Western Midstream Partners

The response of American consumers wounded by soaring gasoline and natural gas prices is summed up in the famous line from Charles Dickens's "Oliver Twist." The starving orphan walks up to the overseer of the workhouse, empty food bowl in hand, and asks, "Please, sir, may I have some more?" And to those who don't understand the energy industry, the lack of response to calls for expanded drilling by U.S. E&Ps seems as uncaring as Oliver's tormentor Mr. Bumble, who confined and caned the poor lad. The truth is that oil and gas producers, whipsawed over the last decade by extreme price volatility and negative investor sentiment, have adopted a new fiscal discipline that prioritizes free cash flow generation to reduce debt and reward shareholders over deficit-inducing growth. Tasked with funding a massive infrastructure buildout to support surging production from the Shale Revolution, midstream companies have also been buffeted by volatile commodity prices, eroding investor support, shifting upstream investment patterns and, finally, a global pandemic. After debt peaked and share prices cratered in early 2020, midstream companies slashed spending and distributions to conserve capital.

However, midstreamers face a different set of challenges than E&P companies in repairing the balance sheet and restoring investor confidence. The primary reason is that midstream investment decisions are determined by E&P development and production activity. Infrastructure buildout is commonly supported by volume commitments from producers. However, infrastructure can't be relocated like rigs, and those contracts eventually expire, leaving midstreamers scrambling to fill pipes and feed processing plants in plays where producers are pulling back or exiting. In contrast, it has become more difficult to find and fund expansion or acquisition opportunities where the recovery in drilling activity has been robust, such as the Permian. Midstream capital allocation has become a delicate balancing act of prioritizing free cash flow to reduce leverage and raise shareholder returns with judicious investment in high-return opportunities and minimizing declines in lower-return areas.

This Spotlight Report focuses on the strategic shifts made by a large ($11.2 billion market cap) midstream master limited partnership (MLP) Western Midstream Partners, LP (NYSE: WES), which faced an added challenge to recovery when its general partner was acquired in one of the major upstream transactions of the last two decades. WES was founded in 2007 by Anadarko Petroleum, which, like several other public E&Ps, decided to drop down assets to a separate entity to take advantage of the higher valuation afforded by investors to higher-return MLP structures. Dropdowns gave WES an initial portfolio that largely consisted of gas gathering, processing, and transportation systems in Anadarko's core Rockies acreage, especially in the DJ Basin, and acreage in the Mid-Continent and Appalachia along with equity stakes in certain interstate pipelines. In 2014, Anadarko began shifting investment to the Permian's burgeoning Delaware Basin, and WES jumpstarted its expansion into the area with the $1.5 billion acquisition of Nuevo Midstream. The midstream partnership, majority owned and controlled by Anadarko, allocated the bulk of its $1 billion annual capex to additional Delaware growth through 2018 to support its parent company's drilling expansion.

©Copyright 2022 RBN Energy, LLC and East Daley

In early 2019, Chevron targeted that prime Permian position with a $50 billion agreement to acquire Anadarko and, along with it, controlling interest in WES. Occidental Petroleum (NYSE: OXY) subsequently outbid Chevron with a heftier, more cash-weighted $57 billion offer. However, the subsequent plunge in commodity prices in late 2019 plunged Oxy into a liquidity crisis that resulted in it initiating a process to divest its majority interest in WES as part of a significant and urgent divestiture process to reduce debt. But the effort to monetize the WES stake was unsuccessful, hampered by restricted access to capital markets for potential acquirers along with growing concerns about WES's ballooning debt and future production in the DJ Basin and other Rockies plays. In early 2020, Oxy transferred employment of the WES management team to WES, which insured independent management control of the partnership's strategic initiatives and day-to-day operations.

Still WES's unit price plunged to an all-time low of just over $3.00 with onset of the pandemic in March 2020, a fraction of the $65/unit high in early 2015 and $30/unit price at the time of the Chevron bid. WES's newly independent management responded by embracing a new, conservative financial discipline that included slashing quarterly distributions and capital expenditures. In this Spotlight Report, we chronicle the subsequent recovery triggered by the new investment strategy over the subsequent two years. The achievements include over 15% debt reduction, achieving a 3.6x year-end 2021 leverage ratio; a 53% increase in the quarterly dividend; and a $1 billion share repurchase authorization. As a result, the unit price has rebounded to over $28.

However, WES's prioritization of financial stability has not allayed concerns about long-term EBITDA growth. A continued strong drilling rebound across its extensive gathering and processing systems in the core of the Delaware has boosted the EBITDA contribution of those assets to 50% of the company total. But the restrictive Colorado regulatory permitting system and major M&A consolidation is forecast to contribute to continued declines in DJ Basin volumes and revenues, and contract expirations and sharply reduced drilling are lowering returns from other Rockies assets. All this raises critical questions. What additional investments could WES make to benefit further from the strong Permian rebound, including possible infrastructure expansions and acquisitions? What are the impacts of the erosion in volumes and EBITDA from non-Permian assets? What are the prospects for increased shareholder returns?

