development timeline for the project remains.

Key Risks

1) Noble faces heightened geopolitical risk, due to its recent natural gas discoveries in both Cyprus and Israel. Protracted negotiations with the Israeli government over a regulatory framework for developing Leviathan have deferred first production from the field. While negotiations appear to be reaching their final stages, it is difficult to have certainty on a project development timeline. Extended discussions on the framework also defer expansion plans for Tamar.

2) NBL shareholders face potential dilution risk if a large Permian Basin acquisition ultimately gets announced and is financed with an equity issuance.

3) Noble has commodity price risk on its unhedged production. A sustained decrease in crude oil and/or natural gas prices could make its drilling program economically unfeasible and result in low/no production growth. The company has no natural gas hedges in place for 2017, and currently has only 8% of oil production hedged.

4) The company also has project execution risk related to potential future development of Leviathan. Noble needs to secure final government approval, project financing, and contracts from purchasers of gas to proceed. Delays in any one of these three areas could defer first production.

Oasis Petroleum Inc.

PT Calculation

Our methodology for assessing ratings and a price target (PT) includes qualitative and quantitative factors, and both a "top down" and "bottoms up" process. Continuing assessment of industry conditions and metrics is done. Management philosophy and actions are examined for effectiveness. Historical and estimated balance sheets, cash flows, earnings, returns, valuation multiples, dividend yields, and other metrics are compared to peers. The market capitalizations of various energy companies sometimes makes them candidates for either acquiring other companies or being a target of an acquiring company.

For Oasis, we rely on a combination of multiples-based analysis and sum-of-the-parts (SOTP) work. Our SOTP work acknowledges much of the value in OAS shares reflects: 1) unbooked resource potential that is not reflected in current earnings or cash flow, 2) the value of its Oasis Midstream Services segment, and 3) the value of its Oasis Well Services segment.

Our $17 PT reflects a target 9x 2017E EV/EBITDA multiple, one turn below the group average, reflecting: 1) the market's persistent uncertainty on the relative quality of core Bakken wells versus other domestic shale oil plays, and 2) a more conservative target multiple due to elevated leverage on the balance sheet that could grind higher through 2017 if WTI stays below $50/b.

Key Risks include but are not limited to:

1) Oasis faces balance sheet risk. We forecast Oasis' current 3.1x leverage position will increase to 3.7x at 4Q17, assuming no capital raises and $50/b WTI in 2017. While the company maintains ~$1.1 billion in liquidity and is not close to tripping any borrowing base covenants, the elevated leverage remains a concern, and could weigh on OAS shares.

2) Oasis has commodity price risk on its unhedged production. A sustained decrease in crude oil prices could make its drilling program economically unfeasible outside of its “core of the core” inventory. Oasis hedged ~75% of 2016E oil at an average floor price of $51/b, and 42% of 2017E oil at $48/b. The hedges provide some protection against a drop in oil prices, but also limit upside in earnings should oil prices move significantly higher.

3) Oasis faces midstream risk. The company’s near-term production growth will come from the Wild Basin properties it acquired in 2013. The current build-out of water, oil and gas gathering lines are on track, and drilling is underway, but any delay in hooking the new wells to sales will weigh on production/earnings.

Southwestern Energy Co.

PT Calculation

Our methodology for assessing ratings and a price target (PT) includes qualitative and quantitative factors, and both a "top down" and "bottoms up" process. Continuing assessment of industry conditions and metrics is done. Management philosophy and actions are examined for effectiveness. Historical and estimated balance sheets, cash flows, earnings, returns, valuation multiples, dividend yields, and other metrics are compared to peers. The market capitalizations of various energy companies sometimes makes them candidates for either acquiring other companies or being a target of an acquiring company.

