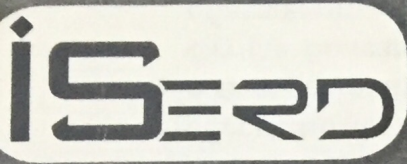


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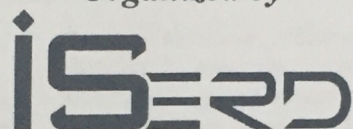
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VALUATION: GLOBAL OIL AND GAS INDUSTRY

¹DIANA KULIBAYEVA, ²DINARA SADYKHANOVA

KazNU Al Farabi State University, Almaty, Kazakhstan, Lecturers of the Department of Finance.

Abstract: This article helps to understand valuation in the global oil and gas industry. It gives a general overview of the oil and gas industry, focusing on the recent developments. The oil and gas industry plays a very important role in the world economy. Nearly 60% of the global population depends on oil and gas for its daily energy requirements. Even on business side, oil and gas fuel the global commerce. Oil and gas companies are classified on the basis of their operation in the value chain – upstream, midstream and downstream. Valuation methodology is based on whether a company operates in the upstream, midstream or downstream. Certain companies operate in more than one segment and for such companies the valuation methodology is a consolidation of two or more methods.

The three main valuation approaches are the income approach, the asset approach, and the market approach. Generally, analysts use more than one methodology to ensure more accurate results. This article gives a brief explanation of the key metrics such as EBITDA, EBIT etc. that are used in valuation. It also refers to the theoretical framework on the accuracy of various valuation methods. Some other points highlighted in this article are industry challenges for valuation, revenue projections in the oil and gas industry, risks involved and mitigation of the same. The article concludes with suggestions on the ways in which oil and gas companies can be successful in the long run amidst difficult business landscape.

Keywords: Valuation, Upstream, Midstream, Downstream, Discounted Cash Flow, Growth, Discount Rate, EBITDA, EBIT.

I. INTRODUCTION

Recent trend in Global Oil & Gas Industry was featured by economic turmoil, untamed competition and mind-numbing price movement. Energy companies need to be bold about transforming their business models.

We believe that there is no point in worrying about the swings in prices. Volatility is mostly out of control of the industry leaders. The future of industry and its strategic plan is a puzzle at the moment. At this juncture oil companies (refiner or producers) should try to find the answer of the following two questions:

- How to lock the demand in such market
- Is business prepared to prosper in environment of oversupply

Once the companies find the answer of both the questions, they should be able to forge a pathway for success, no matter how uncertain the prices for their products.

The ground rule and environment has been shifted dramatically. The future outlook of the industry is very different than the scenario couple of years back when the prices and other fundamentals were controlled by the cartels. Conventional structural discipline has been replaced by the systemic imbalance triggered by vastly increased supply and slower demand. Increase in supply of liquid fuel is twice that of increase in demand. This is coupled with the following reasons:

- Global economic weakness (Slower growth in China and financial woes in Europe)
- Stronger fuel economy regulations
- Increasing viable form of alternate energy
- Major progress in engine efficiency

On top of the above, robust new reserves of shale oil, in numerous regions around the world are flooding the market.

In the above context and driven by its nature of business, the valuation of oil and gas industry is unique. This is because it is subject to constant scrutiny and regulation from multiple angles. It has two distinct elements one is in corporate settings and other in the field. Apart from this, energy companies are also valued by the financial community differently than the other industries. The valuation objective is also very important. A company can be valued for different reasons such as to decide on corporate structure, to find out its capital funding or determine pricing for merger and acquisition. The valuation is also important to provide its accurate assessment to handle debt, expected rate of return and approximate market value.

Literature Review

We can now look at the oil and gas industry from many angles. The importance oil plays in this world is very much closer to inevitable. Over 60% of the world population meets their daily energy needs from oil and gas. Rest 40% is sourced from coal, nuclear and hydroelectric power and emerging renewable energies like wind, solar, tidal and biomass product. Thereby whenever gasoline prices change, public at large get pinch of price effect. This is almost similar in the world over other than some of the developed countries where fuel cost less than a brand of bottled water.

Guigues, V., Sagastizábal, C. & Zubelli, JP. (2014) Insist that the other aspect of oil and gas is feedstocks. The petroleum raw materials are used to manufacture fertilizers, fabrics, synthetic rubber and the plastics. This goes into almost everything we use these days.

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