East Daley's exhaustive analysis of Western Midstream Partners provides detailed forecasts, including the following conclusions:

- Adjusted EBITDA is expected to rise from $1.947 billion in 2021 to $2.117 billion in 2022, then decline back to near the 2021 level at $1.982 billion in 2025.
- Gas Gathering & Processing segment Adjusted EBITDA will decline slightly from $1.287 billion in 2021 to $1.261 billion in 2025 as 65% growth in the Delaware Basin will nearly offset 27% and 52% declines in the DJ Basin and Non-Core Gas G&P assets, respectively.
- Income from Equity Investments will rise a modest 9% to $721 million in 2025.
- New debt will decline 20% from 2022-2025 and the leverage ratio will fall to 3.17x.
- The distribution coverage ratio will remain above 1.6x through 2025, which incorporates a projected 25% increase in the annual dividend.

RBN Backstage Pass subscribers and East Daley guests are invited to join the Spotlight Live Session on Western Midstream.

Spotlight Live Sessions are 30-minute live webinars, with senior members from RBN and East Daley who present key take-aways from the latest Spotlight report and answer live and per-submitted questions from the audience.

June 22nd @ 10:30 AM CT

To register, please visit: https://rbnenergy.com/spotlight/live-sessions/wm

---

RBN Backstage Pass subscribers and East Daley guests are also invited to our Spotlight Happy Hour!

June 22nd @ 5:30-7 PM CT

Houston, TX

Sign up for Backstage Pass to learn more: https://rbnenergy.com/subscriber

This Spotlight Report from RBN Energy and East Daley is available for individual purchase or as part of RBN's Backstage Pass premium content service at rbnenergy.com.

For more information on individual or group subscriptions, send an email to info@rbnenergy.com or call 888-613-8874.

The *Table of Contents* for "Spotlight: Western Midstream Partners" is included on the following page.

Table of Contents

1. Spotlight Reports from RBN Energy and East Daley ... - 4 -
1.1 What is Spotlight? ... - 4 -
1.2 How Can I Get Spotlight? ... - 4 -
2. Western Midstream Overview ... - 4 -
2.1 How It Got Here: Western Midstream Strategic Milestones ... - 5 -
3. Western Midstream: Company Strategy and Challenges ... - 8 -
3.1 Western Midstream Financial Performance ... - 9 -
4. Western Midstream Gas Gathering and Processing Segment ... - 9 -
4.1 Key Takeaways ... - 9 -
4.2 Overview of Gas Gathering and Processing Segment ... - 9 -
4.3 EBITDA Analysis for DJ Basin Gas Gathering and Processing Assets ... - 10 -
4.4 EBITDA Analysis for Permian Basin Gas Gathering and Processing Assets ... - 12 -
4.4.1 Delaware Basin Midstream ... - 12 -
4.4.2 Delaware Basin Joint Venture ... - 13 -
4.4.3 Mentone Processing ... - 14 -
4.5 EBITDA Analysis for Non-Core Gas Gathering and Processing Assets ... - 14 -
4.5.1 Appalachian Basin Gathering and Processing ... - 15 -
4.5.2 Uinta Basin ... - 15 -
4.5.3 Green River Basin ... - 16 -
4.5.4 Powder River Basin ... - 17 -
4.5.5 Eagle Ford Basin ... - 17 -
5. Western Midstream Other Midstream Assets Segment ... - 17 -
5.1 Key Takeaways ... - 17 -
5.2 Overview of the Other Midstream Assets Segment ... - 17 -
5.3 EBITDA Analysis for the Oil Gathering Assets ... - 17 -
5.3.1 Wattenberg Oil Complex ... - 18 -
5.3.2 Delaware Basin Midstream Oil Services (DBM) ... - 18 -
5.4 EBITDA Analysis for Water Disposal Assets ... - 19 -
5.4.1 APC Water Holdings ... - 19 -
5.4.2 Delaware Basin Midstream Water Disposal ... - 20 -
5.5 Western Midstream Equity Interests ... - 20 -
6. Western Midstream Conclusion & Financial Outlook ... - 21 -

1. Spotlight Reports from RBN Energy and East Daley

1.1 What is Spotlight?

Spotlight reports provide a deep dive into the fundamentals that shape the outlook for midstream energy companies. Our goal is to provide a comprehensive, fundamentals-based view of our Spotlight companies built on a bottoms-up analysis of their assets and operations. We tear apart their asset structure to reveal what volumes are flowing, what rates are (and can be) charged, how they are exposed to commodity price risk, how their assets fit together, and what aspects of their operations provide competitive advantages in today's extremely volatile energy marketplace.

Spotlight is a joint venture of RBN Energy and East Daley. We have joined together with the support of Oil & Gas Financial Analytics LLC to provide a comprehensive, detailed insight into the companies we select for our analysis. Our combined teams leverage deep experience to analyze publicly available data to get to the answers that can be overlooked in the more generalized assessments that are more common in the marketplace today. Instead of such a high-level approach, we get into the micro-level detail, integrating fundamentals analysis, market information, and company data in a comprehensive model that provides a clear picture of the company and its prospects.

As with all energy fundamental analysis, Spotlight reports rely on estimates and approximations of volumes, throughputs and fees. No non-public data from the subject company or any other source has been used in the preparation of this report.

1.2 How Can I Get Spotlight?

Spotlight reports are available to RBN Backstage Pass subscribers. Non-subscribers may purchase individual company Spotlight reports separately. For more information about Spotlight, go to rbnenergy.com/spotlight.