For Southwestern, we rely on a combination of multiples-based analysis and sum-of-the-parts (SOTP) work. Our SOTP work acknowledges that much of the value in SWN shares reflects unbooked resource potential and midstream assets that do not appear to be explicitly reflected in current earnings or cash flow. This includes: 1) core inventory in Appalachia that has not yet been accounted for in proved reserves, and 2) Southwestern’s midstream and oil services assets that support drilling and gas gathering in the Fayetteville Shale and Appalachia. Our $20 PT reflects a target 8.5x 2017E EV/EBITDA multiple

Key Risks include but are not limited to:

1) Southwestern faces balance sheet risk. Despite entering into two significant capital-raising transactions in 3Q16 ($1.25 billion equity issuance, $450 million non-core asset sale), the company remains over 3x levered (pro forma). And the company’s new credit facility arrangement is more punitive than the previous unsecured facility, and will limit borrowings. We do note that the company has pro forma liquidity of $1.9 billion, despite the outsized leverage.

2) Southwestern has commodity price risk on its largely unhedged production, especially as it pertains to natural gas, which represents ~90% of total production. Another sustained decrease in natural gas prices to/below $2/mcf could again make its drilling program economically unfeasible and result in low/no production growth. The company currently has hedges on only 14% of 2016E natural gas production and 30% of 2017E natural gas production. This exposure means that the company’s leverage and earnings growth outlook will be almost entirely driven by the near-term movements of natural gas prices.

3) The company also faces midstream risk. Southwestern's main production growth vehicle is its Southwestern Appalachia acreage, mostly in West Virginia. The company has contracts in place on the Rover and Columbia Gas Mountaineer Xpress pipelines, but those pipelines will need to be in service by late 2017 and late 2018, respectively, for the company to fully utilize this acreage as its main growth driver.

IMPORTANT DISCLOSURES

The disclosures for the subject companies of this report as well as the disclosures for Mizuho Securities USA Inc. entire coverage universe can be found at https://msusa.bluematrix.com/sellside/Disclosures.action or obtained by contacting EQSupervisoryAnalystUS@us.mizuho-sc.com or via postal mail at Equity Research Editorial Department, Mizuho Securities USA Inc., 320 Park Avenue, 12th Floor, New York NY, 10022.

Ownership Disclosures and Material Conflicts of Interest or Position as Officer or Director

None

Receipt of Compensation

Mizuho Securities USA Inc. and or its affiliates makes a market in the following securities: Callon Petroleum Company, Diamondback Energy, Inc., Energen Corporation, Gulfport Energy Corporation, Noble Energy, Inc., Oasis Petroleum Inc. and Southwestern Energy Co.

Mizuho Securities USA Inc. and or its affiliates has received compensation for investment banking services for Noble Energy, Inc. and Southwestern Energy Co. in the past 12 months.

Mizuho Securities USA Inc. and or its affiliates has managed or co-managed a public offering of securities for Noble Energy, Inc. and Southwestern Energy Co. in the past 12 months.

Mizuho Securities USA Inc. and or its affiliates have provided investment banking services for Southwestern Energy Co. who is or was a client in the past 12 months.

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I, Timothy Rezvan, hereby certify that the views expressed in this research report accurately reflect my personal views about any and all the subject companies. No part of my compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this research report.

Rating Definitions

Mizuho Securities USA investment ratings are based on the following definitions. Anticipated share price change is based on a 6- to 12-month time frame. Return expectation excludes dividends.

Buy:	Stocks for which the anticipated share price appreciation exceeds 10%.
Neutral:	Stocks for which the anticipated share price appreciation is within 10% of the share price.
Underperform:	Stocks for which the anticipated share price falls by 10% or more.
RS:	Rating Suspended - rating and price objective temporarily suspended.
NR:	No Rating - not covered, and therefore not assigned a rating.

Rating Distribution

(As of 10/24)	**% of coverage**	**IB service past 12 mo**
Buy (Buy)	43.18%	45.61%
Hold (Neutral)	54.55%	29.17%
Sell (Underperform)	2.27%	33.33%

For disclosure purposes only (NYSE and FINRA ratings distribution requirements), our Buy, Neutral and Underperform ratings are displayed as Buy, Hold and Sell, respectively.

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