

# CASH FLOWS

## Shenandoah, Mannix were Profitable to Shell Capital

Two recent **Shell Capital Inc.**, Houston, financings to start-up oil and gas companies resulted in huge success. Within two years of closing, the capital provider had been repaid in full and realized internal rates of returns (IRR) in excess of 30%.

In the first deal, Shell Capital aided **Shenandoah Energy Inc.**, a newly formed Denver company and its recently assembled, but experienced, executive management team. Shenandoah had been created to acquire **Chevron USA Inc.**'s Uintah Basin properties and **The Chandler Co.**, a long-time family company active in the southern Rockies. (See "Ahead of the Curve," *Oil and Gas Investor*, November 2000.) The challenge to financing was this issue of producing "black wax," a type of crude with which most financial investors were ill-equipped to deal. However, Shell Capital was armed with its parent's years of experience in Rockies waxy crudes, so it felt none of the discomfort that may have paralyzed its financial brethren.

Moreover, it so appreciated the experience and competence of Mitch Solich, Shenandoah chief executive officer, and his management team that it was able to proceed quickly. Between Thanksgiving and Christmas 1999, Shell completed due diligence, secured **Prudential Capital Group** as an additional capital partner, and documented and closed the deal by Chevron's deadline.

The financing raised \$90 million: \$70 million as debt and \$20 million as preferred stock. Shell Capital and Prudential Capital Group shared the senior debt two-thirds and one-third, respectively, while the subordinated debt was split 50-50. The preferred shares were owned equally by Shell, Prudential, Chevron and certain former Chandler stockholders. The properties were purchased for \$60 million, and \$30 million was spent on drilling new wells.

Michael Keener, director of Shell Capital, says Shenandoah's performance was outstanding. Within a year, sufficient production and reserves were brought on to permit it to refinance the entire debt through a commercial facility syndicated through **First Union**. Within another six months, Shenandoah was sold to a subsidiary of **Questar Corp.**, Salt Lake City. In the deal, Questar valued Shenandoah at more than \$400 million.

Shenandoah had drilled 235 wells, spent \$118 million, increased proved

reserves 125% at a finding cost of 18 cents per thousand cubic feet of gas equivalent (Mcf), and increased EBITDA (earnings before interest, taxes, depreciation and amortization) 8.5 times. In addition to repayment of their loans, Shell Capital and Prudential Capital Group realized more than three times their equity investments in

*The day the Questar deal closed, Solich had checks delivered to the pump hands and property managers, all of whom he had incentivized with options. Some of the checks were bigger than their annual salaries.*

the preferred stock.

The day the Questar deal closed, Solich had checks delivered to the pump hands and property managers, all of whom he had incentivized with options. Some of the checks were bigger than their annual salaries.

"Any deal Mitch wants to bring us in the future, we will consider favorably," Keener says. "Mitch and his whole team were consummate professionals and a pleasure to work with."

Mannix Oil Co.

Tulsa-based **Mannix Oil Co.** was established by Roy Grossman, Berry Mullenix and Steve Ayers in 1995 to pursue relatively conventional oil acquisitions, followed by enhancement. From 1995-99, the company arranged seven different placements, including equity and debt to high-net-worth individuals, commercial debt, a volumetric production payment, and property-level joint-venture financing with two

venture-capital funds. In January 2000, Shell Capital provided a \$40-million project-debt facility.

Although the Mannix principals also had experience in operating wells in their focus areas, their plan for drilling coalbed-methane wells in thin Hartshorne coalbeds of the Arkoma Basin was nascent. (See "Arkoma Basin," July 2000.) Unlike with black wax, Shell Capital's affiliates had limited experience, but they analyzed Mannix's coalbed-methane development expertise.

Berry recalls, "I trooped through all the financing-source booths at the 1999 NAPE, asking one question: 'If we could demonstrate we had the ability or technology that would prove up commercial reserves over several locations, would you lend me money to drill them?' Only Lee Campbell at Shell Capital would do it."

Fourteen months later, Mannix was merged into **Williams Production Co.**, the upstream subsidiary of **The Williams Cos. Inc.**, Tulsa, for \$36 million. Some \$16.3 million of the proceeds went back to Shell Capital to repay its loan, with the balance split among equity holders, other third-party obligations and Mannix's three principals.

Keener says, "We would love to see them come back to us for new financing. The Mannix financing also exceeded our every expectation."

Grossman and Mullenix already have formed a new company, **Smart Exploration**, with which they intend to pursue more latent coalbed-methane projects. Would they go back to Shell Capital? "You bet," they say.

—Cameron O. Smith,  
Cosco Capital Management

### Shenandoah Sources of Capital & Uses (\$MM)

Sources	Uses
Preferred stock	Cash distribution to Chevron
Subordinated notes	Cash distribution to Chandler
Senior debt	Drilling capital
Cash on hand	Fees, expenses
Total	Total

### Mannix Sources of Capital (\$MM)

1995-97	\$2.0	Angel notes; principals, sweat equity
Dec. 1997	\$0.4	Duke (Pan Energy) vol. prod. payment
March 1998	\$3.0	Compass Bank credit facility (\$5MM)
Dec. 1998	\$10.3	Contra Venture Fund JV
Nov. 1998	\$0.3	Angel Equity @ \$3MM valuation
June 1999	\$3.8	Tailwind Venture Fund JV (\$40MM allocation)
Dec. 1999	\$0.5	Angel equity @ \$10MM valuation
Jan. 2000	\$17.6	Shell Capital \$40MM project debt facility
March 2001	\$36.0	Sale to Williams (effective)